

TRAVELERS COMPANIES, INC.  
Form 10-K  
February 13, 2014

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## UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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### FORM 10-K

ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2013

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to

Commission file number 001-10898

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## The Travelers Companies, Inc.

(Exact name of registrant as specified in its charter)

**Minnesota**  
(State or other jurisdiction of  
incorporation or organization)

**41-0518860**  
(I.R.S. Employer  
Identification No.)

**485 Lexington Avenue,**  
**New York, NY 10017**  
(Address of principal executive offices) (Zip Code)

**(917) 778-6000**  
(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act:**

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
Common stock, without par value	New York Stock Exchange

**Securities registered pursuant to Section 12(g) of the Act:      None**

Indicate by check mark if the registrant is a well-known seasoned issuer (as defined in Rule 405 of the Securities Act).    Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.    Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.    Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).    Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.   

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Act (Check one):

Large accelerated filer   

Accelerated filer   

Non-accelerated filer   

Smaller reporting company   

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).    Yes  No

As of June 30, 2013, the aggregate market value of the registrant's voting and non-voting common equity held by non-affiliates was \$29,744,391,793.

As of February 7, 2014, 352,327,135 shares of the registrant's common stock (without par value) were outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Registrant's Proxy Statement relating to the 2014 Annual Meeting of Shareholders are incorporated by reference into Part III of this report.

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**The Travelers Companies, Inc.**

**Annual Report on Form 10-K**

**For Fiscal Year Ended December 31, 2013**

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**PART I**

**Item 1. BUSINESS**

The Travelers Companies, Inc. (together with its consolidated subsidiaries, the Company) is a holding company principally engaged, through its subsidiaries, in providing a wide range of commercial and personal property and casualty insurance products and services to businesses, government units, associations and individuals. The Company is incorporated as a general business corporation under the laws of the state of Minnesota and is one of the oldest insurance organizations in the United States, dating back to 1853. The principal executive offices of the Company are located at 485 Lexington Avenue, New York, New York 10017, and its telephone number is (917) 778-6000. The Company also maintains executive offices in Hartford, Connecticut, and St. Paul, Minnesota. The term "TRV" in this document refers to The Travelers Companies, Inc., the parent holding company excluding subsidiaries.

For a summary of the Company's revenues, operating income and total assets by reportable business segments, see note 2 of notes to the Company's consolidated financial statements.

**PROPERTY AND CASUALTY INSURANCE OPERATIONS**

The property and casualty insurance industry is highly competitive in the areas of price, service, product offerings, agent relationships and methods of distribution. Distribution methods include the use of independent agents, exclusive agents, direct marketing (including the use of toll-free numbers and the internet) and/or salaried employees. According to A.M. Best, there are approximately 1,300 property and casualty groups in the United States, comprising approximately 2,750 property and casualty companies. Of those groups, the top 150 accounted for approximately 92% of the consolidated industry's total net written premiums in 2012. The Company competes with both foreign and domestic insurers. In addition, several property and casualty insurers writing commercial lines of business, including the Company, offer products for alternative forms of risk protection in addition to traditional insurance products. These products include large deductible programs and various forms of self-insurance, some of which utilize captive insurance companies and risk retention groups. The Company's competitive position in the marketplace is based on many factors, including the following:

- premiums charged;
- contract terms and conditions;
- products and services offered;
- claim service;
- agent, broker and client relationships;
- local presence;
- geographic scope of business;
- overall financial strength;
- ratings assigned by independent rating agencies;

experience and qualifications of employees; and

technology and information systems.

In addition, the marketplace is affected by available capacity of the insurance industry, as measured by policyholders' surplus, and the availability of reinsurance. Industry capacity as measured by policyholders' surplus expands and contracts primarily in conjunction with profit levels generated by the industry, less amounts returned to shareholders through dividends and share repurchases. Capital raised by debt and equity offerings may also increase policyholders' surplus.

Table of Contents**Pricing and Underwriting**

Pricing of the Company's property and casualty insurance products is generally developed based upon an estimation of expected losses, the expenses associated with producing, issuing and servicing business and managing claims, the time value of money related to the expected loss and expense cash flows, and a reasonable allowance for profit that considers the capital needed to support the Company's business. The Company has a disciplined approach to underwriting and risk management that over the long-term emphasizes product returns and profitable growth rather than premium volume or market share. The Company's insurance subsidiaries are subject to state laws and regulations regarding rate and policy form approvals. The applicable state laws and regulations establish standards in certain lines of business to ensure that rates are not excessive, inadequate, unfairly discriminatory, or used to engage in unfair price competition. The Company's ability to increase rates and the relative timing of the process are dependent upon each respective state's requirements, as well as the competitive market environment.

**Geographic Distribution**

The following table shows the geographic distribution of the Company's consolidated direct written premiums for the year ended December 31, 2013:

State	% of Total
California	10.1%
New York	9.9
Texas	7.2
Pennsylvania	4.9
Florida	4.2
New Jersey	4.0
Illinois	4.0
Massachusetts	3.3
Georgia	3.1
All other domestic(1)	44.7
Total domestic	95.4
International	4.6
Consolidated total	100.0%

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- (1) No other single state accounted for 3.0% or more of the total direct written premiums written in 2013 by the Company's domestic operations.

**Catastrophe Exposure**

The wide geographic distribution of the Company's property and casualty insurance operations exposes it to claims arising out of catastrophes. The Company uses various analyses and methods, including proprietary and third-party computer modeling processes, to continually monitor and analyze underwriting risks of business in natural catastrophe-prone areas and target risk areas for conventional terrorist attacks (defined as attacks other than nuclear, biological, chemical or radiological events). The Company relies, in part, upon this analysis to make underwriting decisions designed to manage its exposure on catastrophe-exposed business. For example, the Company has limited the writing of new property and homeowners business in some markets and has selectively taken underwriting actions on new and existing business. These underwriting actions on new and existing business include tightened underwriting standards, selective price increases and changes to deductibles specific to hurricane-, tornado-, wind- and hail-prone areas. See "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Catastrophe Modeling" and " Changing Climate Conditions."



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The Company also utilizes reinsurance to manage its aggregate exposures to catastrophes. See " Reinsurance."

The Company is organized into three reportable business segments: Business Insurance; Financial, Professional & International Insurance; and Personal Insurance.

**BUSINESS INSURANCE**

The Business Insurance segment offers a broad array of property and casualty insurance and insurance-related services to its clients primarily in the United States. Business Insurance is organized into the following six groups, which collectively comprise Business Insurance Core operations:

*Select Accounts* provides small businesses with property and casualty products, including commercial multi-peril, commercial property, general liability, commercial auto and workers' compensation insurance.

*Commercial Accounts* provides mid-sized businesses with property and casualty products, including commercial multi-peril, commercial property, general liability, commercial auto and workers' compensation insurance.

*National Accounts* provides large companies with casualty products and services, including workers' compensation, general liability and automobile liability, generally utilizing loss-sensitive products, on both a bundled and unbundled basis. National Accounts also includes the Company's commercial residual market business, which primarily offers workers' compensation products and services to the involuntary market.

*Industry-Focused Underwriting.* The following units provide targeted industries with differentiated combinations of insurance coverage, risk management, claims handling and other services:

*Construction* serves a broad range of construction businesses, offering guaranteed cost products and loss sensitive programs structured to meet customer needs. Products offered include workers' compensation, general liability and commercial auto coverages, and other risk management solutions.

*Technology* serves small to large companies involved in telecommunications, information technology, medical technology and electronics manufacturing, offering a comprehensive portfolio of products and services. Products offered include commercial property, commercial auto, general liability, workers' compensation, internet liability, technology errors and omissions coverages and global companion products.

*Public Sector Services* provides insurance products and services to public entities including municipalities, counties, Indian Nation gaming organizations and selected special government districts such as water and sewer utilities. Products offered by this unit typically cover commercial property, commercial auto, general liability, professional liability and workers' compensation exposures.

*Oil & Gas* provides specialized property and liability products and services for customers involved in the exploration and production of oil and natural gas, including operators, drilling and well servicing contractors, supply companies and manufacturers that support upstream operations. Products offered include workers' compensation, general liability, commercial auto, commercial property, control of well and other risk management solutions.

*Agribusiness* serves small to medium-sized agricultural businesses, including farms, ranches, wineries and related operations. Products offered include property and liability coverages other than workers' compensation.





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*Target Risk Underwriting.* The following units serve commercial businesses requiring specialized product underwriting, claims handling and risk management services:

*National Property* provides traditional and customized property insurance programs to large and mid-sized customers, including office building owners, manufacturers, municipalities and schools, retailers and service businesses.

*Inland Marine* provides insurance for goods in transit and movable objects for customers such as jewelers, museums, contractors and the transportation industry. Builders' risk insurance is also offered to customers during the construction, renovation or repair of buildings and other structures.

*Ocean Marine* serves the marine transportation industry and related services, as well as other businesses involved in international trade. The Company's product offerings in this unit fall under six main coverage categories: marine liability, cargo, hull and machinery, protection and indemnity, pleasure craft, and marine property and liability.

*Excess Casualty* serves small to mid-sized commercial businesses, offering mono-line umbrella and excess coverage where the Company typically does not write the primary casualty coverage or where other business units within the Company prefer to access the underwriting expertise and/or limit capacity of the Excess Casualty business unit.

*Boiler & Machinery* serves small to large companies, offering comprehensive breakdown coverages for equipment, including property and business interruption coverages. Through the BoilerRe unit, Boiler & Machinery also serves other property and casualty carriers that do not have in-house expertise with reinsurance, underwriting, engineering, claim handling and risk management services for this type of coverage.

*Global Partner Services* provides insurance to foreign organizations with property and liability exposures located in the United States (reverse-flow) as part of a global program.

*Specialized Distribution.* The following units market and underwrite their products to customers predominantly through licensed wholesale agents and program managers that manage customers' unique insurance requirements:

*Northland* provides insurance coverage for the commercial transportation industry, as well as commercial liability and commercial property policies for small, difficult to place specialty classes of commercial business, primarily on an excess and surplus lines basis.

*National Programs* offers tailored property and casualty programs on an admitted basis for customers with common risk characteristics or coverage requirements. Programs available include, but are not limited to, those for entertainment, architects and engineers, equipment rental, golf services and owners of franchised businesses.

Business Insurance also includes the Special Liability Group (which manages the Company's asbestos and environmental liabilities) and the assumed reinsurance and certain other runoff operations, which are collectively referred to as Business Insurance Other.

Table of Contents**Selected Market and Product Information**

The following table sets forth Business Insurance net written premiums by market and product line for the periods indicated. For a description of the markets and product lines referred to in the table, see "Principal Markets and Methods of Distribution" and "Product Lines," respectively.

(for the year ended December 31, in millions)	2013	2012	2011	% of Total 2013
<b>By market:</b>				
Select Accounts	\$ 2,724	\$ 2,775	\$ 2,784	22.3%
Commercial Accounts	3,197	3,101	2,890	26.1
National Accounts	1,010	907	782	8.3
Industry-Focused Underwriting	2,645	2,554	2,407	21.6
Target Risk Underwriting	1,799	1,666	1,587	14.7
Specialized Distribution	858	870	880	7.0
Total Business Insurance Core	12,233	11,873	11,330	100.0
Business Insurance Other		(1)	10	
<b>Total Business Insurance by market</b>	<b>\$ 12,233</b>	<b>\$ 11,872</b>	<b>\$ 11,340</b>	<b>100.0%</b>

<b>By product line:</b>				
Workers' compensation	\$ 3,642	\$ 3,400	\$ 2,959	29.8%
Commercial automobile	1,897	1,924	1,955	15.5
Commercial property	1,748	1,647	1,595	14.3
General liability	1,823	1,765	1,705	14.9
Commercial multi-peril	3,083	3,100	3,096	25.2
Other	40	36	30	0.3
<b>Total Business Insurance by product line</b>	<b>\$ 12,233</b>	<b>\$ 11,872</b>	<b>\$ 11,340</b>	<b>100.0%</b>

**Principal Markets and Methods of Distribution**

Business Insurance distributes its products through approximately 10,500 independent agencies and brokers located throughout the United States that are serviced by 116 field offices and three customer service centers. Business Insurance continues to make significant investments in enhanced technology utilizing internet-based applications to provide real-time interface capabilities with independent agencies and brokers. Business Insurance builds relationships with well-established, independent insurance agencies and brokers. In selecting new independent agencies and brokers to distribute its products, Business Insurance considers, among other attributes, each agency's or broker's financial strength, staff experience and strategic fit with the Company's operating and marketing plans. Once an agency or broker is appointed, Business Insurance carefully monitors its performance. The majority of products offered by the Select Accounts, Commercial Accounts, Industry-Focused Underwriting and Target Risk Underwriting groups are distributed through a common base of independent agents and brokers, many of whom also sell the Company's Personal Insurance products. Additionally, the Industry-Focused Underwriting and Target Risk Underwriting groups may underwrite business with agents that specialize in servicing the needs of certain of the industries served by these groups.

**Select Accounts** is a leading provider of commercial property and casualty insurance products to small businesses, generally with fewer than 50 employees. Products offered by Select Accounts are guaranteed-cost policies, including packaged products covering property and liability exposures. Each small business risk is independently evaluated via an automated underwriting platform which in turn enables agents to

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quote, bind and issue a substantial amount of new small business risks at their desktop in an efficient manner that significantly reduces the time period between quoting a price on a new policy and issuing that policy. Risks with more complex characteristics are underwritten with the assistance of Company personnel. The automated underwriting platform has significantly streamlined

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the agent desktop underwriting process. Select Accounts has established a strong marketing relationship with its distribution network and has provided this network with defined underwriting policies, a broad array of products and competitive prices. In addition, the Company has established centralized service centers to help agents perform many service functions, in return for a fee.

**Commercial Accounts** sells a broad range of commercial property and casualty insurance products through a large network of independent agents and brokers, primarily targeting mid-sized businesses with 50 to 1,000 employees. The Company offers a full line of products to its Commercial Accounts customers with an emphasis on guaranteed cost programs. Each account is underwritten based on the unique risk characteristics, loss history and coverage needs of the account. The ability to underwrite at this detailed level allows Commercial Accounts to have a broad risk appetite and a diversified customer base.

**National Accounts** sells a variety of casualty products and services to large companies through a network of national and regional brokers, primarily utilizing loss-sensitive products in connection with a large deductible or self-insured program and, to a lesser extent, a retrospectively rated or a guaranteed cost insurance policy. National Accounts also provides casualty products and services through retail brokers on an unbundled basis, using third-party administrators for insureds who utilize programs such as collateralized deductibles, captive reinsurers and self-insurance. National Accounts provides insurance-related services, such as risk management services, claims administration, loss control and risk management information services, either in addition to, or in lieu of, pure risk coverage, and generated \$229 million of fee income in 2013, excluding commercial residual market business. The commercial residual market business of National Accounts sells claims and policy management services to workers' compensation pools throughout the United States, and generated \$111 million in fee income in 2013. National Accounts services approximately 34% of the total workers' compensation assigned risk market, making the Company one of the largest servicing carriers in the industry.

Workers' compensation accounted for approximately 75% of sales to National Accounts customers during 2013, based on direct written premiums and fees.

**Industry-Focused Underwriting** markets commercial property and casualty insurance products and services through a large network of agents and brokers. These products and services are tailored to targeted industry segments of significant size and complexity that require unique underwriting, claim, risk management or other insurance-related products and services.

**Target Risk Underwriting** markets commercial property and casualty insurance products and services through a large network of agents and brokers to a wide customer base having specialized property and casualty coverage requirements.

**Specialized Distribution** distributes admitted as well as excess and surplus lines property and casualty products predominantly through selected wholesale agents and program managers, both on a brokerage and delegated authority underwriting basis. These brokers, wholesale agents and program managers operate in certain markets that are not typically served by the Company's appointed retail agents, or they maintain certain affinity arrangements in specialized market segments. The wholesale excess and surplus lines market, which is characterized by the absence of rate and form regulation, allows for more flexibility to write certain classes of business. In working with wholesale agents or program managers on a brokerage basis, Specialized Distribution underwrites the business and sets the premium level. In working with wholesale agents or program managers with delegated underwriting authority, the agents produce and underwrite business subject to underwriting guidelines that have been specifically designed for each facility or program.

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**Pricing and Underwriting**

Business Insurance utilizes underwriting, claims, engineering, actuarial and product development disciplines for particular industries, in conjunction with extensive amounts of proprietary data gathered and analyzed over many years, to facilitate its risk selection process and develop pricing parameters. The Company utilizes both standard industry forms and proprietary forms for the insurance policies it issues.

A portion of business in this segment, particularly in National Accounts and Construction, is written with large deductible insurance policies. Under workers' compensation insurance contracts with deductible features, the Company is obligated to pay the claimant the full amount of the claim. The Company is subsequently reimbursed by the contractholder for the deductible amount and is subject to credit risk until such reimbursement is made. At December 31, 2013, contractholder payables on unpaid losses within the deductible layer of large deductible policies and the associated receivables were each approximately \$4.31 billion. Business Insurance also utilizes retrospectively rated policies for another portion of the business, primarily for workers' compensation coverage. Although the retrospectively rated feature of the policy substantially reduces insurance risk for the Company, it introduces additional credit risk to the Company. Premium receivables from holders of retrospectively rated policies totaled approximately \$99 million at December 31, 2013. Significant collateral, primarily letters of credit and, to a lesser extent, cash collateral or trusts, is generally obtained for large deductible plans and/or retrospectively rated policies that provide for deferred collection of deductible recoveries and/or ultimate premiums. The amount of collateral requested is predicated upon the creditworthiness of the customer and the nature of the insured risks. Business Insurance continually monitors the credit exposure on individual accounts and the adequacy of collateral.

**Product Lines**

The Business Insurance segment writes the following types of coverages:

**Workers' Compensation.** Provides coverage for employers for specified benefits payable under state or federal law for workplace injuries to employees. There are typically four types of benefits payable under workers' compensation policies: medical benefits, disability benefits, death benefits and vocational rehabilitation benefits. The Company emphasizes managed care cost containment strategies, which involve employers, employees and care providers in a cooperative effort that focuses on the injured employee's early return to work and cost-effective quality care. The Company offers the following types of workers' compensation products:

guaranteed-cost insurance products, in which policy premium charges are fixed for the period of coverage and do not vary as a result of the insured's loss experience;

loss-sensitive insurance products, including large deductible and retrospectively rated policies, in which fees or premiums are adjusted based on actual loss experience of the insured during the policy period; and

service programs, which are generally sold to the Company's National Accounts customers, where the Company receives fees rather than premiums for providing loss prevention, risk management, and claim and benefit administration services to organizations under service agreements.

The Company also participates in state assigned risk pools as a servicing carrier and pool participant.

**Commercial Automobile.** Provides coverage for businesses against losses incurred from personal bodily injury, bodily injury to third parties, property damage to an insured's vehicle and property

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damage to other vehicles and other property resulting from the ownership, maintenance or use of automobiles and trucks in a business.

**Commercial Property.** Provides coverage for loss of or damage to buildings, inventory and equipment from a variety of events, including, among others, hurricanes and other windstorms, earthquakes, hail, wildfires, severe winter weather, floods, volcanic eruptions, tsunamis, theft, vandalism, fires, explosions, terrorism and financial loss due to business interruption resulting from covered property damage. For additional information on terrorism coverages, see "Reinsurance Catastrophe Reinsurance Terrorism Risk Insurance Program." Property also includes specialized equipment insurance, which provides coverage for loss or damage resulting from the mechanical breakdown of boilers and machinery, and ocean and inland marine insurance, which provides coverage for goods in transit and unique, one-of-a-kind exposures.

**General Liability.** Insures businesses against third-party claims arising from accidents occurring on their premises or arising out of their operations, including as a result of injuries sustained from products sold. Specialized liability policies may also include coverage for directors' and officers' liability arising in their official capacities, employment practices liability insurance, fiduciary liability for trustees and sponsors of pension, health and welfare, and other employee benefit plans, errors and omissions insurance for employees, agents, professionals and others arising from acts or failures to act under specified circumstances, as well as umbrella and excess insurance.

**Commercial Multi-Peril.** Provides a combination of the property and liability coverages described in the foregoing product line descriptions.

**Net Retention Policy**

The following discussion reflects the Company's retention policy with respect to the Business Insurance segment as of January 1, 2014. For third-party liability, Business Insurance generally limits its net retention, through the use of reinsurance, to a maximum of \$18.8 million per insured, per occurrence. The net retained amount per risk for property exposures is generally limited to \$20.0 million per occurrence, after reinsurance. The Company generally retains its workers' compensation exposures. Reinsurance treaties often have aggregate limits or caps which may result in larger net per-risk retentions if the aggregate limits or caps are reached. The Company utilizes facultative reinsurance to provide additional limits capacity or to reduce retentions on an individual risk basis. The Company may also retain amounts greater than those described herein based upon the individual characteristics of the risk.

Table of Contents**Geographic Distribution**

The following table shows the geographic distribution of Business Insurance's direct written premiums for the states that accounted for the majority of premium volume for the year ended December 31, 2013:

State	% of Total
California	13.2%
New York	7.9
Texas	7.5
Illinois	5.0
Florida	4.0
Pennsylvania	4.0
New Jersey	3.8
Massachusetts	3.4
All others(1)	51.2
 Total	 100.0%

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(1) No other single state accounted for 3.0% or more of the total direct written premiums written in 2013 by the Business Insurance segment.

**Competition**

The insurance industry is represented in the commercial marketplace by many insurance companies of varying size as well as other entities offering risk alternatives, such as self-insured retentions or captive programs. Market competition works within the insurance regulatory framework to set the price charged for insurance products and the levels of coverage and service provided. A company's success in the competitive commercial insurance landscape is largely measured by its ability to profitably provide insurance and services, including claims handling and risk control, at prices and terms that retain existing customers and attract new customers.

Competitors typically write Select Accounts business through independent agents and, to a lesser extent, regional brokers and direct writers. Both national and regional property and casualty insurance companies compete in the Select Accounts market which generally comprises lower-hazard, "Main Street" business customers. Risks are underwritten and priced using standard industry practices and a combination of proprietary and standard industry product offerings. Competition in this market is primarily based on product offerings, service levels, ease of doing business and price.

Competitors typically write Commercial Accounts business through independent agents and brokers. Competitors in this market are primarily national property and casualty insurance companies that write most classes of business using traditional products and pricing, and regional insurance companies. Companies compete based on product offerings, service levels, price and claim and loss prevention services. Efficiency through automation and rapid response time to customer needs is one key to success in this market.

In the National Accounts market, competition is based on price, product offerings, claim and loss prevention services, managed care cost containment, risk management information systems and collateral requirements. National Accounts primarily competes with national property and casualty insurance companies, as well as with other underwriters of property and casualty insurance in the alternative risk transfer market, such as self-insurance plans, captives managed by others, and a variety of other risk-financing vehicles and mechanisms. The residual market division competes for state contracts to provide claims and policy management services.



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There are several other business groups in Business Insurance that compete in focused target markets. Each of these markets is different and requires unique combinations of industry knowledge, customized coverage, specialized risk control and loss handling services, along with partnerships with agents and brokers that also focus on these markets. Some of these business groups compete with national carriers with similarly dedicated underwriting and marketing groups, whereas others compete with smaller regional companies. Each of these business groups has regional structures that allow them to deliver personalized service and local knowledge to their customer base. Specialized agents and brokers, including wholesale agents and program managers, supplement this strategy. In all of these business groups, the competitive strategy typically is the application of focused industry knowledge to insurance and risk needs.

**FINANCIAL, PROFESSIONAL & INTERNATIONAL INSURANCE**

The Financial, Professional & International Insurance segment includes surety and financial liability coverages, which primarily use credit-based underwriting processes, as well as property and casualty products that are primarily marketed on a domestic basis in Canada, the United Kingdom and the Republic of Ireland, and on an international basis as a corporate member of Lloyd's. The segment includes the following groups:

*Bond & Financial Products* provides a wide range of customers with bond and insurance products and risk management services. The range of coverages includes performance, payment and commercial surety and fidelity bonds for construction and general commercial enterprises; management liability coverages for losses caused by the actual or alleged negligence or misconduct of directors and officers or employee dishonesty; employment practices liability coverages and fiduciary coverages for public corporations, private companies and not-for-profit organizations; professional liability coverage for actual or alleged errors and omissions committed in the course of professional conduct or practice for a variety of professionals including, among others, lawyers and design professionals; and professional and management liability, property, workers' compensation, auto and general liability and fidelity insurance for financial institutions.

*International*, through its operations in Canada, the United Kingdom and the Republic of Ireland, offers specialized insurance and risk management services to several customer groups, including, among others, those in the technology, public services, and financial and professional services industry sectors. In addition, International markets personal lines and small commercial insurance business in Canada through The Dominion of Canada General Insurance Company (Dominion), which the Company acquired on November 1, 2013. International, through its Lloyd's syndicate (Syndicate 5000), for which the Company provides 100% of the capital, underwrites through five principal business units marine, global property, accident & special risks, power & utilities and aviation.

The Company owns 49.5% of the common stock of J. Malucelli Participações em Seguros e Resseguros S.A. (JMalucelli), its joint venture in Brazil. JMalucelli is currently the market leader in surety in Brazil based on market share, and commenced writing other property and casualty insurance business in 2012. The Company's investment in JMalucelli is accounted for using the equity method and is included in "other investments" on the consolidated balance sheet.

Table of Contents**Selected Market and Product Information**

The following table sets forth Financial, Professional & International Insurance net written premiums by market and product line for the periods indicated. For a description of the markets and product lines referred to in the table, see "Principal Markets and Methods of Distribution" and "Product Lines," respectively.

(for the year ended December 31, in millions)	2013	2012	2011	% of Total 2013
<b>By market:</b>				
Bond & Financial Products	\$ 2,030	\$ 1,924	\$ 1,953	61.3%
International	1,279	1,057	1,149	38.7
<b>Total Financial, Professional &amp; International Insurance by market</b>	<b>\$ 3,309</b>	<b>\$ 2,981</b>	<b>\$ 3,102</b>	<b>100.0%</b>
<b>By product line:</b>				
Fidelity and surety	\$ 918	\$ 895	\$ 957	27.7%
General liability	934	859	836	28.2
International	1,279	1,057	1,149	38.7
Other	178	170	160	5.4
<b>Total Financial, Professional &amp; International Insurance by product line</b>	<b>\$ 3,309</b>	<b>\$ 2,981</b>	<b>\$ 3,102</b>	<b>100.0%</b>

**Principal Markets and Methods of Distribution**

Within the Financial, Professional & International Insurance segment, Bond & Financial Products distributes the vast majority of its products in the United States through approximately 6,100 of the same independent agencies and brokers that distribute the Business Insurance segment's products. These independent agencies and brokers are located throughout the United States. Bond & Financial Products, in conjunction with the Business Insurance segment, continues to make investments in enhanced technology utilizing internet-based applications to provide real-time interface capabilities with its independent agencies and brokers. Bond & Financial Products builds relationships with well-established, independent insurance agencies and brokers. In selecting new independent agencies and brokers to distribute its products, Bond & Financial Products considers, among other attributes, each agency's or broker's profitability, financial stability, staff experience and strategic fit with its operating and marketing plans. Once an agency or broker is appointed, its ongoing performance is closely monitored. In addition, Bond & Financial Products sells its surety products through independent brokers in the United Kingdom.

The International market distributes its products principally through brokers in the domestic markets of each of the countries in which it operates. It also writes business at Lloyd's, where its products are distributed through Lloyd's wholesale and retail brokers. By virtue of Lloyd's worldwide licenses, Financial, Professional & International Insurance has access to international markets across the world. In late 2008, the Company commenced an exclusive relationship with a broker in the Republic of Ireland that significantly increased the 2009 volume of personal automobile coverage written and also resulted in the Company writing personal household coverages. The Company ceased writing business through this relationship in the fourth quarter of 2010 and ceased writing all remaining personal insurance business in the Republic of Ireland in the fourth quarter of 2011.

**Pricing and Underwriting**

Financial, Professional & International Insurance utilizes underwriting, claims, engineering, actuarial and product development disciplines for specific accounts, industries and countries, in



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conjunction with extensive amounts of proprietary data gathered and analyzed over many years, to facilitate its risk selection process and develop pricing parameters. The Company utilizes both standard industry forms and proprietary forms for the insurance policies it issues.

**Product Lines**

The Financial, Professional & International Insurance segment writes the following types of coverages:

**Fidelity and Surety.** Provides fidelity insurance coverage, which protects an insured for loss due to embezzlement or misappropriation of funds by an employee, and surety, which is a three-party agreement whereby the insurer agrees to pay a third party or make complete an obligation in response to the default, acts or omissions of an insured. Surety is generally provided for construction performance, legal matters such as appeals, trustees in bankruptcy and probate and other performance bonds.

**General Liability.** Provides coverage for specialized liability exposures as described above in more detail in the "Business Insurance" section of this report.

**International.** Provides coverage for employers' liability (similar to workers' compensation coverage in the United States), public and product liability (the equivalent of general liability), professional indemnity (similar to professional liability coverage), auto and motor (similar to automobile coverage in the United States), commercial property, personal property, surety, marine, aviation, personal accident and kidnap & ransom. Marine provides coverage for ship hulls, cargoes carried, private yachts, marine-related liability, offshore energy, ports and terminals, fine art and terrorism. Aviation provides coverage for worldwide aviation risks including physical damage and liabilities for airline, aerospace, general aviation, aviation war and space risks. Personal accident provides financial protection in the event of death or disablement due to accidental bodily injury, while kidnap & ransom provides financial protection against kidnap, hijack, illegal detention and extortion. While the covered hazards may be similar to those in the U.S. market, the different legal environments can make the product risks and coverage terms potentially very different from those the Company faces in the United States.

**Other.** Coverages include Property, Workers' Compensation, Commercial Automobile and Commercial Multi-Peril, which are described above in more detail in the "Business Insurance" section of this report.

**Net Retention Policy**

The following discussion reflects the Company's retention policy with respect to the Financial, Professional & International Insurance segment as of January 1, 2014. In the U.S. operations for third party liability, including but not limited to umbrella liability, professional liability, directors' and officers' liability, and employment practices liability, Financial, Professional & International Insurance generally limits net retentions to \$25.0 million per policy. For surety protection, where insured limits are often significant, the Company generally retains up to \$75.0 million probable maximum loss (PML) per principal but may retain higher amounts based on the type of obligation, credit quality and other credit risk factors. In the International operations, per-risk retentions are limited to a maximum of \$18.8 million, after reinsurance. Reinsurance treaties often have aggregate limits or caps which may result in larger net per risk retentions if the aggregate limits or caps are reached. The Company utilizes facultative reinsurance to provide additional limits capacity or to reduce retentions on an individual risk basis. The Company may also retain amounts greater than those described herein based upon the individual characteristics of the risk.

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**Geographic Distribution**

The following table shows the geographic distribution of Financial, Professional & International's direct written premiums for the states that accounted for the majority of premium volume for the year ended December 31, 2013:

State	% of Total
California	6.6%
Texas	5.3
New York	5.2
Florida	3.1
All other domestic(1)	46.4
Total domestic	66.6
Total international	33.4
Total	100.0%

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(1) No other single state within the United States accounted for 3.0% or more of the total direct written premiums written in 2013 by the Financial, Professional & International Insurance segment.

**Competition**

The competitive landscape in which Bond & Financial Products operates is affected by many of the same factors described previously for the Business Insurance segment. Competitors in this market are primarily national property and casualty insurance companies that write most classes of business using traditional products and pricing and, to a lesser extent, regional insurance companies and companies that have developed niche programs for specific industry segments.

Bond & Financial Products underwrites and markets its products to all sizes of businesses and other organizations, as well as individuals. The Company believes that its reputation for timely and consistent decision making, a nationwide network of local underwriting, claims and industry experts and strong producer and customer relationships, as well as its ability to offer its customers a full range of products, provides Bond & Financial Products an advantage over many of its competitors and enables it to compete effectively in a complex, dynamic marketplace. The Company believes that the ability of Bond & Financial Products to cross-sell its products to customers of the Business Insurance and Personal Insurance segments provides additional competitive advantages for the Company.

International competes with numerous international and domestic insurers in Canada, the United Kingdom and the Republic of Ireland. Companies compete on the basis of price, product offerings and the level of claim and risk management services provided. The Company has developed expertise in various markets in these countries similar to those served in the United States and provides both property and casualty coverage for these markets.

At Lloyd's, International competes with other syndicates operating in the Lloyd's market as well as international and domestic insurers in the various markets where the Lloyd's operation writes business worldwide. Competition is again based on price, product and service. The Company focuses on lines it believes it can underwrite effectively and profitably with an emphasis on short-tail insurance lines.

**PERSONAL INSURANCE**

The Company's Personal Insurance segment writes a broad range of property and casualty insurance covering individuals' personal risks. The primary products of automobile and homeowners insurance are complemented by a broad suite of related coverages.



Table of Contents**Selected Product and Distribution Channel Information**

The following table sets forth net written premiums for the Personal Insurance segment's business by product line for the periods indicated. For a description of the product lines referred to in the following table, see "Product Lines." In addition, see "Principal Markets and Methods of Distribution" for a discussion of distribution channels for Personal Insurance's product lines.

(for the year ended December 31, in millions)	2013	2012	2011	% of Total 2013
<b>By product line:</b>				
Automobile	\$ 3,370	\$ 3,642	\$ 3,788	46.6%
Homeowners and Other	3,855	3,952	3,957	53.4
 Total Personal Insurance	 \$ 7,225	 \$ 7,594	 \$ 7,745	 100.0%

**Principal Markets and Methods of Distribution**

Personal Insurance products are distributed primarily through approximately 11,500 active independent agencies located throughout the United States, supported by personnel in ten sales regions and seven service centers. While the principal markets for Personal Insurance products continue to be in states along the East Coast, California and Texas, the business continues to expand its geographic presence across the United States. See "Competition" below for a discussion of the Company's new private passenger automobile product, Quantum Auto 2.0.

In selecting new independent agencies to distribute its products, Personal Insurance considers, among other attributes, each agency's profitability, financial stability, staff experience and strategic fit with the segment's operating and marketing plans. Once an agency is appointed, Personal Insurance carefully monitors its performance.

Agents can access the Company's agency service portal for a number of resources including customer service, marketing and claims management. In addition, agencies can choose to shift the ongoing service responsibility for Personal Insurance's customers to one of the Company's five Customer Care Centers, where the Company provides, on behalf of an agency, a comprehensive array of customer service needs, including response to billing and coverage inquiries, and policy changes. Approximately 1,700 agents take advantage of this service alternative.

Personal Insurance also distributes its products through additional channels, including corporations that make the company's product offerings available to their employees primarily through payroll deduction, consumer associations and affinity groups. Personal Insurance handles the sales and service for these programs either through a sponsoring independent agent or through two of the Company's call center locations. In addition, since 1995, the Company has had a marketing agreement with GEICO to underwrite homeowners business for certain of their auto customers.

In 2009, the Company began marketing its insurance products directly to consumers, largely through online channels. The investment in the direct-to-consumer initiative generated modest premium volume for Personal Insurance in recent years, which was consistent with the Company's expectations. However, the direct-to-consumer initiative, while intended to enhance the Company's long-term ability to compete successfully in a consumer-driven marketplace, is expected to remain unprofitable for a number of years as the Company continues to develop, test and evaluate this distribution channel.

**Pricing and Underwriting**

Personal Insurance has developed a product management methodology that integrates the disciplines of underwriting, claim, actuarial and product development. This approach is designed to

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maintain high quality underwriting discipline and pricing segmentation. Proprietary data accumulated over many years is analyzed and Personal Insurance uses a variety of risk differentiation models to facilitate its pricing segmentation. The Company's product management area establishes underwriting guidelines integrated with its filed pricing and rating plans, which enable Personal Insurance to effectively execute its risk selection and pricing processes.

Pricing for personal automobile insurance is driven in large part by changes in the frequency of claims and by inflation in the cost of automobile repairs, medical care and litigation of liability claims. Pricing in the homeowners business is driven in large part by changes in the frequency of claims and by inflation in the cost of building supplies, labor and household possessions. In addition to the normal risks associated with any multiple peril coverage, the profitability and pricing of both homeowners and automobile insurance are affected by the incidence of natural disasters, particularly those related to weather and, for homeowners insurance, earthquakes. Insurers writing personal lines property and casualty policies may be unable to increase prices until some time after the costs associated with coverage have increased, primarily because of state insurance rate regulation. The pace at which an insurer can change rates in response to increased costs depends, in part, on whether the applicable state law requires prior approval of rate increases or notification to the regulator either before or after a rate change is imposed. In states with prior approval laws, rates must be approved by the regulator before being used by the insurer. In states having "file-and-use" laws, the insurer must file rate changes with the regulator, but does not need to wait for approval before using the new rates. A "use-and-file" law requires an insurer to file rates within a period of time after the insurer begins using the new rate. Approximately one-half of the states require prior approval of most rate changes. In addition, changes to methods of marketing and underwriting in some jurisdictions are subject to state-imposed restrictions, which can make it more difficult for an insurer to significantly manage catastrophe exposures.

The Company's ability or willingness to raise prices, modify underwriting terms or reduce exposure to certain geographies may be limited due to considerations of public policy, the competitive environment, the evolving political environment and/or changes in the general economic climate. The Company also may choose to write business it might not otherwise write in some states for strategic purposes, such as improving access to other commercial or personal underwriting opportunities. In choosing to write business in some states, the Company also considers the costs and benefits of those states' residual markets and guaranty funds, as well as other property and casualty business the Company writes in those states.

Personal Insurance utilizes technology intended to maximize independent agents' ease of doing business with the Company. Automated quote transactions can be submitted online by independent agents either through Personal Insurance's proprietary platform, their own agency management platform or comparative raters (discussed in more detail in the "Competition" section that follows). Nearly all new business policies can be issued online either by using the agents' own platform or Personal Insurance's platform, both of which interface with Personal Insurance's underwriting and rating systems to monitor transactions for compliance with the company's underwriting and pricing programs. All on-line business is subject to consultative review by Personal Insurance's in-house underwriters. Audits of on-line business are conducted by an internal review team using systematic sampling across all of the Company's distribution channels.

**Product Lines**

The primary coverages in Personal Insurance are personal automobile and homeowners and other insurance sold to individuals. Personal Insurance had approximately 6.4 million active policies (e.g., policies-in-force) at December 31, 2013.



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The Personal Insurance segment writes the following types of coverages:

**Personal Automobile** provides coverage for liability to others for both bodily injury and property damage, uninsured motorist protection, and for physical damage to an insured's own vehicle from collision, fire, flood, hail and theft. In addition, many states require policies to provide first-party personal injury protection, frequently referred to as no-fault coverage.

**Homeowners and Other** provides protection against losses to dwellings and contents from a variety of perils (excluding flooding) as well as coverage for personal liability. The Company writes homeowners insurance for dwellings, condominiums and tenants, and rental properties. The Company also writes coverage for boats and yachts and valuable personal items such as jewelry, and also writes coverages for umbrella liability, identity fraud, and weddings and special events.

**Net Retention Policy**

The following discussion reflects the Company's retention policy with respect to the Personal Insurance segment as of January 1, 2014. The Company generally retains its primary personal auto exposures in their entirety. For personal property insurance, there is an \$8.0 million maximum retention per risk. Personal Insurance retains the first \$10.0 million of umbrella policies and purchases facultative reinsurance to provide additional limits capacity or to reduce retentions on an individual risk basis. The Company may also retain amounts greater than those described herein based upon the individual characteristics of the risk.

**Geographic Distribution**

The following table shows the geographic distribution of Personal Insurance's direct written premiums for the states that accounted for the majority of premium volume for the year ended December 31, 2013:

State	% of Total
New York	15.6%
Texas(1)	7.6
Pennsylvania	7.6
California	6.2
New Jersey	5.2
Florida	5.0
Georgia	4.5
Virginia	4.2
Connecticut	4.2
Massachusetts	3.5
Maryland	3.5
All others(2)	32.9
<b>Total</b>	<b>100.0%</b>

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(1) The percentage for Texas includes business written by the Company through a fronting agreement with another insurer.

(2) No other single state accounted for 3.0% or more of the total direct written premiums written in 2013 by the Personal Insurance segment.



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**Competition**

Although national companies write the majority of this business, Personal Insurance also faces competition from many regional and hundreds of local companies. Personal Insurance primarily competes based on breadth of product offerings, price, service (including claims handling), ease of doing business, stability of the insurer and name recognition. Personal Insurance competes for business within each independent agency since these agencies also offer policies of competing companies. At the agency level, competition is primarily based on price, service (including claims handling), the level of automation and the development of long-term relationships with individual agents. In recent years, most independent personal insurance agents have begun utilizing price comparison rating technology, sometimes referred to as "comparative raters," as a cost-efficient means of obtaining quotes from multiple companies. Because the use of this technology facilitates the process of generating multiple quotes, the technology has increased price comparison on new business and, increasingly, on renewal business. Personal Insurance also competes with insurance companies that use exclusive agents or salaried employees to sell their products, as well as those that employ direct marketing strategies, including the use of toll-free numbers and the internet. See "Item 1A Risk Factors The intense competition that we face could harm our ability to maintain or increase our business volumes and our profitability."

The Agency Automobile line of business has been negatively impacted by various factors, including the use of price comparison technology by agents and brokers as discussed above. The Company has undertaken various actions to reduce costs in order to improve underwriting margins and enable it to have a more competitively-priced product. The Company's actions in response to these factors include, among other things, the reduction of certain claim adjustment and other insurance expenses, with the majority of the impact in the Agency Automobile line of business. The reduction is intended to result in savings of \$140 million pre-tax per year by 2015 when fully implemented. It is also expected to result in a restructuring charge of approximately \$16 million, \$12 million of which was incurred in 2013. Additionally, in the fourth quarter of 2013, the Company launched a new private passenger automobile product, Quantum Auto 2.0. This product, in addition to incorporating the cost savings described above, has a lower base commission rate than the Company's existing Quantum Auto 1.0 product. These changes in cost structure are intended to enable the Company to price Quantum Auto 2.0 more competitively while generating an appropriate return. The new product was launched in 18 states by the end of 2013 and is expected to be offered in all but three states before the end of 2014. The Company currently intends that, in approved states, all new accounts will be on Quantum Auto 2.0. In addition, Quantum Auto 2.0 will also be available to agents at their discretion for existing accounts.

**CLAIMS MANAGEMENT**

The Company's claim functions are managed through its Claims Services operation, with locations in the United States and in the countries where it does business. With more than 12,000 employees, Claims Services employs a diverse group of professionals, including claim adjusters, appraisers, attorneys, investigators, engineers, accountants, system specialists and training, management and support personnel. Approved external service providers, such as investigators, attorneys and, in the rare circumstances when necessary, independent adjusters and appraisers, are available for use as appropriate.

U.S. field claim management teams located in 21 claim centers and 57 satellite and specialty-only offices in 45 states are organized to maintain focus on the specific claim characteristics unique to the businesses within the Company's business segments. Claim teams with specialized skills, required licenses, resources and workflows are matched to the unique exposures of those businesses, with local claims management dedicated to achieving optimal results within each segment. The Company's home office operations provide additional support in the form of workflow design, quality management, information technology, advanced management information and data analysis, training, financial

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reporting and control, and human resources strategy. This structure permits the Company to maintain the economies of scale of a large, established company while retaining the agility to respond promptly to the needs of customers, brokers, agents and underwriters. Claims management for International, while generally provided locally by staff in the respective international locations due to local knowledge of applicable laws and regulations, is also managed by the Company's U.S. Claims Services organization to leverage that knowledge base and to share best practices.

An integral part of the Company's strategy to benefit customers and shareholders is its continuing industry leadership in the fight against insurance fraud through its Investigative Services unit. The Company has a nationwide staff of experts who investigate a wide array of insurance fraud schemes using in-house forensic resources and other technological tools. This staff also has specialized expertise in fire scene examinations, medical provider fraud schemes and data mining. The Company also dedicates investigative resources to ensure that violations of law are reported to and prosecuted by law enforcement agencies.

Claims Services uses technology, management information and data analysis to assist the Company in reviewing its claim practices and results in order to evaluate and improve its claims management performance. The Company's claims management strategy is focused on segmentation of claims and appropriate technical specialization to drive effective claim resolution. The Company continually monitors its investment in claim resources to maintain an effective focus on claim outcomes and a disciplined approach to continual improvement. The Company operates a state-of-the-art claims training facility, offering hands-on experiential learning to help ensure that its claim professionals are properly trained. In recent years, the Company has invested significant additional resources in many of its claim handling operations and routinely monitors the effect of those investments to ensure a consistent optimization among outcomes, cost and service.

Claims Services' catastrophe response strategy is to respond to a significant catastrophic event using its own personnel, enabling it to minimize reliance on independent adjusters and appraisers. The Company has developed a large dedicated catastrophe response team and trained a large Enterprise Response Team of existing employees who can be deployed on short notice in the event of a catastrophe that generates claim volume exceeding the capacity of the dedicated catastrophe response team. In recent years, these internal resources were successfully deployed to respond to a record number of catastrophe claims.

**REINSURANCE**

The Company reinsures a portion of the risks it underwrites in order to control its exposure to losses. The Company cedes to reinsurers a portion of these risks and pays premiums based upon the risk and exposure of the policies subject to such reinsurance. Ceded reinsurance involves credit risk, except with regard to mandatory pools and associations, and is generally subject to aggregate loss limits. Although the reinsurer is liable to the Company to the extent of the reinsurance ceded, the Company remains liable as the direct insurer on all risks reinsured. Reinsurance recoverables are reported after reductions for known insolvencies and after allowances for uncollectible amounts. The Company also holds collateral, including trust agreements, escrow funds and letters of credit, under certain reinsurance agreements. The Company monitors the financial condition of reinsurers on an ongoing basis and reviews its reinsurance arrangements periodically. Reinsurers are selected based on their financial condition, business practices, the price of their product offerings and the value of collateral provided. After reinsurance is purchased, the Company has limited ability to manage the credit risk to a reinsurer. In addition, in a number of jurisdictions, particularly the European Union and the United Kingdom, a reinsurer is permitted to transfer a reinsurance arrangement to another reinsurer, which may be less creditworthy, without a counterparty's consent, provided that the transfer has been approved by the applicable regulatory and/or court authority. For additional information

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concerning reinsurance, see note 5 of notes to the Company's consolidated financial statements and "Item 1A Risk Factors."

The Company utilizes a variety of reinsurance agreements to manage its exposure to large property and casualty losses, including:

facultative reinsurance, in which reinsurance is provided for all or a portion of the insurance provided by a single policy and each policy reinsured is separately negotiated;

quota share reinsurance, in which reinsurance is provided for an agreed-upon fixed percentage of liabilities, premiums and losses for each policy covered on a pro rata basis;

treaty reinsurance, in which reinsurance is provided for a specified type or category of risks; and

catastrophe reinsurance, in which the Company is indemnified for an amount of loss in excess of a specified retention with respect to losses resulting from a catastrophic event.

For a description of reinsurance-related litigation, see note 16 of notes to the Company's consolidated financial statements.

Included in reinsurance recoverables are amounts related to structured settlements, which are annuities purchased from various life insurance companies to settle certain personal physical injury claims, of which workers' compensation claims comprise a significant portion. In cases where the Company did not receive a release from the claimant, the amount due from the life insurance company related to the structured settlement is included in the Company's consolidated balance sheet as a reinsurance recoverable and the related claim cost is included in the liability for claims and claim adjustment expense reserves, as the Company retains the contingent liability to the claimant. If it is expected that the life insurance company is not able to pay, the Company would recognize an impairment of the related reinsurance recoverable if, and to the extent, the purchased annuities are not covered by state guaranty associations. In the event that the life insurance company fails to make the required annuity payments, the Company would be required to make such payments.

**Catastrophe Reinsurance**

Catastrophes can be caused by a variety of events, including, among others, hurricanes, tornadoes and other windstorms, earthquakes, hail, wildfires, severe winter weather, floods, tsunamis and volcanic eruptions. Catastrophes can also result from a terrorist attack (including those involving nuclear, biological, chemical or radiological events), explosions, infrastructure failures or as a consequence of political instability. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are restricted to small geographic areas; however, hurricanes and earthquakes may produce significant damage in larger areas, especially those areas that are heavily populated. The Company generally seeks to manage its exposure to catastrophes through individual risk selection and the purchase of catastrophe reinsurance. The Company utilizes a general catastrophe reinsurance treaty with unaffiliated reinsurers to manage its exposure to losses resulting from catastrophes. In addition to the coverage provided under this treaty, the Company also utilizes catastrophe bonds, as well as a Northeast catastrophe reinsurance treaty, to protect against certain losses resulting from catastrophes in the Northeastern United States. In addition, the Company also has a general catastrophe aggregate excess-of-loss reinsurance treaty, two earthquake excess-of-loss reinsurance treaties and several reinsurance treaties specific to its international operations.

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*General Catastrophe Reinsurance Treaty.* The Company utilizes a general catastrophe reinsurance treaty with unaffiliated reinsurers to help manage its exposure to losses resulting from catastrophes. The general catastrophe reinsurance treaty covers the accumulation of net property losses arising out of one occurrence. The treaty covers all of the Company's exposures in the United States and Canada and their possessions, and waters contiguous thereto, the Caribbean and Mexico. The treaty only provides coverage for terrorism events in limited circumstances and excludes entirely losses arising from nuclear, biological, chemical or radiological attacks.

The following table summarizes the Company's coverage under its General Catastrophe Reinsurance Treaty, effective for the period July 1, 2013 through June 30, 2014, as well as certain other catastrophe-related coverages, other than coverage related to the General Catastrophe Aggregate Excess-of-Loss Treaty which is described later in this section.

Layer of Loss	Reinsurance Coverage In-Force
\$0 - \$1.5 billion	Loss 100% retained by the Company, except for certain losses covered by the Earthquake Excess-of-Loss Reinsurance Treaty as described below.
\$1.5 billion - \$2.25 billion	53.3% (\$400 million) of loss covered by treaty; 46.7% (\$350 million) of loss retained by the Company. Additionally, certain losses incurred in the Northeastern United States are covered by the reinsurance agreements related to the Catastrophe Bonds as described below.
Greater than \$2.25 billion	100% of loss retained by the Company, except for certain losses incurred in the Northeastern United States, which are covered by the reinsurance agreements related to the Catastrophe Bonds and Northeast General Catastrophe Reinsurance Treaty as described below.

*Catastrophe Bonds.* The Company has catastrophe protection through two indemnity reinsurance agreements with Long Point Re III Ltd. (Long Point Re III), an independent Cayman Islands company licensed as a Class B insurer in the Cayman Islands. The reinsurance agreements expire in June 2015 and May 2016, respectively. Both reinsurance agreements meet the requirements to be accounted for as reinsurance in accordance with the guidance for reinsurance contracts. In connection with each reinsurance agreement, Long Point Re III issued notes (generally referred to as "catastrophe bonds") to investors in an amount equal to the full coverage provided under the respective reinsurance agreement as described below.

On June 6, 2012, Long Point Re III completed an offering to unrelated investors of \$250 million aggregate principal amount of catastrophe bonds. In connection with the offering, the Company and Long Point Re III entered into a three-year reinsurance agreement providing coverage to the Company for certain losses from a hurricane in the northeastern United States. The business covered by the reinsurance agreement comprises specified property and related coverages in the Company's Personal Insurance segment, and within the "Select Accounts" and the "Commercial Accounts" business groups within the Company's Business Insurance segment. Covered losses under the agreement are limited to the following geographic locations: Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Virginia and Vermont. The proceeds of the offering were deposited in a reinsurance trust account. The attachment point, maximum limit and insurance percentage are reset annually to maintain modeled probabilities of attachment and expected loss on the respective catastrophe bonds equal to the initial modeled probabilities of attachment and expected loss. The attachment point, maximum limit and insurance percentage were reset in April 2013. Accordingly, for the period May 1, 2013 through April 30, 2014,

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the Company will be entitled to begin recovering amounts under the reinsurance agreement if the losses in the covered area for a single occurrence reach an initial attachment amount of \$1.817 billion. The full \$250 million coverage amount is available on a proportional basis until covered losses reach a maximum \$2.427 billion.

On May 16, 2013, Long Point Re III completed a second offering to unrelated investors of \$300 million aggregate principal amount of catastrophe bonds. In connection with the offering, the Company and Long Point Re III entered into a three-year reinsurance agreement providing for coverage up to \$300 million for losses from a Northeast hurricane. The business covered by the reinsurance agreement is a subset of the Company's overall insurance portfolio, comprising property insurance and related coverages spread across the following geographic locations: Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Virginia and Vermont. The coverage is limited to specified property coverage written in the Company's Personal Insurance segment, and within the "Select Accounts" and the "Commercial Accounts" market groups within the Company's Business Insurance segment. Coverage under the agreement is limited to losses from hurricanes and is initially subject to a \$1.25 billion retention per occurrence, after which the Company is entitled to recover up to \$300 million on a proportional basis until covered losses reach a maximum \$1.80 billion limit. The attachment point and maximum limit will be reset annually, with the ability of the Company to adjust the expected loss of the coverage layer (the difference between the attachment point and the maximum limit) within a predetermined range. Similar to the first arrangement with Long Point Re III, the proceeds of the offering were deposited in a separate reinsurance trust account.

Under the terms of both reinsurance agreements, the Company is obligated to pay annual reinsurance premiums to Long Point Re III for the reinsurance coverage. Amounts payable to the Company under both reinsurance agreements with respect to any covered event cannot exceed the Company's actual losses from such event. The principal amount of the respective catastrophe bond will be reduced by any amounts paid to the Company under the respective reinsurance agreement.

As with any reinsurance agreement, there is credit risk associated with collecting amounts due from reinsurers. With regard to Long Point Re III, the credit risk is mitigated by reinsurance trust accounts that have been funded by Long Point Re III with money market funds that invest solely in direct government obligations and obligations backed by the U.S. government with maturities of no more than 13 months. The money market funds must have a principal stability rating of at least AAAM by Standard & Poor's on the issuance date of the bonds and thereafter must be rated by Standard & Poor's. Other permissible investments include money market funds which invest in repurchase and reverse repurchase agreements collateralized by direct government obligations and obligations of any agency backed by the U.S. government with terms of no more than 397 calendar days, and cash.

At the time the agreements were entered into with Long Point Re III, the Company evaluated the applicability of the accounting guidance that addresses variable interest entities or VIEs. Under this guidance, an entity that is formed for business purposes is considered a VIE if: (a) the equity investors lack the direct or indirect ability through voting rights or similar rights to make decisions about an entity's activities that have a significant effect on the entity's operations, or (b) the equity investors do not provide sufficient financial resources for the entity to support its activities. Additionally, a company that absorbs a majority of the expected losses from a VIE's activities or is entitled to receive a majority of the entity's expected residual returns, or both, is considered to be the primary beneficiary of the VIE and is required to consolidate the VIE in the company's financial statements.

As a result of the evaluation of the reinsurance agreements with Long Point Re III, the Company concluded that it was a VIE because the conditions described in items (a) and (b) above were present. However, while Long Point Re III was determined to be a VIE, the Company concluded that it did not have a variable interest in the entity, as the variability in its results, caused by the reinsurance

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agreements, is expected to be absorbed entirely by the investors in the catastrophe bonds issued by Long Point Re III and residual amounts earned by it, if any, are expected to be absorbed by the equity investors (the Company has neither an equity nor a residual interest in Long Point Re III).

Accordingly, the Company is not the primary beneficiary of Long Point Re III and does not consolidate that entity in the Company's consolidated financial statements. Additionally, because the Company has no intention to pursue any transaction that would result in it acquiring interest in and becoming the primary beneficiary of Long Point Re III, the consolidation of that entity in the Company's consolidated financial statements in future periods is unlikely.

The Company has not incurred any losses that have resulted or are expected to result in a recovery under the Long Point Re III agreements since their inception.

*Northeast General Catastrophe Reinsurance Treaty.* In addition to its general catastrophe treaty and its multi-year catastrophe bonds, the Company also is party to a northeast general catastrophe reinsurance treaty which provides up to \$600 million of coverage, subject to a \$2.25 billion retention, for certain losses arising from hurricanes, tornados, hail storms, earthquakes and winter storm or freeze losses from Virginia to Maine for the period July 1, 2013 through June 30, 2014. Losses from a covered event (occurring over several days) anywhere in the United States, Canada, the Caribbean and Mexico and waters contiguous thereto may be used to satisfy the retention. Recoveries under the catastrophe bonds (if any) would be first applied to reduce losses subject to this treaty.

*General Catastrophe Aggregate Excess-of-Loss Reinsurance Treaty.* For the period January 1, 2014 to December 31, 2014, the Company has entered into a reinsurance agreement that covers the accumulation of certain property losses arising from multiple occurrences. For each occurrence, qualifying losses are 90% of \$1.4 billion in excess of \$100 million. The treaty covers aggregate qualifying losses during 2014 for 40% of \$1.0 billion in excess of \$1.5 billion. The treaty covers all of the Company's exposures in the United States and Canada and their possessions, and waters contiguous thereto, the Caribbean and Mexico.

*Business Insurance Earthquake Excess-of-Loss Reinsurance Treaty.* For the period July 1, 2013 through June 30, 2014, the Company has entered into an earthquake excess-of-loss treaty that provides for up to \$200 million of coverage, subject to a \$160 million retention, for losses arising from an earthquake, including fire following and sprinkler leakage incurred under policies written by the National Property, Technology and Public Sector business units and the Commercial Accounts market group.

*Personal Insurance Earthquake Excess-of-Loss Reinsurance Treaty.* For the period January 1, 2014 through December 31, 2014, the Company has entered into an earthquake excess-of-loss treaty that provides for up to \$200 million of coverage, subject to a \$150 million retention, for losses arising from an earthquake, including fire following and sprinkler leakage incurred under policies written by the Company's Personal Insurance segment.

*Dominion Property and Automobile Physical Damage Catastrophe Excess-of-Loss Reinsurance Contract.* This contract, effective for the period January 1, 2014 through and including June 30, 2014, covers the accumulation of net property losses arising out of one occurrence which may accrue to Dominion. The treaty covers all of Dominion's habitational property, commercial property and auto physical damages exposures with respect to risks located in Canada, written for Canadian insureds, including such insureds' interests abroad. The treaty provides coverage for 100% of loss retained by Dominion in excess of \$15 million, up to \$700 million.

*Other International Reinsurance Treaties.* For other business underwritten in Canada, as well as for business written in the United Kingdom, Republic of Ireland and in the Company's operations at Lloyd's, separate reinsurance protections are purchased locally that have lower net retentions more



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commensurate with the size of the respective local balance sheet. The Company conducts an ongoing review of its risk and catastrophe coverages and makes changes as it deems appropriate.

*Terrorism Risk Insurance Program.* The Terrorism Risk Insurance Program is a Federal program administered by the Department of the Treasury that provides for a system of shared public and private compensation for certain insured losses resulting from certified acts of terrorism. The current program has been authorized through 2014. For a further description of the program, including the Company's estimated deductible under the program in 2014, see note 5 of notes to the Company's consolidated financial statements and "Item 1A Risk Factors Catastrophe losses could materially and adversely affect our results of operations, our financial position and/or liquidity, and could adversely impact our ratings, our ability to raise capital and the availability and cost of reinsurance."

**CLAIMS AND CLAIM ADJUSTMENT EXPENSE RESERVES**

Claims and claim adjustment expense reserves represent management's estimate of ultimate unpaid costs of losses and loss adjustment expenses for claims that have been reported and claims that have been incurred but not yet reported.

The Company continually refines its reserve estimates in a regular ongoing process that includes review of key assumptions, underlying variables and historical loss experience. The Company reflects adjustments to reserves in the results of operations in the periods in which the estimates are changed. In establishing reserves, the Company takes into account estimated recoveries for reinsurance, salvage and subrogation. The reserves are also reviewed regularly by qualified actuaries employed by the Company. For additional information on the process of estimating reserves and a discussion of underlying variables and risk factors, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates."

The process of estimating loss reserves involves a high degree of judgment and is subject to a number of variables. These variables (discussed by product line in the "Critical Accounting Estimates" section of "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations") are affected by both internal and external events, such as changes in claims handling procedures, inflation, judicial trends and legislative changes, among others. The impact of many of these items on ultimate costs for claims and claim adjustment expenses is difficult to estimate. Reserve estimation difficulties also differ significantly by product line due to differences in the underlying insurance contract (e.g., claims-made versus occurrence), claim complexity, the volume of claims, the potential severity of individual claims, the determination of the occurrence date for a claim, and reporting lags (the time between the occurrence of the insured event and when it is actually reported to the insurer). Informed judgment is applied throughout the process.

The Company derives estimates for unreported claims and development on reported claims principally from actuarial analyses of historical patterns of loss development by accident year for each type of exposure and business unit. Similarly, the Company derives estimates of unpaid loss adjustment expenses principally from actuarial analyses of historical development patterns of the relationship of loss adjustment expenses to losses for each line of business and type of exposure. For a description of the Company's reserving methods for asbestos and environmental claims, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Asbestos Claims and Litigation," and " Environmental Claims and Litigation."

**Discounting**

The claims and claim adjustment expense reserves for most long-term disability and annuity claim payments, primarily arising from workers' compensation insurance and workers' compensation excess insurance policies, were discounted to the present value of estimated future payments using a rate of

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5% at both December 31, 2013 and 2012. These discounted reserves totaled \$2.21 billion and \$2.01 billion at December 31, 2013 and 2012, respectively.

**Claims and Claim Adjustment Expense Development Table**

The table that follows sets forth the year-end reserves from 2003 through 2013 and the subsequent changes in those reserves, presented on a historical basis. The original estimates, cumulative amounts paid and re-estimated reserves in the table for 2003 have not been restated to reflect the acquisition by Travelers Property Casualty Corp. (TPC) of The St. Paul Companies, Inc. (SPC) in 2004 (referred to hereafter as the Merger). The table includes SPC reserves beginning at December 31, 2004. In addition, the original estimates, cumulative amounts paid and re-estimated reserves in the table for 2003 through 2012 have not been restated to reflect the acquisition of Dominion in November 2013. The table includes Dominion's reserves beginning at December 31, 2013.

The data in the table is presented in accordance with reporting requirements of the Securities and Exchange Commission (SEC). Care must be taken to avoid misinterpretation by those unfamiliar with this information or familiar with other data commonly reported by the insurance industry. The data in the table is not accident year data, but rather a display of 2003 to 2013 year-end reserves and the subsequent changes in those reserves.

For instance, the "cumulative deficiency (redundancy)" shown in the table for each year represents the aggregate amount by which original estimates of reserves as of that year-end have changed in subsequent years. Accordingly, the cumulative deficiency for a year relates only to reserves at that year-end and those amounts are not additive. Expressed another way, if the original reserves at the end of 2003 included \$4 million for a loss that is finally paid in 2007 for \$5 million, the \$1 million deficiency (the excess of the actual payment of \$5 million over the original estimate of \$4 million) would be included in the cumulative deficiencies in each of the years 2003 to 2006 shown in the accompanying table.

Various factors may distort the re-estimated reserves and cumulative deficiency or redundancy shown in the table. For example, a substantial portion of the cumulative deficiencies shown in the table arise from claims on policies written prior to the mid-1980s involving liability exposures such as asbestos and environmental claims. In the post-1984 period, the Company has developed more stringent underwriting standards and policy exclusions and has significantly contracted or terminated the writing of these risks. See "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Asbestos Claims and Litigation," and " Environmental Claims and Litigation." General conditions and trends that have affected the development of these liabilities in the past will not necessarily recur in the future.

Other factors that affect the data in the table include the discounting of certain reserves (as discussed above) and the use of retrospectively rated insurance policies. For example, reserves for long-term disability and annuity claim payments (tabular reserves), primarily arising from workers' compensation insurance and workers' compensation excess insurance policies, are discounted to reflect the time value of money. Apparent deficiencies will continue to occur as the discount on these workers' compensation reserves is accreted at the appropriate interest rates. Also, a portion of National Accounts business is underwritten with retrospectively rated insurance policies in which the ultimate loss experience is primarily borne by the insured. For this business, increases in loss experience result in an increase in reserves and an offsetting increase in amounts recoverable from insureds. Likewise, decreases in loss experience result in a decrease in reserves and an offsetting decrease in amounts recoverable from these insureds. The amounts recoverable on these retrospectively rated policies mitigate the impact of the cumulative deficiencies or redundancies on the Company's earnings but are not reflected in the table.

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Because of these and other factors, it is difficult to develop a meaningful extrapolation of estimated future redundancies or deficiencies in loss reserves from the data in the table.

(at December 31, in millions)	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Reserves for claims and claim adjustment expense originally estimated	\$ 24,055	\$ 41,446	\$ 42,895	\$ 42,844	\$ 43,098	\$ 41,312	\$ 40,941	\$ 40,255	\$ 40,919	\$ 40,634	\$ 41,585
Cumulative amounts paid as of											
One year later	4,651	8,871	8,632	7,417	8,146	7,519	7,748	7,653	8,326	8,416	
Two years later	8,686	14,666	13,837	13,181	12,798	12,454	12,374	12,567	13,447		
Three years later	11,541	18,733	18,466	16,545	16,264	15,668	15,708	16,081			
Four years later	13,708	22,514	21,025	19,113	18,524	18,053	18,126				
Five years later	15,574	24,572	22,992	20,820	20,244	19,824					
Six years later	16,624	26,189	24,423	22,205	21,609						
Seven years later	17,558	27,469	25,616	23,381							
Eight years later	18,320	28,557	26,675								
Nine years later	18,988	29,543									
Ten years later	19,602										
Reserves re-estimated as of											
One year later	24,222	41,706	42,466	42,172	41,373	39,863	39,524	39,413	39,845	39,690	
Two years later	25,272	42,565	42,311	40,837	39,925	38,640	38,421	38,393	38,964		
Three years later	26,042	42,940	41,692	39,739	38,842	37,613	37,539	37,576			
Four years later	26,501	43,148	40,855	38,734	38,223	36,892	36,889				
Five years later	26,803	42,655	40,026	38,409	37,716	36,361					
Six years later	26,619	42,068	39,849	38,134	37,323						
Seven years later	26,342	42,019	39,694	37,858							
Eight years later	26,382	41,987	39,518								
Nine years later	26,431	41,942									
Ten years later	26,455										
Cumulative deficiency (redundancy)	2,400	496	(3,377)	(4,986)	(5,775)	(4,951)	(4,052)	(2,679)	(1,955)	(944)	
Gross liability end of year	\$ 34,760	\$ 59,438	\$ 61,461	\$ 59,677	\$ 58,094	\$ 55,121	\$ 53,529	\$ 51,537	\$ 51,353	\$ 50,888	\$ 50,865
Reinsurance recoverables	10,705	17,992	18,566	16,833	14,996	13,809	12,588	11,282	10,434	10,254	9,280
Net liability end of year	\$ 24,055	\$ 41,446	\$ 42,895	\$ 42,844	\$ 43,098	\$ 41,312	\$ 40,941	\$ 40,255	\$ 40,919	\$ 40,634	\$ 41,585
Gross re-estimated liability-latest	\$ 37,517	\$ 59,672	\$ 57,336	\$ 53,229	\$ 50,927	\$ 48,579	\$ 48,055	\$ 47,892	\$ 48,787	\$ 50,071	
Re-estimated reinsurance recoverables-latest	11,062	17,730	17,818	15,371	13,604	12,218	11,166	10,316	9,823	10,381	
Net re-estimated liability-latest	\$ 26,455	\$ 41,942	\$ 39,518	\$ 37,858	\$ 37,323	\$ 36,361	\$ 36,889	\$ 37,576	\$ 38,964	\$ 39,690	
Gross cumulative deficiency (redundancy)	\$ 2,757	\$ 234	\$ (4,125)	\$ (6,448)	\$ (7,167)	\$ (6,542)	\$ (5,474)	\$ (3,645)	\$ (2,566)	\$ (817)	

For the year 2003, the table excludes reserves of SPC, which were acquired in the Merger on April 1, 2004. Accordingly, the reserve development (net reserves for claims and claim adjustment expense re-estimated as of subsequent years less net reserves recorded at the end of the year, as originally estimated) for 2003 relates only to losses recorded by TPC and does not include reserve development recorded by SPC. For 2004 and subsequent years, the table includes SPC reserves acquired and subsequent development recorded on those reserves. At

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December 31, 2004, SPC gross reserves were \$23,274 million, and net reserves were \$15,959 million. For years prior to 2013, the table excludes reserves of Dominion, which were acquired by the Company on November 1, 2013. Accordingly, the reserve development for years prior to 2013 does not include reserve development recorded by Dominion. At December 31, 2013, Dominion's gross reserves were \$2,110 million, and net reserves were \$1,779 million.

In December 2008, the Company completed the sale of Unionamerica Holdings Limited (Unionamerica), which comprised its United Kingdom (U.K.)-based runoff insurance and reinsurance businesses. (Unionamerica was acquired in 2004 as part of the Merger.) Immediately before the sale, the claims and claim adjustment expense reserves of Unionamerica totaled \$790 million. As a result of the sale, those obligations ceased being the responsibility of the Company and its affiliates. The sale is reflected in the table as a reduction in December 31, 2008 net reserves of \$790 million and as a \$790 million increase in paid losses for each of the years 2004 through 2007 to reflect the transfer (payment) of the reserves to the buyer, resulting in no impact to incurred losses.

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The gross and net cumulative deficiency (redundancy) by calendar year as set forth in the table above includes the following impact of unfavorable prior year reserve development related to asbestos and environmental claims and claim adjustment expenses, in millions:

<b>Asbestos</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>
Gross	\$ 1,832	\$ 2,103	\$ 1,269	\$ 1,072	\$ 1,073	\$ 1,003	\$ 818	\$ 556	\$ 361	\$ 190
Net	\$ 1,709	\$ 1,922	\$ 1,091	\$ 935	\$ 935	\$ 865	\$ 680	\$ 540	\$ 365	\$ 190

  

<b>Environmental</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>
Gross	\$ 797	\$ 773	\$ 756	\$ 648	\$ 466	\$ 381	\$ 296	\$ 251	\$ 171	\$ 72
Net	\$ 745	\$ 756	\$ 726	\$ 606	\$ 421	\$ 336	\$ 266	\$ 231	\$ 155	\$ 65

**Reserves on Statutory Accounting Basis**

At December 31, 2013, 2012 and 2011, claims and claim adjustment expense reserves (net of reinsurance) shown in the preceding table, which are prepared in accordance with U.S. generally accepted accounting principles (GAAP reserves), were \$17 million higher, \$22 million lower and \$20 million higher, respectively, than those reported in the Company's respective annual reports filed with insurance regulators, which are prepared in accordance with statutory accounting practices (statutory reserves).

The differences between GAAP and statutory reserves are primarily due to the differences in GAAP and statutory accounting for two items, (1) fees associated with billing of required reimbursements under large deductible business, and (2) the accounting for retroactive reinsurance. For large deductible business, the Company pays the deductible portion of a casualty insurance claim and then seeks reimbursement from the insured, plus a fee. This fee is reported as fee income for GAAP reporting, but as an offset to claim expenses paid for statutory reporting. Retroactive reinsurance balances result from reinsurance placed to cover losses on insured events occurring prior to the inception of a reinsurance contract. For GAAP reporting, retroactive reinsurance balances are included in reinsurance recoverables and result in lower net reserve amounts. Statutory accounting practices require retroactive reinsurance balances to be recorded in other liabilities as contra-liabilities rather than in loss reserves.

**Asbestos and Environmental Claims**

Asbestos and environmental claims are segregated from other claims and are handled separately by the Company's Special Liability Group, a separate unit staffed by dedicated legal, claim, finance and engineering professionals. For additional information on asbestos and environmental claims, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Asbestos Claims and Litigation" and " Environmental Claims and Litigation."

**INTERCOMPANY REINSURANCE POOLING ARRANGEMENTS**

Most of the Company's domestic insurance subsidiaries are members of an intercompany property and casualty reinsurance pooling arrangement. Pooling arrangements permit the participating companies to rely on the capacity of the entire pool's policyholders' surplus rather than just on its own policyholder surplus. Under such arrangements, the members share substantially all insurance business that is written and allocate the combined premiums, losses and expenses.

**RATINGS**

Ratings are an important factor in assessing the Company's competitive position in the insurance industry. The Company receives ratings from the following major rating agencies: A.M. Best Company (A.M. Best), Fitch Ratings (Fitch), Moody's Investors Service (Moody's) and Standard & Poor's Corp.

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(S&P). Rating agencies typically issue two types of ratings for insurance companies: claims-paying (or financial strength) ratings which reflect the rating agency's assessment of an insurer's ability to meet its financial obligations to policyholders and debt ratings which reflect the rating agency's assessment of a company's prospects for repaying its debts and are considered by lenders in connection with the setting of interest rates and terms for a company's short- and long-term borrowings. Agency ratings are not a recommendation to buy, sell or hold any security, and they may be revised or withdrawn at any time by the rating agency. Each agency's rating should be evaluated independently of any other agency's rating. The system and the number of rating categories can vary widely from rating agency to rating agency. Customers usually focus on claims-paying ratings, while creditors focus on debt ratings. Investors use both to evaluate a company's overall financial strength. The ratings issued on the Company or its subsidiaries by any of these agencies are announced publicly and are available on the Company's website and from the agencies.

A downgrade in one or more of the Company's claims-paying ratings could negatively impact the Company's business volumes and competitive position because demand for certain of its products may be reduced, particularly because some customers require that the Company maintain minimum ratings to enter into or renew business with it.

Additionally, a downgrade in one or more of the Company's debt ratings could adversely impact the Company's ability to access the capital markets and other sources of funds, including in the syndicated bank loan market, and/or result in higher financing costs. For example, downgrades in the Company's debt ratings could result in higher interest expense under the Company's revolving credit agreement (under which the cost of borrowing could range from LIBOR plus 87.5 basis points to LIBOR plus 150 basis points, depending on the Company's debt ratings), the Company's commercial paper program, or in the event that the Company were to access the capital markets by issuing debt or similar types of securities. See "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources" for a discussion of the Company's revolving credit agreement and commercial paper program. The Company considers the level of increased cash funding requirements in the event of a ratings downgrade as part of the evaluation of the Company's liquidity requirements. The Company currently believes that a one- to two-notch downgrade in its debt ratings would not result in a material increase in interest expense under its existing credit agreement and commercial paper programs. In addition, the Company considers the impact of a ratings downgrade as part of the evaluation of its common share repurchases.

***Claims Paying Ratings***

The following table summarizes the current claims-paying (or financial strength) ratings of the Travelers Reinsurance Pool, Travelers C&S Co. of America, Travelers Personal single state companies, Travelers C&S Co. of Europe, Ltd., Travelers Insurance Company of Canada and Travelers Insurance

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Company Limited as of February 13, 2014. The table presents the position of each rating in the applicable agency's rating scale.

	<b>A.M. Best</b>	<b>Moody's</b>	<b>S&amp;P</b>	<b>Fitch</b>
Travelers Reinsurance Pool(a)(b)	A+ (2 <sup>nd</sup> of 16)	Aa2 (3 <sup>rd</sup> of 21)	AA (3 <sup>rd</sup> of 21)	AA (3 <sup>rd</sup> of 21)
Travelers C&S Co. of America	A+ (2 <sup>nd</sup> of 16)	Aa2 (3 <sup>rd</sup> of 21)	AA (3 <sup>rd</sup> of 21)	AA (3 <sup>rd</sup> of 21)
First Floridian Auto and Home Ins. Co. The Premier Insurance Company of Massachusetts	A- (4 <sup>th</sup> of 16)			AA (3 <sup>rd</sup> of 21)
Travelers C&S Co. of Europe, Ltd.	A (3 <sup>rd</sup> of 16)	Aa2 (3 <sup>rd</sup> of 21)	AA (3 <sup>rd</sup> of 21)	
Travelers Insurance Company of Canada	A+ (2 <sup>nd</sup> of 16)		AA- (4 <sup>th</sup> of 21)	
Travelers Insurance Company Limited	A (3 <sup>rd</sup> of 16)		AA (3 <sup>rd</sup> of 21)	

(a)

The Travelers Reinsurance Pool consists of: The Travelers Indemnity Company, The Charter Oak Fire Insurance Company, The Phoenix Insurance Company, The Travelers Indemnity Company of Connecticut, The Travelers Indemnity Company of America, Travelers Property Casualty Company of America, Travelers Commercial Casualty Company, TravCo Insurance Company, The Travelers Home and Marine Insurance Company, Travelers Casualty and Surety Company, Northland Insurance Company, Northfield Insurance Company, Northland Casualty Company, American Equity Specialty Insurance Company, The Standard Fire Insurance Company, The Automobile Insurance Company of Hartford, Connecticut, Travelers Casualty Insurance Company of America, Farmington Casualty Company, Travelers Commercial Insurance Company, Travelers Casualty Company of Connecticut, Travelers Property Casualty Insurance Company, Travelers Personal Security Insurance Company, Travelers Personal Insurance Company, Travelers Excess and Surplus Lines Company, St. Paul Fire and Marine Insurance Company, St. Paul Surplus Lines Insurance Company, The Travelers Casualty Company, St. Paul Protective Insurance Company, Travelers Constitution State Insurance Company, St. Paul Guardian Insurance Company, St. Paul Mercury Insurance Company, Fidelity and Guaranty Insurance Underwriters, Inc., Discover Property & Casualty Insurance Company, Discover Specialty Insurance Company and United States Fidelity and Guaranty Company.

(b)

The following affiliated companies are 100% reinsured by one of the pool participants noted in (a) above: Fidelity and Guaranty Insurance Company, Gulf Underwriters Insurance Company, American Equity Insurance Company, Select Insurance Company, St. Paul Fire and Casualty Insurance Company, The Travelers Lloyds Insurance Company and Travelers Lloyds of Texas Insurance Company.

**Debt Ratings**

The following table summarizes the current debt, trust preferred securities and commercial paper ratings of the Company and its subsidiaries as of February 13, 2014. The table also presents the position of each rating in the applicable agency's rating scale.

	<b>A.M. Best</b>	<b>Moody's</b>	<b>S&amp;P</b>	<b>Fitch</b>
Senior debt	a (6 <sup>th</sup> of 22)	A2 (6 <sup>th</sup> of 21)	A (6 <sup>th</sup> of 22)	A (6 <sup>th</sup> of 22)
Subordinated debt	a- (7 <sup>th</sup> of 22)	A3 (7 <sup>th</sup> of 21)	A- (7 <sup>th</sup> of 22)	BBB+ (8 <sup>th</sup> of 22)
Junior subordinated debt	bbb+ (8 <sup>th</sup> of 22)	A3 (7 <sup>th</sup> of 21)	BBB+ (8 <sup>th</sup> of 22)	BBB+ (8 <sup>th</sup> of 22)
Trust preferred securities	bbb+ (8 <sup>th</sup> of 22)	A3 (7 <sup>th</sup> of 21)	BBB+ (8 <sup>th</sup> of 22)	BBB+ (8 <sup>th</sup> of 22)
Commercial paper	AMB-1 (2 <sup>nd</sup> of 6)	P-1 (1 <sup>st</sup> of 4)	A-1 (2 <sup>nd</sup> of 10)	F-1 (2 <sup>nd</sup> of 8)

**Rating Agency Actions**

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The following rating agency actions were taken with respect to the Company from March 1, 2013 (the date on which the Company filed its Amended Annual Report on Form 10-K/A for the year ended December 31, 2012), through February 7, 2014:

On May 22, 2013, S&P affirmed all ratings of the Company. The outlook for all ratings is stable.



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On May 30, 2013, A.M. Best affirmed all ratings of the Company. The outlook for all ratings of the Company was revised to positive from stable (except the outlooks for The Premier Insurance Company of Massachusetts, First Trenton Indemnity Company and First Florida Auto and Home Insurance Company, all of which remained stable).

On June 10, 2013, Fitch affirmed all ratings of the Company. The outlook for all ratings is stable.

On October 1, 2013, A.M. Best withdrew its "A" financial strength rating and "a" issuer credit rating for First Trenton Indemnity Company (First Trenton) as a result of First Trenton's merger into an affiliate company, The Travelers Indemnity Company, a member of the Travelers Reinsurance Pool.

On November 15, 2013, A.M. Best affirmed the financial strength rating of "A" for Travelers Insurance Company Limited. The outlook for this rating is stable.

On January 16, 2014, Fitch affirmed all ratings of the Company. The outlook for all ratings is stable.

**INVESTMENT OPERATIONS**

The majority of funds available for investment are deployed in a widely diversified portfolio of high quality, liquid taxable U.S. government, tax-exempt U.S. municipal and taxable corporate and U.S. agency mortgage-backed bonds. The Company closely monitors the duration of its fixed maturity investments, and the Company's investment purchases and sales are executed with the objective of having adequate funds available to satisfy its insurance and debt obligations. Generally, the expected principal and interest payments produced by the Company's fixed maturity portfolio adequately fund the estimated runoff of the Company's insurance reserves. The Company's management of the duration of the fixed maturity investment portfolio, including its use of Treasury futures at times, has produced a duration that is less than the estimated duration of the Company's net insurance liabilities. In 2013, the estimated average effective duration of the Company's portfolio of fixed maturity and short-term security investments increased, primarily reflecting the impact of an increase in interest rates during the year. By the end of the second quarter of 2013, based upon the outlook for interest rates as compared to the carrying cost of its short positions in U.S. Treasury futures, the Company closed all of these positions, which it had used to manage the duration of its fixed maturity portfolio to reduce the Company's exposure to a decrease in its book value resulting from an increase in interest rates. During the second half of 2013, the Company did not enter into any U.S. Treasury futures contracts. The Company has also recently experienced an increase in the estimated average duration of its net insurance liabilities, primarily reflecting the impact of declining market interest rates and, to a lesser degree, an increase in the proportion of workers' compensation insurance reserves as a component of total insurance reserves. The substantial amount by which the fair value of the fixed maturity portfolio exceeds the value of the net insurance liabilities, as well as the positive cash flow from newly sold policies and the large amount of high quality liquid bonds, contributes to the Company's ability to fund claim payments without having to sell illiquid assets or access credit facilities.

The Company also invests much smaller amounts in equity securities, real estate, private equity limited partnerships, hedge funds, and real estate partnerships and joint ventures. These investment classes have the potential for higher returns but also involve varying degrees of risk, including less stable rates of return and less liquidity.

See note 3 of notes to the Company's consolidated financial statements for additional information regarding the Company's investment portfolio.

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**REGULATION**

**U.S. State and Federal Regulation**

TRV's domestic insurance subsidiaries are collectively licensed to transact insurance business in all U.S. states, the District of Columbia, Guam, Puerto Rico and the U.S. Virgin Islands and are subject to regulation in the various states and jurisdictions in which they transact business. The extent of regulation varies, but generally derives from statutes that delegate regulatory, supervisory and administrative authority to a department of insurance in each state. The regulation, supervision and administration relate, among other things, to standards of solvency that must be met and maintained, the licensing of insurers and their agents, the nature of and limitations on investments, premium rates, restrictions on the size of risks that may be insured under a single policy, reserves and provisions for unearned premiums, losses and other obligations, deposits of securities for the benefit of policyholders, approval of policy forms and the regulation of market conduct, including the use of credit information in underwriting as well as other underwriting and claims practices. In addition, many states have enacted variations of competitive ratemaking laws, which allow insurers to set certain premium rates for certain classes of insurance without having to obtain the prior approval of the state insurance department. State insurance departments also conduct periodic examinations of the financial condition and market conduct of insurance companies and require the filing of financial and other reports on a quarterly and annual basis.

State insurance regulation continues to evolve in response to the changing economic and business environment as well as efforts by regulators internationally to develop a consistent approach to regulations. These changes are evidenced by the recent incorporation of supervisory colleges into the U.S. regulatory framework. A supervisory college is a forum of the regulators having jurisdictional authority over a holding company's various insurance subsidiaries, including foreign insurance subsidiaries, convened to meet with the insurer's executive management, to evaluate the insurer from both a group-wide and legal-entity basis. Some of the items evaluated during the colleges include the insurer's business strategies, enterprise risk management and corporate governance.

*Insurance Regulation Concerning Dividends from Insurance Subsidiaries.* TRV's principal domestic insurance subsidiaries are domiciled in the state of Connecticut. The Connecticut insurance holding company laws require notice to, and approval by, the state insurance commissioner for the declaration or payment of any dividend from an insurance subsidiary that, together with other distributions made within the preceding twelve months, exceeds the greater of 10% of the insurance subsidiary's policyholders' surplus as of the preceding December 31, or the insurance subsidiary's net income for the twelve-month period ending the preceding December 31, in each case determined in accordance with statutory accounting practices and by state regulation. This declaration or payment is further limited by adjusted unassigned surplus, as determined in accordance with statutory accounting practices.

The insurance holding company laws of other states in which TRV's domestic insurance subsidiaries are domiciled generally contain similar, although in some instances somewhat more restrictive, limitations on the payment of dividends.

*Rate and Rule Approvals.* TRV's domestic insurance subsidiaries are subject to each state's laws and regulations regarding rate and rule approvals. The applicable laws and regulations are used by states to establish standards to ensure that rates are not excessive, inadequate, unfairly discriminatory or used to engage in unfair price competition. An insurer's ability to increase rates and the relative timing of the process are dependent upon each respective state's requirements.

*Requirements for Exiting Geographic Markets and/or Canceling or Nonrenewing Policies.* Several states have laws and regulations which may impact the timing and/or the ability of an insurer to either discontinue or substantially reduce its writings in that state. These laws and regulations typically require prior notice, and in some instances insurance department approval, prior to discontinuing a line of

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business or withdrawing from that state, and they allow insurers to cancel or non-renew certain policies only for certain specified reasons.

*Assessments for Guaranty Funds and Second-Injury Funds and Other Mandatory Pooling and Reinsurance Arrangements.* Virtually all states require insurers licensed to do business in their state, including TRV's domestic insurance subsidiaries, to bear a portion of the loss suffered by some claimants because of the insolvency of other insurers. Many states also have laws that establish second-injury funds to provide compensation to injured employees for aggravation of a prior condition or injury.

TRV's domestic insurance subsidiaries are also required to participate in various involuntary assigned risk pools, principally involving workers' compensation, automobile insurance, property windpools in states prone to property damage from hurricanes, and FAIR plans, which provide various insurance coverages to individuals or other entities that otherwise are unable to purchase that coverage in the voluntary market.

Assessments may include any charge mandated by statute or regulatory authority that is related directly or indirectly to underwriting activities. Examples of such mechanisms include, but are not limited to, the Florida Hurricane Catastrophe Fund, Florida Citizens Property Insurance Corporation, National Workers' Compensation Reinsurance Pool, North Carolina Beach Plan, Louisiana Citizens Property Insurance Corporation, and the Texas Windstorm Insurance Association. Amounts payable or paid as a result of arrangements that are in substance reinsurance, including certain involuntary pools where insurers are required to assume premiums and losses from those pools, are accounted for as reinsurance (e.g., National Workers' Compensation Reinsurance Pool, North Carolina Beach Plan). Amounts related to assessments from arrangements that are not reinsurance are reported as a component of "General and Administrative Expenses." For additional information concerning assessments for guaranty funds and second-injury funds and other mandatory pooling and reinsurance agreements including state-funding mechanisms, see "Item 1A Risk Factors."

*Insurance Regulatory Information System.* The National Association of Insurance Commissioners (NAIC) developed the Insurance Regulatory Information System (IRIS) to help state regulators identify companies that may require special attention. Financial examiners review annual statements and key financial ratios based on year-end data. These ratios assist state insurance departments in executing their statutory mandate to oversee the financial condition of insurance companies. Each ratio has an established "usual range" of results. A ratio result falling outside the usual range of IRIS ratios, however, is not considered a failing result; rather, unusual values are viewed as part of the regulatory early monitoring system. Furthermore, in some years, it may not be unusual for financially sound companies to have several ratios with results outside the usual ranges. Generally, an insurance company will become subject to regulatory scrutiny if it falls outside the usual ranges of four or more of the ratios.

Based on preliminary 2013 IRIS ratios calculated by the Company for its lead domestic insurance subsidiaries, The Travelers Indemnity Company and St. Paul Fire and Marine Insurance Company had results outside the normal range for one IRIS ratio due to the size of their investments in certain non-fixed maturity securities. Travelers Casualty and Surety Company had results outside the normal range for one IRIS ratio due to the amount of dividends received from its subsidiaries.

In 2012, The Travelers Indemnity Company and St. Paul Fire and Marine Insurance Company had results outside the normal range for one IRIS ratio due to the size of their investments in certain non-fixed maturity securities.

Management does not anticipate regulatory action as a result of the 2013 IRIS ratio results for the lead insurance subsidiaries or their insurance subsidiaries. In all instances in prior years, regulators have been satisfied upon follow-up that no regulatory action was required.

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*Risk-Based Capital (RBC) Requirements.* The NAIC has an RBC requirement for most property and casualty insurance companies. The RBC requirement determines minimum capital requirements and is intended to raise the level of protection for policyholder obligations. Under laws adopted by individual states, insurers having total adjusted capital less than that required by the RBC calculation will be subject to varying degrees of regulatory action, depending on the level of capital inadequacy.

The formulas have not been designed to differentiate among adequately capitalized companies that operate with levels of capital above the RBC requirement. Therefore, it is inappropriate and ineffective to use the formulas to rate or to rank these companies. At December 31, 2013, all of TRV's domestic insurance subsidiaries had total adjusted capital in excess of the RBC requirement.

*Investment Regulation.* Insurance company investments must comply with applicable laws and regulations which prescribe the kind, quality and concentration of investments. In general, these laws and regulations permit investments in federal, state and municipal obligations, corporate bonds, preferred and common equity securities, mortgage loans, real estate and certain other investments, subject to specified limits and certain other qualifications. At December 31, 2013, the Company was in compliance with these laws and regulations.

**International Regulation**

TRV's insurance subsidiaries based in Canada and the Canadian branch of one of the Company's U.S. insurance subsidiaries are regulated by the Office of the Superintendent of Financial Institutions under provisions of the Insurance Companies Act. These Canadian subsidiaries and the Canadian branch are also subject to provincial insurance legislation which regulates pricing, underwriting, coverage and claim conduct, in varying degrees by province and by product line.

TRV's insurance subsidiaries based in the United Kingdom are regulated by two regulatory bodies, The Prudential Regulation Authority (PRA) and The Financial Conduct Authority (FCA). The PRA's primary objective is to promote the safety and soundness of insurers for the protection of policyholders, while the FCA has three operational objectives: (i) to secure an appropriate degree of protection for consumers, (ii) to protect and enhance the integrity of the UK financial system, and (iii) to promote effective competition in the interests of consumers. TRV's insurance operations in the Republic of Ireland are conducted through the Irish branch of Travelers Insurance Company Limited which is regulated by the Insurance Supervision Departments of the Central Bank of Ireland (as to conduct) and also by the PRA.

TRV's managing agency (Travelers Syndicate Management Ltd.) of its Lloyd's syndicate (Travelers Syndicate 5000) is also regulated by the PRA and the FCA, which have delegated certain regulatory responsibilities to the Council of Lloyd's. Travelers Syndicate 5000 is able to write business in over 75 jurisdictions throughout the world by virtue of Lloyd's international licenses. In each such jurisdiction, the policies written by Travelers Syndicate Management Ltd., as part of Lloyd's, are subject to the laws and insurance regulation of that jurisdiction. Travelers Underwriting Agency Limited, which as an insurance intermediary is regulated by the FCA, produces insurance business for Travelers Syndicate 5000.

A TRV subsidiary, Travelers Casualty and Surety Company, has a representative office in China. The representative office is regulated by the China Insurance Regulatory Commission. A TRV subsidiary, TCI Global Services, Inc., has a liaison office in India. Insurance business in India is regulated by the Insurance Regulatory and Development Authority. TRV has a 49.5% investment in JMalucelli, a joint venture holding company in Brazil. JMalucelli's subsidiaries operate in the insurance and reinsurance business in Brazil and are regulated by the Superintendencia de Seguros Privados.

Regulators in these jurisdictions require insurance companies to maintain certain levels of capital depending on, among other things, the type and amount of insurance policies in force.

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**Insurance Holding Company Statutes**

As a holding company, TRV is not regulated as an insurance company. However, since TRV owns capital stock in insurance subsidiaries, it is subject to state insurance holding company statutes, as well as certain other laws, of each of its insurance subsidiaries' states of domicile. All holding company statutes, as well as other laws, require disclosure and, in some instances, prior approval of material transactions between an insurance company and an affiliate. The holding company statutes and other laws also require, among other things, prior approval of an acquisition of control of a domestic insurer, some transactions between affiliates and the payment of extraordinary dividends or distributions.

*Insurance Regulations Concerning Change of Control.* Many state insurance regulatory laws contain provisions that require advance approval by state agencies of any change in control of an insurance company that is domiciled, or, in some cases, having substantial business that it is deemed to be commercially domiciled, in that state.

The laws of many states also contain provisions requiring pre-notification to state agencies prior to any change in control of a non-domestic insurance company admitted to transact business in that state. While these pre-notification statutes do not authorize the state agency to disapprove the change of control, they do authorize issuance of cease and desist orders with respect to the non-domestic insurer if it is determined that some conditions, such as undue market concentration, would result from the acquisition.

Any transactions that would constitute a change in control of any of TRV's insurance subsidiaries would generally require prior approval by the insurance departments of the states in which the insurance subsidiaries are domiciled or commercially domiciled. They may also require pre-acquisition notification in those states that have adopted pre-acquisition notification provisions and in which such insurance subsidiaries are admitted to transact business.

Two of TRV's insurance subsidiaries and its operations at Lloyd's are domiciled in the United Kingdom. Insurers in the United Kingdom are subject to change of control restrictions in the Financial Services Act of 2012, including approval of the PRA and FCA. Some of TRV's other insurance subsidiaries are domiciled in, or authorized to conduct insurance business in, Canada. Authorized insurers in Canada are subject to change of control restrictions in Section 407 of the Insurance Companies Act, including approval of the Office of the Superintendent of Financial Institutions. JMalucelli and its subsidiaries are subject to change of control and other share transfer restrictions and requirements in insurance laws and regulations in Brazil, mainly in Decree 73/1966 and CNSP Resolution no. 166/2007, which may include the need for prior approval of the insurance regulator, Superintendencia de Seguros Privados.

These requirements may deter, delay or prevent transactions affecting the control of or the ownership of common stock, including transactions that could be advantageous to TRV's shareholders.

**Regulatory Developments**

For a discussion of domestic and international regulatory developments, see Part I Item 1A Risk Factors including "Changes in federal regulation could impose significant burdens on us and otherwise adversely impact our results" and "New regulations outside of the U.S., including in the European Union, could adversely impact our results of operations and limit our growth."

**ENTERPRISE RISK MANAGEMENT**

As a large property and casualty insurance enterprise, the Company is exposed to many risks. These risks are a function of the environments within which the Company operates. Since certain risks can be correlated with other risks, an event or a series of events can impact multiple areas of the Company simultaneously and have a material effect on the Company's results of operations, financial

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position and/or liquidity. These exposures require an entity-wide view of risk and an understanding of the potential impact on all aspects of the Company's operations. It also requires the Company to manage its risk-taking to be within its risk appetite in a prudent and balanced effort to create and preserve value for all of the Company's stakeholders. This approach to Company-wide risk evaluation and management is commonly called Enterprise Risk Management (ERM). ERM activities involve both the identification and assessment of a broad range of risks and the execution of synchronized strategies to effectively manage such risks. Effective ERM also includes the determination of the Company's risk capital needs, which takes into account regulatory requirements and credit rating considerations, in addition to economic and other factors.

ERM at the Company is an integral part of its business operations. All risk owners across all functions, all corporate leaders and the board of directors are engaged in ERM. ERM involves risk-based analytics, as well as reporting and feedback throughout the enterprise in support of the Company's long-term financial strategies and objectives.

The Company uses various methods, including proprietary and third-party computer modeling processes, to continually monitor and analyze catastrophic events and the risks associated with them. These analyses and methods are used in making underwriting and reinsurance decisions as part of managing the Company's exposure to catastrophic events. In addition to catastrophe modeling and analysis, the Company also models and analyzes its exposure to other extreme events. The Company also utilizes proprietary and third-party computer modeling processes to evaluate capital adequacy. These analytical techniques are an integral component of the Company's ERM process and further support the Company's long-term financial strategies and objectives.

In addition to the day-to-day ERM activities within the Company's business units, other key internal risk management functions include the Management and Operating Committees (comprised of the Company's Chief Executive Officer and the other most senior members of management), the Enterprise and Underwriting Risk Committees of management, the Credit Committee, the Chief Compliance Officer, the Corporate Actuarial group, the Corporate Audit group, the Accounting Policy group, the Enterprise Underwriting group and many others. A senior executive oversees the ERM process. The mission of this executive is to facilitate risk assessment and to collaborate in implementing effective risk management strategies throughout the Company. Another strategic ERM objective of this executive includes working across the Company to enhance effective and realistic risk modeling capabilities as part of the Company's overall effort to understand and manage its portfolio of risks to be within its risk appetite. Board oversight of ERM is provided by the Risk Committee of the board of directors, which reviews the strategies, processes and controls pertaining to the Company's insurance operations and oversees the implementation, execution and performance of the Company's ERM program.

The Company's ERM efforts build upon the foundation of an effective internal control environment. ERM expands the internal control objectives of effective and efficient operations, reliable financial reporting and compliance with applicable laws and regulations, to fostering, leading and supporting an integrated, risk-based culture within the Company that focuses on value creation and preservation. However, the Company can provide only reasonable, not absolute, assurance that these objectives will be met. Further, the design of any risk management or control system must reflect the fact that there are resource constraints, and the benefits must be considered relative to their costs. As a result, the possibility of material financial loss remains in spite of the Company's significant ERM efforts. An investor should carefully consider the risks and all of the other information set forth in this annual report, including the discussions included in "Item 1A Risk Factors," "Item 7A Quantitative and Qualitative Disclosures About Market Risk," and "Item 8 Financial Statements and Supplementary Data."

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**OTHER INFORMATION**

**Customer Concentration**

In the opinion of the Company's management, no material part of the business of the Company and its subsidiaries is dependent upon a single customer or group of customers, the loss of any one of which would have a material adverse effect on the Company, and no one customer or group of affiliated customers accounts for 10% or more of the Company's consolidated revenues.

**Employees**

At December 31, 2013, the Company had approximately 30,800 employees. The Company believes that its employee relations are satisfactory. None of the Company's employees are subject to collective bargaining agreements.

**Sources of Liquidity**

For a discussion of the Company's sources of funds and maturities of the long-term debt of the Company, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources," and note 8 of notes to the Company's consolidated financial statements.

**Taxation**

For a discussion of tax matters affecting the Company and its operations, see note 12 of notes to the Company's consolidated financial statements.

**Financial Information about Reportable Business Segments**

For financial information regarding reportable business segments of the Company, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations," and note 2 of notes to the Company's consolidated financial statements.

**Intellectual Property**

The Company relies on a combination of contractual rights and copyright, trademark, patent and trade secret laws to establish and protect its intellectual property. With respect to trademarks specifically, the Company has registrations in many countries, including the United States, for material trademarks, including the TRAVELERS name and its iconic umbrella logo. The Company intends to retain material trademark rights in perpetuity, so long as it satisfies the use and registration requirements of all applicable countries. The Company regards its trademarks as highly valuable assets in marketing its products and services and vigorously seek to protect them against infringement. See "Item 1A Risk Factors Intellectual property is important to our business, and we may be unable to protect and enforce our own intellectual property or we may be subject to claims for infringing on the intellectual property of others."

**Recent Transactions**

For information regarding recent transactions of the Company, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations."

**Company Website, Social Media and Availability of SEC Filings**

The Company's Internet website is [www.travelers.com](http://www.travelers.com). Information on the Company's website is not incorporated by reference herein and is not a part of this Form 10-K. The Company makes available

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free of charge on its website or provides a link on its website to the Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as soon as reasonably practicable after those reports are electronically filed with, or furnished to, the SEC. To access these filings, go to the Company's website, then click on "SEC Filings" under the "For Investors" heading.

From time to time, the Company may use its website and/or social media outlets, such as Facebook and Twitter, as distribution channels of material company information. Financial and other important information regarding the Company is routinely posted on and accessible through the Company's website at <http://investor.travelers.com>, its Facebook page at <http://www.facebook.com/travelers> and its Twitter account (@TRV\_Insurance) at [http://www.twitter.com/TRV\\_Insurance](http://www.twitter.com/TRV_Insurance). In addition, you may automatically receive email alerts and other information about the Company when you enroll your email address by visiting the "Email Alert Service" section at <http://investor.travelers.com>.

**Glossary of Selected Insurance Terms**

Accident year	The annual calendar accounting period in which loss events occurred, regardless of when the losses are actually reported, booked or paid.
Adjusted unassigned surplus	Unassigned surplus as of the most recent statutory annual report reduced by twenty-five percent of that year's unrealized appreciation in value or revaluation of assets or unrealized profits on investments, as defined in that report.
Admitted insurer	A company licensed to transact insurance business within a state.
Agent	A licensed individual who sells and services insurance policies, receiving a commission from the insurer for selling the business and a fee for servicing it. An independent agent represents multiple insurance companies and searches the market for the best product for its client.
Annuity	A contract that pays a periodic benefit over the remaining life of a person (the annuitant), the lives of two or more persons or for a specified period of time.
Assigned risk pools	Reinsurance pools which cover risks for those unable to purchase insurance in the voluntary market. Possible reasons for this inability include the risk being too great or the profit being too small under the required insurance rate structure. The costs of the risks associated with these pools are charged back to insurance carriers in proportion to their direct writings.
Assumed reinsurance	Insurance risks acquired from a ceding company.
Average value analysis	A conventional actuarial method used to estimate ultimate losses for a given cohort of claims such as an accident year/product line component. If the paid-to-date losses are then subtracted from the estimated ultimate losses, the result is an indication of the unpaid losses.



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Book value per share	The basic premise of the method is that average claim values are stable and predictable over time for a particular cohort of claims. The method is utilized most often where ultimate claim counts are known or reliably estimable fairly early after the start of an accident year and average values are expected to be fairly predictable from one year to the next.
Bornhuetter-Ferguson method	The method comes up with an estimate of ultimate claims counts by accident year cohort, and multiplies it by an estimate of average claim value by accident year cohort, with multiple methods used to estimate these average claim values. Total common shareholders' equity divided by the number of common shares outstanding. A conventional actuarial method to estimate ultimate losses for a given cohort of claims such as an accident year/product line component. If the paid-to-date losses are then subtracted from the estimated ultimate losses, the result is an indication of the outstanding losses. The basic premise of the method is that the historical ratio of additional claim activity to earned premium for a given product line component/age-to-age period is stable and predictable. It implicitly assumes that the actual activity to date for past periods for that cohort is not a credible predictor of future activity for that cohort, or at least is not credible enough to override the "a priori" assumption as to future activity. It may be applied to either paid or case incurred claim data. It is used most often where the claim data is sparse and/or volatile and for relatively young cohorts with low volumes and/or data credibility. To illustrate, the method may assume that the ratio of additional paid losses from the 12 to 24 month period for an accident year is 10% of the original "a priori" expected losses for that accident year. The original "a priori" expected losses are typically based on the original loss ratio assumption for that accident year, with subsequent adjustment as facts develop. The ultimate losses equal actual activity to date plus the expected values for future periods.
Broker	One who negotiates contracts of insurance or reinsurance on behalf of an insured party, receiving a commission from the insurer or reinsurer for placement and other services rendered.
Capacity	The percentage of surplus, or the dollar amount of exposure, that an insurer or reinsurer is willing or able to place at risk. Capacity may apply to a single risk, a program, a line of business or an entire book of business. Capacity may be constrained by legal restrictions, corporate restrictions or indirect restrictions.
Captive	A closely-held insurance company whose primary purpose is to provide insurance coverage to the company's owners or their affiliates.

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Case-incurred development method	<p>A conventional actuarial method to estimate ultimate losses for a given cohort of claims such as an accident year/product line component. If the paid-to-date losses are then subtracted from the estimated ultimate losses, the result is an indication of the unpaid losses.</p> <p>The approach is the same as that described in this glossary under the "paid loss development method," but based on the growth in cumulative case-incurred losses (i.e., the sum of claim-adjustor incurred estimates for claims in the cohort) rather than paid losses. The basic premise of the method is that cumulative case incurred losses for a given cohort of claims will grow in a stable, predictable pattern from year-to-year, based on the age of the cohort.</p>
Case reserves	<p>Claim department estimates of anticipated future payments to be made on each specific individual reported claim.</p>
Casualty insurance	<p>Insurance which is primarily concerned with the losses caused by injuries to third persons, i.e., not the insured, and the legal liability imposed on the insured resulting therefrom. It includes, but is not limited to, employers' liability, workers' compensation, public liability, automobile liability, personal liability and aviation liability insurance. It excludes certain types of losses that by law or custom are considered as being exclusively within the scope of other types of insurance, such as fire or marine.</p>
Catastrophe	<p>A severe loss, resulting from a variety of events, including, among others, hurricanes, tornadoes and other windstorms, earthquakes, hail, wildfires, severe winter weather, floods, tsunamis and volcanic eruptions. Catastrophes can also result from a terrorist attack (including those involving nuclear, biological, chemical or radiological events), explosions, infrastructure failures or as a consequence of political instability. Each catastrophe has unique characteristics and catastrophes are not predictable as to timing or amount. Their effects are included in net and operating income and claims and claim adjustment expense reserves upon occurrence. A catastrophe may result in the payment of reinsurance reinstatement premiums and assessments from various pools.</p>
Catastrophe loss	<p>Loss and directly identified loss adjustment expenses from catastrophes, and related reinsurance reinstatement premiums.</p>
Catastrophe reinsurance	<p>A form of excess-of-loss reinsurance which, subject to a specified limit, indemnifies the ceding company for the amount of loss in excess of a specified retention with respect to an accumulation of losses resulting from a catastrophic event. The actual reinsurance document is called a "catastrophe cover." These reinsurance contracts are typically designed to cover property insurance losses but can be written to cover casualty insurance losses such as from workers' compensation policies.</p>

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Cede; ceding company	When an insurer reinsures its liability with another insurer or a "cession," it "cedes" business and is referred to as the "ceding company."
Ceded reinsurance	Insurance risks transferred to another company as reinsurance. See "Reinsurance."
Claim	Request by an insured for indemnification by an insurance company for loss incurred from an insured peril.
Claim adjustment expenses	See "Loss adjustment expenses (LAE)."
Claims and claim adjustment expenses	See "Loss" and "Loss adjustment expenses (LAE)."
Claims and claim adjustment expense reserves	See "Loss reserves."
Cohort	A group of items or individuals that share a particular statistical or demographic characteristic. For example, all claims for a given product in a given market for a given accident year would represent a cohort of claims.
Combined ratio (SAP and GAAP)	For SAP, it is the sum of the SAP loss and LAE ratio and the SAP underwriting expense ratio as defined in the statutory financial statements required by insurance regulators. The GAAP combined ratio is the equivalent of, and is calculated in the same manner as, the SAP combined ratio except that the SAP underwriting expense ratio is based on net <i>written</i> premium and the GAAP underwriting expense ratio is based on net <i>earned</i> premiums. The GAAP combined ratio as used in this Annual Report on Form 10-K is an indicator of the Company's underwriting discipline, efficiency in acquiring and servicing its business and overall underwriting profitability. A combined ratio under 100% generally indicates an underwriting profit. A combined ratio over 100% generally indicates an underwriting loss.
Commercial multi-peril policies	Refers to policies which cover both property and third-party liability exposures.
Commutation agreement	An agreement between a reinsurer and a ceding company whereby the reinsurer pays an agreed-upon amount in exchange for a complete discharge of all obligations, including future obligations, between the parties for reinsurance losses incurred.
Debt-to-total capital ratio	The ratio of debt to total capitalization.
Debt-to-total capital ratio excluding net unrealized gain (loss) on investments	The ratio of debt to total capitalization excluding the after-tax impact of net unrealized investment gains and losses.
Deductible	The amount of loss that an insured retains.

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Deferred acquisition costs	Primarily commissions and premium-related taxes that vary with, and are primarily related to, the production of new contracts and are deferred and amortized to achieve a matching of revenues and expenses when reported in financial statements prepared in accordance with U.S. Generally Accepted Accounting Principles (GAAP).
Deficiency	With regard to reserves for a given liability, a deficiency exists when it is estimated or determined that the reserves are insufficient to pay the ultimate settlement value of the related liabilities. Where the deficiency is the result of an estimate, the estimated amount of deficiency (or even the finding of whether or not a deficiency exists) may change as new information becomes available.
Demand surge	Significant short-term increases in building material and labor costs due to a sharp increase in demand for those materials and services, commonly as a result of a large catastrophe resulting in significant widespread property damage.
Direct written premiums	The amounts charged by an insurer to insureds in exchange for coverages provided in accordance with the terms of an insurance contract. The amounts exclude the impact of all reinsurance premiums, either assumed or ceded.
Earned premiums or premiums earned	That portion of property casualty premiums written that applies to the expired portion of the policy term. Earned premiums are recognized as revenues under both Statutory Accounting Practices (SAP) and GAAP.
Excess and surplus lines insurance	Insurance for risks not covered by standard insurance due to the unique nature of the risk. Risks could be placed in excess and surplus lines markets due to any number of characteristics, such as loss experience, unique or unusual exposures, or insufficient experience in business. Excess and surplus lines are less regulated by the states, allowing greater flexibility to design specific insurance coverage and negotiate pricing based on the risks to be secured.
Excess liability	Additional casualty coverage above a layer of insurance exposures.
Excess-of-loss reinsurance	Reinsurance that indemnifies the reinsured against all or a specified portion of losses over a specified dollar amount or "retention."
Exposure	The measure of risk used in the pricing of an insurance product. The change in exposure is the amount of change in premium on policies that renew attributable to the change in portfolio risk.
Facultative reinsurance	The reinsurance of all or a portion of the insurance provided by a single policy. Each policy reinsured is separately negotiated.

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Fair Access to Insurance Requirements (FAIR) Plan	A residual market mechanism which provides property insurance to those unable to obtain such insurance through the regular (voluntary) market. FAIR plans are set up on a state-by-state basis to cover only those risks in that state. For more information, see "residual market (involuntary business)."
Fidelity and surety programs	Fidelity insurance coverage protects an insured for loss due to embezzlement or misappropriation of funds by an employee. Surety is a three-party agreement in which the insurer agrees to pay a third party or make complete an obligation in response to the default, acts or omissions of an insured.
GAAP combined ratio excluding incremental impact of direct to consumer initiative Gross written premiums	The GAAP combined ratio adjusted to exclude the direct, variable impact of the Company's direct-to-consumer initiative in the Personal Insurance segment. The direct and assumed contractually determined amounts charged to the policyholders for the effective period of the contract based on the terms and conditions of the insurance contract.
Ground-up analysis	A method to estimate ultimate claim costs for a given cohort of claims such as an accident year/product line component. It involves analyzing the exposure and claim activity at an individual insured level and then through the use of deterministic or stochastic scenarios and/or simulations, estimating the ultimate losses for those insureds. The total losses for the cohort are then the sum of the losses for each individual insured. In practice, the method is sometimes simplified by performing the individual insured analysis only for the larger insureds, with the costs for the smaller insureds estimated via sampling approaches (extrapolated to the rest of the smaller insured population) or aggregate approaches (using assumptions consistent with the ground-up larger insured analysis).
Guaranteed cost products	An insurance policy where the premiums charged will not be adjusted for actual loss experience during the covered period.
Guaranty fund	A state-regulated mechanism that is financed by assessing insurers doing business in those states. Should insolvencies occur, these funds are available to meet some or all of the insolvent insurer's obligations to policyholders.
Holding company liquidity	Total cash, short-term invested assets and other readily marketable securities held by the holding company.
Incurred but not reported (IBNR) reserves	Reserves for estimated losses and LAE that have been incurred but not yet reported to the insurer. This includes amounts for unreported claims, development on known cases, and re-opened claims.

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Inland marine	A broad type of insurance generally covering articles that may be transported from one place to another, as well as bridges, tunnels and other instrumentalities of transportation. It includes goods in transit, generally other than transoceanic, and may include policies for movable objects such as personal effects, personal property, jewelry, furs, fine art and others.
IRIS ratios	Financial ratios calculated by the NAIC to assist state insurance departments in monitoring the financial condition of insurance companies.
Large deductible policy	An insurance policy where the customer assumes at least \$25,000 or more of each loss. Typically, the insurer is responsible for paying the entire loss under those policies and then seeks reimbursement from the insured for the deductible amount.
Lloyd's	An insurance marketplace based in London, England, where brokers, representing clients with insurable risks, deal with Lloyd's underwriters, who represent investors. The investors are grouped together into syndicates that provide capital to insure the risks.
Loss	An occurrence that is the basis for submission and/or payment of a claim. Losses may be covered, limited or excluded from coverage, depending on the terms of the policy.
Loss adjustment expenses (LAE)	The expenses of settling claims, including legal and other fees and the portion of general expenses allocated to claim settlement costs.
Loss and LAE ratio (SAP and GAAP)	For SAP, it is the ratio of incurred losses and loss adjustment expenses less certain administrative services fee income to net earned premiums as defined in the statutory financial statements required by insurance regulators. The GAAP ratio is calculated in the same manner as the SAP ratio. The GAAP loss and LAE ratio as used in this Annual Report on Form 10-K is an indicator of the Company's underwriting discipline and underwriting profitability.
Loss reserves	Liabilities established by insurers and reinsurers to reflect the estimated cost of claims incurred that the insurer or reinsurer will ultimately be required to pay in respect of insurance or reinsurance it has written. Reserves are established for losses and for LAE, and consist of case reserves and IBNR reserves. As the term is used in this document, "loss reserves" is meant to include reserves for both losses and LAE.
Loss reserve development	The increase or decrease in incurred claims and claim adjustment expenses as a result of the re-estimation of claims and claim adjustment expense reserves at successive valuation dates for a given group of claims. Loss reserve development may be related to prior year or current year development.

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Losses incurred	The total losses sustained by an insurance company under a policy or policies, whether paid or unpaid. Incurred losses include a provision for IBNR.
National Association of Insurance Commissioners (NAIC)	An organization of the insurance commissioners or directors of all 50 states, the District of Columbia and the five U.S. territories organized to promote consistency of regulatory practice and statutory accounting standards throughout the United States.
Net written premiums	Direct written premiums plus assumed reinsurance premiums less premiums ceded to reinsurers.
New business volume	The amount of written premium related to new policyholders and additional products sold to existing policyholders.
Operating income (loss)	Net income (loss) excluding the after-tax impact of net realized investment gains (losses), discontinued operations and cumulative effect of changes in accounting principles when applicable.
Operating income (loss) per share	Operating income (loss) on a per share basis.
Operating return on equity	The ratio of operating income to average equity excluding net unrealized investment gains and losses and discontinued operations, net of tax.
Paid development method	<p>A conventional actuarial method to estimate ultimate losses for a given cohort of claims such as an accident year/product line component. If the paid-to-date losses are then subtracted from the estimated ultimate losses, the result is an indication of the unpaid losses.</p> <p>The basic premise of the method is that cumulative paid losses for a given cohort of claims will grow in a stable, predictable pattern from year-to-year, based on the age of the cohort. These age-to-age growth factors are sometimes called "link ratios."</p> <p>For example, if cumulative paid losses for a product line XYZ for accident year 2004 were \$100 as of December 31, 2004 (12 months after the start of that accident year), then grew to \$120 as of December 31, 2005 (24 months after the start), the link ratio for that accident year from 12 to 24 months would be 1.20. If the link ratio for other recent accident years from 12 to 24 months for that product line were also at or around 1.20, then the method would assume a similar result for the most recent accident year, i.e., that it too would have its cumulative paid losses grow 20% from the 12 month to 24 month valuation.</p> <p>This is repeated for each age-to-age period into the future until the age-to-age link ratios for future periods are assumed to be 1.0 (i.e., the age at which cumulative losses are assumed to have stopped growing).</p>

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	<p>A given accident year's cumulative losses are then projected to ultimate by multiplying current cumulative losses by successive age-to-age link ratios up to that future age where growth is expected to end. For example, if growth is expected to end at 60 months, then the ultimate indication for an accident year with cumulative losses at 12 months equals those losses times a 12 to 24 month link ratio, times a 24 to 36 month link ratio, times a 36 to 48 month link ratio, times a 48 to 60 month link ratio.</p> <p>Advanced applications of the method include adjustments for changing conditions during the historical period and anticipated changes in the future.</p>
Policyholders' surplus	<p>As determined under SAP, the amount remaining after all liabilities, including loss reserves, are subtracted from all admitted assets. Admitted assets are assets of an insurer prescribed or permitted by a state to be recognized on the statutory balance sheet. Policyholders' surplus is also referred to as "surplus" or "statutory surplus" for statutory accounting purposes.</p>
Pool	<p>An organization of insurers or reinsurers through which particular types of risks are underwritten with premiums, losses and expenses being shared in agreed-upon percentages.</p>
Premiums	<p>The amount charged during the year on policies and contracts issued, renewed or reinsured by an insurance company.</p>
Property insurance	<p>Insurance that provides coverage to a person or business with an insurable interest in tangible property for that person's or business's property loss, damage or loss of use.</p>
Quota share reinsurance	<p>Reinsurance wherein the insurer cedes an agreed-upon fixed percentage of liabilities, premiums and losses for each policy covered on a pro rata basis.</p>
Rates	<p>Amounts charged per unit of insurance.</p>
Redundancy	<p>With regard to reserves for a given liability, a redundancy exists when it is estimated or determined that the reserves are greater than what will be needed to pay the ultimate settlement value of the related liabilities. Where the redundancy is the result of an estimate, the estimated amount of redundancy (or even the finding of whether or not a redundancy exists) may change as new information becomes available.</p>
Reinstatement premiums	<p>Additional premiums payable to reinsurers to restore coverage limits that have been exhausted as a result of reinsured losses under certain excess-of-loss reinsurance treaties.</p>
Reinsurance	<p>The practice whereby one insurer, called the reinsurer, in consideration of a premium paid to that insurer, agrees to indemnify another insurer, called the ceding company, for part or all of the liability of the ceding company under one or more policies or contracts of insurance which it has issued.</p>
Reinsurance agreement	<p>A contract specifying the terms of a reinsurance transaction.</p>



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Renewal premium change	The estimated change in average premium on policies that renew, including rate and exposure changes. Such statistics are subject to change based on a number of factors, including changes in actuarial estimates.
Renewal rate change	The estimated change in average premium on policies that renew, excluding exposure changes. Such statistics are subject to change based on a number of factors, including changes in actuarial estimates.
Reported claim development method	A conventional actuarial method to estimate ultimate claim counts for a given cohort of claims such as an accident year/product line component. If the reported-to-date counts are then subtracted from the estimated ultimate counts, the result is an indication of the IBNR counts.  The approach is the same as that described in this glossary under the "paid loss development method", but based on the growth in cumulative claim counts rather than paid losses. The basic premise of the method is that cumulative claim counts for a given cohort of claims will grow in a stable, predictable pattern from year-to-year, based on the age of the cohort.
Residual market (involuntary business)	Insurance market which provides coverage for risks for those unable to purchase insurance in the voluntary market. Possible reasons for this inability include the risks being too great or the profit potential too small under the required insurance rate structure. Residual markets are frequently created by state legislation either because of lack of available coverage such as: property coverage in a windstorm prone area or protection of the accident victim as in the case of workers' compensation. The costs of the residual market are usually charged back to the direct insurance carriers in proportion to the carriers' voluntary market shares for the type of coverage involved.
Retention	The amount of exposure a policyholder company retains on any one risk or group of risks. The term may apply to an insurance policy, where the policyholder is an individual, family or business, or a reinsurance policy, where the policyholder is an insurance company.
Retention rate	The percentage of prior period premiums (excluding renewal premium changes), accounts or policies available for renewal in the current period that were renewed. Such statistics are subject to change based on a number of factors, including changes in actuarial estimates.
Retrospective premiums	Premiums related to retrospectively rated policies.
Retrospective rating	A plan or method which permits adjustment of the final premium or commission on the basis of actual loss experience, subject to certain minimum and maximum limits.

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Return on equity	The ratio of net income (loss) less preferred dividends to average shareholders' equity.
Risk-based capital (RBC)	A measure adopted by the NAIC and enacted by states for determining the minimum statutory policyholders' surplus requirements of insurers. Insurers having total adjusted capital less than that required by the RBC calculation will be subject to varying degrees of regulatory action depending on the level of capital inadequacy.
Risk retention group	An alternative form of insurance in which members of a similar profession or business band together to self insure their risks.
Runoff business	An operation which has been determined to be nonstrategic; includes non-renewals of in-force policies and a cessation of writing new business, where allowed by law.
Salvage	The amount of money an insurer recovers through the sale of property transferred to the insurer as a result of a loss payment.
S-curve method	A mathematical function which depicts an initial slow change, followed by a rapid change and then ending in a slow change again. This results in an "S" shaped line when depicted graphically. The actuarial application of these curves fit the reported data to date for a particular cohort of claims to an S-curve to project future activity for that cohort.
Second-injury fund	The employer of an injured, impaired worker is responsible only for the workers' compensation benefit for the most recent injury; the second-injury fund would cover the cost of any additional benefits for aggravation of a prior condition. The cost is shared by the insurance industry and self-insureds, funded through assessments to insurance companies and self-insureds based on either premiums or losses.
Self-insured retentions	That portion of the risk retained by a person for its own account.
Servicing carrier	An insurance company that provides, for a fee, various services including policy issuance, claims adjusting and customer service for insureds in a reinsurance pool.
Statutory accounting practices (SAP)	The practices and procedures prescribed or permitted by domiciliary state insurance regulatory authorities in the United States for recording transactions and preparing financial statements. Statutory accounting practices generally reflect a modified going concern basis of accounting.
Statutory basis surplus	The excess of an insurance company's assets over its liabilities in accordance with the statutory accounting practices required by state laws and regulations.
Structured settlements	Periodic payments to an injured person or survivor for a determined number of years or for life, typically in settlement of a claim under a liability policy, usually funded through the purchase of an annuity.

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Subrogation	A principle of law incorporated in insurance policies, which enables an insurance company, after paying a claim under a policy, to recover the amount of the loss from another person or entity who is legally liable for it.
Third-party liability	A liability owed to a claimant (third party) who is not one of the two parties to the insurance contract. Insured liability claims are referred to as third-party claims.
Total capitalization	The sum of total shareholders' equity and debt.
Treaty reinsurance	The reinsurance of a specified type or category of risks defined in a reinsurance agreement (a "treaty") between a primary insurer or other reinsured and a reinsurer. Typically, in treaty reinsurance, the primary insurer or reinsured is obligated to offer and the reinsurer is obligated to accept a specified portion of all that type or category of risks originally written by the primary insurer or reinsured.
Umbrella coverage	A form of insurance protection against losses in excess of amounts covered by other liability insurance policies or amounts not covered by the usual liability policies.
Unassigned surplus	The undistributed and unappropriated amount of policyholders' surplus.
Underlying GAAP combined ratio	The sum of the underlying GAAP loss and LAE ratio and the underlying GAAP underwriting expense ratio. The underlying GAAP combined ratio is an indicator of the Company's underwriting discipline and underwriting profitability for the current accident year.
Underlying GAAP loss and LAE ratio	The GAAP loss and LAE ratio, excluding the impact of catastrophe losses and prior year reserve development. The underlying GAAP loss and LAE ratio is an indicator of the Company's underwriting discipline and underwriting profitability for the current accident year.
Underlying GAAP underwriting expense ratio	The GAAP underwriting expense ratio, excluding the impact of catastrophe losses.
Underlying underwriting margin	Net earned premiums and fee income less claims and claim adjustment expenses (excluding catastrophe losses and prior year reserve development) and insurance-related expenses.
Underwriter	An employee of an insurance company who examines, accepts or rejects risks and classifies accepted risks in order to charge an appropriate premium for each accepted risk. The underwriter is expected to select business that will produce an average risk of loss no greater than that anticipated for the class of business.

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Underwriting	The insurer's or reinsurer's process of reviewing applications for insurance coverage, and the decision as to whether to accept all or part of the coverage and determination of the applicable premiums; also refers to the acceptance of that coverage.
Underwriting expense ratio (SAP and GAAP)	For SAP, it is the ratio of underwriting expenses incurred (including commissions paid), less certain administrative services fee income and billing and policy fees, to net <i>written</i> premiums as defined in the statutory financial statements required by insurance regulators. For GAAP, it is the ratio of underwriting expenses (including the amortization of deferred acquisition costs), less certain administrative services fee income and billing and policy fees, to net <i>earned</i> premiums. The GAAP underwriting expense ratio as used in this Annual Report on Form 10-K is an indicator of the Company's efficiency in acquiring and servicing its business.
Underwriting gain or loss	Net earned premiums and fee income less claims and claim adjustment expenses and insurance-related expenses.
Unearned premium	The portion of premiums written that is allocable to the unexpired portion of the policy term.
Voluntary market	The market in which a person seeking insurance obtains coverage without the assistance of residual market mechanisms.
Wholesale broker	An independent or exclusive agent that represents both admitted and nonadmitted insurers in market areas, which include standard, non-standard, specialty and excess and surplus lines of insurance. The wholesaler does not deal directly with the insurance consumer. The wholesaler deals with the retail agent or broker.
Workers' compensation	A system (established under state and federal laws) under which employers provide insurance for benefit payments to their employees for work-related injuries, deaths and diseases, regardless of fault.

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**Item 1A. RISK FACTORS**

You should carefully consider the following risks and all of the other information set forth in this report, including our consolidated financial statements and the notes thereto.

**Catastrophe losses could materially and adversely affect our results of operations, our financial position and/or liquidity, and could adversely impact our ratings, our ability to raise capital and the availability and cost of reinsurance.** Our property and casualty insurance operations expose us to claims arising out of catastrophes. Catastrophes can be caused by various natural events, including, among others, hurricanes, tornadoes and other windstorms, earthquakes, hail, wildfires, severe winter weather, floods, tsunamis and volcanic eruptions. Catastrophes can also be man-made, such as a terrorist attack (including those involving nuclear, biological, chemical or radiological events), explosions, infrastructure failures or a consequence of political instability. The geographic distribution of our business subjects us to catastrophe exposures in the United States, which include, but are not limited to: hurricanes from Maine through Texas; tornadoes throughout the Central, Mid-Atlantic and Southeastern regions of the United States; earthquakes in California, the New Madrid region and the Pacific Northwest region of North America; wildfires, particularly in the Southwest; and terrorism in major cities in the United States. In addition, our international operations subject us to catastrophe exposures in Canada, the United Kingdom and the Republic of Ireland, as well as to a variety of world-wide catastrophe exposures through our Lloyd's operations, and in Brazil through our joint venture investment.

The incidence and severity of catastrophes are inherently unpredictable, and it is possible that both the frequency and severity of natural and man-made catastrophic events could increase. Severe weather events over the last several years have underscored the unpredictability of future climate trends, and potentially changing climate conditions could add to the frequency and severity of natural disasters and create additional uncertainty as to future trends and exposures. For example, over the last decade, hurricane activity has impacted areas further inland than previously experienced, thus expanding the Company's potential for losses from hurricanes. Additionally, both the frequency and severity of tornado and hail storms in the United States have been greater in recent years. Moreover, we could experience more than one highly severe catastrophic event in any given period.

All of the catastrophe modeling tools that we use, or that we rely on from outside parties, to help manage certain of our catastrophe exposures are based on assumptions and judgments that are subject to error and mis-estimation and may produce estimates that are materially different than actual results. In addition, compared to models for hurricanes, models for earthquakes are less reliable due to there being a more limited number of significant historical events to analyze, while models for tornadoes and hail storms are newer and may be even less reliable due to the highly random geographic nature and size of these events. As a result, models for earthquakes and especially for tornado and hail storms may have even greater difficulty predicting risks and estimating losses. Further, changes in climate conditions could cause our underlying modeling data to be less predictive, thus limiting our ability to effectively evaluate and manage catastrophe risk. See "We may be adversely affected if our pricing and capital models provide materially different indications than actual results" below as well as "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Catastrophe Modeling" and " Changing Climate Conditions."

The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Increases in the value and geographic concentration of insured property and the effects of inflation could increase the severity of claims from catastrophic events in the future. For example, the specific geographic location impacted by tornadoes is inherently random and unpredictable and the specific location impacted by a tornado may or may not be highly populated and may or may not have a high concentration of our insured exposures.

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States have from time to time passed legislation, and regulators have taken action, that have the effect of limiting the ability of insurers to manage catastrophe risk, such as legislation prohibiting insurers from reducing exposures or withdrawing from catastrophe-prone areas or mandating that insurers participate in residual markets. Participation in residual market mechanisms has resulted in, and may continue to result in, significant losses or assessments to insurers, including us, and, in certain states, those losses or assessments may not be commensurate with our direct catastrophe exposure in those states. If our competitors leave those states having residual market mechanisms, remaining insurers, including us, may be subject to significant increases in losses or assessments following a catastrophe. In addition, following catastrophes, there are sometimes legislative and administrative initiatives and court decisions that seek to expand insurance coverage for catastrophe claims beyond the original intent of the policies or seek to prevent the application of deductibles. Also, our ability to adjust terms, including deductible levels, or to increase pricing to the extent necessary to offset rising costs of catastrophes, particularly in the Personal Insurance segment, requires approval of regulatory authorities of certain states. Our ability or our willingness to manage our catastrophe exposure by raising prices, modifying underwriting terms or reducing exposure to certain geographies may be limited due to considerations of public policy, the evolving political environment and/or changes in the general economic climate. We also may choose to write business in catastrophe-prone areas that we might not otherwise write for strategic purposes, such as improving our access to other underwriting opportunities.

There are also factors that impact the estimation of ultimate costs for catastrophes. For example, the estimation of claims and claim adjustment expense reserves related to hurricanes can be affected by the inability to access portions of the impacted areas, the complexity of factors contributing to the losses, the legal and regulatory uncertainties and the nature of the information available to establish the claims and claim adjustment expense reserves. Complex factors include, but are not limited to: determining whether damage was caused by flooding versus wind; evaluating general liability and pollution exposures; estimating additional living expenses; the impact of demand surge; infrastructure disruption; fraud; the effect of mold damage; business interruption costs; and reinsurance collectability. In recent years, increased late reporting of weather-related losses by claimants, particularly losses from hail damage, has led to higher costs than we previously expected. The timing of a catastrophe's occurrence, such as at or near the end of a reporting period, can also affect the information available to us in estimating claims and claim adjustment expense reserves for that reporting period. The estimates related to catastrophes are adjusted in subsequent periods as actual claims emerge and additional information becomes available.

Exposure to catastrophe losses or actual losses resulting from a catastrophe could adversely affect our financial strength and claims-paying ratings and could impair our ability to raise capital on acceptable terms or at all. Also, as a result of our exposure to catastrophe losses or actual losses following a catastrophe, rating agencies may further increase capital requirements, which may require us to raise capital to maintain our ratings or adversely affect our ratings. A ratings downgrade could hurt our ability to compete effectively or attract new business. In addition, catastrophic events could cause us to exhaust our available reinsurance limits and could adversely impact the cost and availability of reinsurance. Such events can also impact the credit of our reinsurers. For a discussion of our catastrophe reinsurance coverage, see "Item 1 Business Reinsurance Catastrophe Reinsurance." Catastrophic events could also adversely impact the credit of the issuers of securities, such as states or municipalities, in whom we have invested.

In addition, coverage in our reinsurance program for terrorism is limited. Although the Terrorism Risk Insurance Program provides benefits in the event of certain acts of terrorism, those benefits are subject to a deductible and other limitations. Under this program, once our losses exceed 20% of our commercial property and casualty insurance premium for the preceding calendar year, the federal government will reimburse us for 85% of our losses attributable to certain acts of terrorism which

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exceed this deductible up to a total industry program cap of \$100 billion. Our estimated deductible under the program is \$2.35 billion for 2014. In addition, because the interpretation of this law is untested, there is substantial uncertainty as to how it will be applied to specific circumstances. The program is due to expire at the end of 2014; however, legislation to extend the program has been introduced in Congress. It is possible that Congress could decide not to renew the program or could otherwise modify or eliminate the program, which could adversely affect our business by increasing our exposure to terrorism losses, or by lowering our business volume through efforts to avoid that exposure.

Because of the risks set forth above, catastrophes such as those caused by various natural events or man-made events such as a terrorist attack, including "unconventional" acts of terrorism involving nuclear, biological, chemical or radiological events, could materially and adversely affect our results of operations, financial position and/or liquidity. Further, we may not have sufficient resources to respond to claims arising from a high frequency of high severity natural catastrophes and/or of man-made catastrophic events involving conventional means. In addition, while we seek to manage our exposure to man-made catastrophic events involving conventional means, we may not have sufficient resources to respond to claims arising out of one or more man-made catastrophic events involving nuclear, biological, chemical or radiological means.

**During or following a period of financial market disruption or economic downturn, our business could be materially and adversely affected.** Over the past seven years and particularly during the financial crisis, worldwide financial markets have experienced significant disruption. During a portion of this period, the United States and many other economies experienced a prolonged economic downturn, resulting in heightened credit risk, reduced valuation of certain investments and decreased economic activity. While economic conditions have generally stabilized and improved, there is continued uncertainty regarding the duration and strength of the economic recovery. Even if growth continues, it may be at a slow rate for an extended period of time, and other economic conditions, such as employment rates, may continue to be weak.

Furthermore, financial markets may again experience significant and prolonged disruption. In recent years, the federal government, particularly the Federal Reserve, has taken extraordinary steps to stabilize financial markets, encourage economic growth and keep interest rates low. While inflation has recently been limited and that trend may continue, it is possible that the steps taken by the federal government to stabilize financial markets and improve economic conditions could lead to an inflationary environment. Further, such steps may be ineffective and, in the case of the Federal Reserve, actual or anticipated efforts to continue to unwind some of such steps (including the so-called "tapering" of quantitative easing) could disrupt financial markets and/or could adversely impact the value of our investment portfolio or general economic conditions.

Economic uncertainty has been exacerbated in recent years by the increased potential for default by one or more European sovereign debt issuers, the potential partial or complete dissolution of the Eurozone and its common currency and the negative impact of such events on global financial institutions and capital markets generally. Actions or inactions of European governments may impact these actual or perceived risks. In the U.S. during 2011, one rating agency downgraded the U.S.'s long-term debt credit rating from AAA. Future actions or inactions of the United States government, including a failure to increase the government debt limit or a shutdown of the federal government, could increase the actual or perceived risk that the U.S. may not ultimately pay its obligations when due and may disrupt financial markets, including capital markets. Further, issues related to the U.S. Federal budget and taxes, implementation of the Affordable Care Act and the regulatory environment have added to the uncertainty regarding economic conditions generally.

If economic conditions deteriorate, or if financial markets experience significant disruption, it could materially adversely affect our results of operations, financial position and/or liquidity. Several of the risk factors discussed below identify risks that result from, or are exacerbated by, an economic

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slowdown or financial disruption. These include risks discussed below related to our investment portfolio, reinsurance arrangements, other credit exposures, our estimates of claims and claim adjustment expense reserves, emerging claim and coverage issues, the competitive environment, regulatory developments and the impact of rating agency actions. You should also refer to "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations", particularly the "Outlook" section.

Many of these risks could materialize, and our financial results could be negatively impacted, even after the end of an economic downturn or financial disruption. During or following an economic downturn, lower levels of economic activity could reduce (and historically have reduced) exposure changes at renewal. They also could adversely impact (and historically have adversely impacted) audit premium adjustments, policy endorsements and mid-term cancellations after policies are written, particularly in our business units within Business Insurance, which could adversely impact our written premiums. In addition, because earned premiums lag written premiums, our results can be adversely affected after general economic conditions have improved. An inflationary environment (which may follow government efforts to stabilize the economy) may also, as we discuss below, adversely impact our loss costs and could adversely impact the valuation of our investment portfolio. Finally, as a result of financial market disruption, we may, as discussed below, face increased regulation.

**If actual claims exceed our claims and claim adjustment expense reserves, or if changes in the estimated level of claims and claim adjustment expense reserves are necessary, our financial results could be materially and adversely affected.** Claims and claim adjustment expense reserves do not represent an exact calculation of liability, but instead represent management estimates of what the ultimate settlement and administration of claims will cost, generally utilizing actuarial expertise and projection techniques, at a given accounting date.

The process of estimating claims and claim adjustment expense reserves involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events, such as: changes in claims handling procedures; adverse changes in loss cost trends, including inflationary pressures on medical costs and auto and home repair costs; economic conditions including general inflation; legal trends and legislative changes; and varying judgments and viewpoints of the individuals involved in the estimation process, among others. The impact of many of these items on ultimate costs for claims and claim adjustment expenses is difficult to estimate. Claims and claim adjustment expense reserve estimation difficulties also differ significantly by product line due to differences in claim complexity, the volume of claims, the potential severity of individual claims, the determination of occurrence date for a claim and reporting lags (the time between the occurrence of the policyholder event and when it is actually reported to the insurer).

As discussed above, it is possible that steps taken by the federal government to stabilize the economy could lead to higher inflation than we had anticipated, which could in turn lead to an increase in our loss costs. The impact of inflation on loss costs could be more pronounced for those lines of business that are considered "long tail", such as general liability, as they require a relatively long period of time to finalize and settle claims for a given accident year. In addition, inflationary pressures in medical costs may be increased by the healthcare reform legislation and its implementation. The estimation of claims and claim adjustment expense reserves may also be more difficult during times of adverse or uncertain economic conditions due to unexpected changes in behavior of claimants and policyholders, including an increase in fraudulent reporting of exposures and/or losses, reduced maintenance of insured properties or increased frequency of small claims or delays in the reporting of claims.

We continually refine our claims and claim adjustment expense reserve estimates in a regular, ongoing process as historical loss experience develops, additional claims are reported and settled and the legal, regulatory and economic environment evolves. Business judgment is applied throughout the



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process, including the application of various individual experiences and expertise to multiple sets of data and analyses. Different experts may choose different assumptions when faced with material uncertainty, based on their individual backgrounds, professional experiences and areas of focus. Hence, such experts may at times produce estimates materially different from each other. This risk may be exacerbated in the context of an acquisition. Experts providing input to the various estimates and underlying assumptions include actuaries, underwriters, claim personnel and lawyers, as well as other members of management. Therefore, management may have to consider varying individual viewpoints as part of its estimation of claims and claim adjustment expense reserves.

We attempt to consider all significant facts and circumstances known at the time claims and claim adjustment expense reserves are established or reviewed. Due to the inherent uncertainty underlying claims and claim adjustment expense reserve estimates, the final resolution of the estimated liability for claims and claim adjustment expenses will likely be higher or lower than the related claims and claim adjustment expense reserves at the reporting date. Therefore, actual paid losses in the future may yield a materially different amount than is currently reserved.

Because of the uncertainties set forth above, additional liabilities resulting from one insured event, or an accumulation of insured events, may exceed the current related reserves. In addition, our estimate of claims and claim adjustment expenses may change. These additional liabilities or increases in estimates, or a range of either, cannot now be reasonably estimated and could materially and adversely affect our results of operations and/or our financial position.

For a discussion of claims and claim adjustment expense reserves by product line, including examples of common factors that can affect required reserves, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates Claims and Claim Adjustment Expense Reserves."

**Our investment portfolio may suffer reduced returns or material realized or unrealized losses.** Investment returns are an important part of our overall profitability. Fixed maturity and short-term investments comprised approximately 93% of the carrying value of our investment portfolio as of December 31, 2013. Changes in interest rates caused by inflation or other factors (inclusive of credit spreads) affect the carrying value of our fixed maturity investments and returns on our fixed maturity and short-term investments. A decline in interest rates reduces the returns available on short-term investments and new fixed maturity investments (including those purchased to re-invest maturities from the existing portfolio), thereby negatively impacting our net investment income, while rising interest rates reduce the market value of existing fixed maturity investments, thereby negatively impacting our book value. During 2013, the net unrealized gain in our fixed income portfolio declined from \$4.56 billion to \$1.76 billion as interest rates increased. It is possible that further increases in interest rates (inclusive of credit spreads) could result in further declines in that unrealized gain position or even result in an unrealized loss, thereby adversely impacting our book value. Notwithstanding increases in interest rates in 2013, interest rates in recent years have been and remain at very low levels relative to historical experience, and it is possible that rates may remain at low levels for a prolonged period. The value of our fixed maturity and short-term investments is also subject to the risk that certain investments may default or become impaired due to a deterioration in the financial condition of one or more issuers of the securities held in our portfolio, or due to a deterioration in the financial condition of an insurer that guarantees an issuer's payments of such investments. Such defaults and impairments could reduce our net investment income and result in realized investment losses. During an economic downturn, fixed maturity and short-term investments could be subject to a higher risk of default.

Our fixed maturity investment portfolio is invested, in substantial part, in obligations of states, municipalities and political subdivisions (collectively referred to as the municipal bond portfolio). Notwithstanding the relatively low historical rates of default on many of these obligations and

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notwithstanding that we typically seek to invest in high-credit-quality securities (including those with structural protections such as being secured by dedicated or pledged sources of revenue), our municipal bond portfolio could be subject to default or impairment. In particular:

The prolonged economic downturn that began in 2008, and the limited economic recovery that has followed, has resulted in many states and local governments operating under deficits or projected deficits. The severity and duration of these deficits could have an adverse impact on the collectability and valuation of our municipal bond portfolio. These deficits may be exacerbated by the impact of unfunded pension plan obligations and other postretirement obligations or by declining municipal tax bases and revenues in times of financial stress.

Some issuers may be unwilling to increase tax rates, or to reduce spending, to fund interest or principal payments on their municipal bonds, or may be unable to access the municipal bond market to fund such payments. The risk of widespread defaults may increase if some issuers voluntarily choose to default, instead of implementing difficult fiscal measures, and the actual or perceived consequences (such as reduced access to capital markets) are less severe than expected.

The risk of widespread defaults may also increase if there are changes in legislation that permit states, municipalities and political subdivisions to file for bankruptcy protection where they were not permitted before. In addition, the collectability and valuation of municipal bonds may be adversely affected if there are judicial interpretations in a bankruptcy or other proceeding that lessen the value of structural protections. For example, debtors may challenge the effectiveness of structural protections thought to be provided by municipal securities backed by a dedicated source of revenue. The collectability and valuation may also be adversely affected if there are judicial interpretations in a bankruptcy or other proceeding that question the payment priority of municipal bonds.

A substantial portion of our fixed maturity portfolio will mature within the next few years. Approximately 40% of the fixed maturity portfolio is expected to mature over the next three years (this includes the early redemption of bonds, assuming interest rates (including credit spreads) do not rise significantly by applicable call dates). For a schedule of the contractual maturities of our fixed maturity portfolio by year for the next several years, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Investment Portfolio." Of that maturing portfolio, a substantial amount includes municipal bonds that have been pre-refunded with U.S. treasury securities. As a result, even if our investment strategy does not significantly change over the next few years, the overall yield on and composition of our portfolio could be meaningfully impacted by the types of investments available for reinvestment with the proceeds of matured bonds. For example, if yields remain low when we reinvest such proceeds, our future net investment income would be adversely affected. In addition, depending on the specific bonds available for purchase at the time of re-investment, the mix of specific issuers in our fixed-income and municipal bond portfolio will change. As a result, the overall credit profile and other aspects of our portfolio could be adversely impacted. Also, a decrease in municipal bonds that have been pre-refunded with U.S. Treasury securities could reduce the credit quality of our portfolio.

Our portfolio has benefited from tax exemptions and certain other tax laws, including, but not limited to, those governing dividends-received deductions and tax credits (such as foreign tax credits). Changes in these laws could adversely impact the value of our investment portfolio. See "Changes in U.S. tax laws or in the tax laws of other jurisdictions in which we operate could adversely impact us" below.

Our investment portfolio includes: residential mortgage-backed securities; collateralized mortgage obligations; pass-through securities and asset-backed securities collateralized by sub-prime mortgages; commercial mortgage-backed securities; and wholly-owned real estate and real estate partnerships, all

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of which could be adversely impacted by further declines in real estate valuations and/or financial market disruption.

We also invest a portion of our assets in equity securities, private equity limited partnerships, hedge funds and real estate partnerships. From time to time, we may also invest in other types of non-fixed maturity investments, including commodities. All of these asset classes are subject to greater volatility in their investment returns than fixed maturity investments. General economic conditions, changes in applicable tax laws and many other factors beyond our control can adversely affect the value of our non-fixed maturity investments and the realization of net investment income, and/or result in realized investment losses. As a result of these factors, we may realize reduced returns on these investments, incur losses on sales of these investments and be required to write down the value of these investments, which could reduce our net investment income and result in realized investment losses. From time to time, the Company enters into short positions in U.S. Treasury futures contracts to manage the duration of its fixed maturity portfolio. Although the use of U.S. Treasury futures contracts in 2013 resulted in realized investment gains, U.S. Treasury futures contracts can also result in realized investment losses.

Our investment portfolio is also subject to increased valuation uncertainties when investment markets are illiquid. The valuation of investments is more subjective when markets are illiquid, thereby increasing the risk that the estimated fair value (i.e., the carrying amount) of the portion of the investment portfolio that is carried at fair value as reflected in our financial statements is not reflective of prices at which actual transactions could occur.

Given that economic and market conditions are highly uncertain, we may, depending on circumstances in the future, make changes to the mix of investments in our investment portfolio. These changes may impact the duration, volatility and risk of our investment portfolio.

Because of the risks set forth above, the value of our investment portfolio could decrease, we could experience reduced net investment income and we could experience realized and/or unrealized investment losses, which could materially and adversely affect our results of operations, financial position and/or liquidity.

**Our business could be harmed because of our potential exposure to asbestos and environmental claims and related litigation.**

With regard to asbestos claims, we have received and continue to receive a significant number of asbestos claims from policyholders (including others seeking coverage under a policy). Factors underlying these claim filings include intensive advertising by lawyers seeking asbestos claimants and the continued focus by plaintiffs on previously peripheral defendants. The focus on these defendants is primarily the result of the number of traditional asbestos defendants who have sought bankruptcy protection in previous years. The bankruptcy of many traditional defendants has prompted plaintiffs to aggressively seek out potential new defendants and has caused increased settlement demands against those policyholders who are not in bankruptcy but who remain in the tort system. Currently, in many jurisdictions, those who allege very serious injury and who can present credible medical evidence of their injuries are receiving priority trial settings in the courts, while those who have not shown any credible disease manifestation are having their hearing dates delayed or placed on an inactive docket. This trend of prioritizing claims involving credible evidence of injuries, along with the focus on previously peripheral defendants, contributes to the claims and claim adjustment expense payments we experienced.

We also continue to be involved in coverage litigation concerning a number of policyholders, some of whom have filed for bankruptcy, who in some instances have asserted that all or a portion of their asbestos-related claims are not subject to aggregate limits on coverage. In these instances, policyholders also may assert that each individual bodily injury claim should be treated as a separate occurrence

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under the policy. It is difficult to predict whether these policyholders will be successful on both issues. To the extent both issues are resolved in a policyholder's favor and our other defenses are not successful, our coverage obligations under the policies at issue would be materially increased and bounded only by the applicable per-occurrence limits and the number of asbestos bodily injury claims against the policyholders. Accordingly, although we have seen a moderation in the overall risk associated with these lawsuits, it remains difficult to predict the ultimate cost of these claims.

Further, in addition to asbestos claims against policyholders, proceedings have been launched directly against insurers, including us, by individuals challenging insurers' conduct with respect to the handling of past asbestos claims and by individuals seeking damages arising from alleged asbestos-related bodily injuries. It is possible that the filing of other direct actions against insurers, including us, could be made in the future. It is not possible to predict the outcome of these proceedings, including whether the plaintiffs will be able to sustain these actions against insurers based on novel legal theories of liability.

With regard to environmental claims, we have received and continue to receive claims from policyholders who allege that they are liable for injury or damage arising out of their alleged disposition of toxic substances. Mostly, these claims are due to various legislative as well as regulatory efforts aimed at environmental remediation. For instance, the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), enacted in 1980 and later modified, enables private parties as well as federal and state governments to take action with respect to releases and threatened releases of hazardous substances. This federal statute permits the recovery of response costs from some liable parties and may require liable parties to undertake their own remedial action. Liability under CERCLA may be joint and several with other responsible parties.

The Company has been, and continues to be, involved in litigation involving insurance coverage issues pertaining to environmental claims. The Company believes that some court decisions have interpreted the insurance coverage to be broader than the original intent of the insurers and policyholders. These decisions continue to be inconsistent and vary from jurisdiction to jurisdiction.

Uncertainties surrounding the final resolution of these asbestos and environmental claims continue, and it is difficult to estimate our ultimate liability for such claims and related litigation. As a result, these reserves are subject to revision as new information becomes available and as claims develop. The continuing uncertainties include, without limitation:

the risks and lack of predictability inherent in complex litigation;

any impact from the bankruptcy protection sought by various asbestos producers and other asbestos defendants;

a further increase in the cost to resolve, and/or the number of, asbestos and environmental claims beyond that which is anticipated;

the emergence of a greater number of asbestos claims than anticipated as a result of extended life expectancies resulting from medical advances and lifestyle improvements;

the role of any umbrella or excess policies we have issued;

the resolution or adjudication of disputes pertaining to the amount of available coverage for asbestos and environmental claims in a manner inconsistent with our previous assessment of these claims;

the number and outcome of direct actions against us;

future developments pertaining to our ability to recover reinsurance for asbestos and environmental claims;

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the unavailability of other insurance sources potentially available to policyholders, whether through exhaustion of policy limits or through the insolvency of other participating insurers; and

uncertainties arising from the insolvency or bankruptcy of policyholders and other defendants.

It is also not possible to predict changes in the legal, regulatory and legislative environment and their impact on the future development of asbestos and environmental claims. This environment could be affected by changes in applicable legislation and future court and regulatory decisions and interpretations, including the outcome of legal challenges to legislative and/or judicial reforms establishing medical criteria for the pursuit of asbestos claims. It is also difficult to predict the ultimate outcome of complex coverage disputes until settlement negotiations near completion and significant legal questions are resolved or, failing settlement, until the dispute is adjudicated. This is particularly the case with policyholders in bankruptcy where negotiations often involve a large number of claimants and other parties and require court approval to be effective.

While the ongoing evaluation of asbestos and environmental claims and associated liabilities considers the inconsistencies of court decisions as to coverage, plaintiffs' expanded theories of liability and the risks inherent in complex litigation and other uncertainties, it is possible that the outcome of the continued uncertainties regarding these claims could result in liability in future periods that differs from current reserves by an amount that could materially and adversely affect our results of operations. See the "Asbestos Claims and Litigation" and "Environmental Claims and Litigation" sections of "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations." Also see "Item 3 Legal Proceedings."

**We are exposed to, and may face adverse developments involving, mass tort claims such as those relating to exposure to potentially harmful products or substances.** In addition to asbestos and environmental claims, we face exposure to other types of mass tort claims, including claims related to exposure to potentially harmful products or substances, including lead paint, silica and welding rod fumes. Establishing claims and claim adjustment expense reserves for mass tort claims is subject to uncertainties because of many factors, including expanded theories of liability, disputes concerning medical causation with respect to certain diseases, geographical concentration of the lawsuits asserting the claims and the potential for a large rise in the total number of claims without underlying epidemiological developments suggesting an increase in disease rates. Moreover, evolving judicial interpretations regarding the application of various tort theories and defenses, including application of various theories of joint and several liabilities, as well as the application of insurance coverage to these claims, make it difficult to estimate our ultimate liability for such claims.

Because of the uncertainties set forth above, additional liabilities may arise for amounts in excess of the current related reserves. In addition, our estimate of claims and claim adjustment expenses may change, and such change could be material. These additional liabilities or increases in estimates, or a range of either, cannot now be reasonably estimated and could materially and adversely affect our results of operations.

**The effects of emerging claim and coverage issues on our business are uncertain.** As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended issues related to claim and coverage may emerge. These issues may adversely affect our business, including by extending coverage beyond our underwriting intent, by increasing the number, size or types of claims or by mandating changes to our underwriting practices. Examples of emerging claims and coverage issues include, but are not limited to:

judicial expansion of policy coverage and the impact of new or expanded theories of liability;

plaintiffs targeting property and casualty insurers, including us, in purported class action litigation relating to claims-handling and other practices;

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claims relating to construction defects, which often present complex coverage and damage valuation questions;

claims under directors' & officers' insurance policies relating to losses from involvement in financial market activities, such as mortgage or financial product origination, distribution, structuring or servicing and foreclosure procedures; failed financial institutions; fraud; possible accounting irregularities; and corporate governance issues;

claims related to data security breaches, information system failures or cyber-attacks;

the assertion of "public nuisance" or similar theories of liability, pursuant to which plaintiffs seek to recover monies spent to administer public health care programs, abate hazards to public health and safety and/or recover damages purportedly attributable to a "public nuisance";

claims relating to molestation by an employee or a volunteer of an insured;

medical developments that link health issues to particular causes (for example, cumulative trauma), resulting in liability or workers' compensation claims;

claims alleging that one or more of our underwriting criteria have a disparate impact on persons belonging to a protected class in violation of the law, including the Fair Housing Act;

claims arising out of techniques to expand access to oil and gas resources, such as hydraulic fracturing;

claims relating to unanticipated consequences of current or new technologies; and

claims relating to potentially changing climate conditions, including higher frequency and severity of weather-related events.

In some instances, these emerging issues may not become apparent for some time after we have issued the affected insurance policies. As a result, the full extent of liability under our insurance policies may not be known for many years after the policies are issued.

In addition, the potential passage of new legislation designed to expand the right to sue, to remove limitations on recovery, to deem by statute the existence of a covered occurrence, to extend the statutes of limitations or otherwise to repeal or weaken tort reforms could have an adverse impact on our business.

The effects of these and other unforeseen emerging claim and coverage issues are extremely hard to predict and could harm our business and materially and adversely affect our results of operations.

**The intense competition that we face could harm our ability to maintain or increase our business volumes and our profitability.** The property and casualty insurance industry is highly competitive, and we believe that it will remain highly competitive for the foreseeable future. We compete with both domestic and foreign insurers which may offer products at prices and on terms that are not consistent with our economic standards in an effort to maintain or increase their business. The competitive environment in which we operate could also be impacted by current general economic conditions, which could reduce the volume of business available to us as well as to our competitors. In recent years, pension and hedge funds and other entities with substantial available capital have increasingly sought to participate in the property and casualty insurance and reinsurance industries. Well-capitalized new entrants to the property and casualty insurance and reinsurance industries, or existing competitors that receive substantial infusions of capital may conduct business in ways that adversely impact our business volumes and profitability. Further, an expanded supply of reinsurance capital may lower costs for insurers that rely on reinsurance and, as a consequence, those insurers may be able to price their products more competitively. In addition, the competitive environment could be impacted by changes in customer preferences, including customer demand for direct distribution channels.



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In Personal Insurance, the use of comparative rating technologies has impacted, and may continue to impact, our business as well as the industry as a whole. A substantial amount of the Company's Personal Insurance new business is written after an agent compares quotes using comparative rating technologies, a cost-efficient means of obtaining quotes from multiple companies. Because the use of this technology, whether by agents or directly by customers, facilitates the process of generating multiple quotes, the technology has increased price comparison on new business and, increasingly, on renewal business. It also has resulted in an increase in the level of quote activity and a lower percentage of quotes that result in new business from customers, and these trends may continue or accelerate. If we are not able to operate with a competitive cost structure or accurately estimate and price for claims and claim adjustment expenses, our underwriting margins could be adversely affected over time. Additionally, there is potential for similar technology to be used to access comparative rates for small commercial business. Agents, brokers or other third parties may also create alternate distribution channels for personal or commercial business, such as insurance exchanges, that may adversely impact product differentiation and pricing.

Other technological changes may present competitive risks. For example, innovations, such as telematics and other usage-based methods of determining premiums, can impact product design and pricing and may become an increasingly important competitive factor. Other potential technological changes, such as driverless cars, could disrupt the demand for our products from current customers, and we may not be able to respond effectively. In addition, our competitive position could be impacted by our ability to deploy, in a cost effective manner, technology that collects and analyzes a wide variety of data points (so-called "big data" analysis) to make underwriting or other decisions. See also "Our business success and profitability depend, in part, on effective information technology systems and on continuing to develop and implement improvements in technology" below.

In recent years, we have undertaken various actions to improve our underwriting margins on many of our insurance products, and competitive dynamics may impact the success of these efforts. These efforts include seeking improved rates, as well as improved terms and conditions, and also include other initiatives, such as reducing operating expenses and acquisition costs. These efforts may not be successful and/or may result in lower retention and new business levels and therefore lower business volumes. In addition, if our underwriting is not effective, efforts to increase rates could also lead to "adverse selection", whereby accounts retained have higher losses, and are less profitable, than accounts lost. For more detail, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Outlook."

In particular, in our Agency Automobile line of business, we have undertaken various actions to improve our underwriting margins, which have been negatively impacted by various factors. See "Item 1 Business Personal Insurance Competition" above for a description of some of these actions, including the offer of a new, more competitively-priced product. These factors include (i) changes in customer preferences and demand for direct distribution channels, (ii) utilization of comparative rating technologies by agents and (iii) other technological changes, as described above. If our strategies to increase profitability in the Agency Automobile line of business are not effective, we may need to explore other actions or initiatives to improve our competitive position and profitability in this line of business.

Overall, our competitive position in our various businesses is based on many factors, including but not limited to our:

ability to profitably price our business, retain existing customers and obtain new business;

premiums charged, contract terms and conditions, products and services offered (including the ability to design customized programs);

agent, broker and client relationships;

ability to keep pace relative to our competitors with changes in technology and information systems;



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speed of claims payment;

ability to provide our products and services in a cost effective manner;

perceived overall financial strength and corresponding ratings assigned by independent rating agencies;

reputation, experience and qualifications of employees;

geographic scope of business; and

local presence.

We may have difficulty in continuing to compete successfully on any of these bases in the future. If competition limits our ability to retain existing business or write new business at adequate rates, our results of operations could be materially and adversely affected. See "Competition" sections of the discussion on business segments in "Item 1 Business."

**We may not be able to collect all amounts due to us from reinsurers and reinsurance coverage may not be available to us in the future at commercially reasonable rates or at all.** Although the reinsurer is liable to us to the extent of the ceded reinsurance, we remain liable as the direct insurer on all risks reinsured. As a result, ceded reinsurance arrangements do not eliminate our obligation to pay claims. Accordingly, we are subject to credit risk with respect to our ability to recover amounts due from reinsurers.

In the past, certain reinsurers have ceased writing business and entered into runoff. Some of our reinsurance claims may be disputed by the reinsurers, and we may ultimately receive partial or no payment. This is a particular risk in the case of claims that relate to insurance policies written many years ago, including those relating to asbestos and environmental claims. In addition, in a number of jurisdictions, particularly the European Union and the United Kingdom, a reinsurer is permitted to transfer a reinsurance arrangement to another reinsurer, which may be less creditworthy, without a counterparty's consent, provided that the transfer has been approved by the applicable regulatory and/or court authority.

Included in reinsurance recoverables are certain amounts related to structured settlements. Structured settlements are annuities purchased from various life insurance companies to settle certain personal physical injury claims, of which workers' compensation claims comprise a significant portion. In cases where we did not receive a release from the claimant, the structured settlement is included in reinsurance recoverables and the related claim cost is included in the liability for claims and claim adjustment expense reserves, as we retain the contingent liability to the claimant. If it is expected that the life insurance company is not able to pay, we would recognize an impairment of the related reinsurance recoverable if, and to the extent, the purchased annuities are not covered by state guaranty associations. In the event that the life insurance company fails to make the required annuity payments, we would be required to make such payments.

Many life insurance companies were negatively impacted by the financial markets disruption and the economic downturn. A number of these companies, including certain of those with which we conduct business or to which we otherwise have credit exposure, were downgraded by various rating agencies during this time period. For a discussion of our top reinsurance groups by reinsurance recoverable and the top five groups by amount of structured settlements provided, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Reinsurance Recoverables."

The availability and cost of reinsurance are subject to prevailing market conditions, both in terms of price and available capacity. The availability of reinsurance capacity can be impacted by general economic conditions and conditions in the reinsurance market, such as the occurrence of significant

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reinsured events. The availability and cost of reinsurance could affect our business volume and profitability.

Because of the risks set forth above, we may not be able to collect all amounts due to us from reinsurers, and reinsurance coverage may not be available to us in the future at commercially reasonable rates or at all, and/or life insurance companies may fail to make required annuity payments, and thus our results of operations could be materially and adversely affected.

**We are exposed to credit risk in certain of our business operations.** In addition to exposure to credit risk related to our investment portfolio and reinsurance recoverables (discussed above), we are exposed to credit risk in several other areas of our business operations, including credit risk relating to policyholders, independent agents and brokers.

We are exposed to credit risk in our surety insurance operations, where we guarantee to a third party that our customer will satisfy certain performance obligations (e.g., a construction contract) or certain financial obligations. If a customer of ours defaults, we may suffer losses and not be reimbursed by that customer. In addition, it is customary practice in the surety business for multiple insurers to participate as co-sureties on large surety bonds. Under these arrangements, the co-surety obligations are typically joint and several, in which case we are also exposed to credit risk with respect to our co-sureties.

In addition, a portion of our business is written with large deductible insurance policies. Under workers' compensation insurance contracts with deductible features, we are obligated to pay the claimant the full amount of the claim. We are subsequently reimbursed by the contractholder for the deductible amount, and, as a result, we are exposed to credit risk to the policyholder. Moreover, certain policyholders purchase retrospectively rated workers' compensation policies (i.e., policies in which premiums are adjusted after the policy period based on the actual loss experience of the policyholder during the policy period). Retrospectively rated policies expose us to additional credit risk to the extent that the adjusted premium is greater than the original premium.

Our efforts to mitigate the credit risk that we have to our insureds may not be successful. To reduce such credit risk, we require certain insureds to post collateral for some or all of these obligations, often in the form of pledged securities such as money market funds or letters of credit provided by banks. In cases where we receive pledged securities and the insureds are unable to honor their obligations, we may be exposed to credit risk on the securities pledged and/or the risk that our access to that collateral may be stayed during an insured's bankruptcy. In cases where we receive letters of credit from banks and the insureds are unable to honor their obligations, we are exposed to the credit risk of the banks that issued the letters of credit.

In accordance with industry practice, when policyholders purchase insurance policies from us through independent agents and brokers, the premiums relating to those policies are often paid to the agents and brokers for payment to us. In most jurisdictions, the premiums will be deemed to have been paid to us whether or not they are actually received by us. Consequently, we assume a degree of credit risk associated with amounts due from independent agents and brokers.

To a large degree, the credit risk we face is a function of the economy; accordingly, we face a greater risk in an economic downturn. While we attempt to manage the risks discussed above through underwriting and investment guidelines, collateral requirements and other oversight mechanisms, our efforts may not be successful. For example, collateral obtained may subsequently have little or no value. As a result, our exposure to the above credit risks could materially and adversely affect our results of operations.

**Within the United States, our businesses are heavily regulated by the states in which we conduct business, including licensing and supervision, and changes in regulation may reduce our profitability and limit our growth.** These regulatory systems are generally designed to protect the interests of

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policyholders, and not necessarily the interests of insurers, their shareholders and other investors. For example, to protect policyholders whose insurance company becomes financially insolvent, guaranty funds have been established in all 50 states to pay the covered claims of policyholders in the event of an insolvency of an insurer, subject to applicable state limits. The funding of guaranty funds is provided through assessments levied against remaining insurers in the marketplace. As a result, the insolvency of one or more insurance companies could result in additional assessments levied against us.

These regulatory systems also address authorization for lines of business, policyholders' surplus requirements, limitations on the types and amounts of certain investments, underwriting limitations, transactions with affiliates, dividend limitations, changes in control, premium rates and a variety of other financial and non-financial components of an insurer's business.

In recent years, the state insurance regulatory framework has come under increased scrutiny, and some state legislatures have considered or enacted laws that may alter or increase state authority to regulate insurance companies and insurance holding companies. Further, the NAIC and state insurance regulators continually re-examine existing laws and regulations, specifically focusing on modifications to holding company regulations, interpretations of existing laws and the development of new laws and regulations. The NAIC recently amended the Insurance Holding Company Model Regulation requiring insurers who are part of a holding company system to complete an enterprise risk report to provide a summary of the holding company's enterprise risk management (ERM) framework. It is possible that our states of domicile will require changes in our ERM process or take other regulatory actions that could limit our ability to write additional business or require that we hold additional capital. See "Enterprise Risk Management" herein for further discussion of the Company's ERM.

In a time of financial uncertainty or a prolonged economic downturn or otherwise, regulators may choose to adopt more restrictive insurance laws and regulations. For example, insurance regulators may choose to restrict the ability of insurance subsidiaries to make payments to their parent companies or reject rate increases due to the economic environment. The state insurance regulators may also increase the statutory capital requirements for our insurance subsidiaries. In addition, state tax laws that specifically impact the insurance industry, such as premium taxes or other taxes, may be enacted or changed by states to raise revenues.

State laws or regulations that are adopted or amended may be more restrictive than current laws or regulations and may result in lower revenues and/or higher costs of compliance and thus could materially and adversely affect our results of operations and limit our growth.

**Changes in federal regulation could impose significant burdens on us and otherwise adversely impact our results.** While the U.S. federal government has not historically regulated the insurance business, in 2010 the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) established a Federal Insurance Office (the FIO) within the U.S. Department of the Treasury. The FIO has limited regulatory authority and is empowered to gather data and information regarding the insurance industry and insurers. In December 2013, the FIO released a report recommending ways to modernize and improve the system of insurance regulation in the United States. While the report did not recommend full federal regulation of insurance, it did suggest an expanded federal role in some circumstances. In addition, the report suggested that Congress should consider direct federal involvement to fill regulatory gaps identified in the report, should those gaps persist, for example, by considering either establishing a federal coordinating body or a direct regulator of select aspects of the industry, such as large complex institutions or institutions that seek a federal charter, if a law is passed to allow a federal charter. It is not clear as to the extent, if any, the report will lead to regulatory changes or how any such changes would impact the Company.

The Dodd-Frank Act also gives the Federal Reserve supervisory authority over a number of nonbank financial services holding companies, including insurance companies, if they are designated by a two-thirds vote of a Financial Stability Oversight Council (the FSOC) as "systemically important"

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financial institutions" (SIFI). The FSOC, chaired by the Secretary of the Treasury, is a group of federal financial regulators, a state insurance regulator and an independent insurance expert. The FSOC finalized its first set of SIFI designations in July and September 2013 and, based upon the FSOC's rules and interpretive guidance, the Company was not included in the designated companies. Nonetheless, it is possible that the Council may change its rules or interpretations in the future and conclude that we are a SIFI. If we were designated as a SIFI, the Federal Reserve's supervisory authority could include the ability to impose heightened financial regulation and could impact requirements regarding our capital, liquidity and leverage as well as our business and investment conduct. As a result of the foregoing, the Dodd-Frank Act, or other additional federal regulation that is adopted in the future, could impose significant burdens on us, including impacting the ways in which we conduct our business, increasing compliance costs and duplicating state regulation, and could result in a competitive disadvantage, particularly relative to other insurers that may not be subject to the same level of regulation. Changes in the U.S. regulatory framework could impact the overall competitive environment by imposing additional burdens on us and allowing other competitors not subject to these same burdens to enter or expand their insurance businesses.

Even if we are not subject to additional regulation by the federal government, significant financial sector regulatory reform, including the Dodd-Frank Act, could have a significant impact on us. For example, regulatory reform could have an unexpected impact on our rights as a creditor or on our competitive position. In particular, the Dodd-Frank Act authorizes assessments to pay for the resolution of systemically important financial institutions that have become insolvent. We (as a financial company with more than \$50 billion in assets) could be assessed, and, although any such assessment is required to be risk weighted (i.e., riskier firms pay more), such costs could be material to us and are not currently estimable.

Other potential changes in U.S. federal legislation, regulation and/or administrative policies, including the potential repeal of the McCarran-Ferguson Act (which exempts insurance from most federal regulation) and potential changes in federal taxation, could also significantly harm the insurance industry, including us.

**A downgrade in our claims-paying and financial strength ratings could adversely impact our business volumes, adversely impact our ability to access the capital markets and increase our borrowing costs.** Claims-paying and financial strength ratings are important to an insurer's competitive position. Rating agencies periodically review insurers' ratings and change their ratings criteria; therefore, our current ratings may not be maintained in the future. A downgrade in one or more of our ratings could negatively impact our business volumes because demand for certain of our products may be reduced, particularly because many customers may require that we maintain minimum ratings to enter into or renew business with us. Additionally, we may find it more difficult to access the capital markets and we may incur higher borrowing costs. If significant losses, including, but not limited to, those resulting from one or more major catastrophes, or significant reserve additions or significant investment losses were to cause our capital position to deteriorate significantly, or if one or more rating agencies substantially increase their capital requirements, we may need to raise equity capital in the future (which we may not be able to do at a reasonable cost or at all, especially at a time of financial market disruption) in order to maintain our ratings or limit the extent of a downgrade. A continued trend of more frequent and severe weather-related catastrophes or a prolonged financial market disruption or economic downturn may lead rating agencies to substantially increase their capital requirements. See also "During or following a period of financial market disruption or economic downturn, our business could be materially and adversely affected." For further discussion about our ratings, see, "Item 1 Business Ratings."

**The inability of our insurance subsidiaries to pay dividends to our holding company in sufficient amounts would harm our ability to meet our obligations, pay future shareholder dividends or make future share repurchases.** Our holding company relies on dividends from our U.S. insurance

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subsidiaries to meet our obligations for payment of interest and principal on outstanding debt, to pay dividends to shareholders, to make contributions to our qualified domestic pension plan, to pay other corporate expenses and to make share repurchases. The ability of our insurance subsidiaries to pay dividends to our holding company in the future will depend on their statutory surplus, earnings and regulatory restrictions.

We are subject to state insurance regulation as an insurance holding company system. Our U.S. insurance subsidiaries are subject to various regulatory restrictions that limit the maximum amount of dividends available to be paid to their parent without prior approval of insurance regulatory authorities. In a time of prolonged economic downturn or otherwise, insurance regulators may choose to further restrict the ability of insurance subsidiaries to make payments to their parent companies. The ability of our insurance subsidiaries to pay dividends to our holding company is also restricted by regulations that set standards of solvency that must be met and maintained.

The inability of our insurance subsidiaries to pay dividends to our holding company in an amount sufficient to meet our debt service obligations and other cash requirements could harm our ability to meet our obligations, to pay future shareholder dividends and to make share repurchases.

**Disruptions to our relationships with our independent agents and brokers could adversely affect us.** We market our insurance products primarily through independent agents and brokers. An important part of our business is written through less than a dozen such intermediaries. Further, there has been a trend of increased consolidation by agents and brokers, which could impact our relationships with, and fees paid to, some agents and brokers, and/or otherwise negatively impact the pricing or distribution of our products. Loss of all or a substantial portion of the business provided through such agents and brokers could materially and adversely affect our future business volume and results of operations.

We may also seek to develop new products or distribution channels, including our current efforts to establish a direct-to-consumer platform in the Personal Insurance segment and our new Quantum 2.0 auto product. In addition, agents and brokers may create alternate distribution channels for commercial business, such as insurance exchanges, that may adversely impact product differentiation and pricing. Access to greater levels of data and increased utilization of technology by agents and brokers may also impact our relationship with them and our competitive position. Our efforts or their efforts with respect to new products or alternate distribution channels, as well as changes in the way agents and brokers utilize data and technology, could adversely impact our business relationship with independent agents and brokers who currently market our products, resulting in a lower volume of business generated from these sources.

We rely on internet applications for the marketing and sale of certain of our products, and we may increasingly rely on internet applications and toll-free numbers for distribution. In some instances, our agents and brokers are required to access separate business platforms to execute the sale of our personal insurance or commercial insurance products. Should internet disruptions occur, or frustration with our business platforms or distribution initiatives develop among our independent agents and brokers, any resulting loss of business could materially and adversely affect our future business volume and results of operations. See "If we experience difficulties with technology, data security and/or outsourcing relationships, our ability to conduct our business could be negatively impacted" below.

Customers in the past have brought claims against us for the actions of our agents. Even with proper controls in place, actual or alleged errors or inaccuracies by our agents could result in our involvement in disputes, litigation or regulatory actions related to actions taken or not taken by our agents.

**Our efforts to develop new products or expand in targeted markets may not be successful and may create enhanced risks.** A number of our recent and planned business initiatives involve

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developing new products or expanding existing products in targeted markets. This includes the following efforts, from time to time, to protect or grow market share:

We may develop products that insure risks we have not previously insured, contain new coverage or coverage terms or contain different commission terms. For example, in response to the competitive environment in personal auto insurance, we have started to roll-out a new product called Quantum Auto 2.0 that is intended to be more competitively-priced. See "Item 1 Business Personal Insurance Competition."

We may refine our underwriting processes. For example, in certain of our businesses in recent years, we have substantially increased the volume of business that flows through our automated underwriting and pricing systems.

We may seek to expand distribution channels, such as our efforts to develop a direct-to-consumer platform in Personal Insurance.

We may focus on geographic markets within or outside of the United States where we have had relatively little or no market share.

We may not be successful in introducing new products or expanding in targeted markets and, even if we are successful, these efforts may create enhanced risks. Among other risks:

Demand for new products or in new markets may not meet our expectations.

To the extent we are able to market new products or expand in new markets, our risk exposures may change, and the data and models we use to manage such exposures may not be as sophisticated or effective as those we use in existing markets or with existing products. This, in turn, could lead to losses in excess of our expectations.

Models underlying automated underwriting and pricing decisions may not be effective.

Efforts to develop new products or markets have the potential to create or increase distribution channel conflict, such as described above under " Disruptions to our relationships with our independent agents and brokers could adversely affect us."

In connection with the conversion of existing policyholders to a new product, some policyholders' pricing may increase, while the pricing for other policyholders may decrease, the net impact of which could negatively impact retention and margins.

To develop new products or markets, we may need to make substantial capital and operating expenditures, which may also negatively impact results in the near term.

If our efforts to develop new products or expand in targeted markets are not successful, our results of operations could be materially and adversely affected.

**We may be adversely affected if our pricing and capital models provide materially different indications than actual results.** The profitability of our property and casualty business substantially depends on the extent to which our actual claims experience is consistent with the assumptions we use in pricing our policies. We utilize third-party and proprietary models to help us price business in a manner that is intended to be consistent, over time, with actual results and return objectives. We incorporate the Company's historical loss experience, external industry data and economic indices into our modeling processes, and we use various methods, including predictive modeling, forecasting and sophisticated simulation modeling techniques, to analyze loss trends and the risks associated with our assets and liabilities. We also use these

modeling processes, analyses and methods in making underwriting, pricing and reinsurance decisions as part of managing our exposure to catastrophes and other extreme adverse events. These modeling processes incorporate numerous assumptions and forecasts about the future level and variability of: interest rates, inflation, capital requirements, and

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frequency and severity of losses, among others, that are difficult to make and may differ materially from actual results.

Whether we use a proprietary or third-party model, future experience may be materially different from past and current experience incorporated in a model's forecasts or simulations. This includes the likelihood of events occurring or continuing or the correlation among events. Third party models may provide substantially different indications than what our proprietary modeling processes provide. As a result, third-party model estimates of losses can be, and often have been, materially different for similar events in comparison to our proprietary estimates. The differences between third-party model estimates and our proprietary estimates are driven by the use of different data sets as well as different assumptions and forecasts regarding the frequency and severity of events and claims arising from the events.

If we fail to appropriately price the risks we insure, or fail to change our pricing model to appropriately reflect our current experience, or if our claims experience is more frequent or severe than our underlying risk assumptions, our profit margins may be negatively affected. If we underestimate the frequency and/or severity of extreme adverse events occurring, our financial condition may be adversely affected. If we overestimate the risks we are exposed to, we may overprice our products, and new business growth and retention of our existing business may be adversely affected. As we expand into different markets and geographies, we will write more policies in markets and geographical areas where we have less data specific to these new markets and geographies, and, accordingly, we may be more susceptible to error in our models and strategy. See "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Catastrophe Modeling."

**Our business success and profitability depend, in part, on effective information technology systems and on continuing to develop and implement improvements in technology.** We depend in large part on our technology systems for conducting business and processing claims, as well as for providing the data and analytics we utilize to manage our business, and thus our business success is dependent on maintaining the effectiveness of existing technology systems and on continuing to develop and enhance technology systems that support our business processes and strategic initiatives in a cost and resource efficient manner. Some system development projects are long-term in nature, may negatively impact our expense ratios as we invest in the projects and may cost more than we expect to complete. In addition, system development projects may not deliver the benefits we expect once they are complete, or may be replaced or become obsolete more quickly than expected, which could result in accelerated recognition of expenses. If we do not effectively and efficiently manage and upgrade our technology portfolio, including with respect to the technology portfolio of our recently acquired businesses, or if the costs of doing so are higher than we expect, our ability to provide competitive services to new and existing customers in a cost effective manner and our ability to implement our strategic initiatives could be adversely impacted.

**If we experience difficulties with technology, data security and/or outsourcing relationships, our ability to conduct our business could be negatively impacted.** While technology can streamline many business processes and ultimately reduce the cost of operations, technology initiatives present significant risks. Our business is highly dependent upon our employees' ability to perform, in an efficient and uninterrupted fashion, necessary business functions. A shut-down of, or inability to access, one or more of our facilities (including our primary data processing facility); a power outage; or a failure of one or more of our information technology, telecommunications or other systems could significantly impair our ability to perform such functions on a timely basis, particularly if such an interruption lasts for an extended period of time. In the event of a disaster such as a natural catastrophe, terrorist attack or industrial accident, or due to a computer virus, our systems could be inaccessible for an extended period of time. In addition, because our information technology and telecommunications systems increasingly interface with and depend on third-party systems, we could experience service denials or failures of controls if demand for our service exceeds capacity or a third-party system fails or



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experiences an interruption. Business interruptions and failures of controls could also result if our internal systems do not interface with each other as intended, including as it relates to recently acquired businesses. If our business continuity plans did not sufficiently address such a business interruption, system failure or service denial, this could result in a deterioration of our ability to write and process new and renewal business, provide customer service, pay claims in a timely manner or perform other necessary business functions.

Our operations rely on the reliable and secure processing, storage and transmission of confidential and other information in our computer systems and networks. Computer viruses, hackers, employee misconduct and other external hazards could expose our data systems to security breaches, cyber-attacks or other disruptions. In addition, we routinely transmit and receive personal, confidential and proprietary information by e-mail and other electronic means. While we attempt to develop secure transmission capabilities with third-party vendors and others with whom we do business, we may be unable to put in place secure capabilities with all of such vendors and third parties and, in addition, these third parties may not have appropriate controls in place to protect the confidentiality of the information.

Like other global companies, our computer systems are regularly subject to and will continue to be the target of computer viruses or other malicious codes, unauthorized access, cyber-attacks or other computer-related penetrations. While we have experienced threats to our data and systems, to date, we are not aware that we have experienced a material breach of cyber security. Over time, the sophistication of these threats continues to increase, however, and our administrative and technical controls as well as other preventative actions we take to reduce the risk of cyber incidents and protect our information may be insufficient to detect or prevent unauthorized access, other physical and electronic break-ins, cyber-attacks or other security breaches to our computer systems or those of third parties with whom we do business. In addition, new technology that could result in greater operational efficiency may further expose our computer systems to the risk of cyber-attacks.

We have increasingly outsourced certain technology and business process functions to third parties and may continue to do so in the future. If we do not effectively develop, implement and monitor our outsourcing relationships, third party providers do not perform as anticipated or we experience technological or other problems with a transition, we may not realize expected productivity improvements or cost efficiencies and may experience operational difficulties, increased costs and a loss of business. Our outsourcing of certain technology and business process functions to third parties may expose us to increased risk related to data security or service disruptions, which could result in monetary and reputational damages. For example, while we do not believe it will materially and adversely impact our operations or results, we terminated a contract with one of our outsourcing vendors in the fourth quarter of 2013 because they breached that contract by providing proprietary Company information to one of our competitors. In addition to risks caused by third party providers, our ability to receive services from third party providers outside of the United States might be impacted by cultural differences, political instability, unanticipated regulatory requirements or public policy inside or outside of the United States.

The increased risks identified above could expose us to data loss, disruption of service, monetary and reputational damages and significant increases in compliance costs and costs to improve the security and resiliency of our computer systems. The compromise of personal, confidential or proprietary information could also subject us to legal liability or regulatory action under data protection and privacy laws and regulations enacted by the U.S. federal and state governments, the European Union or other jurisdictions or by various regulatory organizations or exchanges. As a result, our ability to conduct our business and our results of operations might be materially and adversely affected.

**We are subject to a number of risks associated with our business outside the United States.** We conduct business outside the United States primarily in Canada, the United Kingdom and the Republic

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of Ireland. In addition, we have a joint venture in Brazil and may also explore opportunities in other countries, including Latin American countries and other emerging markets such as India and China.

In conducting business outside of the United States, we are subject to a number of significant risks, particularly in emerging economies. These risks include restrictions such as price controls, capital controls, currency exchange limits, ownership limits and other restrictive or anti-competitive governmental actions, which could have an adverse effect on our business and our reputation. Following the completion of our acquisition of Dominion, a larger portion of our premiums from outside of the United States will be comprised of premiums generated in Canada, a substantial portion of which will consist of automobile premiums from the province of Ontario, which is a highly-regulated market. Our business activities outside the United States may also subject us to currency risk and, in some markets, it may be difficult to effectively hedge that risk. In addition, in some markets, we may invest as part of a joint venture with a local counterparty. Because our governance rights may be limited, we may not have control over the ability of the joint venture to make certain decisions and/or mitigate risks it faces, and significant disagreements with a joint venture counterparty may adversely impact our investment. Our business activities outside the United States also subject us to additional domestic and foreign laws and regulations, including the Foreign Corrupt Practices Act and similar laws in other countries that prohibit the making of improper payments to foreign officials. Although we have policies and controls in place that are designed to ensure compliance with these laws, if those controls are ineffective and an employee or intermediary fails to comply with applicable laws and regulations, we could suffer civil and criminal penalties and our business and our reputation could be adversely affected. Some countries, particularly emerging economies, have laws and regulations that lack clarity and, even with local expertise and effective controls, it can be difficult to determine the exact requirements of, and potential liability under, the local laws. For example, in some jurisdictions, including Brazil, parties to a joint venture may, in some circumstances, have liability for some obligations of the venture, and that liability may extend beyond the capital invested. Failure to comply with local laws in a particular market may result in substantial liability and could have a significant and negative effect not only on our business in that market but also on our reputation generally.

In addition, competition for skilled employees in developing markets and other non-U.S. locations may be intense. If we are not able to hire, integrate, motivate and retain a sufficient number of employees with the knowledge and background necessary for our global businesses, those businesses and our results of operations may be adversely affected.

**New regulations outside of the U.S., including in the European Union, could adversely impact our results of operations and limit our growth.** Insurance laws or regulations that are adopted or amended in jurisdictions outside the U.S. may be more restrictive than current laws or regulations and may result in lower revenues and/or higher costs of compliance and thus could materially and adversely affect our results of operations and limit our growth.

In particular, the European Union's executive body, the European Commission, is implementing new capital adequacy and risk management regulations called Solvency II that would apply to the Company's businesses across the European Union. The implementation date of Solvency II has been delayed until January 1, 2016, although some aspects, including governance guidelines, own-risk assessments and regulatory reporting, will be phased in before the full implementation date. Under Solvency II, it is possible that the U.S. parent of a European Union subsidiary could be subject to certain Solvency II requirements if the regulator determines that the subsidiary's capital position is dependent on the parent company and the U.S. company is not already subject to regulations deemed "equivalent" to Solvency II. In addition, regulators in countries where the Company has operations are working with the International Association of Insurance Supervisors (IAIS) (and with the NAIC in the U.S.) to consider changes to insurance company supervision, including group supervision.

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In July 2013, the IAIS published a methodology for identifying "global systemically important insurers" (G-SIIs) and high level policy measures that will apply to the G-SIIs. The methodology and measures were endorsed by the Financial Stability Board (FSB) created by the G-20. Using the IAIS methodology, the FSB, working with national authorities and the IAIS, identified nine insurers that they designated as G-SIIs. The IAIS is working on the policy measures which include higher capital requirements and enhanced supervision. The Company was not named a G-SII by the FSB in the initial designation. The FSB will update the list annually, and it is possible that the methodologies could be amended or interpreted differently in the future and the Company could be named as a G-SII.

The IAIS also is in the process of developing the Common Framework for the Supervision of Internationally Active Insurance Groups (Comframe). The IAIS released a Consultation Draft in October 2013, which may lead to similar policy measures as those being developed for G-SIIs, including group supervision and an Insurance Capital Standard (i.e., global group capital requirement). The Company would be considered an Internationally Active Insurance Group under the current Consultation Draft. It is possible that Comframe could lead to enhanced supervision and higher capital standards on a global basis if the IAIS, the NAIC and the individual states adopt the proposed or similar provisions.

While it is not yet known how or if these actions will impact us, such regulation could result in increased costs of compliance, increased disclosure and less flexibility in our capital management, and could adversely impact our results of operations and limit our growth.

**Loss of or significant restrictions on the use of particular types of underwriting criteria, such as credit scoring, in the pricing and underwriting of our products could reduce our future profitability.** Our underwriting profitability depends in large part on our ability to competitively price our products at a level that will adequately compensate us for the risks assumed. As a result, risk selection and pricing through the application of actuarially sound and segmented underwriting criteria is critical. However, laws or regulations, or judicial or administrative findings, could significantly curtail the use of particular types of underwriting criteria. For example, we may use credit scoring as a factor in pricing decisions where allowed by state law. Some consumer groups and/or regulators have alleged that the use of credit scoring violates the law by discriminating against persons belonging to a protected class and are calling for the prohibition or restrictions on the use of credit scoring in underwriting and pricing. A variety of other underwriting criteria used in personal and commercial insurance have been and continue to be criticized by regulators, government agencies, consumer groups or individuals on similar or other grounds. Resulting regulatory actions or litigation could result in negative publicity and/or generate adverse rules or findings, such as curtailing the use of important underwriting criteria, each of which could adversely affect our future profitability.

**Acquisitions and integration of acquired businesses may result in operating difficulties and other unintended consequences.** From time to time we may investigate and pursue acquisition opportunities if we believe that such opportunities are consistent with our long-term objectives and that the potential rewards of an acquisition justify the risks. For example, in November 2013, we acquired Dominion and significantly expanded our Canadian operations. The process of integrating an acquired company or business can be complex and costly, however, and may create unforeseen operating difficulties and expenditures. For example, acquisitions may present significant risks, including:

the potential disruption of our ongoing business;

the ineffective integration of, or other difficulties with, underwriting, risk management, claims handling, information technology and actuarial practices;

uncertainties related to an acquiree's reserve estimates and its design and operation of internal controls over financial reporting;

the diversion of management time and resources to acquisition integration challenges;

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the loss of key employees;

unforeseen liabilities;

the cultural challenges associated with integrating employees; and

the impact on our financial position and/or credit ratings.

Acquired businesses may not perform as projected, any cost savings and other synergies anticipated from the acquisition may not materialize and costs associated with the integration may be greater than anticipated. Acquired businesses may not be successfully integrated, resulting in substantial costs or delays and adversely affecting our ability to compete. Accordingly, our results of operations might be materially and adversely affected.

**We could be adversely affected if our controls designed to ensure compliance with guidelines, policies and legal and regulatory standards are not effective.** Our business is highly dependent on our ability to engage on a daily basis in a large number of insurance underwriting, claim processing and investment activities, many of which are highly complex. These activities often are subject to internal guidelines and policies, as well as legal and regulatory standards. A control system, no matter how well designed and operated, can provide only reasonable assurance that the control system's objectives will be met. If our controls are not effective, it could lead to financial loss, unanticipated risk exposure (including underwriting, credit and investment risk) or damage to our reputation.

In addition, ineffective controls, including with respect to our recently acquired businesses, could lead to litigation or regulatory action. The volume of claims and amount of damages and penalties claimed in litigation and regulatory proceedings against various types of financial institutions have increased in recent years. Substantial legal liability or significant regulatory action against us could have a material adverse financial impact. See note 16 of notes to our consolidated financial statements for a discussion of certain legal proceedings in which we are involved.

**Our businesses may be adversely affected if we are unable to hire and retain qualified employees.** There is significant competition from within the property and casualty insurance industry and from businesses outside the industry for qualified employees, especially those in key positions and those possessing highly specialized underwriting knowledge. Our performance is largely dependent on the talents, efforts and proper conduct of highly-skilled individuals, including our senior executives, many of whom have decades of experience in the insurance industry. See "Item 10 Directors, Executive Officers and Corporate Governance" for more information relating to our executive officers. For many of our senior positions, we compete for talent not just with insurance or financial service companies, but with other large companies and other businesses. Our continued ability to compete effectively in our businesses and to expand into new business areas depends on our ability to attract new employees and to retain and motivate our existing employees. If we are not able to successfully attract, retain and motivate our employees, our business, financial results and reputation could be materially and adversely affected.

**Intellectual property is important to our business, and we may be unable to protect and enforce our own intellectual property or we may be subject to claims for infringing on the intellectual property of others.** Our success depends in part upon our ability to protect our proprietary trademarks, technology and other intellectual property. See "Item 1 Other Information Intellectual Property." We may not, however, be able to protect our intellectual property from unauthorized use and disclosure by others. For example, the laws of intellectual property may not prevent our competitors from independently developing trademarks, products and services that are similar to ours. Moreover, the agreements we execute to protect our intellectual property rights may be breached, and we may not have adequate remedies in response. Our attempts to patent or register our intellectual property rights in the U.S. and worldwide may not succeed initially or may later be challenged by third parties.

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Further, the laws of certain countries outside the United States may not adequately protect our intellectual property rights. We may incur significant costs in our efforts to protect and enforce our intellectual property, including the initiation of expensive and protracted litigation, and we may not prevail. Any inability to enforce our intellectual property rights could have a material adverse effect on our business and our ability to compete.

We may be subject to claims by third parties from time to time that our products, services and technologies infringe on their intellectual property rights. In recent years, certain entities have acquired patents in order to allege claims of infringement against companies, including in some cases us. Any intellectual property infringement claims brought against us could cause us to spend significant time and money to defend ourselves, regardless of the merits of the claims. If we are found to infringe on any third-party intellectual property rights, it could result in reputational harm, payment of significant monetary damages, payment of license fees (if licenses are even available to us, on reasonable terms or otherwise) and/or substantial time and expense to redesign our products, services or technologies to avoid the infringement. In addition, we use third-party software in some of our products, services and technologies. If any of our software vendors or licensors are faced with infringement claims, we may lose our ability to use such software until the dispute is resolved. If we cannot successfully redesign an infringing product, service or technology (or procure a substitute version), this could have a material adverse effect on our business and our ability to compete.

**Changes to existing accounting standards may adversely impact our reported results.** As a U.S.-based SEC registrant, we are currently required to prepare our financial statements in accordance with U.S. Generally Accepted Accounting Principles (US GAAP), as promulgated by the Financial Accounting Standards Board (FASB), subject to the accounting-related rules and interpretations of the Securities and Exchange Commission (SEC). During the last several years, the SEC has been evaluating whether, when and how International Financial Reporting Standards (IFRS) should be incorporated into the U.S. financial reporting system, including for companies such as us. The FASB and the International Accounting Standards Board (IASB) have also embarked on a long-term project to converge US GAAP and IFRS. In June 2012, the FASB issued a statement that indicated that based on the nature and totality of differences between the FASB's and IASB's views, it is not likely that the two Boards will achieve convergence on their joint project on the accounting for insurance contracts. The FASB further noted that the FASB and IASB have very different perspectives on the project. In June 2013, each Board issued for comment exposure drafts on the accounting for insurance contracts that have significant differences from the other board's draft as well as from current US GAAP. Both exposure drafts propose changes that, if ultimately adopted, could significantly impact the accounting by insurers, including the Company, for premiums and unearned premium reserves, the liability for claims and claims adjustment expenses, reinsurance, and deferred acquisition costs. The Boards are reviewing the comments received on the exposure drafts and are expected to begin re-deliberations in the first quarter of 2014. It is currently unclear what changes, if any, may be made to the accounting for insurance contracts under US GAAP as a result of this project, and we are not able to predict whether we will choose to, or be required to, adopt IFRS or how the adoption of IFRS (or the convergence of US GAAP and IFRS, including the project on the accounting for insurance contracts) may impact our financial statements in the future. Changes in accounting standards, particularly those that specifically apply to insurance company operations, may impact the content and presentation of our reported financial results and could cause increased volatility in reported earnings, resulting in other adverse impacts on the Company's ratings and cost of capital, and decrease the understandability of our financial results as well as the comparability of our reported results with other insurers.

**Changes in U.S. tax laws or in the tax laws of other jurisdictions in which we operate could adversely impact us.** Tax laws may change in ways that adversely impact us. For example, federal tax legislation could be enacted to reduce the existing statutory U.S. federal corporate income tax rate from 35%, which would, accordingly, reduce any U.S. deferred tax asset. The amount of any net

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deferred tax asset is volatile and significantly impacted by changes in unrealized investment gains and losses. The effect of a reduction in a tax rate on net deferred tax assets is required to be recognized, in full, as a reduction of income from continuing operations in the period when enacted and, along with other changes in the tax rules that may increase the Company's actual tax expense, could materially and adversely affect our results of operations.

Our investment portfolio has benefited from tax exemptions and certain other tax laws, including, but not limited to, those governing dividends-received deductions and tax credits (such as foreign tax credits). Federal and/or state tax legislation could be enacted in connection with deficit reduction or various types of fundamental tax reform that would lessen or eliminate some or all of the tax advantages currently benefiting us and therefore could materially and adversely impact our results of operations. In addition, such legislation could adversely affect the value of our investment portfolio, particularly changes to the taxation of interest from municipal bonds (which comprise 49% of our investment portfolio as of December 31, 2013) could materially and adversely impact the value of those bonds.

Other tax law changes could adversely impact us. The size of the federal deficit, as well as the budget constraints faced by many states and localities, increases the likelihood that Congress and state and local governments will raise revenue by enacting legislation increasing the taxes paid by individuals and corporations.

**Item 1B. UNRESOLVED STAFF COMMENTS**

NONE.

**Item 2. PROPERTIES**

The Company leases its principal executive offices in New York, New York, as well as 201 field and claim offices totaling approximately 4.7 million square feet throughout the United States under leases or subleases with third parties. The Company also leases offices in Canada, the United Kingdom, India, China and the Republic of Ireland that house operations (primarily for the Financial, Professional & International Insurance segment) in those locations. The Company owns six buildings in Hartford, Connecticut, consisting of approximately 1.8 million square feet of office space. The Company also owns two office buildings in St. Paul, Minnesota, which are adjacent to one another and consist of approximately 1.1 million square feet of office space. The Company also owns a building located in Norcross, Georgia, and land outside of Omaha, Nebraska where an additional building is under construction. The Company owns a building in London, England, which houses a portion of its Financial, Professional & International Insurance segment's operations in the United Kingdom.

The Company, through its subsidiaries, owns an investment portfolio of income-producing properties and real estate funds. Included in this portfolio are four office buildings in which the Company holds a 50% ownership interest located in New York, New York, which collectively accounted for approximately 12% of the carrying value of the property portfolio at December 31, 2013.

In the opinion of the Company's management, the Company's properties are adequate and suitable for its business as presently conducted and are adequately maintained.

**Item 3. LEGAL PROCEEDINGS**

The information required with respect to this item can be found under "Contingencies" in note 16 of notes to the Company's consolidated financial statements in this annual report and is incorporated by reference into this Item 3.

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**Item 4. MINE SAFETY DISCLOSURES**

NONE.

**EXECUTIVE OFFICERS OF THE REGISTRANT**

Information about the Company's executive officers is incorporated by reference from Part III, Item 10 of this annual report.

Table of Contents**PART II****Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

The Company's common stock is traded on the New York Stock Exchange under the symbol "TRV." The number of holders of record, including individual owners, of the Company's common stock was 53,194 as of February 7, 2014. This is not the actual number of beneficial owners of the Company's common stock, as shares are held in "street name" by brokers and others on behalf of individual owners. The following table sets forth the high and low closing sales prices of the Company's common stock for each quarter during the last two fiscal years and the amount of cash dividends declared per share.

	High	Low	Cash Dividend Declared
<b>2013</b>			
First Quarter	\$ 84.19	\$ 72.86	\$ 0.46
Second Quarter	87.90	77.85	0.50
Third Quarter	86.90	79.42	0.50
Fourth Quarter	90.99	82.35	0.50
<b>2012</b>			
First Quarter	\$ 61.59	\$ 56.87	\$ 0.41
Second Quarter	64.77	57.75	0.46
Third Quarter	68.61	60.89	0.46
Fourth Quarter	74.33	68.07	0.46

The Company paid cash dividends per share of \$1.96 in 2013 and \$1.79 in 2012. Future dividend decisions will be based on, and affected by, a number of factors, including the operating results and financial requirements of the Company and the impact of dividend restrictions. For information on dividends, as well as restrictions on the ability of certain of the Company's subsidiaries to transfer funds to the Company in the form of cash dividends or otherwise, see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources." Dividends will be paid by the Company only if declared by its board of directors out of funds legally available, and subject to any other restrictions that may be applicable to the Company.



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**SHAREHOLDER RETURN PERFORMANCE GRAPH**

The following graph shows a five-year comparison of the cumulative total return to shareholders for the Company's common stock and the common stock of companies included in the S&P 500 Index and the S&P 500 Property & Casualty Insurance Index, which the Company believes is the most appropriate comparative index.

**COMPARISON OF CUMULATIVE FIVE YEAR TOTAL RETURN TO SHAREHOLDERS(1)**

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- (1) The cumulative return to shareholders is a concept used to compare the performance of a company's stock over time and is the ratio of the net stock price change plus the cumulative amount of dividends over the specified time period (assuming dividend reinvestment), to the stock price at the beginning of the time period.
- (2) Assumes \$100 invested in common shares of The Travelers Companies, Inc. on December 31, 2008.
- (3) Companies in the S&P 500 Property-Casualty Index as of December 31, 2013 were the following: The Travelers Companies, Inc., The Chubb Corporation, Cincinnati Financial Corporation, Progressive Corporation, Allstate Corporation, XL Group, plc., and ACE Ltd.

Returns of each of the companies included in this index have been weighted according to their respective market capitalizations.



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The table below sets forth information regarding repurchases by the Company of its common stock during the periods indicated.

<b>Period Beginning</b>	<b>Period Ending</b>	<b>Total number of shares purchased</b>	<b>Average price paid per share</b>	<b>Total number of shares purchased as part of publicly announced plans or programs</b>	<b>Approximate dollar value of shares that may yet be purchased under the plans or programs (in millions)</b>
Oct. 1, 2013	Oct. 31, 2013	1,529,140	\$ 86.98	1,528,341	\$ 5,626
Nov. 1, 2013	Nov. 30, 2013	5,129,458	88.40	5,127,287	5,173
Dec. 1, 2013	Dec. 31, 2013	4,701,332	88.13	4,695,930	4,759
<b>Total</b>		11,359,930	88.09	11,351,558	4,759

The Company's board of directors has approved common share repurchase authorizations under which repurchases may be made from time to time in the open market, pursuant to pre-set trading plans meeting the requirements of Rule 10b5-1 under the Securities Exchange Act of 1934, in private transactions or otherwise. The authorizations do not have a stated expiration date. The timing and actual number of shares to be repurchased in the future will depend on a variety of factors, including the Company's financial position, earnings, share price, catastrophe losses, maintaining capital levels commensurate with the Company's desired ratings from independent rating agencies, funding of the Company's qualified pension plan, capital requirements of the Company's operating subsidiaries, legal requirements, regulatory constraints, other investment opportunities (including mergers and acquisitions and related financings), market conditions and other factors. In October 2013, the board of directors approved a share repurchase authorization that added an additional \$5.0 billion of repurchase capacity.

The Company acquired 8,372 shares during the three months ended December 31, 2013 that were not part of the publicly announced share repurchase authorization. These shares consisted of shares retained to cover payroll withholding taxes in connection with the vesting of restricted stock awards and shares used by employees to cover the exercise price of certain stock options that were exercised.

Information relating to compensation plans under which the Company's equity securities are authorized for issuance is set forth in Part III Item 12 of this Report.

Table of Contents**Item 6. SELECTED FINANCIAL DATA**

	At and for the year ended December 31,				
	2013	2012	2011	2010	2009
	(in millions, except per share amounts)				
Total revenues	\$ 26,191	\$ 25,740	\$ 25,446	\$ 25,112	\$ 24,680
Net income	\$ 3,673	\$ 2,473	\$ 1,426	\$ 3,216	\$ 3,622
Total investments	\$ 73,160	\$ 73,838	\$ 72,701	\$ 72,722	\$ 74,965
Total assets	103,812	104,938	104,575	105,631	110,013
Claims and claim adjustment expense reserves	50,895	50,922	51,392	51,581	53,580
Total long-term debt	6,246	5,750	6,255	6,502	6,154
Total liabilities	79,016	79,533	80,098	80,156	82,598
Total shareholders' equity	24,796	25,405	24,477	25,475	27,415
<b>Net income per share:</b>					
Basic	\$ 9.84	\$ 6.35	\$ 3.40	\$ 6.69	\$ 6.38
Diluted	\$ 9.74	\$ 6.30	\$ 3.36	\$ 6.62	\$ 6.33
Year-end common shares outstanding	353.5	377.4	392.8	434.6	520.3
<b>Per common share amounts:</b>					
Cash dividends	\$ 1.96	\$ 1.79	\$ 1.59	\$ 1.41	\$ 1.23
Book value	\$ 70.15	\$ 67.31	\$ 62.32	\$ 58.47	\$ 52.54

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**Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following is a discussion and analysis of the Company's financial condition and results of operations.

On November 1, 2013, the Company acquired all of the issued and outstanding shares of Dominion for an aggregate purchase price of approximately \$1.034 billion. The results of operations of the acquired business are reported in the Company's Financial, Professional & International Insurance segment from the closing date.

**FINANCIAL HIGHLIGHTS**

**2013 Consolidated Results of Operations**

Net income of \$3.67 billion, or \$9.84 per share basic and \$9.74 per share diluted

Net earned premiums of \$22.64 billion

Catastrophe losses of \$591 million (\$387 million after-tax)

Net favorable prior year reserve development of \$840 million (\$552 million after-tax)

GAAP combined ratio of 89.8%

Net investment income of \$2.72 billion (\$2.19 billion after-tax)

Benefit of \$91 million (\$59 million after-tax) from settlement of legal matter

Benefit of \$63 million from resolution of prior year tax matters

Operating cash flows of \$3.82 billion

Net realized investment gains of \$166 million (\$106 million after-tax)

**2013 Consolidated Financial Condition**

Total investments of \$73.16 billion; fixed maturities and short-term securities comprise 93% of total investments

Total assets of \$103.81 billion

Total debt of \$6.35 billion, resulting in a debt-to-total capital ratio of 20.4% (21.3% excluding net unrealized investment gains, net of tax)

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Repurchased 28.4 million common shares for a total cost of \$2.40 billion under share repurchase authorization

Share repurchase authorization increased by \$5.0 billion in 2013

Shareholders' equity of \$24.80 billion

Book value per common share of \$70.15

Holding company liquidity of \$1.59 billion

Table of Contents**CONSOLIDATED OVERVIEW****Consolidated Results of Operations**

(for the year ended December 31, in millions except per share amounts)	2013	2012	2011
<b>Revenues</b>			
Premiums	\$ 22,637	\$ 22,357	\$ 22,090
Net investment income	2,716	2,889	2,879
Fee income	395	323	296
Net realized investment gains	166	51	55
Other revenues	277	120	126
<b>Total revenues</b>	<b>26,191</b>	<b>25,740</b>	<b>25,446</b>
<b>Claims and expenses</b>			
Claims and claim adjustment expenses	13,307	14,676	16,276
Amortization of deferred acquisition costs	3,821	3,910	3,876
General and administrative expenses	3,757	3,610	3,556
Interest expense	361	378	386
<b>Total claims and expenses</b>	<b>21,246</b>	<b>22,574</b>	<b>24,094</b>
<b>Income before income taxes</b>	<b>4,945</b>	<b>3,166</b>	<b>1,352</b>
Income tax expense (benefit)	1,272	693	(74)
<b>Net income</b>	<b>\$ 3,673</b>	<b>\$ 2,473</b>	<b>\$ 1,426</b>
<b>Net income per share</b>			
Basic	\$ 9.84	\$ 6.35	\$ 3.40
Diluted	\$ 9.74	\$ 6.30	\$ 3.36
<b>GAAP combined ratio</b>			
Loss and loss adjustment expense ratio	57.9%	64.9%	72.9%
Underwriting expense ratio	31.9	32.2	32.2
<b>GAAP combined ratio</b>	<b>89.8%</b>	<b>97.1%</b>	<b>105.1%</b>

<b>Incremental impact of direct to consumer initiative on GAAP combined ratio</b>	<b>0.5%</b>	0.8%	0.9%
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The following discussions of the Company's net income and segment operating income (loss) are presented on an after-tax basis. Discussions of the components of net income and segment operating income are presented on a pretax basis, unless otherwise noted. Discussions of earnings per common share are presented on a diluted basis.

*Overview*

Diluted net income per share of \$9.74 in 2013 increased by 55% over diluted net income per share of \$6.30 in 2012. Net income of \$3.67 billion in 2013 increased by 49% over net income of \$2.47 billion in 2012. The higher rate of increase in diluted net income per share reflected the impact of share repurchases in recent periods. The increase in net income primarily reflected the pretax impacts of (i) lower catastrophe losses, (ii) higher underwriting margins excluding catastrophe losses and prior year reserve development ("underlying underwriting margins"), (iii) an increase in net realized investment gains and (iv) a gain from the settlement of a legal proceeding, partially offset by (v) lower net investment income and (vi) lower net favorable prior year reserve development. The improvement in underlying underwriting margins primarily resulted from the impact of earned pricing that exceeded loss cost trends in each of the Company's business segments. Partially offsetting this net pretax increase



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in income was the related tax expense. Additionally, net income in 2013 benefited from a reduction in income tax expense resulting from the resolution of prior year tax matters. The effective tax rate in 2013 was higher than in 2012. This resulted from interest on municipal bonds, which is effectively taxed at a rate that is lower than the corporate tax rate of 35%, comprising a lower percentage of pretax income, partially offset by the resolution of prior year tax matters discussed above. Catastrophe losses in 2013 were \$591 million, compared with \$1.86 billion in 2012. Net favorable prior year reserve development in 2013 was \$840 million, compared with \$940 million in 2012.

Diluted net income per share of \$6.30 in 2012 increased by 88% over diluted net income per share of \$3.36 in 2011. Net income of \$2.47 billion in 2012 increased by 73% over net income of \$1.43 billion in 2011. The higher rate of increase in diluted net income per share reflected the impact of share repurchases in recent periods. The increase in net income primarily reflected the pretax impact of (i) higher underlying underwriting margins, (ii) a decline in catastrophe losses and (iii) higher net favorable prior year reserve development. The improvement in underlying underwriting margins primarily resulted from lower non-catastrophe weather-related losses in the Business Insurance and Personal Insurance segments and the impact of earned pricing that exceeded loss cost trends in the Business Insurance and Financial, Professional & International Insurance segments. Partially offsetting this pretax increase was the related tax expense. Additionally, net income in 2011 benefited from a reduction in income tax expense resulting from the resolution of various prior year tax matters. The effective tax rate in 2012 was higher than in 2011. This resulted from interest on municipal bonds, which is effectively taxed at a rate that is lower than the corporate tax rate of 35%, comprising a lower percentage of pretax income, and the resolution of prior year tax matters in 2011 discussed above. Catastrophe losses in 2012 were \$1.86 billion, compared with \$2.56 billion in 2011. Net favorable prior year reserve development in 2012 was \$940 million, compared with \$715 million in 2011.

**Revenues**

*Earned Premiums*

Earned premiums in 2013 were \$22.64 billion, \$280 million or 1% higher than in 2012. In the Business Insurance segment, earned premiums in 2013 increased by 3% over 2012. In the Financial, Professional & International Insurance segment, earned premiums in 2013 increased by 6% over 2012. In the Personal Insurance segment, earned premiums in 2013 decreased by 4% from 2012.

Earned premiums in 2012 were \$22.36 billion, \$267 million or 1% higher than in 2011. In the Business Insurance segment, earned premiums in 2012 increased by 3% over 2011. In the Financial, Professional & International Insurance segment, earned premiums in 2012 decreased by 4% from 2011. In the Personal Insurance segment, earned premiums in 2012 increased by less than 1% over 2011.

Factors contributing to the changes in earned premiums in each segment in 2013 and 2012 compared with the respective prior year are discussed in more detail in the segment discussions that follow.

Table of Contents*Net Investment Income*

The following table sets forth information regarding the Company's investments.

<b>(for the year ended December 31, in millions)</b>	<b>2013</b>	<b>2012</b>	<b>2011</b>
Average investments(1)	\$ 70,697	\$ 69,863	\$ 70,471
Pretax net investment income	2,716	2,889	2,879
After-tax net investment income	2,186	2,316	2,330
Average pretax yield(2)	3.8%	4.1%	4.1%
Average after-tax yield(2)	3.1%	3.3%	3.3%

(1) Excludes net unrealized investment gains and losses, net of tax, and reflects cash, receivables for investment sales, payables on investment purchases and accrued investment income.

(2) Excludes net realized and unrealized investment gains and losses.

Net investment income in 2013 was \$2.72 billion, \$173 million or 6% lower than in 2012. Net investment income from fixed maturity investments in 2013 was \$2.31 billion in 2013, a decrease of \$129 million from 2012, primarily resulting from lower long-term reinvestment yields available in the market. Net investment income from non-fixed maturity investments was \$432 million in 2013, a decrease of \$44 million from 2012, primarily reflecting lower results from the Company's real estate partnership investments.

Net investment income in 2012 was \$2.89 billion, \$10 million or less than 1% higher than in 2011. Net investment income from fixed maturity investments was \$2.44 billion in 2012, a decrease of \$104 million from 2011, primarily resulting from lower long-term reinvestment yields available in the market. Net investment income generated by non-fixed maturity investments was \$476 million in 2012, an increase of \$121 million over 2011, primarily driven by improved results from the Company's real estate partnerships and hedge fund investments. On an after-tax basis, net investment income in 2012 was \$14 million, or less than 1% lower than in 2011, reflecting a higher proportion of taxable net investment income in 2012 compared with 2011.

*Fee Income*

The National Accounts market in the Business Insurance segment is the primary source of the Company's fee-based business. The \$72 million and \$27 million increases in fee income in 2013 and 2012, respectively, compared with the respective prior years are described in the Business Insurance segment discussion that follows.

*Net Realized Investment Gains*

The following table sets forth information regarding the Company's net pretax realized investment gains.

<b>(for the year ended December 31, in millions)</b>	<b>2013</b>	<b>2012</b>	<b>2011</b>
<b>Net Realized Investment Gains</b>			
Other-than-temporary impairment losses	(15)	(15)	(25)
Other net realized investment gains	181	66	80
<b>Net realized investment gains</b>	<b>\$ 166</b>	<b>\$ 51</b>	<b>\$ 55</b>

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*Other Net Realized Investment Gains*

Other net realized gains in 2013 of \$181 million were primarily driven by \$115 million of net realized gains associated with U.S. Treasury futures contracts (which require daily mark-to-market settlement and are used to shorten the duration of the Company's fixed maturity investment portfolio). The remaining \$66 million of other net realized investment gains in 2013 were primarily driven by \$41 million of net realized investment gains related to fixed maturity investments, \$15 million of net realized investment gains related to equity securities and \$10 million of net realized investment gains related to other investments.

Other net realized investment gains in 2012 of \$66 million were primarily driven by \$61 million of net realized investment gains related to fixed maturity investments, \$19 million of net realized investment gains related to real estate and \$8 million of net realized investment gains related to equity securities. These net realized investment gains were partially offset by \$14 million of net realized investment losses associated with U.S. Treasury futures contracts and \$8 million of net realized investment losses related to other investments.

Other net realized investment gains in 2011 of \$80 million were primarily driven by \$52 million of net realized investment gains related to fixed maturity investments, \$46 million of net realized investment gains related to equity securities and \$41 million of net realized investment gains related to other investments, partially offset by net realized investment losses of \$62 million associated with U.S. Treasury futures contracts.

*Other Revenues*

Other revenues in 2013 included a \$91 million gain from the settlement of a legal proceeding, which is discussed in more detail in note 16 of notes to the consolidated financial statements. Other revenues in 2013 also included a \$20 million gain from the sale of renewal rights related to the Company's National Flood Insurance Program business. The remainder of other revenues in all years presented primarily consisted of installment premium charges.

**Claims and Expenses**

*Claims and Claim Adjustment Expenses*

Claims and claim adjustment expenses in 2013 were \$13.31 billion, \$1.37 billion or 9% lower than in 2012, primarily reflecting (i) a decline in catastrophe losses and (ii) the impact of lower volumes of insured exposures (excluding the impact of the acquisition of Dominion), partially offset by (iii) the impact of loss cost trends, (iv) the impact of the acquisition of Dominion and (v) lower net favorable prior year reserve development. Catastrophe losses in 2013 and 2012 were \$591 million and \$1.86 billion, respectively. Catastrophe losses in 2013 resulted from multiple tornado, wind and hail storms in several regions of the United States, as well as floods in Alberta, Canada and Storm Xaver in the United Kingdom that impacted the Financial, Professional & International Insurance segment. Catastrophe losses in 2012 primarily resulted from Storm Sandy, as well as multiple tornado, wind and hail storms in several regions of the United States. Net favorable prior year reserve development in 2013 and 2012 was \$840 million and \$940 million, respectively. Net favorable prior year reserve development in 2013 was reduced by a \$42 million charge that was precipitated by legislation in New York enacted during the first quarter of 2013 related to the New York Fund for Reopened Cases for workers' compensation. Factors contributing to net favorable prior year reserve development in each segment are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.

Claims and claim adjustment expenses in 2012 were \$14.68 billion, \$1.60 billion or 10% lower than in 2011. The decrease primarily reflected (i) a decline in catastrophe losses, (ii) lower levels of

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non-catastrophe weather-related losses and (iii) higher net favorable prior year reserve development, partially offset by (iv) the impact of loss cost trends. Catastrophe losses in 2012 and 2011 were \$1.86 billion and \$2.56 billion, respectively. Catastrophe losses in 2011 primarily resulted from Hurricane Irene and Tropical Storm Lee, multiple tornadoes and hail storms in the Midwest and Southeast regions of the United States and severe winter storms throughout the United States. Catastrophe losses in 2011 also included losses from floods in Thailand and an earthquake in Japan that impacted the Financial, Professional & International Insurance segment. Net favorable prior year reserve development in 2012 and 2011 was \$940 million and \$715 million, respectively. Factors contributing to net favorable prior year reserve development in each segment are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.

*Significant Catastrophe Losses*

The Company defines a "catastrophe" as an event that:

is designated a catastrophe by internationally recognized organizations that track and report on insured losses from catastrophic events, such as Property Claim Services (PCS) for events in the United States and Canada; and

the Company's estimates of its ultimate losses before reinsurance and taxes exceed a pre-established dollar threshold.

The Company's threshold for disclosing catastrophes is determined at its reportable segment level, or at a combination thereof, and ranged from approximately \$17 million to \$30 million of losses before reinsurance and taxes.

The following table presents for significant catastrophes the amount of losses recorded in each of the years ended December 31, 2013, 2012, and 2011, and the amount of related net unfavorable (favorable) prior year reserve development recognized in subsequent years. For purposes of the table, a significant catastrophe is an event for which the Company estimates its ultimate losses will be \$100 million or more after reinsurance and before taxes.

(for the year ended December 31, in millions, pretax and net of reinsurance)	2013	2012	2011
<b>2011</b>			
PCS Serial Number:			
35 Severe winter storms	\$ (6)	\$ 1	\$ 100
42 Severe thunderstorms and tornadoes	(2)	(5)	130
43 Severe thunderstorms and tornadoes	(1)	2	149
44 Severe thunderstorms and tornadoes	(9)	(10)	121
46 Severe thunderstorms and tornadoes (including Tuscaloosa, AL)	2	(76)	648
48 Severe thunderstorms and tornadoes (including Joplin, MO)	(14)	(24)	430
59 Hurricane Irene	(17)	(47)	375
61 Tropical Storm Lee	(21)	(7)	119
<b>2012</b>			
PCS Serial Number:			
67 Severe wind and hail storms	(2)	140	
74 Severe wind and hail storms	(20)	171	
76 Severe wind and hail storms	(10)	148	
83 Severe wind storms	2	136	
90 Storm Sandy	(52)	1,024	
<b>2013</b>			
PCS Serial Number:			
93 Severe wind and hail storms	114		
15 Severe wind and hail storms	128		

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*Amortization of Deferred Acquisition Costs*

Amortization of deferred acquisition costs in 2013 was \$3.82 billion, \$89 million or 2% lower than in 2012. Amortization of deferred acquisition costs in 2012 was \$3.91 billion, \$34 million or 1% higher than in 2011. Amortization of deferred acquisition costs is discussed in more detail in the segment discussions that follow.

*General and Administrative Expenses*

General and administrative expenses in 2013 were \$3.76 billion, \$147 million or 4% higher than in 2012. General and administrative expenses in 2012 were \$3.61 billion, \$54 million or 2% higher than in 2011. General and administrative expenses are discussed in more detail in the segment discussions that follow.

*Interest Expense*

Interest expense in 2013, 2012 and 2011 was \$361 million, \$378 million and \$386 million, respectively. The declines both in 2013 and 2012 compared with the respective prior years primarily reflected lower average levels of debt outstanding.

*Income Tax Expense (Benefit)*

Income tax expense in 2013 was \$1.27 billion, \$579 million or 84% higher than in 2012, primarily reflecting the impact of a \$1.66 billion increase in underwriting margins (including the impacts of decreases in catastrophe losses and net favorable prior year reserve development), partially offset by the impact of lower net investment income and a reduction in income tax expense of \$63 million resulting from the resolution of prior year tax matters. Income tax expense in 2012 was \$693 million, compared to an income tax benefit of \$74 million in 2011. The increase in income tax expense of \$767 million in 2012 from 2011 primarily reflected the \$1.77 billion increase in underwriting margins in 2012 (including the impacts of a decrease in catastrophe losses and an increase in net favorable prior year reserve development) over 2011 and the \$121 million increase in net investment income from non-fixed maturity investments over 2011, as well as the reduction in income tax expense of \$104 million in 2011 resulting from the resolution of prior year tax matters.

The Company's effective tax rate was 26%, 22% and (5)% in 2013, 2012 and 2011, respectively. The effective tax rates in all years were lower than the statutory rate of 35% primarily due to the impact of tax-exempt investment income on the calculation of the Company's income tax provision. The effective tax rate of (5)% in 2011 also reflected the impact of the significant underwriting loss that primarily resulted from catastrophe losses. In addition, the effective tax rates for 2013 and 2011 were reduced by the impact of the resolution of prior year tax matters.

**GAAP Combined Ratios**

The consolidated GAAP combined ratio of 89.8% in 2013 was 7.3 points lower than the consolidated GAAP combined ratio of 97.1% in 2012.

The consolidated loss and loss adjustment expense ratio of 57.9% in 2013 was 7.0 points lower than the consolidated loss and loss adjustment expense ratio of 64.9% in 2012. Catastrophe losses accounted for 2.6 points and 8.3 points of the 2013 and 2012 loss and loss adjustment expense ratios, respectively. The 2013 and 2012 loss and loss adjustment expense ratios included 3.7 points and 4.2 points of benefit from net favorable prior year reserve development, respectively. The consolidated 2013 loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development ("underlying loss and loss adjustment expense ratio") was 1.8 points lower than the 2012

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ratio on the same basis, primarily reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above.

The consolidated underwriting expense ratio of 31.9% in 2013 was lower than the consolidated underwriting expense ratio of 32.2% in 2012, primarily reflecting the impact of growth in earned premiums in 2013.

The consolidated GAAP combined ratio of 97.1% in 2012 was 8.0 points lower than the consolidated GAAP combined ratio of 105.1% in 2011.

The consolidated loss and loss adjustment expense ratio of 64.9% in 2012 was 8.0 points lower than the consolidated loss and loss adjustment expense ratio of 72.9% in 2011. Catastrophe losses accounted for 8.3 points and 11.6 points of the 2012 and 2011 loss and loss adjustment expense ratios, respectively. The 2012 and 2011 loss and loss adjustment expense ratios included 4.2 points and 3.2 points of benefit from net favorable prior year reserve development, respectively. The consolidated 2012 loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development ("underlying loss and loss adjustment expense ratio") was 3.7 points lower than the 2011 ratio on the same basis, primarily reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above.

The consolidated underwriting expense ratio of 32.2% in 2012 was level with the consolidated underwriting expense ratio of 32.2% in 2011.

**Written Premiums**

Consolidated gross and net written premiums were as follows:

(for the year ended December 31, in millions)	Gross Written Premiums		
	2013	2012	2011
Business Insurance	\$ 13,577	\$ 13,111	\$ 12,418
Financial, Professional & International Insurance	3,546	3,275	3,408
Personal Insurance	7,534	7,923	8,061
<b>Total</b>	<b>\$ 24,657</b>	<b>\$ 24,309</b>	<b>\$ 23,887</b>

(for the year ended December 31, in millions)	Net Written Premiums		
	2013	2012	2011
Business Insurance	\$ 12,233	\$ 11,872	\$ 11,340
Financial, Professional & International Insurance	3,309	2,981	3,102
Personal Insurance	7,225	7,594	7,745
<b>Total</b>	<b>\$ 22,767</b>	<b>\$ 22,447</b>	<b>\$ 22,187</b>

Gross and net written premiums in 2013 both increased by 1% over 2012. Gross and net written premiums in 2012 increased by 2% and 1%, respectively, over 2011. Factors contributing to the changes in gross and net written premiums in each segment in 2013 and 2012 as compared with the respective prior year are discussed in more detail in the segment discussions that follow.

Table of Contents**RESULTS OF OPERATIONS BY SEGMENT****Business Insurance**

Results of the Company's Business Insurance segment were as follows:

(for the year ended December 31, in millions)	2013	2012	2011
<b>Revenues:</b>			
Earned premiums	\$ 12,084	\$ 11,691	\$ 11,327
Net investment income	1,975	2,090	2,041
Fee income	393	322	295
Other revenues	158	40	31
<b>Total revenues</b>	<b>\$ 14,610</b>	<b>\$ 14,143</b>	<b>\$ 13,694</b>
<b>Total claims and expenses</b>	<b>\$ 11,541</b>	<b>\$ 11,761</b>	<b>\$ 12,206</b>
<b>Operating income</b>	<b>\$ 2,329</b>	<b>\$ 1,843</b>	<b>\$ 1,354</b>
Loss and loss adjustment expense ratio	61.2%	65.9%	73.1%
Underwriting expense ratio	30.7	31.5	31.6
<b>GAAP combined ratio</b>	<b>91.9%</b>	<b>97.4%</b>	<b>104.7%</b>

*Overview*

Operating income in 2013 was \$2.33 billion, \$486 million or 26% higher than operating income of \$1.84 billion in 2012. The increase in operating income primarily reflected the pretax impact of (i) lower catastrophe losses, (ii) higher underlying underwriting margins and (iii) the settlement of a legal matter, partially offset by (iv) lower net favorable prior year reserve development and (v) lower net investment income. The improvement in underlying underwriting margins primarily resulted from the impact of earned pricing that exceeded loss cost trends. Partially offsetting this net pretax increase in operating income was the related tax expense. Additionally, operating income in 2013 benefited from a reduction in income tax expense resulting from the resolution of prior year tax matters. The effective tax rate in 2013 was higher than in 2012. This resulted from the impact of interest on municipal bonds, which is effectively taxed at a rate that is lower than the corporate tax rate of 35%, comprising a lower percentage of pretax income, partially offset by the resolution of prior year tax matters described above. Catastrophe losses in 2013 were \$285 million, compared with \$794 million in 2012. Net favorable prior year reserve development in 2013 was \$325 million, compared with \$467 million in 2012. Net favorable prior year reserve development in 2013 was reduced by a \$42 million charge that was precipitated by legislation in New York as described in the consolidated "Claims and Claim Adjustment Expenses" section above.

Operating income in 2012 was \$1.84 billion, \$489 million or 36% higher than operating income of \$1.35 billion in 2011. The increase in operating income primarily reflected the pretax impact of (i) higher underlying underwriting margins, (ii) a decline in catastrophe losses, (iii) an

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increase in net favorable prior year reserve development and (iv) an increase in net investment income. The improvement in underlying underwriting margins primarily resulted from the impact of earned pricing that exceeded loss cost trends, lower non-catastrophe weather-related losses and higher business volume. Partially offsetting this pretax increase was the related tax expense. Additionally, net income in 2011 benefited from a reduction in income tax expense resulting from the resolution of various prior year tax matters. The effective tax rate in 2012 was higher than in 2011. This resulted from interest on municipal bonds, which is effectively taxed at a rate that is lower than the corporate tax rate of 35%, comprising a lower percentage of pretax income, and the resolution of prior year tax matters discussed



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above. Catastrophe losses in 2012 were \$794 million, compared with \$1.02 billion in 2011. Net favorable prior year reserve development in 2012 was \$467 million, compared with \$245 million in 2011.

**Revenues**

*Earned Premiums*

Earned premiums in 2013 were \$12.08 billion, \$393 million or 3% higher than in 2012. Earned premiums in 2012 were \$11.69 billion, \$364 million or 3% higher than in 2011. The increases in both years primarily reflected the impact of increases in net written premiums over the preceding twelve months.

*Net Investment Income*

Net investment income in 2013 was \$1.98 billion, \$115 million or 6% lower than in 2012. Net investment income in 2012 was \$2.09 billion, \$49 million or 2% higher than in 2011. Refer to the "Net Investment Income" section of the "Consolidated Results of Operations" discussion herein for a description of the factors contributing to the changes in the Company's consolidated net investment income in 2013 and 2012 compared with the respective prior years. In addition, refer to note 2 of notes to the Company's consolidated financial statements herein for a discussion of the Company's net investment income allocation methodology.

*Fee Income*

National Accounts is the primary source of fee income due to its service businesses, which include claim and loss prevention services to large companies that choose to self-insure a portion of their insurance risks, as well as claims and policy management services to workers' compensation residual market pools. Fee income in 2013 increased by \$71 million or 22% over 2012. Fee income in 2012 increased by \$27 million or 9% over 2011. The increases in both years primarily reflected higher serviced premium volume in workers' compensation residual market pools and higher claim volume in the large deductible business.

*Other Revenues*

Other revenues in 2013 included a \$91 million gain from the settlement of a legal proceeding, which is discussed in more detail in note 16 of notes to the consolidated financial statements.

**Claims and Expenses**

*Claims and Claim Adjustment Expenses*

Claims and claim adjustment expenses in 2013 were \$7.58 billion, \$281 million or 4% lower than in 2012, primarily reflecting (i) a decline in catastrophe losses and (ii) the impact of a modest decline in volumes of insured exposures, partially offset by (iii) the impact of loss cost trends and (iv) a decrease in net favorable prior year reserve development. Catastrophe losses in 2013 were \$285 million, compared with \$794 million in 2012. Net favorable prior year reserve development in 2013 was \$325 million, compared with \$467 million in 2012. Factors contributing to net favorable prior year reserve development are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.

Claims and claim adjustment expenses in 2012 were \$7.86 billion, \$590 million or 7% lower than in 2011, primarily reflecting (i) lower catastrophe losses, (ii) lower non-catastrophe weather-related losses and (iii) an increase in net favorable prior year reserve development, partially offset by (iv) the impact of loss cost trends. Catastrophe losses in 2012 were \$794 million, compared with \$1.02 billion in 2011. Net favorable prior year reserve development in 2012 was \$467 million, compared with \$245 million in

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2011. Factors contributing to net favorable prior year reserve development are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.

*Amortization of Deferred Acquisition Expenses*

Amortization of deferred acquisition costs in 2013 was \$1.91 billion, \$29 million or 2% higher than in 2012. Amortization of deferred acquisition costs in 2012 was \$1.88 billion, \$69 million or 4% higher than in 2011. The increases in both 2013 and 2012 were generally consistent with the increases in earned premiums compared to the respective prior year.

*General and Administrative Expenses*

General and administrative expenses in 2013 were \$2.05 billion, \$32 million or 2% higher than in 2012, as increases in employee- and technology-related costs were partially offset by a reduction in assessments from certain states. General and administrative expenses in 2012 were \$2.02 billion, \$76 million or 4% higher than in 2011, primarily driven by increases in employee- and technology-related costs.

*Income Tax Expense*

Income tax expense in 2013 was \$740 million, \$201 million or 37% higher than in 2012, primarily reflecting the impacts of a \$684 million increase in underwriting margins (including the impact of decreases in catastrophe losses and net favorable prior year reserve development), partially offset by lower net investment income and a reduction in income tax expense of \$43 million resulting from the resolution of prior year tax matters in 2013.

Income tax expense in 2012 was \$539 million, \$405 million higher than in 2011, primarily reflecting the impacts of an \$836 million increase in underwriting margins (including the impact of a decrease in catastrophes and an increase in net favorable prior year reserve development), an increase in net investment income from non-fixed maturity investments and a reduction in income tax expense of \$76 million resulting from the resolution of prior year tax matters in 2011.

**GAAP Combined Ratios**

The GAAP combined ratio of 91.9% in 2013 was 5.5 points lower than the GAAP combined ratio of 97.4% in 2012.

The loss and loss adjustment expense ratio of 61.2% in 2013 was 4.7 points lower than the loss and loss adjustment expense ratio of 65.9% in 2012. Catastrophe losses in 2013 and 2012 accounted for 2.4 points and 6.8 points, respectively, of the loss and loss adjustment expense ratio. Net favorable prior year reserve development in 2013 and 2012 provided 2.7 points and 4.0 points of benefit, respectively, to the loss and loss adjustment expense ratio. The 2013 underlying loss and loss adjustment expense ratio was 1.6 points lower than the 2012 ratio on the same basis, reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above, partially offset by the impact of a change in business mix due to an increase in longer-tail loss-sensitive business in the National Accounts business group.

The underwriting expense ratio of 30.7% in 2013 was 0.8 points lower than the 2012 underwriting expense ratio of 31.5%. The decrease in 2013 primarily reflected the impact of growth in earned premiums.

The GAAP combined ratio of 97.4% in 2012 was 7.3 points lower than the GAAP combined ratio of 104.7% in 2011.

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The loss and loss adjustment expense ratio of 65.9% in 2012 was 7.2 points lower than the loss and loss adjustment expense ratio of 73.1% in 2011. Catastrophe losses in 2012 and 2011 accounted for 6.8 points and 9.0 points, respectively, of the loss and loss adjustment expense ratio. Net favorable prior year reserve development in 2012 and 2011 provided 4.0 points and 2.2 points of benefit, respectively, to the loss and loss adjustment expense ratio. The 2012 underlying loss and loss adjustment expense ratio was 3.2 points lower than the 2011 ratio on the same basis, reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above.

The underwriting expense ratio of 31.5% in 2012 was 0.1 points lower than the 2011 underwriting expense ratio of 31.6%.

**Written Premiums**

The Business Insurance segment's gross and net written premiums by market were as follows:

(for the year ended December 31, in millions)	Gross Written Premiums		
	2013	2012	2011
Select Accounts	\$ 2,774	\$ 2,827	\$ 2,830
Commercial Accounts	3,375	3,280	3,076
National Accounts	1,606	1,387	1,112
Industry-Focused Underwriting	2,719	2,627	2,473
Target Risk Underwriting	2,244	2,116	2,035
Specialized Distribution	862	876	886
<b>Total Business Insurance Core</b>	<b>13,580</b>	<b>13,113</b>	<b>12,412</b>
Business Insurance Other	(3)	(2)	6
<b>Total Business Insurance</b>	<b>\$ 13,577</b>	<b>\$ 13,111</b>	<b>\$ 12,418</b>

(for the year ended December 31, in millions)	Net Written Premiums		
	2013	2012	2011
Select Accounts	\$ 2,724	\$ 2,775	\$ 2,784
Commercial Accounts	3,197	3,101	2,890
National Accounts	1,010	907	782
Industry-Focused Underwriting	2,645	2,554	2,407
Target Risk Underwriting	1,799	1,666	1,587
Specialized Distribution	858	870	880
<b>Total Business Insurance Core</b>	<b>12,233</b>	<b>11,873</b>	<b>11,330</b>
Business Insurance Other		(1)	10
<b>Total Business Insurance</b>	<b>\$ 12,233</b>	<b>\$ 11,872</b>	<b>\$ 11,340</b>

Gross and net written premiums in 2013 increased by 4% and 3%, respectively, over 2012. The increases in gross and net written premiums in 2013 were concentrated in Target Risk Underwriting, National Accounts, Commercial Accounts and Industry-Focused Underwriting, partially offset by declines in Select Accounts and Specialized Distribution. In 2013, business retention rates remained strong and were virtually level

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with 2012. Renewal premium changes remained positive in 2013 but were lower than in 2012, primarily due to a decline in insured exposures. Renewal rate changes continued to exceed expected loss cost trends. New business premiums in 2013 increased over 2012.

Gross and net written premiums in 2012 increased by 6% and 5%, respectively, over 2011. The increases in gross and net written premiums were concentrated in Commercial Accounts, Industry-Focused Underwriting, National Accounts and Target Risk Underwriting, and were largely driven by

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rate increases and positive audit premium adjustments (which were higher than in 2011). In 2012, business retention rates remained strong but were lower than in 2011. Renewal premium changes remained positive in 2012 and were higher than in 2011. New business premiums in 2012 decreased from 2011.

*Select Accounts.* Net written premiums of \$2.72 billion in 2013 decreased by 2% from 2012. Business retention rates in 2013 remained strong and were level with 2012. Renewal premium changes remained positive in 2013 and were slightly higher than in 2012, primarily due to higher renewal rate increases. New business premiums in 2013 declined from 2012. Net written premiums of \$2.78 billion in 2012 were virtually level with 2011. Business retention rates in 2012 remained strong but were lower than in 2011. Renewal premium changes remained positive in 2012 and were higher than in 2011, primarily due to higher renewal rate increases. New business premiums in 2012 decreased from 2011. Net written premiums in both 2013 and 2012 were favorably impacted by positive audit premium adjustments.

*Commercial Accounts.* Net written premiums of \$3.20 billion in 2013 increased by 3% over 2012. Business retention rates in 2013 remained strong but were lower than in 2012. Renewal premium changes remained positive in 2013 but were lower than in 2012, due to a decline in both insured exposures and renewal price changes. New business premiums in 2013 increased over 2012. Net written premiums of \$3.10 billion in 2012 increased by 7% over 2011. Business retention rates remained strong but were lower than in 2011. Renewal premium changes remained positive in 2012 and were higher than in 2011, primarily due to renewal rate increases. New business premiums in 2012 decreased from 2011. Net written premiums in 2012 were favorably impacted by positive audit premium adjustments (which were higher than in 2011).

*National Accounts.* Net written premiums of \$1.01 billion in 2013 increased by 11% over 2012, primarily due to continuing strong retention, positive renewal premium changes, increased new business and growth in workers' compensation residual market pools. Business retention rates remained strong in 2013 but were lower than in 2012. Renewal premium changes in 2013 remained positive but were lower than in 2012, driven by a decline in payroll exposure growth. New business premiums in 2013 were higher than in 2012. Net written premiums of \$907 million in 2012 increased by 16% over 2011. Business retention rates remained strong in 2012 and were level with 2011. Renewal premium changes were positive and were higher than in 2011, driven by payroll exposure growth. New business premiums in 2012 increased over 2011. Growth in workers' compensation residual market pools also contributed to premium growth in both 2013 and 2012.

*Industry-Focused Underwriting.* Net written premiums of \$2.65 billion in 2013 increased by 4% over 2012, as premium growth in the Construction and Technology business units was partially offset by a decline in the Public Sector Services business unit. Business retention rates remained strong in 2013 and were higher than in 2012. Renewal premium changes remained positive in 2013 but were lower than in 2012. New business premiums in 2013 increased over 2012. Net written premiums of \$2.55 billion in 2012 increased by 6% over 2011, driven by growth in the Construction, Oil & Gas and Technology business units. Business retention rates in 2012 remained strong and were virtually level with 2011. Renewal premium changes remained positive in 2012 and were higher than in 2011, primarily due to renewal rate increases. New business premiums in 2012 decreased from 2011.

*Target Risk Underwriting.* Net written premiums of \$1.80 billion in 2013 increased by 8% over 2012, driven by the National Property and Inland Marine business units. Business retention rates remained strong in 2013 and were slightly higher than in 2012. Renewal premium changes remained positive in 2013 but were lower than in 2012. New business premiums in 2013 increased over 2012. Net written premiums of \$1.67 billion in 2012 increased by 5% over 2011, also driven by the National Property and Inland Marine business units. Business retention rates in 2012 remained strong but were

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lower than in 2011. Renewal premium changes remained positive in 2012 and were higher than in 2011, primarily due to renewal rate increases. New business premiums in 2012 increased over 2011.

*Specialized Distribution.* Net written premiums of \$858 million in 2013 declined by 1% from 2012, driven by premium decreases in National Programs. Business retention rates remained strong in 2013 but were lower than in 2012. Renewal premium changes remained positive in 2013 and were slightly lower than in 2012. New business premiums in 2013 increased over 2012. Net written premiums of \$870 million in 2012 decreased by 1% from 2011. Premium decreases in the Northland business unit were largely offset by premium growth in the National Programs business unit. Business retention rates in 2012 remained strong but were lower than in 2011. Renewal premium changes remained positive in 2012 and were higher than in 2011, primarily due to renewal rate increases. New business premiums in 2012 decreased from 2011.

**Financial, Professional & International Insurance**

Results of the Company's Financial, Professional & International Insurance segment were as follows:

(for the year ended December 31, in millions)	2013	2012	2011
<b>Revenues:</b>			
Earned premiums	\$ 3,229	\$ 3,045	\$ 3,174
Net investment income	372	395	414
Fee income	2	1	1
Other revenues	22	26	26
<b>Total revenues</b>	<b>\$ 3,625</b>	<b>\$ 3,467</b>	<b>\$ 3,615</b>
<b>Total claims and expenses</b>	<b>\$ 2,732</b>	<b>\$ 2,570</b>	<b>\$ 2,738</b>
<b>Operating income</b>	<b>\$ 648</b>	<b>\$ 642</b>	<b>\$ 647</b>
Loss and loss adjustment expense ratio	43.2%	42.8%	46.4%
Underwriting expense ratio	41.1	41.3	39.4
<b>GAAP combined ratio</b>	<b>84.3%</b>	<b>84.1%</b>	<b>85.8%</b>

*Overview*

Operating income in 2013 was \$648 million, \$6 million or 1% higher than operating income of \$642 million in 2012. The increase in operating income primarily reflected the pretax impact of (i) higher underlying underwriting margins and (ii) higher net favorable prior year reserve development, largely offset by (iii) lower net investment income and (iv) higher catastrophe losses. The increase in underlying underwriting margins was driven by (i) earned pricing that exceeded loss cost trends, partially offset by (ii) the impact of lower volumes of insured exposures, (iii) a higher level of what the Company defines as large losses, (iv) higher general and administrative expenses and (v) higher non-catastrophe weather-related losses. Partially offsetting this net pretax increase in operating income was the related tax expense.

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Additionally, operating income in 2013 benefited from a reduction in income tax expense resulting from the resolution of prior year tax matters in 2013. The effective tax rate in 2013 decreased from 2012, primarily due to the impact of the resolution of prior year tax matters described above. Catastrophe losses in 2013 were \$56 million, compared with \$50 million in 2012. Net favorable prior year reserve development in 2013 was \$306 million, compared with \$298 million in 2012.

Operating income in 2012 was \$642 million, \$5 million or 1% lower than operating income in 2011. The decrease in operating income in 2012 compared with 2011 primarily reflected the pretax

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declines in (i) net favorable prior year reserve development and (ii) net investment income, largely offset by (iii) higher underlying underwriting margins. The increase in underlying underwriting margins resulted from the pretax impact of (i) lower levels of what the Company defines as large losses and (ii) earned pricing that exceeded loss cost trends, partially offset by (iii) the impact of lower volumes of insured exposures. Partially offsetting this net pretax decrease in operating income was the related reduction in tax expense. Additionally, tax expense in 2011 was reduced by the resolution of prior year tax matters. The effective tax rate in 2012 increased over 2011, primarily due to the impact of the resolution of prior year tax matters in 2011 described above. Net favorable prior year reserve development in 2012 was \$298 million, compared with \$360 million in 2011. Catastrophe losses in 2012 were \$50 million, compared with \$55 million in 2011.

**Revenues**

*Earned Premiums*

Earned premiums in 2013 were \$3.23 billion, \$184 million or 6% higher than in 2012, primarily reflecting the impact of the acquisition of Dominion.

Earned premiums in 2012 were \$3.05 billion, \$129 million or 4% lower than in 2011, primarily reflecting the impact of lower construction surety premium volumes over the preceding twelve months, intentional underwriting actions undertaken in the Company's operations at Lloyd's intended to improve risk and reward (particularly in the catastrophe-exposed lines of business), the impact of the termination of an exclusive broker relationship in the Republic of Ireland, the Company's withdrawal from personal insurance business in the Republic of Ireland, competitive market conditions and, to a lesser extent, foreign currency rates of exchange.

*Net Investment Income*

Net investment income in 2013 was \$372 million, \$23 million or 6% lower than in 2012. Net investment income in 2012 was \$395 million, \$19 million or 5% lower than in 2011. Included in the Financial, Professional & International Insurance segment are certain legal entities whose invested assets and related net investment income are reported exclusively in this segment and not allocated among all business segments. As a result, reported net investment income in the Financial, Professional & International Insurance segment reflects a significantly smaller proportion of allocated net investment income, including that from the Company's non-fixed maturity investments that experienced a decrease in investment income in 2013 and an increase in investment income in 2012. Net investment income in 2013 also benefited from the acquisition of Dominion. Refer to the "Net Investment Income" section of the "Consolidated Results of Operations" discussion herein for a description of the factors contributing to the changes in the Company's consolidated net investment income in 2013 and 2012 compared with the respective prior years. In addition, refer to note 2 of notes to the Company's consolidated financial statements herein for a discussion of the Company's net investment income allocation methodology.

**Claims and Expenses**

*Claims and Claim Adjustment Expenses*

Claims and claim adjustment expenses in 2013 were \$1.40 billion, \$90 million or 7% higher than in 2012, primarily reflecting (i) the impact of the acquisition of Dominion, (ii) a higher level of what the Company defines as large losses, (iii) higher non-catastrophe weather-related losses and (iv) an increase in catastrophe losses, partially offset by (v) reduced loss cost trends, (vi) the impact of lower volumes of insured exposures and (vii) higher net favorable prior year reserve development. Catastrophe losses in 2013 were \$56 million, primarily resulting from floods in Alberta, Canada, and Storm Xaver in the United Kingdom, compared with \$50 million in 2012, which primarily resulted from Storm Sandy. Net favorable prior year reserve development in 2013 was \$306 million, compared with \$298 million in 2012. Factors contributing to net favorable prior year reserve development are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.



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Claims and claim adjustment expenses in 2012 were \$1.31 billion, \$173 million or 12% lower than in 2011, primarily reflecting (i) lower levels of large losses and (ii) the impact of lower volumes of construction surety insured exposures and intentional underwriting actions as discussed above, partially offset by (iii) a decline in net favorable prior year reserve development. Net favorable prior year reserve development in 2012 was \$298 million, compared with \$360 million in 2011. Factors contributing to net favorable prior year reserve development are discussed in more detail in note 7 of notes to the Company's consolidated financial statements. Catastrophe losses in 2012 were \$50 million, compared with \$55 million in 2011.

*Amortization of Deferred Acquisition Costs*

Amortization of deferred acquisition costs in 2013 was \$623 million, \$34 million or 6% higher than in 2012. The increase in 2013 primarily reflected the impact of the acquisition of Dominion and a change in business mix. Amortization of deferred acquisition costs in 2012 was \$589 million, \$14 million or 2% lower than in 2011. The decrease in 2012 was generally consistent with the decrease in earned premiums.

*General and Administrative Expenses*

General and administrative expenses in 2013 were \$705 million, \$38 million or 6% higher than in 2012. The increase in 2013 primarily reflected the impact of the acquisition of Dominion, including related legal expenses, and higher employee-related expenses. General and administrative expenses in 2012 were \$667 million, \$19 million or 3% higher than in 2011. The increase in 2012 primarily reflected increases in employee- and technology-related costs to enhance operations and support future business growth.

*Income Tax Expense*

Income tax expense in 2013 was \$245 million, \$10 million or 4% lower than in 2012, primarily reflecting the impact of the \$15 million reduction in income tax expense resulting from the resolution of prior year tax matters, partially offset by the impact of a \$23 million increase in underwriting margins (including the impact of catastrophe losses and net favorable prior year reserve development). Income tax expense in 2012 was \$255 million, \$25 million or 11% higher than in 2011, primarily reflecting the impact of a \$14 million benefit in 2011 from the resolution of prior year tax matters and, to a lesser extent, an increase in underwriting margins in 2012 (including the impact of catastrophe losses and net favorable prior year reserve development) compared with 2011.

**GAAP Combined Ratios**

The GAAP combined ratio of 84.3% in 2013 was 0.2 points higher than the GAAP combined ratio of 84.1% in 2012.

The loss and loss adjustment expense ratio of 43.2% in 2013 was 0.4 points higher than the 2012 ratio of 42.8%. Catastrophe losses in 2013 and 2012 accounted for 1.8 and 1.7 points of the loss and loss adjustment expense ratio, respectively. Net favorable prior year reserve development provided 9.5 points and 9.8 points of benefit to the loss and loss adjustment expense ratio in 2013 and 2012, respectively. The 2013 underlying loss and loss adjustment expense ratio was level with the 2012 ratio on the same basis, reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above, offset by the impact of the acquisition of Dominion and an increase in what the Company defines as large losses. Historically, Dominion has had a higher loss and loss adjustment expense ratio than the pre-existing business in the Financial, Professional & International Insurance segment.

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The underwriting expense ratio of 41.1% in 2013 was 0.2 points lower than the underwriting expense ratio of 41.3% in 2012. The decrease in 2013 primarily reflected the impact of the acquisition of Dominion, partially offset by the increases in amortization of deferred acquisition costs and general and administrative expenses described above. Historically, Dominion has had a lower underwriting expense ratio than the pre-existing business in the Financial, Professional & International Insurance segment, as the underwriting expense ratio of pre-existing business reflects investment in the Company's International business to enhance operations, improve underwriting results and support future business growth, as well as the business mix in Bond & Financial Products.

The GAAP combined ratio of 84.1% in 2012 was 1.7 points lower than the GAAP combined ratio of 85.8% in 2011.

The loss and loss adjustment expense ratio of 42.8% in 2012 was 3.6 points lower than the loss and loss adjustment expense ratio of 46.4% in 2011. The 2012 and 2011 ratios included 9.8 points and 11.3 points of benefit, respectively, from net favorable prior year reserve development. Catastrophe losses in 2012 and 2011 accounted for 1.7 points of the loss and loss adjustment expense ratio in each year. The 2012 underlying loss and loss adjustment expense ratio was 5.1 points lower than the 2011 ratio on the same basis, reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above.

The underwriting expense ratio of 41.3% in 2012 was 1.9 points higher than the underwriting expense ratio of 39.4% in 2011, primarily reflecting the impact of a decline in earned premiums and, to a lesser extent, the impact of an increase in general and administrative expenses.

**Written Premiums**

Financial, Professional & International Insurance gross and net written premiums by market were as follows:

(for the year ended December 31, in millions)	Gross Written Premiums		
	2013	2012	2011
Bond & Financial Products	\$ 2,131	\$ 2,059	\$ 2,092
International	1,415	1,216	1,316
<b>Total Financial, Professional &amp; International Insurance</b>	<b>\$ 3,546</b>	<b>\$ 3,275</b>	<b>\$ 3,408</b>

(for the year ended December 31, in millions)	Net Written Premiums		
	2013	2012	2011
Bond & Financial Products	\$ 2,030	\$ 1,924	\$ 1,953
International	1,279	1,057	1,149
<b>Total Financial, Professional &amp; International Insurance</b>	<b>\$ 3,309</b>	<b>\$ 2,981</b>	<b>\$ 3,102</b>

Gross and net written premiums in 2013 increased by 8% and 11%, respectively, over 2012. Gross and net written premiums in 2012 both decreased by 4% from 2011. Renewal rate changes continued to exceed expected loss cost trends.

Net written premiums in Bond & Financial Products in 2013 were \$2.03 billion, \$106 million or 6% higher than in 2012, primarily driven by higher contract surety volume, rate increases in the management liability business and lower reinsurance costs primarily resulting from a change in a reinsurance treaty. Excluding the surety line of business, for which the following are not relevant measures, business retention rates in 2013 remained strong but were lower than in 2012. Renewal premium changes in 2013 remained positive and were virtually level with 2012, as increases in renewal



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rate changes were largely offset by a decline in insured exposures. Renewal rate changes continued to exceed expected loss cost trends in 2013. New business premiums in 2013 decreased from 2012.

Net written premiums in Bond & Financial Products in 2012 were \$1.92 billion, \$29 million or 1% lower than in 2011. The decrease was primarily driven by lower business volume in construction surety due to the continued low levels of government construction spending, which was largely offset by growth in management liability business volume. Excluding the surety line of business, for which the following are not relevant measures, business retention rates in 2012 remained strong and were slightly higher than in 2011. Renewal premium changes in 2012 were positive and significantly higher than in 2011, primarily driven by positive renewal rate changes. New business premiums in 2012 decreased from 2011.

Net written premiums in International in 2013 were \$1.28 billion, \$222 million or 21% higher than in 2012. The increase in 2013 primarily reflected the impact of the acquisition of Dominion. Excluding the surety line of business, for which the following are not relevant measures, business retention rates remained strong and were higher than in 2012. Renewal premium changes in 2013 were positive and increased over 2012, as growth in insured exposures in 2013, compared with a decline in 2012, was partially offset by lower positive renewal rate changes in 2013 compared with 2012. New business premiums in 2013 increased over 2012.

Net written premiums in International in 2012 were \$1.06 billion, \$92 million or 8% lower than in 2011. The decrease in 2012 primarily reflected lower business volume in the Company's operations at Lloyd's, lower surety volumes in Canada, the impact of the Company's withdrawal from personal insurance business in the Republic of Ireland and, to a lesser extent, the impact of foreign currency rates of exchange. Excluding the surety line of business, for which the following are not relevant measures, business retention rates in 2012 were strong and higher than in 2011. Renewal premium changes in 2012 were negative and lower than in 2011, as positive renewal rate changes were more than offset by a decline in insured exposures. New business premiums in 2012 were lower than in 2011.

## Personal Insurance

Results of the Company's Personal Insurance segment were as follows:

(for the year ended December 31, in millions)	2013	2012	2011
<b>Revenues:</b>			
Earned premiums	\$ 7,324	\$ 7,621	\$ 7,589
Net investment income	369	404	424
Other revenues	103	66	70
<b>Total revenues</b>	<b>\$ 7,796</b>	<b>\$ 8,091</b>	<b>\$ 8,083</b>
Total claims and expenses	\$ 6,592	\$ 7,842	\$ 8,708
<b>Operating income (loss)</b>	<b>\$ 838</b>	<b>\$ 217</b>	<b>\$ (332)</b>
Loss and loss adjustment expense ratio	59.1%	72.3%	83.5%
Underwriting expense ratio	29.8	29.6	30.1
<b>GAAP combined ratio</b>	<b>88.9%</b>	<b>101.9%</b>	<b>113.6%</b>

<b>Incremental impact of direct to consumer initiative on GAAP combined ratio</b>	<b>1.8%</b>	<b>2.3%</b>	<b>2.5%</b>
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*Overview*

Operating income in 2013 was \$838 million, \$621 million higher than operating income of \$217 million in 2012. The increase in operating income primarily reflected the pretax impact of

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(i) lower catastrophe losses, (ii) higher underlying underwriting margins, (iii) an increase in other revenues and (iv) higher net favorable prior year reserve development, partially offset by (v) lower net investment income. The higher underlying underwriting margins resulted from the impact of earned pricing that exceeded loss cost trends and lower non-catastrophe weather-related losses. Partially offsetting this net pretax increase in operating income was the related tax expense. Additionally, operating income in 2013 benefited from a reduction in income tax expense resulting from the resolution of prior year tax matters. The effective tax rate in 2013 increased over 2012. This resulted from interest on municipal bonds, which is effectively taxed at a rate that is lower than the corporate tax rate of 35%, comprising a lower percentage of pretax income. Catastrophe losses in 2013 were \$250 million, compared with \$1.02 billion in 2012. Net favorable prior year reserve development in 2013 was \$209 million, compared with \$175 million in 2012.

Operating income in 2012 was \$217 million, \$549 million higher than the operating loss of (\$332) million in 2011. The improvement in operating income in 2012 compared with 2011 primarily reflected the pretax impact of (i) a decline in catastrophe losses, (ii) higher underlying underwriting margins and (iii) an increase in net favorable prior year reserve development. The higher underlying underwriting margins resulted from lower non-catastrophe weather-related losses and lower fire-related losses. Partially offsetting this net pretax increase in operating income was the related tax expense. Additionally, operating income in 2011 benefited from a reduction in income tax expense resulting from the resolution of prior year tax matters. The effective tax rate in 2012 increased over 2011. This resulted from interest on municipal bonds, which is effectively taxed at a rate that is lower than the corporate tax rate of 35%, comprising a lower percentage of pretax income, as well as the resolution of prior year tax matters discussed above. Catastrophe losses in 2012 were \$1.02 billion, compared with \$1.49 billion in 2011. Net favorable prior year reserve development in 2012 was \$175 million, compared with \$110 million in 2011.

**Revenues**

*Earned Premiums*

Earned premiums in 2013 were \$7.32 billion, \$297 million or 4% lower than in 2012. Earned premiums in 2012 were \$7.62 billion, \$32 million or less than 1% higher than in 2011. The changes in both years reflected changes in net written premiums over the preceding twelve months.

*Net Investment Income*

Net investment income in 2013 was \$369 million, \$35 million or 9% lower than in 2012. Net investment income in 2012 was \$404 million, \$20 million or 5% lower than in 2011. Refer to the "Net Investment Income" section of "Consolidated Results of Operations" herein for a discussion of the change in the Company's net investment income in 2013 and 2012 as compared with the respective prior year. In addition, refer to note 2 of notes to the Company's consolidated financial statements herein for a discussion of the Company's net investment income allocation methodology.

*Other Revenues*

Other revenues in 2013 included a \$20 million gain from the sale of renewal rights in the third quarter of 2013 related to the Company's National Flood Insurance Program (NFIP) business. The Company was a participant in the NFIP Write Your Own (WYO) Program administered by the Federal Emergency Management Agency (FEMA) and the Federal Insurance & Mitigation Administration (FIMA).

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**Claims and Expenses**

*Claims and Claim Adjustment Expenses*

Claims and claim adjustment expenses in 2013 were \$4.33 billion, \$1.18 billion or 21% lower than in 2012. The decrease primarily reflected (i) lower catastrophe losses, (ii) lower non-catastrophe weather-related losses, (iii) the impact of lower volumes of insured exposures and (iv) higher net favorable prior year reserve development, partially offset by (v) the impact of loss cost trends. Catastrophe losses in 2013 and 2012 were \$250 million and \$1.02 billion, respectively. Net favorable prior year reserve development in 2013 and 2012 was \$209 million and \$175 million, respectively. Factors contributing to net favorable prior year reserve development are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.

Claims and claim adjustment expenses in 2012 were \$5.50 billion, \$837 million or 13% lower than in 2011. The decrease primarily reflected (i) lower catastrophe losses, (ii) lower non-catastrophe weather-related losses, (iii) lower fire-related losses and (iv) higher net favorable prior year reserve development, partially offset by (v) the impact of loss cost trends, including a higher number of severe bodily injury claims in the automobile line of business. Catastrophe losses in 2012 were \$1.02 billion, compared with \$1.49 billion in 2011. Net favorable prior year reserve development in 2012 was \$175 million, compared with \$110 million in 2011. Factors contributing to net favorable prior year reserve development are discussed in more detail in note 7 of notes to the Company's consolidated financial statements.

*Amortization of Deferred Acquisition Costs*

Amortization of deferred acquisition costs in 2013 was \$1.29 billion, \$152 million or 11% lower than in 2012. The decrease in 2013 reflected (i) the decline in earned premiums compared with 2012, (ii) a reclassification of fee income related to the National Flood Insurance Program from general and administrative expenses to a component of acquisition costs to conform to the presentation prescribed by insurance regulators, and (iii) lower fixed-value commission expense. Amortization of deferred acquisition costs in 2012 was \$1.44 billion, \$21 million or 1% lower than in 2011, primarily due to lower fixed-value commission expense. The lower fixed-value commission expense in 2013 resulted from an increase in the number of agents reverting to a contingent commission compensation program (the costs of which are classified in "general and administrative expenses") from a fixed-value compensation program (the costs of which are classified in "amortization of deferred acquisition costs").

*General and Administrative Expenses*

General and administrative expenses in 2013 were \$980 million, \$80 million or 9% higher than in 2012. The increase in 2013 included an increase in contingent commission expense due to the increase in the number of agents reverting to a contingent commission compensation program and the impact of the reclassification of fee income described above. The increase in 2013 also included the impact of \$12 million of restructuring charges, primarily comprised of severance costs related to the Company's announced plan to reduce certain claim and other insurance expenses in this segment. These factors were partially offset by a decline in advertising expense. General and administrative expenses in 2012 were \$900 million, \$8 million or 1% lower than in 2011.

*Income Tax Expense*

Income tax expense in 2013 was \$366 million, \$334 million higher than in 2012, primarily reflecting the impacts of the \$953 million increase in underwriting margins (including the impact of a decrease in catastrophe losses and the increase in net favorable prior year reserve development), partially offset by lower net investment income and a reduction in income tax expense of \$5 million resulting from the resolution of prior year tax matters in 2013. Income tax expense in 2012 was \$32 million, compared to

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an income tax benefit of \$293 million in 2011. The change in income tax expense of \$325 million in 2012 from 2011 primarily reflected the \$898 million decrease in underwriting loss (including the impact of a decrease in catastrophes and an increase in net favorable prior year reserve development) from 2011, as well as the reduction in income tax expense of \$10 million resulting from the resolution of prior year tax matters in 2011.

**GAAP Combined Ratio**

The GAAP combined ratio of 88.9% in 2013 was 13.0 points lower than the GAAP combined ratio of 101.9% in 2012.

The loss and loss adjustment expense ratio of 59.1% in 2013 was 13.2 points lower than the 2012 ratio of 72.3%. Catastrophe losses accounted for 3.4 and 13.4 points of the loss and loss adjustment expense ratio in 2013 and 2012, respectively. Net favorable prior year reserve development provided 2.8 points and 2.3 points of benefit to the loss and loss adjustment expense ratio in 2013 and 2012, respectively. The 2013 underlying loss and loss adjustment expense ratio was 2.7 points lower than the 2012 ratio on the same basis, reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above.

The underwriting expense ratio of 29.8% in 2013 was 0.2 points higher than the underwriting expense ratio of 29.6% in 2012. The increase in 2013 primarily reflected the decrease in earned premiums and the expense factors discussed above.

The GAAP combined ratio of 101.9% in 2012 was 11.7 points lower than the GAAP combined ratio of 113.6% in 2011.

The loss and loss adjustment expense ratio of 72.3% in 2012 was 11.2 points lower than the loss and loss adjustment expense ratio of 83.5% in 2011. Catastrophe losses accounted for 13.4 points and 19.6 points of the loss and loss adjustment expense ratios in 2012 and 2011, respectively. The loss and loss adjustment expense ratio for 2012 and 2011 included 2.3 points and 1.5 points of benefit, respectively, from net favorable prior year reserve development. The 2012 underlying loss and loss adjustment expense ratio was 4.2 points lower than the 2011 ratio on the same basis, reflecting the improvement in underlying underwriting margins discussed in the "Overview" section above.

The underwriting expense ratio of 29.6% in 2012 was 0.5 points lower than the underwriting expense ratio of 30.1% in 2011. The decrease in 2012 primarily reflected the increase in earned premiums discussed above.

**Agency Written Premiums**

Gross and net written premiums by product line were as follows for the Personal Insurance segment's Agency business, which comprises business written through agents, brokers and other intermediaries and represents almost all of the segment's gross and net written premiums:

(for the year ended December 31, in millions)	Gross Written Premiums		
	2013	2012	2011
Agency Automobile	\$ 3,277	\$ 3,544	\$ 3,706
Agency Homeowners and Other	4,094	4,220	4,221
<b>Total Agency Personal Insurance</b>	<b>\$ 7,371</b>	<b>\$ 7,764</b>	<b>\$ 7,927</b>

(for the year ended December 31, in millions)	Net Written Premiums		
	2013	2012	2011
Agency Automobile	\$ 3,258	\$ 3,527	\$ 3,688
Agency Homeowners and Other	3,805	3,909	3,923
<b>Total Agency Personal Insurance</b>	<b>\$ 7,063</b>	<b>\$ 7,436</b>	<b>\$ 7,611</b>





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In 2013, gross and net Agency written premiums were 5% lower than in 2012. Renewal rate changes continued to exceed expected loss cost trends, assuming weather patterns consistent with the Company's expectations. In 2012, gross and net Agency written premiums were 2% lower than in 2011.

In 2013 in the Agency Automobile line of business, net written premiums were 8% lower than in 2012. Business retention rates in 2013 remained strong but were slightly lower than in 2012, while new business premiums in 2013 decreased from 2012, largely as a result of the Company's continued pricing strategies and other profitability improvement initiatives. Renewal premium changes in 2013 remained positive and were higher than in 2012, primarily driven by renewal rate changes. In 2012, net written premiums were 4% lower than in 2011. Business retention rates remained strong but were lower than in 2011, while new business premiums in 2012 decreased from 2011, largely as a result of the Company's pricing strategy and other profitability improvement initiatives. Renewal premium changes remained positive in 2012 and were higher than in 2011.

In 2013 in the Agency Homeowners and Other line of business, net written premiums were 3% lower than in 2012. Business retention rates remained strong but were slightly lower than in 2012. Renewal premium changes in 2013 remained positive but were slightly lower than in 2012. New business premiums in 2013 decreased from 2012. Net written premiums in 2012 were slightly lower than in 2011. Business retention rates remained strong but were lower than in 2011. New business premiums in 2012 decreased from 2011, largely as a result of the Company's pricing strategy, higher deductibles and other profitability improvement initiatives. Renewal premium changes remained positive in 2012 and were higher than in 2011.

For its Agency business, the Personal Insurance segment had approximately 6.2 million and 6.9 million active policies at December 31, 2013 and 2012, respectively. In the third quarter of 2013, the Company sold the renewal rights related to its National Flood Insurance Program (NFIP) business. Active policies in force at both dates have been adjusted to exclude the NFIP business.

**Direct to Consumer Written Premiums**

In its direct to consumer business, net written premiums in 2013 were \$162 million, \$4 million or 3% higher than in 2012. In 2013, homeowners and other net written premiums increased by \$7 million, or 16% over 2012, partially offset by a decline of \$3 million, or 3%, in automobile net written premiums compared to 2012. Net written premiums in 2012 were \$158 million, \$24 million or 18% higher than in 2011. The increase in net written premiums in 2012 resulted from a \$15 million or 15% increase in automobile net written premiums and a \$9 million or 26% increase in homeowners and other net written premiums compared to 2011. The direct to consumer business had 166,000 and 161,000 active policies at December 31, 2013 and 2012, respectively.

**Interest Expense and Other**

(for the year ended December 31, in millions)	2013	2012	2011
Operating loss	\$ (248)	\$ (261)	\$ (279)

The operating loss for Interest Expense and Other in 2013 was \$13 million lower than in 2012. The operating loss for Interest Expense and Other in 2012 was \$18 million lower than in 2011. After-tax interest expense in 2013, 2012 and 2011 was \$235 million, \$246 million and \$251 million, respectively. The decline in interest expense in both 2013 and 2012 compared with the respective prior year primarily reflected a lower level of average debt outstanding.

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**ASBESTOS CLAIMS AND LITIGATION**

The Company believes that the property and casualty insurance industry has suffered from court decisions and other trends that have expanded insurance coverage for asbestos claims far beyond the original intent of insurers and policyholders. The Company has received and continues to receive a significant number of asbestos claims from the Company's policyholders (which includes others seeking coverage under a policy). Factors underlying these claim filings include continued intensive advertising by lawyers seeking asbestos claimants and the continued focus by plaintiffs on defendants who were not traditionally primary targets of asbestos litigation. The focus on these defendants is primarily the result of the number of traditional asbestos defendants who have sought bankruptcy protection in previous years. In addition to contributing to the overall number of claims, bankruptcy proceedings may increase the volatility of asbestos-related losses by initially delaying the reporting of claims and later by significantly accelerating and increasing loss payments by insurers, including the Company. The bankruptcy of many traditional defendants has also caused increased settlement demands against those policyholders who are not in bankruptcy but remain in the tort system. Currently, in many jurisdictions, those who allege very serious injury and who can present credible medical evidence of their injuries are receiving priority trial settings in the courts, while those who have not shown any credible disease manifestation are having their hearing dates delayed or placed on an inactive docket. Prioritizing claims involving credible evidence of injuries, along with the focus on defendants who were not traditionally primary targets of asbestos litigation, contributes to the claims and claim adjustment expense payment patterns experienced by the Company. The Company's asbestos-related claims and claim adjustment expense experience also has been impacted by the unavailability of other insurance sources potentially available to policyholders, whether through exhaustion of policy limits or through the insolvency of other participating insurers.

The Company continues to be involved in coverage litigation concerning a number of policyholders, some of whom have filed for bankruptcy, who in some instances have asserted that all or a portion of their asbestos-related claims are not subject to aggregate limits on coverage. In these instances, policyholders also may assert that each individual bodily injury claim should be treated as a separate occurrence under the policy. It is difficult to predict whether these policyholders will be successful on both issues. To the extent both issues are resolved in a policyholder's favor and other Company defenses are not successful, the Company's coverage obligations under the policies at issue would be materially increased and bounded only by the applicable per-occurrence limits and the number of asbestos bodily injury claims against the policyholders. Although the Company has seen a moderation in the overall risk associated with these lawsuits, it remains difficult to predict the ultimate cost of these claims.

Many coverage disputes with policyholders are only resolved through settlement agreements. Because many policyholders make exaggerated demands, it is difficult to predict the outcome of settlement negotiations. Settlements involving bankrupt policyholders may include extensive releases which are favorable to the Company but which could result in settlements for larger amounts than originally anticipated. There also may be instances where a court may not approve a proposed settlement, which may result in additional litigation and potentially less beneficial outcomes for the Company. As in the past, the Company will continue to pursue settlement opportunities.

In addition to claims against policyholders, proceedings have been launched directly against insurers, including the Company, by individuals challenging insurers' conduct with respect to the handling of past asbestos claims and by individuals seeking damages arising from alleged asbestos-related bodily injuries. It is possible that the filing of other direct actions against insurers, including the Company, could be made in the future. It is difficult to predict the outcome of these proceedings, including whether the plaintiffs will be able to sustain these actions against insurers based on novel legal theories of liability. The Company believes it has meritorious defenses to these claims and has received favorable rulings in certain jurisdictions.

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TPC had entered into settlement agreements, which are subject to a number of contingencies, in connection with a number of these direct action claims (Direct Action Settlements). For a full discussion of these settlement agreements, see the "Asbestos Direct Action Litigation" section of note 16 of notes to the consolidated financial statements.

Because each policyholder presents different liability and coverage issues, the Company generally reviews the exposure presented by each policyholder at least annually. Among the factors which the Company may consider in the course of this review are: available insurance coverage, including the role of any umbrella or excess insurance the Company has issued to the policyholder; limits and deductibles; an analysis of the policyholder's potential liability; the jurisdictions involved; past and anticipated future claim activity and loss development on pending claims; past settlement values of similar claims; allocated claim adjustment expense; potential role of other insurance; the role, if any, of non-asbestos claims or potential non-asbestos claims in any resolution process; and applicable coverage defenses or determinations, if any, including the determination as to whether or not an asbestos claim is a products/completed operation claim subject to an aggregate limit and the available coverage, if any, for that claim.

In the third quarter of 2013, the Company completed its annual in-depth asbestos claim review, including a review of active policyholders and litigation cases for potential product and "non-product" liability, and noted the continuation of the following trends:

continued high level of litigation activity in certain jurisdictions involving individuals alleging serious asbestos-related illness;

while overall payment patterns have been generally stable, there has been an increase in severity for certain policyholders due to the continued high level of litigation activity;

continued moderate level of asbestos-related bankruptcy activity; and

the absence of new theories of liability or new classes of defendants.

While the Company believes that over the past several years there has been a reduction in the volatility associated with the Company's overall asbestos exposure, there nonetheless remains a high degree of uncertainty with respect to future exposure from asbestos claims.

The Home Office and Field Office categories, which account for the vast majority of policyholders with active asbestos-related claims, experienced a slight increase in the number of policyholders with open asbestos claims at December 31, 2013 compared with December 31, 2012, while net asbestos-related payments in these categories decreased slightly in 2013 compared with 2012. Payments on behalf of policyholders in these categories continue to be influenced by the high level of litigation activity in a limited number of jurisdictions where individuals alleging serious asbestos-related injury continue to target defendants who were not traditionally primary targets of asbestos litigation.

The Company's quarterly asbestos reserve reviews include an analysis of exposure and claim payment patterns by policyholder category, as well as recent settlements, policyholder bankruptcies, judicial rulings and legislative actions. The Company also analyzes developing payment patterns among policyholders in the Home Office, Field Office and Assumed Reinsurance and Other categories as well as projected reinsurance billings and recoveries. In addition, the Company reviews its historical gross and net loss and expense paid experience, year-by-year, to assess any emerging trends, fluctuations, or characteristics suggested by the aggregate paid activity. Conventional actuarial methods are not utilized to establish asbestos reserves nor have the Company's evaluations resulted in any way of determining a meaningful average asbestos defense or indemnity payment.

The completion of these reviews and analyses in 2013, 2012 and 2011 resulted in \$190 million, \$175 million and \$175 million increases, respectively, in the Company's net asbestos reserves in each period. In each year, the reserve increases were primarily driven by increases in the Company's

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estimate of projected settlement and defense costs related to a broad number of policyholders in the Home Office category and by higher projected payments on assumed reinsurance accounts. The increase in the estimate of projected settlement and defense costs resulted from payment trends that continue to be moderately higher than previously anticipated due to the impact of the current litigation environment discussed above. Notwithstanding these trends, the Company's overall view of the underlying asbestos environment is essentially unchanged from recent periods, and there remains a high degree of uncertainty with respect to future exposure to asbestos claims.

Net asbestos losses paid in 2013, 2012 and 2011 were \$218 million, \$236 million and \$284 million, respectively. Approximately 1%, 6% and 19% of total net paid losses in 2013, 2012 and 2011, respectively, related to policyholders with whom the Company had entered into settlement agreements limiting the Company's liability.

The Company categorizes its asbestos reserves as follows:

(at and for the year ended December 31, \$ in millions)	Number of Policyholders		Total Net Paid		Net Asbestos Reserves	
	2013	2012	2013	2012	2013	2012
Policyholders with settlement agreements	15	15	\$ 3	\$ 13	\$ 108	\$ 91
Home office and field office	1,690	1,678	195	199	2,047	2,089
Assumed reinsurance and other			20	24	195	198
<b>Total</b>	<b>1,705</b>	1,693	<b>\$ 218</b>	\$ 236	<b>\$ 2,350</b>	\$ 2,378

The "policyholders with settlement agreements" category includes structured settlements, coverage in place arrangements and, with respect to TPC, Wellington accounts. Reserves are based on the expected payout for each policyholder under the applicable agreement. Structured settlements are arrangements under which policyholders and/or plaintiffs agree to fixed financial amounts to be paid at scheduled times. Coverage in place arrangements represent agreements with policyholders on specified amounts of coverage to be provided. Payment obligations may be subject to annual maximums and are only made when valid claims are presented. Wellington accounts refer to the 35 defendants that are parties to a 1985 agreement settling certain disputes concerning insurance coverage for their asbestos claims. Many of the aspects of the Wellington agreement are similar to those of coverage in place arrangements in which the parties have agreed on specific amounts of coverage and the terms under which the coverage can be accessed.

The "home office and field office" category relates to all other policyholders and also includes unallocated IBNR reserves and reserves for the costs of defending asbestos-related coverage litigation. Policyholders are identified for the annual home office review based upon, among other factors: a combination of past payments and current case reserves in excess of a specified threshold (currently \$100,000), perceived level of exposure, number of reported claims, products/completed operations and potential "non-product" exposures, size of policyholder and geographic distribution of products or services sold by the policyholder. In addition to IBNR amounts contained in the reserves for "home office and field office" policyholders and the costs of litigating asbestos coverage matters, the Company has established a reserve for further adverse development related to existing policyholders, new claims from policyholders reporting claims for the first time and policyholders for which there is, or may be, litigation and direct actions against the Company. During 2012, \$502 million of reserves included in "Policyholders with settlement agreements" were reclassified to the unallocated IBNR component in the "home office and field office" category as a result of the U.S. District Court ruling on March 1, 2012 that the conditions of the Direct Action Settlements had not been satisfied. For a full discussion of these settlement agreements see the "Asbestos Direct Action Litigation" section of note 16 of notes to the consolidated financial statements. The "assumed reinsurance and other" category primarily consists of reinsurance of excess coverage, including various pool participations.

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On January 29, 2009, the Company and PPG Industries, Inc. ("PPG"), along with approximately 30 other insurers of PPG, agreed in principle to an agreement to settle asbestos-related coverage litigation under insurance policies issued to PPG. The tentative settlement agreement has been incorporated into the Modified Third Amended Plan of Reorganization ("Amended Plan") proposed as part of the Pittsburgh Corning Corp. ("PCC," which is 50% owned by PPG) bankruptcy proceeding. Pursuant to the proposed Amended Plan, which was filed on January 30, 2009, PCC, along with enumerated other companies (including PPG as well as the Company as a participating insurer), are to receive protections afforded by Section 524(g) of the Bankruptcy Code from certain asbestos-related bodily injury claims. Under the agreement in principle, the Company has the option to make a series of payments over the next 20 years totaling approximately \$620 million to the Trust to be created under the Amended Plan, or it may elect to make a one-time discounted payment, which, as of March 31, 2014, would total approximately \$493 million (approximately \$464 million after reinsurance). The agreement in principle with PPG is subject to numerous contingencies, including final court approval of the Amended Plan, and the Company has no obligation to make the settlement payment until all contingencies are satisfied. The Company's obligations under this agreement in principle are included in the "home office and field office" category in the preceding table.

The following table displays activity for asbestos losses and loss expenses and reserves:

(at and for the year ended December 31, in millions)	2013	2012	2011
<b>Beginning reserves:</b>			
Gross	\$ 2,689	\$ 2,780	\$ 2,941
Ceded	(311)	(341)	(393)
 Net	 2,378	 2,439	 2,548
<b>Incurred losses and loss expenses:</b>			
Gross	190	171	195
Ceded	4	(20)	(20)
 Net	 190	 175	 175
<b>Losses paid:</b>			
Gross	273	262	356
Ceded	(55)	(26)	(72)
 Net	 218	 236	 284
<b>Ending reserves:</b>			
Gross	2,606	2,689	2,780
Ceded	(256)	(311)	(341)
 Net	 \$ 2,350	 \$ 2,378	 \$ 2,439

See " Uncertainty Regarding Adequacy of Asbestos and Environmental Reserves."

**ENVIRONMENTAL CLAIMS AND LITIGATION**

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The Company has received and continues to receive claims from policyholders who allege that they are liable for injury or damage arising out of their alleged disposition of toxic substances. Mostly, these claims are due to various legislative as well as regulatory efforts aimed at environmental remediation. For instance, the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), enacted in 1980 and later modified, enables private parties as well as federal and state governments to take action with respect to releases and threatened releases of hazardous substances. This federal statute permits the recovery of response costs from some liable parties and may require liable parties to undertake their own remedial action. Liability under CERCLA may be joint and several with other responsible parties.

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The Company has been, and continues to be, involved in litigation involving insurance coverage issues pertaining to environmental claims. The Company believes that some court decisions have interpreted the insurance coverage to be broader than the original intent of the insurers and policyholders. These decisions often pertain to insurance policies that were issued by the Company prior to the mid-1980s. These decisions continue to be inconsistent and vary from jurisdiction to jurisdiction. Environmental claims when submitted rarely indicate the monetary amount being sought by the claimant from the policyholder, and the Company does not keep track of the monetary amount being sought in those few claims which indicate a monetary amount.

The resolution of environmental exposures by the Company generally occurs through settlements with policyholders as opposed to claimants. Generally, the Company strives to extinguish any obligations it may have under any policy issued to the policyholder for past, present and future environmental liabilities and extinguish any pending coverage litigation dispute with the policyholder. This form of settlement is commonly referred to as a "buy-back" of policies for future environmental liability. In addition, many of the agreements have also extinguished any insurance obligation which the Company may have for other claims, including but not limited to asbestos and other cumulative injury claims. The Company and its policyholders may also agree to settlements which extinguish any liability arising from known specified sites or claims. Where appropriate, these agreements also include indemnities and hold harmless provisions to protect the Company. The Company's general purpose in executing these agreements is to reduce the Company's potential environmental exposure and eliminate the risks presented by coverage litigation with the policyholder and related costs.

In establishing environmental reserves, the Company evaluates the exposure presented by each policyholder and the anticipated cost of resolution, if any. In the course of this analysis, the Company generally considers the probable liability, available coverage, relevant judicial interpretations and historical value of similar exposures. In addition, the Company considers the many variables presented, such as: the nature of the alleged activities of the policyholder at each site; the number of sites; the total number of potentially responsible parties at each site; the nature of the alleged environmental harm and the corresponding remedy at each site; the nature of government enforcement activities at each site; the ownership and general use of each site; the overall nature of the insurance relationship between the Company and the policyholder, including the role of any umbrella or excess insurance the Company has issued to the policyholder; the involvement of other insurers; the potential for other available coverage, including the number of years of coverage; the role, if any, of non-environmental claims or potential non-environmental claims in any resolution process; and the applicable law in each jurisdiction. The evaluation of the exposure presented by a policyholder can change as information concerning that policyholder and the many variables presented is developed. Conventional actuarial techniques are not used to estimate these reserves.

In its review of environmental reserves, the Company considers: past settlement payments; changing judicial and legislative trends; its reserves for the costs of litigating environmental coverage matters; the potential for policyholders with smaller exposures to be named in new clean-up actions for both on-and off-site waste disposal activities; the potential for adverse development; the potential for additional new claims beyond previous expectations; and the potential higher costs for new settlements.

The duration of the Company's investigation and review of these claims and the extent of time necessary to determine an appropriate estimate, if any, of the value of the claim to the Company vary significantly and are dependent upon a number of factors. These factors include, but are not limited to, the cooperation of the policyholder in providing claim information, the pace of underlying litigation or claim processes, the pace of coverage litigation between the policyholder and the Company and the willingness of the policyholder and the Company to negotiate, if appropriate, a resolution of any dispute pertaining to these claims. Because these factors vary from claim-to-claim and policyholder-by-policyholder, the Company cannot provide a meaningful average of the duration of an



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environmental claim. However, based upon the Company's experience in resolving these claims, the duration may vary from months to several years.

The Company continues to receive notices from policyholders tendering claims for the first time, frequently under policies issued prior to the mid-1980's. These policyholders continue to present smaller exposures, have fewer sites and are lower tier defendants. Further, in many instances, clean-up costs have been reduced because regulatory agencies are willing to accept risk-based site analyses and more efficient clean-up technologies. Over the past several years, the Company has experienced generally favorable trends in the number of new policyholders tendering environmental claims for the first time and in the number of pending declaratory judgment actions relating to environmental matters. However, the degree to which those favorable trends have continued has been less than anticipated. In addition, reserve development on existing environmental claims has been greater than anticipated. As a result, in 2013, 2012 and 2011, the Company increased its net environmental reserves by \$65 million, \$90 million and \$76 million, respectively.

Net environmental losses paid in 2013, 2012 and 2011 were \$84 million, \$84 million and \$86 million, respectively. At December 31, 2013, approximately 91% of the net environmental reserve (approximately \$314 million) was carried in a bulk reserve and included unresolved environmental claims, incurred but not reported environmental claims and the anticipated cost of coverage litigation disputes relating to these claims. The bulk reserve the Company carries is established and adjusted based upon the aggregate volume of in-process environmental claims and the Company's experience in resolving those claims. The balance, approximately 9% of the net environmental reserve (approximately \$30 million), consists of case reserves.

The following table displays activity for environmental losses and loss expenses and reserves:

(at and for the year ended December 31, in millions)	2013	2012	2011
<b>Beginning reserves:</b>			
Gross	\$ 352	\$ 346	\$ 354
Ceded	(5)	(5)	(3)
<b>Net</b>	<b>347</b>	341	351
<b>Incurred losses and loss expenses:</b>			
Gross	72	99	80
Ceded	(7)	(9)	(4)
<b>Net</b>	<b>65</b>	90	76
<b>Losses paid:</b>			
Gross	87	93	88
Ceded	(3)	(9)	(2)
<b>Net</b>	<b>84</b>	84	86
<b>Acquired reserves, foreign exchange and other:(1)</b>			
Gross	18		
Ceded	(2)		
<b>Net</b>	<b>16</b>		
<b>Ending reserves:</b>			

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Gross	355	352	346
Ceded	(11)	(5)	(5)

Net \$ 344 \$ 347 \$ 341

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(1) Represents acquired reserves of Dominion at November 1, 2013.

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**UNCERTAINTY REGARDING ADEQUACY OF ASBESTOS AND ENVIRONMENTAL RESERVES**

As a result of the processes and procedures discussed above, management believes that the reserves carried for asbestos and environmental claims at December 31, 2013 are appropriately established based upon known facts, current law and management's judgment. However, the uncertainties surrounding the final resolution of these claims continue, and it is difficult to determine the ultimate exposure for asbestos and environmental claims and related litigation. As a result, these reserves are subject to revision as new information becomes available and as claims develop. The continuing uncertainties include, without limitation, the risks and lack of predictability inherent in complex litigation, any impact from the bankruptcy protection sought by various asbestos producers and other asbestos defendants, a further increase or decrease in the cost to resolve, and/or the number of, asbestos and environmental claims beyond that which is anticipated, the emergence of a greater number of asbestos claims than anticipated as a result of extended life expectancies resulting from medical advances and lifestyle improvements, the role of any umbrella or excess policies the Company has issued, the resolution or adjudication of disputes pertaining to the amount of available coverage for asbestos and environmental claims in a manner inconsistent with the Company's previous assessment of these claims, the number and outcome of direct actions against the Company, future developments pertaining to the Company's ability to recover reinsurance for asbestos and environmental claims and the unavailability of other insurance sources potentially available to policyholders, whether through exhaustion of policy limits or through the insolvency of other participating insurers. In addition, uncertainties arise from the insolvency or bankruptcy of policyholders and other defendants. It is also not possible to predict changes in the legal, regulatory and legislative environment and their impact on the future development of asbestos and environmental claims. This environment could be affected by changes in applicable legislation and future court and regulatory decisions and interpretations, including the outcome of legal challenges to legislative and/or judicial reforms establishing medical criteria for the pursuit of asbestos claims. It is also difficult to predict the ultimate outcome of complex coverage disputes until settlement negotiations near completion and significant legal questions are resolved or, failing settlement, until the dispute is adjudicated. This is particularly the case with policyholders in bankruptcy where negotiations often involve a large number of claimants and other parties and require court approval to be effective. As part of its continuing analysis of asbestos and environmental reserves, the Company continues to study the implications of these and other developments. (Also see note 16 of notes to the consolidated financial statements).

Because of the uncertainties set forth above, additional liabilities may arise for amounts in excess of the Company's current reserves. In addition, the Company's estimate of claims and claim adjustment expenses may change. These additional liabilities or increases in estimates, or a range of either, cannot now be reasonably estimated and could result in income statement charges that could be material to the Company's operating results in future periods.

**INVESTMENT PORTFOLIO**

The Company's invested assets at December 31, 2013 were \$73.16 billion, of which 93% was invested in fixed maturity and short-term investments, 1% in equity securities, 1% in real estate and 5% in other investments. As a result of the acquisition of Dominion, total investments increased by \$2.62 billion at November 1, 2013, of which \$1.83 billion were fixed maturity investments. Because the primary purpose of the investment portfolio is to fund future claims payments, the Company employs a conservative investment philosophy. A significant majority of funds available for investment are deployed in a widely diversified portfolio of high quality, liquid taxable U.S. government, tax-exempt U.S. municipal and taxable corporate and U.S. agency mortgage-backed bonds.

The carrying value of the Company's fixed maturity portfolio at December 31, 2013 was \$63.96 billion. The Company closely monitors the duration of its fixed maturity investments, and investment purchases and sales are executed with the objective of having adequate funds available to

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satisfy the Company's insurance and debt obligations. The weighted average credit quality of the Company's fixed maturity portfolio, both including and excluding U.S. Treasury securities, was "Aa2" at both December 31, 2013 and 2012. Below investment grade securities represented 3.0% and 3.1% of the total fixed maturity investment portfolio at December 31, 2013 and 2012, respectively. The average effective duration of fixed maturities and short-term securities was 3.7 (3.9 excluding short-term securities) at December 31, 2013 and 3.2 (3.4 excluding short-term securities) at December 31, 2012. The increase in the average effective duration of the Company's fixed maturities and short-term securities at December 31, 2013 when compared to year-end 2012 primarily reflected an increase in interest rates during 2013. See the "Outlook" section in "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations."

The carrying values of investments in fixed maturities classified as available for sale at December 31, 2013 and 2012 were as follows:

(at December 31, in millions)	Carrying Value	2013 Average Credit Quality(1)	Carrying Value	2012 Average Credit Quality(1)
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,315	Aaa/Aa1	\$ 2,222	Aaa/Aa1
Obligations of states, municipalities and political subdivisions:				
Pre-refunded	9,518	Aa1	9,025	Aa1
All other	26,044	Aa1	29,656	Aa1
<b>Total obligations of states, municipalities and political subdivisions</b>	<b>35,562</b>		<b>38,681</b>	
Debt securities issued by foreign governments	2,577	Aaa/Aa1	2,257	Aaa
Mortgage-backed securities, collateralized mortgage obligations, and pass-through securities	2,424	A1	2,997	A1
All other corporate bonds and redeemable preferred stock:				
Financial:				
Bank	2,314	Aa3	1,808	A1
Insurance	605	A2	433	A1
Finance/leasing	68	Baa1	39	Baa3
Brokerage and asset management	30	A1	34	A2
<b>Total financial</b>	<b>3,017</b>		<b>2,314</b>	
Industrial	12,859	A3	12,076	A3
Public utility	2,166	A3	2,151	A3
Canadian municipal securities(2)	1,207	Aa1	643	Aa1
Sovereign corporate securities(3)	756	Aaa	1,011	Aaa
Commercial mortgage-backed securities and project loans(4)	475	Aaa	453	Aaa
Asset-backed and other	598	A1	588	A2
<b>Total all other corporate bonds and redeemable preferred stock</b>	<b>21,078</b>		<b>19,236</b>	
<b>Total fixed maturities</b>	<b>\$ 63,956</b>	<b>Aa2</b>	<b>\$ 65,393</b>	<b>Aa2</b>

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(1)

Rated using external rating agencies or by the Company when a public rating does not exist.

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- (2) As a result of the acquisition of Dominion, total investments in Canadian municipal securities increased by \$473 million at November 1, 2013.
- (3) Sovereign corporate securities include corporate securities that are backed by a government and include sovereign banks and securities issued under the Temporary Liquidity Guaranty and the Federal Ship Financing Programs.
- (4) Included in commercial mortgage-backed securities and project loans at December 31, 2013 and 2012 were \$45 million and \$50 million of securities guaranteed by the U.S. government, respectively, and \$14 million of securities guaranteed by government sponsored enterprises at both dates.

The following table sets forth the Company's fixed maturity investment portfolio rated using external ratings agencies or by the Company when a public rating does not exist:

(at December 31, 2013, in millions)	Carrying Value	Percent of Total Carrying Value
Quality Rating:		
Aaa	\$ 27,209	42.5%
Aa	19,430	30.4
A	9,331	14.6
Baa	6,054	9.5
Total investment grade	62,024	97.0
Below investment grade	1,932	3.0
Total fixed maturities	\$ 63,956	100.0%

The amortized cost and fair value of fixed maturities by contractual maturity follow. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(at December 31, 2013, in millions)	Amortized Cost	Fair Value
Due in one year or less	\$ 8,386	\$ 8,525
Due after 1 year through 2 years	7,253	7,534
Due after 2 years through 3 years	5,152	5,458
Due after 3 years through 4 years	4,200	4,442
Due after 4 years through 5 years	3,754	3,973
Due after 5 years through 10 years	17,225	17,579
Due after 10 years	13,963	14,021
	59,933	61,532
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2,263	2,424
Total	\$ 62,196	\$ 63,956

*Obligations of States, Municipalities and Political Subdivisions*

The Company's fixed maturity investment portfolio at December 31, 2013 and 2012 included \$35.56 billion and \$38.68 billion, respectively, of securities which are obligations of states, municipalities and political subdivisions (collectively referred to as the municipal bond portfolio). The municipal bond portfolio is diversified across the United States, the District of Columbia and Puerto Rico and includes general obligation and revenue bonds issued by states, cities, counties, school districts and similar issuers. Included in the municipal bond portfolio at December 31, 2013 and 2012 were \$9.52 billion and

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\$9.03 billion, respectively, of pre-refunded bonds, which are bonds for which states or municipalities have established irrevocable trusts, almost exclusively comprised of U.S. Treasury securities, which were created to satisfy their responsibility for payments of principal and interest. The irrevocable trusts are verified as to their sufficiency by an independent verification agent of the underwriter, issuer or trustee. In August 2013, Moody's Investor Service revised its outlook for U.S. states to stable from negative, and in December 2013, Moody's revised its local government outlook to stable from negative.

The following table shows the geographic distribution of the \$26.04 billion of municipal bonds at December 31, 2013 that were not pre-refunded.

(at December 31, 2013, in millions)	State General Obligation	Local General Obligation	Revenue	Total Carrying Value	Average Credit Quality(1)
State:					
Texas	\$ 390	\$ 2,297	\$ 1,186	\$ 3,873	Aaa/Aa1
California	45	1,418	387	1,850	Aa2
Washington	244	735	518	1,497	Aa1
Virginia	144	607	720	1,471	Aaa/Aa1
Illinois	150	776	272	1,198	Aa2
Minnesota	186	725	177	1,088	Aaa/Aa1
Massachusetts	126	30	895	1,051	Aaa/Aa1
Florida	276	38	688	1,002	Aa1
North Carolina	106	605	200	911	Aaa
Arizona		483	397	880	Aa1
Maryland	285	345	143	773	Aaa/Aa1
Colorado		551	216	767	Aa1
Georgia	126	281	280	687	Aaa/Aa1
All others(2)(3)	1,480	3,349	4,167	8,996	Aa1
<b>Total</b>	<b>\$ 3,558</b>	<b>\$ 12,240</b>	<b>\$ 10,246</b>	<b>\$ 26,044</b>	<b>Aa1</b>

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- (1) Rated using external rating agencies or by the Company when a public rating does not exist. Ratings shown are the higher of the rating of the underlying issuer or the insurer in the case of securities enhanced by third-party insurance for the payment of principal and interest in the event of issuer default.
- (2) No other single state accounted for 2.5% or more of the total non-pre-refunded municipal bonds.
- (3) The Company owns \$64 million of non-pre-refunded bonds issued by Puerto Rico, of which \$45 million are enhanced by third-party insurance for the payment of principal and interest in the event of an issuer default. The Company does not own any municipal securities issued by the city of Detroit, MI.



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The following table displays the funding sources for the \$10.25 billion of municipal bonds identified as revenue bonds in the foregoing table at December 31, 2013.

(at December 31, 2013, in millions)	Carrying Value	Average Credit Quality(1)
Source:		
Water and sewer	\$ 3,479	Aaa/Aa1
Higher education	1,806	Aaa/Aa1
Power and utilities	985	Aa2
Transportation	930	Aa1
Special tax	658	Aa1
Lease	437	Aa2
Housing	107	Aaa/Aa1
Government funded/grant revenue	104	Aaa
Healthcare	92	Aa2
General fund	57	Aa3
Industrial revenue	52	A1
Property tax	24	Aa2
Other revenue sources	1,515	Aaa/Aa1
<b>Total</b>	<b>\$ 10,246</b>	<b>Aa1</b>

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(1)

Rated using external rating agencies or by the Company when a public rating does not exist. Ratings shown are the higher of the rating of the underlying issuer or the insurer in the case of securities enhanced by third-party insurance for the payment of principal and interest in the event of issuer default.

The Company bases its investment decision on the underlying credit characteristics of the municipal security. While its municipal bond portfolio includes a number of securities that were enhanced by third-party insurance for the payment of principal and interest in the event of an issuer default, the Company does not rely on enhanced credit characteristics provided by such third-party insurance as part of its investing decisions. Of the insured municipal securities in the Company's investment portfolio at December 31, 2013, approximately 99% were rated at "A3" or above, and approximately 91% were rated at "Aa3" or above, without the benefit of insurance. The Company believes that a loss of the benefit of insurance would not result in a material adverse impact on the Company's results of operations, financial position or liquidity, due to the underlying credit strength of the issuers of the securities, as well as the Company's ability and intent to hold the securities. The average credit rating of the underlying issuers of these securities was "Aa2" at December 31, 2013. The average credit rating of the entire municipal bond portfolio was "Aa1" at December 31, 2013 with and without the enhancement provided by third-party insurance.

Table of Contents*Debt Securities Issued by Foreign Governments*

The following table shows the geographic distribution of the Company's long-term fixed maturity investments in debt securities issued by foreign governments at December 31, 2013.

(at December 31, 2013, in millions)	Carrying Value	Average Credit Quality(1)
Foreign Government:		
Canada	\$ 1,350	Aaa
United Kingdom	971	Aaa/Aa1
Norway	97	Aaa
All Others(2)(3)	159	Aaa/Aa1
<b>Total</b>	<b>\$ 2,577</b>	<b>Aaa/Aa1</b>

- 
- (1) Rated using external rating agencies or by the Company when a public rating does not exist. Ratings shown are the higher of the rating of the underlying issuer or the insurer in the case of securities enhanced by third-party insurance for the payment of principal and interest in the event of issuer default.
- (2) The Company does not have direct exposure to sovereign debt issued by the Republic of Ireland, Italy, Greece, Portugal or Spain.
- (3) No other country accounted for 2.5% or more of total debt securities issued by foreign governments.

The following table shows the Company's Eurozone exposure at December 31, 2013 to all debt securities issued by foreign governments, financial companies, sovereign corporations (including sovereign banks) whose securities are backed by the respective country's government and all other

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corporate securities (comprised of industrial corporations and utility companies) which could be affected if economic conditions deteriorated due to a prolonged recession.

(at December 31, 2013, in millions)	Debt Securities Issued by Foreign Governments				Corporate Securities			
	Average		Financial Average		Sovereign Corporates Average		All Other Average	
	Carrying Value	Credit Quality(1)	Carrying Value	Credit Quality(1)	Carrying Value	Credit Quality(1)	Carrying Value	Credit Quality(1)
<b>Eurozone Periphery</b>								
Spain	\$		\$ 11	Baa2	\$		\$ 36	Baa1
Ireland			2	A3			54	A3
Italy							17	Ba1
Greece							2	Baa2
Portugal								
Subtotal			13				109	
<b>Eurozone Non-Periphery</b>								
Germany	41	Aaa	3	Baa1	277	Aaa	256	A3
France	28	Aa1	18	A2	3	Aaa/Aa1	371	A2
Netherlands			45	A1	84	Aaa/Aa1	305	A2
Austria					7	Aaa/Aa1		
Finland	17	Aaa					13	Ba1
Belgium							166	A3
Luxembourg							22	Ba1
Subtotal	86		66		371		1,133	
<b>Total</b>	<b>\$ 86</b>		<b>\$ 79</b>		<b>\$ 371</b>		<b>\$ 1,242</b>	

(1)

Rated using external rating agencies or by the Company when a public rating does not exist. The table includes \$116 million of short-term securities which have the highest ratings issued by external rating agencies for short-term issuances. For purposes of this table, the short-term securities, which are rated "A-1+" and/or "P-1," are included as "Aaa" rated securities.

In addition to fixed maturities noted in the foregoing table, the Company has exposure totaling \$267 million to private equity limited partnerships and real estate partnerships (both of which are included in other investments in the Company's consolidated balance sheet) whose primary investing focus is across Europe. The Company has unfunded commitments totaling \$178 million to these partnerships. The Company also has \$5 million of nonredeemable preferred stock (included in equity securities on the Company's consolidated balance sheet) issued by companies in the Eurozone.

*Mortgage-Backed Securities, Collateralized Mortgage Obligations and Pass-Through Securities*

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The Company's fixed maturity investment portfolio at December 31, 2013 and 2012 included \$2.42 billion and \$3.00 billion, respectively, of residential mortgage-backed securities, including pass-through-securities and collateralized mortgage obligations (CMO), all of which are subject to prepayment risk (either shortening or lengthening of duration). While prepayment risk for securities and its effect on income cannot be fully controlled, particularly when interest rates move dramatically, the Company's investment strategy generally favors securities that reduce this risk within expected interest rate ranges. Included in the totals at December 31, 2013 and 2012 were \$1.06 billion and \$1.44 billion, respectively, of GNMA, FNMA and FHLMC (excluding FHA project loans) guaranteed residential mortgage-backed pass-through securities classified as available for sale. Also included in those totals were residential CMOs classified as available for sale with a fair value of \$1.36 billion and

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\$1.56 billion, at December 31, 2013 and 2012, respectively. Approximately 42% and 43% of the Company's CMO holdings at December 31, 2013 and 2012, respectively, were guaranteed by or fully collateralized by securities issued by GNMA, FNMA or FHLMC. The average credit rating of the \$790 million and \$893 million of non-guaranteed CMO holdings at December 31, 2013 and 2012, respectively, was "Ba3" and "B2," respectively. The average credit rating of all of the above securities was "A1" at both December 31, 2013 and 2012.

The Company makes investments in residential CMOs that are either guaranteed by GNMA, FNMA or FHLMC, or if not guaranteed, are senior or super-senior positions within their respective securitizations. Both guaranteed and non-guaranteed residential CMOs allocate the distribution of payments from the underlying mortgages among different classes of bondholders. In addition, non-guaranteed residential CMOs provide structures that allocate the impact of credit losses to different classes of bondholders. Senior and super-senior CMOs are protected, to varying degrees, from credit losses as those losses are initially allocated to subordinated bondholders. The Company's investment strategy is to purchase CMO tranches that are expected to offer the most favorable return given the Company's assessment of associated risks. The Company does not purchase residual interests in CMOs.

*Alternative Documentation Mortgages and Sub-Prime Mortgages*

At December 31, 2013 and 2012, the Company's fixed maturity investment portfolio included collateralized mortgage obligations backed by alternative documentation mortgages and asset-backed securities collateralized by sub-prime mortgages with a collective fair value of \$293 million and \$347 million, respectively (comprising less than 1% of the Company's total fixed maturity investments at both dates). The Company defines sub-prime mortgage-backed securities as investments in which the underlying loans primarily exhibit one or more of the following characteristics: low FICO scores, above-prime interest rates, high loan-to-value ratios or high debt-to-income ratios. Alternative documentation securitizations are those in which the underlying loans primarily meet the government-sponsored entities' requirements for credit score but do not meet the government-sponsored entities' guidelines for documentation, property type, debt and loan-to-value ratios. The average credit rating on these securities and obligations held by the Company was "Ba2" and "Ba1" at December 31, 2013 and 2012, respectively. The Company does not believe this portfolio exposes it to a material adverse impact on its results of operations, financial position or liquidity, due to the portfolio's relatively small size.

*Commercial Mortgage-Backed Securities and Project Loans*

At December 31, 2013 and 2012, the Company held commercial mortgage-backed securities (including FHA project loans) of \$475 million and \$453 million, respectively. The Company does not believe this portfolio exposes it to a material adverse impact on its results of operations, financial position or liquidity, due to the portfolio's relatively small size and the underlying credit strength of these securities.

*Equity Securities Available for Sale, Real Estate and Short-Term Investments*

See note 1 of notes to the Company's consolidated financial statements for further information about these invested asset classes.

*Other Investments*

The Company also invests much smaller amounts in equity securities, real estate, private equity limited partnerships, hedge funds, and real estate partnerships and joint ventures, which are subject to more volatility than the Company's fixed maturity investments. These asset classes have historically provided a higher return than fixed maturities but are subject to more volatility. At December 31, 2013 and 2012, the carrying value of the Company's other investments was \$3.44 billion and \$3.43 billion, respectively.

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*Securities Lending*

The Company has engaged in securities lending activities from which it generates net investment income by lending certain of its investments to other institutions for short periods of time. At December 31, 2013 and 2012, the Company had \$131 million and \$403 million of securities on loan, respectively, as part of a tri-party lending agreement. The average monthly balance of securities on loan during 2013 and 2012 was \$168 million and \$197 million, respectively. Borrowers of these securities provide collateral equal to at least 102% of the market value of the loaned securities plus accrued interest. The Company has not incurred any investment losses in its securities lending program for the years ended December 31, 2013, 2012 and 2011.

*Lloyd's Trust Deposit*

The Company utilizes a Lloyd's trust deposit, whereby owned securities with a fair value of approximately \$181 million held by a wholly-owned subsidiary at December 31, 2013 were pledged into a Lloyd's trust account to provide a portion of the capital needed to support the Company's obligations at Lloyd's.

*Net Unrealized Investment Gains*

The net unrealized investment gains that were included as a separate component of accumulated other comprehensive income were as follows:

(at December 31, in millions)	2013	2012	2011
Fixed maturities	\$ 1,760	\$ 4,564	\$ 4,238
Equity securities	257	183	145
Other investments	13	14	16
Unrealized investment gains before tax	2,030	4,761	4,399
Tax expense	708	1,658	1,528
Net unrealized investment gains at end of year	\$ 1,322	\$ 3,103	\$ 2,871

Net unrealized investment gains at December 31, 2013 declined from the prior year-end, primarily reflecting the impact of an increase in market interest rates during 2013. Net unrealized investment gains at December 31, 2012 increased over the prior year-end, primarily reflecting the impact of a decline in market interest rates during 2012.

The following table summarizes, for all fixed maturities and equity securities reported at fair value for which fair value is less than 80% of amortized cost at December 31, 2013, the gross unrealized investment loss by length of time those securities have continuously been in an unrealized loss position of greater than 20% of amortized cost:

(in millions)	Period For Which Fair Value Is Less Than 80% of Amortized Cost				Total
	3 Months or Less	Greater Than 3 Months, 6 Months or Less	Greater Than 6 Months, 12 Months or Less	Greater Than 12 Months	
<b>Fixed maturities:</b>					
Mortgage-backed securities	\$	\$	\$	\$	\$
Other	7	3	1	3	14
Total fixed maturities	7	3	1	3	14
<b>Equity securities</b>					

Total                                    \$        7    \$        3    \$        1    \$        3    \$    14

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These unrealized investment losses at December 31, 2013 represent less than 1% of the combined fixed maturity and equity security portfolios on a pretax basis and less than 1% of shareholders' equity on an after-tax basis.

For fixed maturity investments where fair value is less than the carrying value and the Company did not reach a decision to impair, the Company continues to have the intent and ability to hold such investments to a projected recovery in value, which may not be until maturity.

At December 31, 2013 and 2012, below investment grade securities comprised 3.0% and 3.1% of the Company's fixed maturity investment portfolio, respectively. Included in below investment grade securities at December 31, 2013 were securities in an unrealized loss position that, in the aggregate, had an amortized cost of \$390 million and a fair value of \$373 million, resulting in a net pretax unrealized investment loss of \$17 million. These securities in an unrealized loss position represented less than 1% of both the total amortized cost and the fair value of the fixed maturity portfolio at December 31, 2013 and accounted for 2.4% of the total gross pretax unrealized investment loss in the fixed maturity portfolio at December 31, 2013.

### *Impairment Charges*

Impairment charges included in net realized investment gains in the consolidated statement of income were as follows:

(for the year ended December 31, in millions)	2013	2012	2011
<b>Fixed maturities</b>			
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$	\$	\$
Obligations of states, municipalities and political subdivisions			
Debt securities issued by foreign governments			
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2	4	13
All other corporate bonds	3	4	5
Redeemable preferred stock			
Total fixed maturities	5	8	18
<b>Equity securities</b>			
Common stock	5	3	6
Non-redeemable preferred stock		1	
Total equity securities	5	4	6
<b>Other investments</b>	5	3	1
Total	\$ 15	\$ 15	\$ 25

Following are the pretax realized losses on investments sold during the year ended December 31, 2013:

(for the year ended December 31, 2013, in millions)	Loss	Fair Value
Fixed maturities	\$ 25	\$ 688
Equity securities	1	27
Total	\$ 26	\$ 715



Purchases and sales of investments are based on cash requirements, the characteristics of the insurance liabilities and current market conditions. The Company identifies investments to be sold to

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achieve its primary investment goals of assuring the Company's ability to meet policyholder obligations as well as to optimize investment returns, given these obligations.

**CATASTROPHE MODELING**

The Company uses various analyses and methods, including proprietary and third-party computer modeling processes, to analyze catastrophic events and the risks associated with them. The Company uses these analyses and methods to make underwriting and reinsurance decisions designed to manage its exposure to catastrophic events. There are no industry-standard methodologies or assumptions for projecting catastrophe exposure. Accordingly, catastrophe estimates provided by different insurers may not be comparable.

The Company actively monitors and evaluates changes in third-party models and, when necessary, calibrates the catastrophe risk model estimates delivered via its own proprietary modeling processes. The Company considers historical loss experience, recent events, underwriting practices, market share analyses, external scientific analysis and various other factors to account for non-modeled losses to refine its proprietary view of catastrophe risk. These proprietary models are continually updated as new information emerges.

The tables below set forth the probabilities that estimated losses, comprising claims and allocated claim adjustment expenses (but excluding unallocated claim adjustment expenses), from a single event occurring in a one-year timeframe will equal or exceed the indicated loss amounts (expressed in dollars and as a percentage of the Company's common equity), based on the current version of the proprietary and third-party computer models utilized by the Company at December 31, 2013. For example, on the basis described below the tables, the Company estimates that there is a one percent chance that the Company's loss from a single U.S. hurricane in a one-year timeframe would equal or exceed \$1.3 billion, or 6% of the Company's common equity at December 31, 2013.

Likelihood of Exceedance(1)	Dollars (in billions)	
	Single U.S. Hurricane	Single U.S. and Canadian Earthquake
2.0% (1-in-50)	\$ 1.0	\$ 0.4
1.0% (1-in-100)	\$ 1.3	\$ 0.6
0.4% (1-in-250)	\$ 2.2	\$ 0.8
0.1% (1-in-1,000)	\$ 4.7	\$ 1.7

Likelihood of Exceedance	Percentage of Common Equity(2)	
	Single U.S. Hurricane	Single U.S. and Canadian Earthquake
2.0% (1-in-50)	4%	2%
1.0% (1-in-100)	6%	2%
0.4% (1-in-250)	9%	3%
0.1% (1-in-1,000)	20%	7%

(1)

An event that has, for example, a 2% likelihood of exceedance is sometimes described as a "1-in-50 year event." As noted above, however, the probabilities in the table represent the likelihood of losses from a single event equaling or exceeding the indicated threshold loss amount in a one-year timeframe, not over a multi-year timeframe. Also, because the probabilities relate to a single event, the probabilities do not address the likelihood of more than one event occurring in a particular period, and, therefore, the amounts do not address potential aggregate catastrophe losses occurring in a one-year timeframe.

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- (2) The percentage of common equity is calculated by dividing (a) indicated loss amounts in dollars by (b) total common equity excluding net unrealized investment gains and losses, net of taxes. Net unrealized investment gains and losses can be significantly impacted by both discretionary and other economic factors and are not necessarily indicative of operating trends. Accordingly, the Company's management uses the percentage of common equity calculated on this basis as a metric to evaluate the potential impact of a single hurricane or single earthquake on the Company's financial position for purposes of making underwriting and reinsurance decisions.

The threshold loss amounts in the tables above, which are based on the Company's in-force portfolio at December 31, 2013 and catastrophic reinsurance program at January 1, 2014, are net of reinsurance, after-tax and exclude unallocated claim adjustment expenses, which historically have been less than 10% of loss estimates. The amounts for hurricanes reflect U.S. exposures and include property exposures, property residual market exposures and an adjustment for certain non-property exposures. The hurricane loss amounts are based on the Company's catastrophe risk model estimates and include losses from the hurricane hazards of wind and storm surge. The amounts for earthquakes reflect U.S. and Canadian property and workers' compensation exposures. The Company does not believe that the inclusion of hurricane or earthquake losses arising from other geographical areas or other exposures would materially change the estimated threshold loss amounts.

Catastrophe modeling relies upon inputs based on experience, science, engineering and history. These inputs reflect a significant amount of judgment and are subject to changes which may result in volatility in the modeled output. Catastrophe modeling output may also fail to account for risks that are outside the range of normal probability or are otherwise unforeseeable. Catastrophe modeling assumptions include, among others, the portion of purchased reinsurance that is collectible after a catastrophic event, which may prove to be materially incorrect. Consequently, catastrophe modeling estimates are subject to significant uncertainty. In the tables above, the uncertainty associated with the estimated threshold loss amounts increases significantly as the likelihood of exceedance decreases. In other words, in the case of a relatively more remote event (e.g., 1-in-1,000), the estimated threshold loss amount is relatively less reliable. Actual losses from an event could materially exceed the indicated threshold loss amount. In addition, more than one such event could occur in any period.

Moreover, the Company is exposed to the risk of material losses from other than property and workers' compensation coverages arising out of hurricanes and earthquakes, and it is exposed to catastrophe losses from perils other than hurricanes and earthquakes, such as tornadoes and other windstorms, hail, wildfires, severe winter weather, floods, volcanic eruptions, tsunamis and acts of terrorism.

For more information about the Company's exposure to catastrophe losses, see "Item 1A Risk Factors Catastrophe losses could materially and adversely affect our results of operations, our financial position and/or liquidity, and could adversely impact our ratings, our ability to raise capital and the availability and cost of reinsurance" and "Item 1A Risk Factors We may be adversely affected if our pricing and capital models provide materially different indications than actual results."

**CHANGING CLIMATE CONDITIONS**

Severe weather events over the last several years have underscored the unpredictability of future climate trends and created uncertainty regarding insurers' exposures to financial loss as a result of catastrophes and other weather-related events. For example, over the last decade hurricane activity has impacted areas further inland than previously experienced, thus expanding the Company's potential for losses from hurricanes. Additionally, both the frequency and severity of tornado and hail storms in the United States have been greater in recent years. Further, any reduction in arctic sea ice may contribute to rising sea levels that could impact flooding in coastal areas. Accordingly, the Company may be

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subject to increased losses from catastrophes and other weather-related events. Additionally, the Company's catastrophe models may be less reliable due to the increased unpredictability, frequency and severity of severe weather events.

The Company discusses how potentially changing climate conditions may present other issues for its business under "Risk Factors" in Item 1A of this report and under " Outlook" herein. For example, among other things:

Increasingly unpredictable and severe weather conditions could result in increased frequency and severity of claims under policies issued by the Company. See "Risk Factors Catastrophe losses could materially and adversely affect our results of operations, our financial position and/or liquidity, and could adversely impact our ratings, our ability to raise capital and the availability and cost of reinsurance" and " Outlook Underwriting Gain/Loss."

Changing climate conditions could also impact the creditworthiness of issuers of securities in which the Company invests. For example, water supply adequacy could impact the creditworthiness of bond issuers in the Southwestern United States, and more frequent and/or severe hurricanes could impact the creditworthiness of issuers in the Southeastern United States, among other areas. See "Risk Factors Our investment portfolio may suffer reduced returns or material realized or unrealized losses."

Increased regulation adopted in response to potential changes in climate conditions may impact the Company and its customers. For example, state insurance regulation could impact the Company's ability to manage property exposures in areas vulnerable to significant climate driven losses. If the Company is unable to implement risk based pricing, modify policy terms or reduce exposures to the extent necessary to address rising losses related to catastrophes and smaller scale weather events (should those increased losses occur), its business may be adversely affected. See "Risk Factors Catastrophe losses could materially and adversely affect our results of operations, our financial position and/or liquidity, and could adversely impact our ratings, our ability to raise capital and the availability and cost of reinsurance."

The full range of potential liability exposures related to climate change continues to evolve. Through the Company's Emerging Issues Committee and its Committee on Climate, Energy and the Environment, the Company works with its business units and corporate groups, as appropriate, to identify and try to assess climate change-related liability issues, which are continually evolving and often hard to fully evaluate. See "Risk Factors The effects of emerging claim and coverage issues on our business are uncertain."

Climate change regulation also could increase the Company's customers' costs of doing business. For example, insureds faced with carbon management regulatory requirements may have less available capital for investment in loss prevention and safety features which may, over time, increase loss exposures. Also, increased regulation may result in reduced economic activity, which would decrease the amount of insurable assets and businesses.

The Company regularly reviews emerging issues, such as changing climate conditions, to consider potential changes to its modeling and the use of such modeling, as well as to help determine the need for new underwriting strategies, coverage modifications or new products.

**REINSURANCE RECOVERABLES**

The Company reinsures a portion of the risks it underwrites in order to control its exposure to losses. For additional discussion regarding the Company's reinsurance coverage, see "Part I Item 1 Reinsurance."

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The following table summarizes the composition of the Company's reinsurance recoverables:

(at December 31, in millions)	2013	2012
Gross reinsurance recoverables on paid and unpaid claims and claim adjustment expenses	\$ 4,707	\$ 5,256
Allowance for uncollectible reinsurance	(239)	(258)
<b>Net reinsurance recoverables</b>	<b>4,468</b>	<b>4,998</b>
Mandatory pools and associations	1,897	2,549
Structured settlements	3,348	3,165
<b>Total reinsurance recoverables</b>	<b>\$ 9,713</b>	<b>\$ 10,712</b>

The \$530 million decline in net reinsurance recoverables from December 31, 2012 primarily reflected the impacts of (i) cash collections, including commutation agreements and (ii) net favorable prior year reserve development, partially offset by (iii) the acquisition of Dominion. As a result of the acquisition of Dominion, total reinsurance recoverables increased by \$352 million at November 1, 2013. The \$652 million decline in mandatory pools and associations from December 31, 2012 primarily reflected catastrophe-related collections and, to a lesser extent the impact of the sale of renewal rights, in connection with the Company's National Flood Insurance Program business.

The following table presents the Company's top five reinsurer groups by reinsurance recoverable at December 31, 2013 (in millions). Also included is the A.M. Best rating of each reinsurer group at February 13, 2014:

Reinsurer Group	Reinsurance Recoverable	A.M. Best Rating of Group's Predominant Reinsurer	
Munich Re Group	\$ 525	A+	second highest of 16 ratings
Swiss Re Group	491	A+	second highest of 16 ratings
Alleghany Group	254	A	third highest of 16 ratings
XL Capital Group	242	A	third highest of 16 ratings
NKSJ Holdings Inc. Group	242	A+	second highest of 16 ratings

At December 31, 2013, the Company held \$1.37 billion of collateral in the form of letters of credit, funds and trust agreements held to fully or partially collateralize certain reinsurance recoverables.

For a discussion of a pending reinsurance dispute pertaining to a portion of the Company's reinsurance recoverable from the Munich Re Group in the foregoing table, see note 16 of notes to the consolidated financial statements.

Included in reinsurance recoverables are amounts related to structured settlements, which are annuities purchased from various life insurance companies to settle certain personal physical injury claims, of which workers' compensation claims comprise a significant portion. In cases where the Company did not receive a release from the claimant, the amount due from the life insurance company related to the structured settlement is included in the Company's consolidated balance sheet as a reinsurance recoverable and the related claim cost is included in the liability for claims and claim adjustment expense reserves, as the Company retains the contingent liability to the claimant. If it is expected that the life insurance company is not able to pay, the Company would recognize an impairment of the related reinsurance recoverable if, and to the extent, the purchased annuities are not covered by state guaranty associations. In the event that the life insurance company fails to make the required annuity payments, the Company would be required to make such payments. The following table presents the Company's top five groups by structured settlements at December 31, 2013 (in

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millions). Also included is the A.M. Best rating of the Company's predominant insurer from each insurer group at February 13, 2014:

Group	Structured Settlements	A.M. Best Rating of Group's Predominant Insurer	
Fidelity & Guaranty Life Group	\$ 972	B++	fifth highest of 16 ratings
MetLife Group	456	A+	second highest of 16 ratings
Genworth Financial Group	429	A	third highest of 16 ratings
John Hancock Group	255	A+	second highest of 16 ratings
Symetra Financial Group	248	A	third highest of 16 ratings

Reinsurance companies and life insurance companies have been negatively impacted by turbulent economic conditions, significant catastrophe events and investment portfolio challenges in recent years. A number of such companies have been subjected to downgrades and/or negative outlook changes by various ratings agencies, including those with which the Company conducts business. The Company considers these factors in assessing the adequacy of its allowance for uncollectible amounts.

**OUTLOOK**

The following discussion provides outlook information for certain key drivers of the Company's results of operations and capital position.

*Premiums.* The Company's earned premiums are a function of net written premium volume. Net written premiums comprise both renewal business and new business and are recognized as earned premium over the life of the underlying policies. When business renews, the amount of net written premiums associated with that business may increase or decrease (renewal premium change) as a result of increases or decreases in rate and/or insured exposures, which the Company considers as a measure of units of exposure (such as the number and value of vehicles or properties insured). Net written premiums from both renewal and new business, and therefore earned premiums, are impacted by competitive market conditions as well as general economic conditions, which, particularly in the case of the Business Insurance segment, affect audit premium adjustments, policy endorsements and mid-term cancellations. Net written premiums are also impacted by the structure of reinsurance programs and related costs.

Given the possibility that more active weather patterns such as the Company experienced in a number of recent periods may continue, as well as the possibility that interest rates may remain low for some period of time, along with the current level of profitability in certain of its product lines, the Company has undertaken various efforts, and expects to undertake additional efforts, to improve its underwriting margins. These efforts include seeking improved rates where the Company believes it is appropriate, as well as improved terms and conditions, on many of its insurance products, and also include other initiatives, such as reducing operating expenses and acquisition costs. In the Agency Automobile line of business, given new business levels, the Company has undertaken various actions (which are discussed in more detail in the "Underwriting Gain/Loss" section below) to reduce expenses and costs in order to improve underwriting margins and enable it to have a more competitively priced product. These and other actions to improve profitability with respect to Agency Automobile or the Company's other business units may not be successful and/or may result in lower retention and new business levels and therefore lower business volumes. If these actions are not effective, the Company may need to explore other actions or initiatives to improve its competitive position and profitability. Refer to "Part I Item 1A Risk Factors The intense competition that we face could harm our ability to maintain or increase our business volumes and our profitability" and " Disruptions to our relationships with our independent agents and brokers could adversely affect us."

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Overall, the Company expects retention levels (the amount of expiring premium that renews, before the impact of renewal premium changes) will remain strong relative to historical experience. The Company also expects to continue to achieve, in the aggregate, price increases on renewal business during 2014 that exceed loss cost trends. In the Business Insurance segment, the Company expects that renewal premium changes during 2014 will be broadly consistent with the levels attained in the fourth quarter of 2013 and will be driven by both positive renewal rate changes and, subject to the economic uncertainties discussed below, growth in insured exposures. In the Financial, Professional & International Insurance segment, the Company expects that renewal premium changes during 2014 will be broadly consistent with 2013. With respect to surety, the Company expects net written premium volumes during 2014 that are broadly consistent with 2013. In the Personal Insurance segment, the Company expects both Agency Automobile and Agency Homeowners and Other renewal premium changes during 2014 will decline as compared to 2013, but the Company expects such renewal premium changes will remain positive and exceed underlying loss cost trends, assuming weather patterns and other loss trends consistent with the Company's expectations. Renewal premium changes for both Agency Automobile and Agency Homeowners and Other in 2014 are expected to be driven by both positive renewal rate changes (based on the Company's actions to file for rate increases) and, subject to the economic uncertainties discussed below, growth in insured exposures. The need for state regulatory approval for changes to personal property and casualty insurance prices, as well as competitive market conditions, may impact the timing and extent of renewal premium changes.

The pricing environment for new business generally has less of an impact on underwriting profitability than renewal rate changes, given the volume of new business relative to renewal business. Property and casualty insurance market conditions are expected to remain competitive during 2014 for new business, not only in Business Insurance and Financial, Professional & International Insurance, but especially in Personal Insurance, where price comparison technology used by agents and brokers, sometimes referred to as "comparative raters," has facilitated the process of generating multiple quotes, thereby increasing price comparison on new business and, increasingly, on renewal business.

Modest economic growth in the United States experienced in recent periods may or may not continue, or may continue at a slower rate for an extended period of time. In addition, some economic conditions, such as employment rates, may continue to be weak. Future actions or inactions of the United States government, such as a failure to increase the government debt limit or a shutdown of the federal government, could increase the actual or perceived risk that the U.S. may not ultimately pay its obligations when due and may disrupt financial markets. Further, general uncertainty regarding the U.S. Federal budget and taxes, implementation of the Affordable Care Act and the regulatory environment has added to the uncertainty regarding economic conditions generally. If weak economic conditions persist or deteriorate, the resulting low levels of economic activity could impact exposure changes at renewal and the Company's ability to write business at acceptable rates. Additionally, low levels of economic activity could adversely impact audit premium adjustments, policy endorsements and mid-term cancellations after policies are written. All of the foregoing, in turn, could adversely impact net written premiums during 2014, and because earned premiums are a function of net written premiums, earned premiums could be adversely impacted in 2014.

*Underwriting Gain/Loss.* The Company's underwriting gain/loss can be significantly impacted by catastrophe losses and net favorable or unfavorable prior year reserve development, as well as underlying underwriting margins.

Catastrophe and other weather-related losses are inherently unpredictable from period to period. The Company experienced significant catastrophe and other weather-related losses in a number of recent periods which adversely impacted its results of operations. The Company's results of operations would continue to be adversely impacted if significant catastrophe and other weather-related losses were to occur during 2014.

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For the last several years, the Company's results have included significant amounts of net favorable prior year reserve development, although at lower levels in some recent years, driven by better than expected loss experience in all of the Company's segments. The lower level of net favorable prior year reserve development in a number of recent periods may have been in part due to the Company's reserve estimation process incorporating those factors that led to the higher levels of net favorable prior year reserve development in previous years. If that trend continues, the better than expected loss experience may continue at these recent lower levels, or even lower levels. However, given the inherent uncertainty in estimating claims and claim adjustment expense reserves, loss experience could develop such that the Company recognizes higher or lower levels of favorable prior year reserve development, no favorable prior year reserve development or unfavorable prior year reserve development in future periods. In addition, the ongoing review of prior year claims and claim adjustment expense reserves, or other changes in current period circumstances, may result in the Company revising current year loss estimates upward or downward in future periods of the current year.

In Business Insurance, the Company expects that the anticipated impact of increases in renewal premium changes, partially offset by consistent modest loss cost trends, and assuming weather patterns consistent with the Company's expectations, will likely result in underlying underwriting margins during 2014 that are higher than in 2013.

In Financial, Professional & International Insurance, the Company expects underlying underwriting margins in 2014 will be broadly consistent with 2013 as the anticipated impact of recent underwriting actions and positive renewal premium changes will be offset by consistent modest loss cost trends and the inclusion of Dominion. This also assumes that weather patterns and what the Company defines as large losses are consistent with the Company's expectations. While the Company is taking actions to improve profitability at Dominion, it will be a number of years before these actions, to the extent successful, will be fully realized.

In Personal Insurance, the Company anticipates underlying underwriting margins during 2014 that are broadly consistent with 2013. In Agency Automobile, the Company anticipates an improvement in underlying underwriting margins during 2014 compared to 2013 due to the anticipated impact of continued positive renewal premium changes, combined with the Company's announced plan to reduce certain claim adjustment and other insurance expenses, partially offset by loss cost trends. The Company anticipates that the recently announced launch of Quantum Auto 2.0, as discussed below, will increase new business premiums but will not have a meaningful impact on underlying underwriting margins during 2014. In Agency Homeowners and Other, the Company anticipates a modest decline in underlying underwriting margins during 2014 compared to 2013, reflecting a return to non-catastrophe weather-related loss levels and loss cost trends consistent with the Company's expectations, partially offset by the anticipated impact of continued positive renewal premium changes. Also in Personal Insurance, the Company's direct to consumer initiative, the distribution channel that the Company launched in 2009, while intended to enhance the Company's long-term ability to compete successfully in a consumer-driven marketplace, is expected to remain unprofitable for a number of years as this book of business grows and matures.

The Agency Automobile line of business has been negatively impacted by various factors, including the use of price comparison technology by agents and brokers as discussed above. The Company's actions in response to these factors include, among other things, an announced plan to reduce certain claim adjustment and other insurance expenses, with the majority of the impact in the Agency Automobile line of business. That plan is intended to result in savings of \$140 million pre-tax per year by 2015 when fully implemented. It will also result in a restructuring charge of approximately \$16 million, \$12 million of which was incurred in 2013. Additionally, in the fourth quarter of 2013, the Company launched a new private passenger automobile product, Quantum Auto 2.0. This product, in addition to incorporating the cost savings described above, has a lower base commission rate than the Company's existing Quantum Auto 1.0 product. These changes in cost structure are intended to enable



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the Company to price Quantum Auto 2.0 more competitively while generating an expected appropriate return. The new product was launched in 18 states by December 31, 2013 and is expected to be eventually offered in all but three states before the end of 2014. The Company currently intends that, in approved states, all new accounts will be on the new product; in addition, the product will also be available to agents at their discretion for existing accounts.

*Investment Portfolio.* The Company expects to continue to focus its investment strategy on maintaining a high-quality investment portfolio and a relatively short average effective duration. The average effective duration of fixed maturities and short-term securities was 3.7 (3.9 excluding short-term securities) at December 31, 2013. From time to time, the Company enters into short positions in U.S. Treasury futures contracts to manage the duration of its fixed maturity portfolio. The Company continually evaluates its investment alternatives and mix. Currently, the majority of the Company's investments are comprised of a widely diversified portfolio of high-quality, liquid taxable U.S. government, tax-exempt U.S. municipal and taxable corporate and U.S. agency mortgage-backed bonds.

The Company also invests much smaller amounts in equity securities, real estate, private equity limited partnerships, hedge funds, and real estate partnerships and joint ventures. These investment classes have the potential for higher returns but also the potential for higher degrees of risk, including less stable rates of return and less liquidity.

Net investment income is a material contributor to the Company's results of operations. Interest rates remain at very low levels by historical standards. Based on the current interest rate environment, the Company estimates that the impact of lower reinvestment yields on the Company's fixed maturity portfolio could, in 2014, result in approximately \$25 million of lower after-tax net investment income from that portfolio on a quarterly basis as compared to the corresponding prior year quarter. Given recent general economic and investment market conditions, the Company expects investment income from the non-fixed maturity portfolio in 2014 will be lower than in 2013. If general economic conditions and/or investment market conditions deteriorate during 2014, the Company could also experience a further reduction in net investment income and/or significant realized investment losses, including impairments. Future actions or inactions of the United States government, such as a failure to increase the government debt limit or a shutdown of the federal government, could increase the actual or perceived risk that the U.S. may not ultimately pay its obligations when due and may disrupt financial markets. The carrying value of the Company's investments in U.S. Treasury securities and obligations of U.S. government and government agencies and authorities was \$2.32 billion at December 31, 2013. Additionally, the carrying value of the Company's investments in obligations of states, municipalities and political subdivisions included pre-refunded bonds of \$9.52 billion at December 31, 2013. Pre-refunded bonds are bonds for which states or municipalities have established irrevocable trusts, almost exclusively comprised of U.S. Treasury securities, which were created to satisfy their responsibility for payments of principal and interest. For further discussion of the Company's investment portfolio, see "Investment Portfolio." For a discussion of the risks to the Company's business during or following a financial market disruption and risks to the Company's investment portfolio, see the risk factors entitled "During or following a period of financial market disruption or economic downturn, our business could be materially and adversely affected" and "Our investment portfolio may suffer reduced returns or material realized or unrealized losses" included in "Part I Item 1A Risk Factors."

*Capital Position.* The Company believes it has a strong capital position and, as part of its ongoing efforts to create shareholder value, expects to continue to return capital not needed to support its business operations to its shareholders. The Company expects that, generally over time, the combination of dividends to common shareholders and common share repurchases will likely not exceed operating income. In addition, the timing and actual number of shares to be repurchased in the future will depend on a variety of additional factors, including the Company's financial position, earnings, share price, catastrophe losses, maintaining capital levels commensurate with the Company's

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desired ratings from independent rating agencies, funding of the Company's qualified pension plan, capital requirements of the Company's operating subsidiaries, legal requirements, regulatory constraints, other investment opportunities (including mergers and acquisitions and related financings), market conditions and other factors. For information regarding the Company's common share repurchases in 2013, see "Liquidity and Capital Resources."

The Company had a net after-tax unrealized investment gain of \$1.15 billion in its fixed maturity investment portfolio at December 31, 2013. While the Company does not attempt to predict future interest rate movements, a rising interest rate environment would reduce the market value of fixed maturity investments and, therefore, reduce shareholders' equity, and a declining interest rate environment would have the opposite effects. For a discussion of the risks to the Company's business during or following a financial market disruption and risks to the Company's investment portfolio, see the risk factors entitled "During or following a period of financial market disruption or economic downturn, our business could be materially and adversely affected" and "Our investment portfolio may suffer reduced returns or material realized or unrealized losses" included in "Part I Item 1A Risk Factors."

Many of the statements in this "Outlook" section are forward-looking statements, which are subject to risks and uncertainties that are often difficult to predict and beyond the Company's control. Actual results could differ materially from those expressed or implied by such forward-looking statements. Further, such forward-looking statements speak only as of the date of this report and the Company undertakes no obligation to update them. See "Forward-Looking Statements." For a discussion of potential risks and uncertainties that could impact the Company's results of operations or financial position, see "Item 1A Risk Factors" and "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates."

## **LIQUIDITY AND CAPITAL RESOURCES**

Liquidity is a measure of a company's ability to generate sufficient cash flows to meet the cash requirements of its business operations and to satisfy general corporate purposes when needed.

*Operating Company Liquidity.* The liquidity requirements of the Company's insurance subsidiaries are met primarily by funds generated from premiums, fees, income received on investments and investment maturities. Cash provided from these sources is used primarily for claims and claim adjustment expense payments and operating expenses. The insurance subsidiaries' liquidity requirements can be impacted by, among other factors, the timing and amount of catastrophe claims, which are inherently unpredictable, as well as the timing and amount of reinsurance recoveries, which may be affected by reinsurer solvency and reinsurance coverage disputes. Additionally, the variability of asbestos-related claim payments, as well as the volatility of potential judgments and settlements arising out of litigation, may also result in increased liquidity requirements. It is the opinion of the Company's management that the insurance subsidiaries' future liquidity needs will be adequately met from all of sources described above. Subject to restrictions imposed by states in which the Company's insurance subsidiaries are domiciled, the Company's principal insurance subsidiaries pay dividends to their respective parent companies, which in turn pay dividends to the corporate holding (parent) company (TRV). For further information regarding restrictions on dividends paid by the Company's insurance subsidiaries, see Part I Item 1 Regulation."

*Holding Company Liquidity.* TRV's liquidity requirements primarily include shareholder dividends, debt servicing, common share repurchases and, from time to time, contributions to its qualified domestic pension plan. At December 31, 2013, TRV held total cash and short-term invested assets in the United States aggregating \$1.59 billion and having a weighted average maturity of 84 days. These assets are sufficient to meet TRV's current liquidity requirements and are in excess of TRV's minimum target level, which comprises TRV's estimated annual pretax interest expense and common shareholder dividends, and currently totals approximately \$1.1 billion.

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TRV is not dependent on dividends or other forms of repatriation from its foreign operations to support its liquidity needs. U.S. income taxes have not been recognized on \$714 million of the Company's foreign operations' undistributed earnings as of December 31, 2013, as such earnings are intended to be permanently reinvested in those operations. Furthermore, taxes paid to foreign governments on these earnings may be used as credits against the U.S. tax on dividend distributions if such earnings were to be distributed to the holding company. The amount of undistributed earnings from foreign operations and related taxes on those undistributed earnings were not material to the Company's financial position or liquidity at December 31, 2013.

TRV has a shelf registration statement with the Securities and Exchange Commission which permits it to issue securities from time to time. TRV also has a \$1.0 billion line of credit facility with a syndicate of financial institutions that expires in June 2018. This line of credit also supports TRV's \$800 million commercial paper program, of which \$100 million was outstanding at December 31, 2013. TRV is not reliant on its commercial paper program to meet its operating cash flow needs.

The Company utilized uncollateralized letters of credit issued by major banks with an aggregate limit of approximately \$206 million, to provide a portion of the capital needed to support its obligations at Lloyd's at December 31, 2013. If uncollateralized letters of credit are not available at a reasonable price or at all in the future, the Company can collateralize these letters of credit or may have to seek alternative means of supporting its obligations at Lloyd's, which could include utilizing holding company funds on hand.

**Operating Activities**

Net cash flows provided by operating activities were \$3.82 billion, \$3.23 billion and \$2.17 billion in 2013, 2012 and 2011, respectively. Cash flows in 2013 primarily reflected a decrease in losses paid related to catastrophes and a higher level of collected premiums, partially offset by an increase in income tax payments. Cash flows in 2012 primarily reflected a decrease in losses paid related to catastrophes, a lower level of paid losses related to asbestos claims and operations in runoff and a higher level of collected premiums, partially offset by an increase in paid losses related to non-catastrophe ongoing business (including the impact of increased loss costs). In 2013, the Company made no contributions to its qualified domestic pension plan, which was 106% funded at December 31, 2013. In 2012 and 2011, the Company voluntarily made contributions totaling \$217 million and \$185 million, respectively, to its qualified domestic pension plan.

**Investing Activities**

Net cash flows used in investing activities in 2013 and 2012 were \$910 million and \$972 million, compared with net cash flows provided by investing activities of \$1.15 billion in 2011. The 2013 total included \$997 million related to the Company's acquisition of Dominion (net of cash acquired). The Company's consolidated total investments at December 31, 2013 decreased by \$678 million, or 1% from year-end 2012, primarily reflecting the impact of a significant decline in net unrealized appreciation of investments driven by an increase in interest rates, common share repurchases and dividends paid to shareholders, partially offset by net cash flows provided by operating activities and the impact of the acquisition of Dominion.

On December 5, 2012, the Company increased its ownership in J. Malucelli Participações em Seguros e Resseguros S.A, its Brazilian joint venture (JMalucelli), through the exercise of a pre-existing option. As a result, the Company increased its ownership to 49.5% of the venture. JMalucelli is currently the market leader in surety in Brazil based on market share. The Company's investment was funded with cash provided internally from an operating subsidiary of the Company.

The Company's investment portfolio is managed to support its insurance operations; accordingly, the portfolio is positioned to meet obligations to policyholders. As such, the primary goals of the

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Company's asset-liability management process are to satisfy the insurance liabilities and maintain sufficient liquidity to cover fluctuations in projected liability cash flows. Generally, the expected principal and interest payments produced by the Company's fixed maturity portfolio adequately fund the estimated runoff of the Company's insurance reserves. Although this is not an exact cash flow match in each period, the substantial amount by which the market value of the fixed maturity portfolio exceeds the value of the net insurance liabilities, as well as the positive cash flow from newly sold policies and the large amount of high quality liquid bonds, contributes to the Company's ability to fund claim payments without having to sell illiquid assets or access credit facilities.

**Financing Activities**

Net cash flows used in financing activities were \$2.94 billion, \$2.15 billion and \$3.31 billion in 2013, 2012 and 2011, respectively. The totals in each year reflected common share repurchases, dividends to shareholders and the repayment of debt, partially offset by the proceeds from employee stock option exercises and, in 2013, proceeds from the issuance of debt.

*Debt Transactions.*

*2013.* On July 25, 2013, the Company issued \$500 million aggregate principal amount of 4.60% senior notes that will mature on August 1, 2043. The net proceeds of the issuance, after original issuance discount and the deduction of underwriting expenses and commissions and other expenses, totaled approximately \$494 million. Interest on the senior notes is payable semi-annually in arrears on February 1 and August 1, commencing on February 1, 2014. The senior notes are redeemable in whole at any time or in part from time to time, at the Company's option, at a redemption price equal to the greater of (a) 100% of the principal amount of senior notes to be redeemed or (b) the sum of the present value of the remaining scheduled payments of principal and interest on the senior notes to be redeemed (exclusive of interest accrued to the date of redemption) discounted to the date of redemption on a semi-annual basis (assuming a 360-day year consisting of twelve 30-day months) at the then current treasury rate (as defined) plus 15 basis points.

On March 15, 2013, the Company's \$500 million, 5.00% senior notes matured and were fully paid.

*2012.* On May 29, 2012, the Company purchased and retired \$8.5 million aggregate principal amount of its 6.25% fixed-to-floating rate junior subordinated debentures due March 15, 2067 in an open market transaction. The Company's \$250 million, 5.375% senior notes matured on June 15, 2012 and were paid from existing holding company liquidity.

*2011.* On June 1, 2011, the Company repaid the remaining \$9 million principal balance on its 7.22% real estate non-recourse debt.

In 2014, no debt obligations, other than commercial paper, become due. In 2015, the amount of debt obligations, other than commercial paper, that comes due is \$400 million. The Company may refinance maturing debt through funds generated internally or, depending on market conditions, through funds generated externally, including as a result of the issuance of debt or other securities.

*Dividends.* Dividends paid to shareholders were \$729 million, \$694 million and \$665 million in 2013, 2012 and 2011, respectively. The declaration and payment of future dividends to holders of the Company's common stock will be at the discretion of the Company's board of directors and will depend upon many factors, including the Company's financial position, earnings, capital requirements of the Company's operating subsidiaries, legal requirements, regulatory constraints and other factors as the board of directors deems relevant. Dividends will be paid by the Company only if declared by its board of directors out of funds legally available, subject to any other restrictions that may be applicable to the Company. On January 21, 2014, the Company announced that it declared a regular quarterly dividend of \$0.50 per share, payable March 31, 2014, to shareholders of record on March 10, 2014.

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*Share Repurchases.* The Company's board of directors has approved common share repurchase authorizations under which repurchases may be made from time to time in the open market, pursuant to pre-set trading plans meeting the requirements of Rule 10b5-1 under the Securities Exchange Act of 1934, in private transactions or otherwise. The authorizations do not have a stated expiration date. The timing and actual number of shares to be repurchased in the future will depend on a variety of factors, including the Company's financial position, earnings, share price, catastrophe losses, maintaining capital levels commensurate with the Company's desired ratings from independent rating agencies, funding of the Company's qualified pension plan, capital requirements of the Company's operating subsidiaries, legal requirements, regulatory constraints, other investment opportunities (including mergers and acquisitions and related financings), market conditions and other factors. In October 2013, the board of directors approved a share repurchase authorization that added an additional \$5.0 billion of repurchase capacity. The following table summarizes repurchase activity in 2013 and remaining repurchase capacity at December 31, 2013.

Quarterly Period Ending (in millions, except per share amounts)	Number of shares purchased	Cost of shares repurchased	Average price paid per share	Remaining capacity under share repurchase authorization
March 31, 2013	3.7	\$ 300	\$ 81.01	\$ 1,859
June 30, 2013	3.6	300	82.99	1,559
September 30, 2013	9.7	800	82.21	759
December 31, 2013	11.4	1,000	88.10	4,759
<b>Total</b>	<b>28.4</b>	<b>\$ 2,400</b>	<b>84.51</b>	<b>4,759</b>

From the inception of the first authorization in May 2006 through December 31, 2013, the Company repurchased a cumulative total of 390.8 million shares for a total cost of \$21.24 billion, or an average of \$54.35 per share.

In 2013, 2012 and 2011, the Company acquired 0.8 million, 0.9 million and 1.4 million shares, respectively, of common stock from employees as treasury stock primarily to cover payroll withholding taxes related to the vesting of restricted stock awards and exercises of stock options.

### Capital Resources

Capital resources reflect the overall financial strength of the Company and its ability to borrow funds at competitive rates and raise new capital to meet its needs. The following table summarizes the components of the Company's capital structure at December 31, 2013 and 2012.

(at December 31, in millions)	2013	2012
<b>Debt:</b>		
Short-term	\$ 100	\$ 600
Long-term	6,261	5,761
Net unamortized fair value adjustments and debt issuance costs	(15)	(11)
<b>Total debt</b>	<b>6,346</b>	6,350
<b>Shareholders' equity:</b>		
Common stock and retained earnings, less treasury stock	23,986	23,169
Accumulated other comprehensive income	810	2,236
<b>Total shareholders' equity</b>	<b>24,796</b>	25,405
<b>Total capitalization</b>	<b>\$ 31,142</b>	\$ 31,755

Total capitalization at December 31, 2013 was \$31.14 billion, \$613 million lower than at December 31, 2012, primarily reflecting the impact of a decrease in net unrealized appreciation of investments, common share repurchases totaling \$2.40 billion under the Company's share repurchase

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authorization, shareholder dividends of \$734 million and debt repayments of \$500 million, partially offset by net income of \$3.67 billion and the issuance of debt for net proceeds of \$494 million.

The following table provides a reconciliation of total capitalization excluding net unrealized gains on investments to total capitalization presented in the foregoing table.

(at December 31, dollars in millions)	2013	2012
Total capitalization excluding net unrealized gains on investments	\$ 29,820	\$ 28,652
Net unrealized gain on investments, net of taxes	1,322	3,103
<b>Total capitalization</b>	<b>\$ 31,142</b>	<b>\$ 31,755</b>

Debt-to-total capital ratio	20.4%	20.0%
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Debt-to-total capital ratio excluding net unrealized gains on investments	21.3%	22.2%
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The debt-to-total capital ratio excluding net unrealized gain on investments is calculated by dividing (a) debt by (b) total capitalization excluding net unrealized gains and losses on investments, net of taxes. Net unrealized gains and losses on investments can be significantly impacted by both interest rate movements and other economic factors. Accordingly, in the opinion of the Company's management, the debt-to-total capital ratio calculated on this basis provides another useful metric for investors to understand the Company's financial leverage position. The Company's ratio of debt-to-total capital (excluding after-tax net unrealized investment gains) was 21.3% at December 31, 2013, within the Company's target range of 15% to 25%.

*Credit Agreement.* On June 7, 2013, the Company entered into a five-year, \$1.0 billion revolving credit agreement with a syndicate of financial institutions, replacing its three-year \$1.0 billion credit agreement that was due to expire on June 10, 2013. Terms of the credit agreement are discussed in more detail in note 8 of notes to the Company's consolidated financial statements.

*Shelf Registration.* The Company has filed with the Securities and Exchange Commission a universal shelf registration statement for the potential offering and sale of securities. The Company may offer these securities from time to time at prices and on other terms to be determined at the time of offering.

*Share Repurchase Authorization.* At December 31, 2013, the Company had \$4.76 billion of capacity remaining under its share repurchase authorization approved by the board of directors.

### **Contractual Obligations**

The following table summarizes, as of December 31, 2013, the Company's future payments under contractual obligations and estimated claims and claim-related payments. The table excludes short-term obligations and includes only liabilities at December 31, 2013 that are expected to be settled in cash.

The table below includes the amount and estimated future timing of claims and claim-related payments. The amounts do not represent the exact liability, but instead represent estimates, generally utilizing actuarial projections techniques, at a given accounting date. These estimates include expectations of what the ultimate settlement and administration of claims will cost based on the Company's assessment of facts and circumstances known, review of historical settlement patterns, estimates of trends in claims severity, frequency, legal theories of liability and other factors. Variables in the reserve estimation process can be affected by both internal and external events, such as changes in claims handling

procedures, economic inflation or deflation, legal trends and legislative changes. Many of these items are not directly quantifiable, particularly on a prospective basis. Additionally, there may be significant reporting lags between the occurrence of the policyholder event and the time it is actually reported to the insurer. The future cash flows related to the items contained in the table below



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required estimation of both amount (including severity considerations) and timing. Amount and timing are frequently estimated separately. An estimation of both amount and timing of future cash flows related to claims and claim-related payments has some unavoidable estimation uncertainty.

The contractual obligations related to debt, operating leases, purchase obligations, long-term unfunded investment commitments, estimated claims and claim-related payments (gross of the estimated reinsurance recoveries) and liabilities related to unrecognized tax benefits, at December 31, 2013 were as follows:

<b>Payments Due by Period (in millions)</b>	<b>Total</b>	<b>Less than 1 Year</b>	<b>1 - 3 Years</b>	<b>3 - 5 Years</b>	<b>After 5 Years</b>
<b>Debt</b>					
Senior notes	\$ 5,900	\$	\$ 800	\$ 950	\$ 4,150
Junior subordinated debentures	361				361
<b>Total debt principal</b>	<b>6,261</b>		<b>800</b>	<b>950</b>	<b>4,511</b>
<b>Interest</b>	<b>5,572</b>	<b>365</b>	<b>696</b>	<b>590</b>	<b>3,921</b>
<b>Total long-term debt obligations(1)</b>	<b>11,833</b>	<b>365</b>	<b>1,496</b>	<b>1,540</b>	<b>8,432</b>
<b>Operating leases(2)</b>	<b>816</b>	<b>178</b>	<b>297</b>	<b>175</b>	<b>166</b>
<b>Purchase obligations</b>					
Information systems administration and maintenance commitments(3)	129	48	62	17	2
Other purchase commitments(4)	49	30	15	4	
<b>Total purchase obligations</b>	<b>178</b>	<b>78</b>	<b>77</b>	<b>21</b>	<b>2</b>
<b>Long-term unfunded investment commitments(5)</b>	<b>1,516</b>	<b>333</b>	<b>452</b>	<b>502</b>	<b>229</b>
<b>Estimated claims and claim-related payments</b>					
Claims and claim adjustment expenses(6)	48,637	10,622	11,405	6,395	20,215
Claims from large deductible policies(7)					
Loss-based assessments(8)	174	37	52	19	66
Payout from ceded funds withheld(9)	229	27	54	30	118
<b>Total estimated claims and claim-related payments</b>	<b>49,040</b>	<b>10,686</b>	<b>11,511</b>	<b>6,444</b>	<b>20,399</b>
<b>Liabilities related to unrecognized tax benefits(10)</b>	<b>381</b>		<b>381</b>		
<b>Total</b>	<b>\$ 63,764</b>	<b>\$ 11,640</b>	<b>\$ 14,214</b>	<b>\$ 8,682</b>	<b>\$ 29,228</b>

- (1) The Company's \$107 million remaining aggregate principal amount of 6.25% fixed-to-floating rate debentures bear interest at an annual rate of 6.25% from the date of issuance to, but excluding, March 15, 2017 and at a rate of three-month LIBOR plus 2.215% thereafter. The table above includes interest payments through the scheduled maturity date of March 15, 2037. Interest payments beginning March 15, 2017 through March 15, 2037 were calculated using the three-month LIBOR rate as of December 31, 2013.

See note 8 of notes to the Company's consolidated financial statements for a further discussion of outstanding indebtedness. Because the amounts reported in the foregoing table include principal and interest, the total long-term debt obligations will not agree with the amounts reported in note 8.

- (2) Represents agreements entered into in the ordinary course of business to lease office space, equipment and furniture.

- (3) Includes agreements with vendors to purchase system software administration and maintenance services.

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- (4) Includes commitments to vendors entered into in the ordinary course of business for goods and services including property, plant and equipment, office supplies, archival services, etc.
- (5) Represents estimated timing for fulfilling unfunded commitments for private equity limited partnerships and real estate partnerships.
- (6) The amounts in "Claims and claim adjustment expenses" in the table above represent the estimated timing of future payments for both reported and unreported claims incurred and related claim adjustment expenses, gross of reinsurance recoverables, excluding structured settlements expected to be paid by annuity companies.

The Company has entered into reinsurance agreements to protect itself from potential losses in excess of the amount it is prepared to accept as described in note 5 of notes to the Company's consolidated financial statements.

In order to qualify for reinsurance accounting, a reinsurance agreement must indemnify the insurer from insurance risk, i.e., the agreement must transfer amount and timing risk. Since the timing and amount of cash inflows from such reinsurance agreements are directly related to the underlying payment of claims and claim adjustment expenses by the insurer, reinsurance recoverables are recognized in a manner consistent with the liabilities (the estimated liability for claims and claim adjustment expenses) relating to the underlying reinsured contracts. The presence of any feature that can delay timely reimbursement of claims by a reinsurer results in the reinsurance contract being accounted for as a deposit rather than reinsurance. The assumptions used in estimating the amount and timing of the reinsurance recoverables are consistent with those used in estimating the amount and timing of the related liabilities.

The estimated future cash inflows from the Company's reinsurance contracts that qualify for reinsurance accounting are as follows:

(in millions)	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	After 5 Years
<b>Reinsurance recoverables</b>	<b>\$ 6,071</b>	<b>\$ 1,090</b>	<b>\$ 1,129</b>	<b>\$ 837</b>	<b>\$ 3,015</b>

The Company manages its business and evaluates its liabilities for claims and claim adjustment expenses on a net of reinsurance basis. The estimated cash flows on a net of reinsurance basis are as follows:

(in millions)	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	After 5 Years
<b>Claims and claim adjustment expenses, net</b>	<b>\$ 42,566</b>	<b>\$ 9,532</b>	<b>\$ 10,276</b>	<b>\$ 5,558</b>	<b>\$ 17,200</b>

For business underwritten by non-U.S. operations, future cash flows related to reported and unreported claims incurred and related claim adjustment expenses were translated at the spot rate on December 31, 2013.

The amounts reported in the table above and in the table of reinsurance recoverables above are presented on a nominal basis and have not been adjusted to reflect the time value of money. Accordingly, the amounts above will differ from the Company's balance sheet to the extent that the liability for claims and claim adjustment expenses and the related reinsurance recoverables have been discounted in the balance sheet. (See note 1 of notes to the Company's consolidated financial statements.)

- (7) Workers' compensation large deductible policies provide third party coverage in which the Company typically is responsible for paying the entire loss under such policies and then seeks reimbursement from the insured for the deductible amount. "Claims from large deductible policies" represent the estimated future payment for claims and claim related expenses below the deductible amount, net of the estimated recovery of the deductible. The liability and the related deductible receivable for unpaid claims are presented in the consolidated balance sheet as "contractholder payables" and "contractholder receivables," respectively. Most deductibles for such policies are paid directly from the policyholder's escrow which is periodically replenished by the



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policyholder. The payment of the loss amounts above the deductible are reported within "Claims and claim adjustment expenses" in the above table. Because the timing of the collection of the deductible (contractholder receivables) occurs shortly after the payment of the deductible to a claimant (contractholder payables), these cash flows offset each other in the table.

The estimated timing of the payment of the contractholder payables and the collection of contractholder receivables for workers' compensation policies is presented below:

(in millions)	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	After 5 Years
<b>Contractholder payables/receivables</b>	<b>\$ 4,328</b>	<b>\$ 1,091</b>	<b>\$ 1,204</b>	<b>\$ 633</b>	<b>\$ 1,400</b>

- (8) The amounts in "Loss-based assessments" relate to estimated future payments of second-injury fund assessments which would result from payment of current claim liabilities. Second injury funds cover the cost of any additional benefits for aggravation of a pre-existing condition. For loss-based assessments, the cost is shared by the insurance industry and self-insureds, funded through assessments to insurance companies and self-insureds based on losses. Amounts relating to second-injury fund assessments are included in "other liabilities" in the consolidated balance sheet.
- (9) The amounts in "Payout from ceded funds withheld" represent estimated payments for losses and return of funds held related to certain reinsurance arrangements whereby the Company holds a portion of the premium due to the reinsurer and is allowed to pay claims from the amounts held.
- (10) The Company's current liabilities related to unrecognized tax benefits from uncertain tax positions are \$381 million. Offsetting these liabilities are deferred tax assets of \$362 million associated with the temporary differences that would exist if these positions become realized.

The above table does not include an analysis of liabilities reported for structured settlements for which the Company has purchased annuities and remains contingently liable in the event of default by the company issuing the annuity. The Company is not reasonably likely to incur material future payment obligations under such agreements. In addition, the Company is not currently subject to any minimum funding requirements for its qualified pension plan. Accordingly, future contributions are not included in the foregoing table.

**Dividend Availability**

The Company's principal insurance subsidiaries are domiciled in the state of Connecticut. The insurance holding company laws of Connecticut applicable to the Company's subsidiaries requires notice to, and approval by, the state insurance commissioner for the declaration or payment of any dividend that, together with other distributions made within the preceding twelve months, exceeds the greater of 10% of the insurer's capital and surplus as of the preceding December 31, or the insurer's net income for the twelve-month period ending the preceding December 31, in each case determined in accordance with statutory accounting practices and by state regulation. This declaration or payment is further limited by adjusted unassigned surplus, as determined in accordance with statutory accounting practices. The insurance holding company laws of other states in which the Company's subsidiaries are domiciled generally contain similar, although in some instances somewhat more restrictive, limitations on the payment of dividends. A maximum of \$3.33 billion is available by the end of 2014 for such dividends to the holding company, TRV, without prior approval of the Connecticut Insurance Department. The Company may choose to accelerate the timing within 2014 and/or increase the amount of dividends from its insurance subsidiaries in 2014, which could result in certain dividends being subject to approval by the Connecticut Insurance Department.

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TRV is not dependent on dividends or other forms of repatriation from its foreign operations to support its liquidity needs. The undistributed earnings of the Company's foreign operations are not material and are intended to be permanently reinvested in those operations.

TRV and its two non-insurance holding company subsidiaries received \$2.90 billion of dividends in 2013, all of which was received from their U.S. insurance subsidiaries.

**Pension and Other Postretirement Benefit Plans**

The Company sponsors a qualified non-contributory defined benefit pension plan (the Qualified Plan), which covers substantially all U.S. domestic employees and provides benefits primarily under a cash balance formula. In addition, the Company sponsors: a nonqualified defined benefit pension plan which covers certain highly-compensated employees, pension plans for employees of its foreign subsidiaries, and a postretirement health and life insurance benefit plan for employees satisfying certain age and service requirements and for certain retirees.

The Qualified Plan is subject to regulations under the Employee Retirement Income Act of 1974 as amended (ERISA), which requires plans to meet minimum standards of funding and requires such plans to subscribe to plan termination insurance through the Pension Benefit Guaranty Corporation (PBGC). The Company does not have a minimum funding requirement for the Qualified Plan for 2014 and does not anticipate having a minimum funding requirement in 2015. The Company has significant discretion in making contributions above those necessary to satisfy the minimum funding requirements. In 2013, there was no minimum funding requirement for the Qualified Plan, and the Company made no voluntary contributions to the Qualified Plan. In 2012 and 2011, the Company voluntarily made contributions totaling \$217 million and \$185 million, respectively, to the Qualified Plan. In determining future contributions, the Company will consider the performance of the plan's investment portfolio, the effects of interest rates on the projected benefit obligation of the plan and the Company's other capital requirements. The Company has not determined whether or not additional voluntary funding will be made in the 2014. However, the Company currently believes, subject to actual plan performance and funded status at the time, that it may make voluntary pension contributions of approximately \$75 million to \$100 million annually beginning in 2015 as well as over the following several years.

The Qualified Plan assets are managed to maximize long-term total return. The Company's overall strategy is to achieve a mix of approximately 85% to 90% of investments for long-term growth and 10% to 15% for near-term benefit payments with a wide diversification of asset types, fund strategies and fund managers. The current target allocations for plan assets are 55% to 65% equity securities and 20% to 40% fixed income securities, with the remainder allocated to short-term securities. For 2014, the Company plans to apply an expected long-term rate of return on plan assets of 7.50%, the same rate as in 2013. The rates of return reflect the Company's current expectations of long-term returns on the plan's invested assets, taking into account the current low level of long-term interest rates as well as the Federal Reserve's commentary in November 2013 regarding its expectation to maintain interest rates at their current low levels until the national labor market is sufficiently strong. The Company's expected long-term rate of return on plan assets also contemplates a return to more normal levels of long-term interest rates in the future.

For further discussion of the pension and other postretirement benefit plans, see note 14 of notes to the consolidated financial statements.

**Risk-Based Capital**

The NAIC has Risk-Based Capital (RBC) requirements for property casualty companies to be used as minimum capital requirements by the NAIC and states to identify companies that merit further regulatory action. The formulas have not been designed to differentiate among adequately capitalized companies that operate with levels of capital above the RBC requirements. Therefore, it is

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inappropriate and ineffective to use the formulas to rate or to rank these companies. At December 31, 2013, all of the Company's insurance subsidiaries had adjusted capital in excess of amounts requiring any company or regulatory action.

**Off-Balance Sheet Arrangements**

The Company has entered into certain contingent obligations for guarantees related to the sale of business entities, certain investments, third-party loans related to certain investments, certain insurance policy obligations of former insurance subsidiaries and various other indemnifications. See note 16 of notes to the Company's consolidated financial statements. The Company does not expect these arrangements will have a material effect on the Company's financial position, changes in financial position, revenues and expenses, results of operations, liquidity, capital expenditures or capital resources.

**CRITICAL ACCOUNTING ESTIMATES**

The Company considers its most significant accounting estimates to be those applied to claims and claim adjustment expense reserves and related reinsurance recoverables, investment valuation and impairments, and goodwill and other intangible assets impairments.

**Claims and Claim Adjustment Expense Reserves**

Gross claims and claim adjustment expense reserves by product line were as follows:

(at December 31, in millions)	2013			2012		
	Case	IBNR	Total	Case	IBNR	Total
General liability	\$ 5,355	\$ 8,604	\$ 13,959	\$ 5,525	\$ 9,109	\$ 14,634
Commercial property	778	542	1,320	992	638	1,630
Commercial multi-peril	1,879	1,707	3,586	2,018	1,723	3,741
Commercial automobile	2,305	1,219	3,524	2,343	1,241	3,584
Workers' compensation	9,918	7,856	17,774	9,684	7,589	17,273
Fidelity and surety	426	818	1,244	479	934	1,413
Personal automobile	1,793	785	2,578	1,980	722	2,702
Homeowners and personal other	635	551	1,186	1,335	809	2,144
International and other	3,585	2,109	5,694	2,216	1,551	3,767
Property-casualty	26,674	24,191	50,865	26,572	24,316	50,888
Accident and health	30		30	34		34
<b>Claims and claim adjustment expense reserves</b>	<b>\$ 26,704</b>	<b>\$ 24,191</b>	<b>\$ 50,895</b>	<b>\$ 26,606</b>	<b>\$ 24,316</b>	<b>\$ 50,922</b>

Gross claims and claim adjustment expense reserves at December 31, 2013 decreased by \$27 million from December 31, 2012, primarily reflecting the impact of net favorable prior year reserve development, payments related to catastrophes and payments related to operations in runoff, including asbestos and environmental claims, partially offset by the impact of the acquisition of Dominion. Dominion's reserves at December 31, 2013 were included in the "International and other" category in the foregoing table.

Asbestos and environmental reserves are included in the General liability, Commercial multi-peril and International and other lines in the foregoing summary table. Asbestos and environmental reserves are discussed separately; see "Asbestos Claims and Litigation", "Environmental Claims and Litigation" and "Uncertainty Regarding Adequacy of Asbestos and Environmental Reserves."

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Claims and claim adjustment expense reserves represent management's estimate of ultimate unpaid costs of losses and loss adjustment expenses for claims that have been reported and claims that have been incurred but not yet reported (IBNR). Claims and claim adjustment expense reserves do not represent an exact calculation of liability, but instead represent management estimates, generally utilizing actuarial expertise and projection techniques, at a given accounting date. These estimates are expectations of what the ultimate settlement and administration of claims will cost upon final resolution in the future, based on the Company's assessment of facts and circumstances then known, review of historical settlement patterns, estimates of trends in claims severity and frequency, expected interpretations of legal theories of liability and other factors. In establishing gross claims and claim adjustment expense reserves, the Company also considers salvage and subrogation. Estimated recoveries from reinsurance are included in "Reinsurance Recoverables" as an asset on the Company's consolidated balance sheet. The claims and claim adjustment expense reserves are reviewed regularly by qualified actuaries employed by the Company.

The process of estimating claims and claim adjustment expense reserves involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events, such as changes in claims handling procedures, changes in individuals involved in the reserve estimation process, economic inflation, legal trends and legislative changes, among others. The impact of many of these items on ultimate costs for claims and claim adjustment expenses is difficult to estimate. Estimation difficulties also differ significantly by product line due to differences in claim complexity, the volume of claims, the potential severity of individual claims, the determination of occurrence date for a claim and reporting lags (the time between the occurrence of the policyholder event and when it is actually reported to the insurer). Informed judgment is applied throughout the process, including the application of various individual experiences and expertise to multiple sets of data and analyses. The Company continually refines its estimates in a regular ongoing process as historical loss experience develops and additional claims are reported and settled. The Company rigorously attempts to consider all significant facts and circumstances known at the time claims and claim adjustment expense reserves are established. Due to the inherent uncertainty underlying these estimates including, but not limited to, the future settlement environment, final resolution of the estimated liability for claims and claim adjustment expenses may be higher or lower than the related claims and claim adjustment expense reserves at the reporting date. Therefore, actual paid losses, as claims are settled in the future, may be materially different than the amount currently recorded favorable or unfavorable.

Because establishment of claims and claim adjustment expense reserves is an inherently uncertain process involving estimates, currently established claims and claim adjustment expense reserves may change. The Company reflects adjustments to the reserves in the results of operations in the period the estimates are changed.

There are also additional risks which impact the estimation of ultimate costs for catastrophes. For example, the estimation of reserves related to hurricanes, tornadoes and other catastrophic events can be affected by the inability of the Company and its insureds to access portions of the impacted areas, the complexity of factors contributing to the losses, the legal and regulatory uncertainties, including the interpretation of policy terms and conditions, and the nature of the information available to establish the reserves. Complex factors include, but are not limited to: determining whether damage was caused by flooding versus wind; evaluating general liability and pollution exposures; estimating additional living expenses; estimating the impact of demand surge, infrastructure disruption, fraud, the effect of mold damage and business interruption costs; and reinsurance collectibility. The timing of a catastrophe, such as at or near the end of a reporting period, can also affect the information available to the Company in estimating reserves for that reporting period. The estimates related to catastrophes are adjusted as actual claims emerge.



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A portion of the Company's gross claims and claim adjustment expense reserves (totaling \$2.96 billion at December 31, 2013) are for asbestos and environmental claims and related litigation. While the ongoing review of asbestos and environmental claims and associated liabilities considers the inconsistencies of court decisions as to coverage, plaintiffs' expanded theories of liability and the risks inherent in complex litigation and other uncertainties, in the opinion of the Company's management, it is possible that the outcome of the continued uncertainties regarding these claims could result in liability in future periods that differs from current reserves by an amount that could be material to the Company's future operating results. See the preceding discussion of "Asbestos Claims and Litigation" and "Environmental Claims and Litigation."

General Discussion

The process for estimating the liabilities for claims and claim adjustment expenses begins with the collection and analysis of claim data. Data on individual reported claims, both current and historical, including paid amounts and individual claim adjuster estimates, are grouped by common characteristics (components) and evaluated by actuaries in their analyses of ultimate claim liabilities by product line. Such data is occasionally supplemented with external data as available and when appropriate. The process of analyzing reserves for a component is undertaken on a regular basis, generally quarterly, in light of continually updated information.

Multiple estimation methods are available for the analysis of ultimate claim liabilities. Each estimation method has its own set of assumption variables and its own advantages and disadvantages, with no single estimation method being better than the others in all situations and no one set of assumption variables being meaningful for all product line components. The relative strengths and weaknesses of the particular estimation methods when applied to a particular group of claims can also change over time. Therefore, the actual choice of estimation method(s) can change with each evaluation. The estimation method(s) chosen are those that are believed to produce the most reliable indication at that particular evaluation date for the claim liabilities being evaluated.

In most cases, multiple estimation methods will be valid for the particular facts and circumstances of the claim liabilities being evaluated. This will result in a range of reasonable estimates for any particular claim liability. The Company uses such range analyses to back test whether previously established estimates for reserves at the reporting segments are reasonable, given subsequent information. Reported values found to be closer to the endpoints of a range of reasonable estimates are subject to further detailed reviews. These reviews may substantiate the validity of management's recorded estimate or lead to a change in the reported estimate.

The exact boundary points of these ranges are more qualitative than quantitative in nature, as no clear line of demarcation exists to determine when the set of underlying assumptions for an estimation method switches from being reasonable to unreasonable. As a result, the Company does not believe that the endpoints of these ranges are or would be comparable across companies. In addition, potential interactions among the different estimation assumptions for different product lines make the aggregation of individual ranges a highly judgmental and inexact process.

Property-casualty insurance policies are either written on a claims-made or on an occurrence basis. Claims-made policies generally cover, subject to requirements in individual policies, claims reported during the policy period. Policies that are written on an occurrence basis require that the insured demonstrate that a loss occurred in the policy period, even if the insured reports the loss many years later.

Most general liability policies are written on an occurrence basis. These policies are subject to substantial loss development over time as facts and circumstances change in the years following the policy issuance. The occurrence form, which accounts for much of the reserve development in asbestos and environmental exposures, is also used to provide coverage for construction general liability,

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including construction defect. Occurrence-based forms of insurance for general liability exposures require substantial projection of various trends, including future inflation, judicial interpretations and societal litigation trends (e.g., size of jury awards and propensity of individuals to pursue litigation), among others.

A basic premise in most actuarial analyses is that past patterns demonstrated in the data will repeat themselves in the future, absent a material change in the associated risk factors discussed below. To the extent a material change affecting the ultimate claim liability is known, such change is quantified to the extent possible through an analysis of internal company data and, if available and when appropriate, external data. Such a measurement is specific to the facts and circumstances of the particular claim portfolio and the known change being evaluated. Significant structural changes to the available data, product mix or organization can materially impact the reserve estimation process.

Informed judgment is applied throughout the reserving process. This includes the application of various individual experiences and expertise to multiple sets of data and analyses. In addition to actuaries, experts involved with the reserving process also include underwriting and claims personnel and lawyers, as well as other company management. Therefore, management may have to consider varying individual viewpoints as part of its estimation of claims and claim adjustment expense reserves. It is also likely that during periods of significant change, such as a merger, consistent application of informed judgment becomes even more complicated and difficult.

The variables discussed above in this general discussion have different impacts on reserve estimation uncertainty for a given product line, depending on the length of the claim tail, the reporting lag, the impact of individual claims and the complexity of the claim process for a given product line.

Product lines are generally classifiable as either long tail or short tail, based on the average length of time between the event triggering claims under a policy and the final resolution of those claims. Short tail claims are reported and settled quickly, resulting in less estimation variability. The longer the time before final claim resolution, the greater the exposure to estimation risks and hence the greater the estimation uncertainty.

A major component of the claim tail is the reporting lag. The reporting lag, which is the time between the event triggering a claim and the reporting of the claim to the insurer, makes estimating IBNR inherently more uncertain. In addition, the greater the reporting lag, the greater the proportion of IBNR to the total claim liability for the product line. Writing new products with material reporting lags can result in adding several years' worth of IBNR claim exposure before the reporting lag exposure becomes clearly observable, thereby increasing the risk associated with pricing and reserving such products. The most extreme example of claim liabilities with long reporting lags are asbestos claims.

For some lines, the impact of large individual claims can be material to the analysis. These lines are generally referred to as being "low frequency/high severity," while lines without this "large claim" sensitivity are referred to as "high frequency/low severity." Estimates of claim liabilities for low frequency/high severity lines can be sensitive to the impact of a small number of potentially large claims. As a result, the role of judgment is much greater for these reserve estimates. In contrast, for high frequency/low severity lines the impact of individual claims is relatively minor and the range of reasonable reserve estimates is narrower and more stable.

Claim complexity can also greatly affect the estimation process by impacting the number of assumptions needed to produce the estimate, the potential stability of the underlying data and claim process, and the ability to gain an understanding of the data. Product lines with greater claim complexity, such as for certain surety and construction exposures, have inherently greater estimation uncertainty.

Actuaries have to exercise a considerable degree of judgment in the evaluation of all these factors in their analysis of reserves. The human element in the application of actuarial judgment is unavoidable

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when faced with material uncertainty. Different actuaries may choose different assumptions when faced with such uncertainty, based on their individual backgrounds, professional experiences and areas of focus. Hence, the estimates selected by the various actuaries may differ materially from each other.

Lastly, significant structural changes to the available data, product mix or organization can also materially impact the reserve estimation process. Events such as mergers increase the inherent uncertainty of reserve estimates for a period of time, until stable trends re-establish themselves within the new organization.

Risk factors

The major causes of material uncertainty ("risk factors") generally will vary for each product line, as well as for each separately analyzed component of the product line. In a few cases, such risk factors are explicit assumptions of the estimation method, but in most cases, they are implicit. For example, a method may explicitly assume that a certain percentage of claims will close each year, but will implicitly assume that the legal interpretation of existing contract language will remain unchanged. Actual results will likely vary from expectations for each of these assumptions, causing actual paid losses, as claims are settled in the future, to be different in amount than the reserves being estimated currently.

Some risk factors will affect more than one product line. Examples include changes in claim department practices, changes in settlement patterns, regulatory and legislative actions, court actions, timeliness of claim reporting, state mix of claimants and degree of claimant fraud. The extent of the impact of a risk factor will also vary by components within a product line. Individual risk factors are also subject to interactions with other risk factors within product line components.

The effect of a particular risk factor on estimates of claim liabilities cannot be isolated in most cases. For example, estimates of potential claim settlements may be impacted by the risk associated with potential court rulings, but the final settlement agreement typically does not delineate how much of the settled amount is due to this and other factors.

The evaluation of data is also subject to distortion from extreme events or structural shifts, sometimes in unanticipated ways. For example, the timing of claims payments in one geographic region will be impacted if claim adjusters are temporarily reassigned from that region to help settle catastrophe claims in another region.

While some changes in the claim environment are sudden in nature (such as a new court ruling affecting the interpretation of all contracts in that jurisdiction), others are more evolutionary. Evolutionary changes can occur when multiple factors affect final claim values, with the uncertainty surrounding each factor being resolved separately, in stepwise fashion. The final impact is not known until all steps have occurred.

Sudden changes generally cause a one-time shift in claim liability estimates, although there may be some lag in reliable quantification of their impact. Evolutionary changes generally cause a series of shifts in claim liability estimates, as each component of the evolutionary change becomes evident and estimable.

Actuarial methods for analyzing and estimating claims and claim adjustment expense reserves

The principal estimation and analysis methods utilized by the Company's actuaries to evaluate management's existing estimates for prior accident periods are the paid development method, the case incurred development method, the Bornhuetter-Ferguson (BF) method, and average value analysis combined with the reported claim development method. The BF method is usually utilized for more recent accident periods, with a transition to other methods as the underlying claim data becomes more voluminous and therefore more credible. These are typically referred to as conventional actuarial methods. (See Glossary for an explanation of these methods).

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While these are the principal methods utilized throughout the Company, actuaries evaluating a particular component for a product line have available to them the full range of methods developed within the casualty actuarial profession. The Company's actuaries are also continually monitoring developments within the profession for advances in existing techniques or the creation of new techniques that might improve current and future estimates.

Some components of product line reserves are susceptible to relatively infrequent large claims that can materially impact the total estimate for that component. In such cases, the Company's actuarial analysis generally isolates and analyzes separately such large claims. The reserves excluding such large claims are generally analyzed using the conventional methods described above. The reserves associated with large claims are then analyzed utilizing various methods, such as:

Estimating the number of large claims and their average values based on historical trends from prior accident periods, adjusted for the current environment and supplemented with actual data for the accident year analyzed to the extent available.

Utilizing individual claim adjuster estimates of the large claims, combined with continual monitoring of the aggregate accuracy of such claim adjuster estimates. (This monitoring may lead to supplemental adjustments to the aggregate of such claim estimates.)

Utilizing historic longer-term average ratios of large claims to small claims, and applying such ratios to the estimated ultimate small claims from conventional analysis.

Ground-up analysis of the underlying exposure (typically used for asbestos and environmental).

The results of such methodologies are subjected to various reasonability and diagnostic tests, including paid-to-incurred loss ratios, implied incurred-loss-to-earned-premium ratios and non-zero claim severity trends. An actual versus expected analysis is also performed comparing actual loss development to expected development embedded within management's best estimate. Additional analyses may be performed based on the results of these diagnostics, including the investigation of other actuarial methods.

The methods described above are generally utilized to evaluate management's existing estimate for prior accident periods. For the initial estimate of the current accident year, the available claim data is typically insufficient to produce a reliable indication. Hence, the initial estimate for an accident year is generally based on a loss ratio projection method, which uses the earned premium for the current year multiplied by a projected loss ratio. The projected loss ratio is determined through an analysis of prior periods' experience, using loss trend, rate level differences, mix of business changes and other known or observed factors influencing the current accident year relative to prior accident years. The exact number of prior accident years utilized varies by product line component, based on the volume of business for that component and the reliability of an individual accident year estimate.

Management's estimates

At least once per quarter, certain members of Company management meet with the Company's actuaries to review the latest claims and claim adjustment expense reserve analyses. Based on these analyses, management determines whether its ultimate claim liability estimates should be changed. In doing so, it must evaluate whether the new data provided represents credible actionable information or an anomaly that will have no effect on estimated ultimate claim liability. For example, as described above, payments may have decreased in one geographic region due to fewer claim adjusters being available to process claims. The resulting claim payment patterns would be analyzed to determine whether or not the change in payment pattern represents a change in ultimate claim liability.

Such an assessment requires considerable judgment. It is frequently not possible to determine whether a change in the data is an anomaly until sometime after the event. Even if a change is

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determined to be permanent, it is not always possible to reliably determine the extent of the change until sometime later. The overall detailed analyses supporting such an effort can take several months to perform. This is because the underlying causes of the trends observed need to be evaluated, which may require the gathering or assembling of data not previously available. It may also include interviews with experts involved with the underlying processes. As a result, there can be a time lag between the emergence of a change and a determination that the change should be reflected in the Company's estimated claim liabilities. The final estimate selected by management in a reporting period is based on these various detailed analyses of past data, adjusted to reflect any new actionable information.

The Audit Committee of the Board of Directors is responsible for providing oversight of reserving propriety, and annually reviews the process by which the Company establishes reserves.

Discussion of Product Lines

The following section details reserving considerations and common risk factors by product line. There are many additional risk factors that may impact ultimate claim costs. Each risk factor presented will have a different impact on required reserves. Also, risk factors can have offsetting or compounding effects on required reserves. For example, in workers' compensation, the use of expensive medical procedures that result in medical cost inflation may enable workers to return to work faster, thereby lowering indemnity costs. Thus, in almost all cases, it is impossible to discretely measure the effect of a single risk factor and construct a meaningful sensitivity expectation.

In order to provide information on reasonably possible reserving changes by product line, the historical changes in year-end claims and claim adjustment expense reserves over a one-year period are provided for the U.S. product lines. This information is provided for both the Company and the industry for the nine most recent years, and is based on the most recent publicly available data for the reported line(s) that most closely match the individual product line being discussed. These changes were calculated, net of reinsurance, from statutory annual statement data found in Schedule P of those statements, and represent the reported reserve development on the beginning-of-the-year claim liabilities divided by the beginning claim liabilities, all accident years combined, excluding non-defense related claim adjustment expense. Data presented for the Company includes history for the entire Travelers group (U.S. companies only), whether or not the individual subsidiaries were originally part of SPC or TPC. This treatment is required by the statutory reporting instructions promulgated by state regulatory authorities for Schedule P. Comparable data for non-U.S. companies is not available.

General Liability

General liability is generally considered a long tail line, as it takes a relatively long period of time to finalize and settle claims from a given accident year. The speed of claim reporting and claim settlement is a function of the specific coverage provided, the jurisdiction and specific policy provisions such as self-insured retentions. There are numerous components underlying the general liability product line. Some of these have relatively moderate payment patterns (with most of the claims for a given accident year closed within five to seven years), while others can have extreme lags in both reporting and payment of claims (e.g., a reporting lag of a decade or more for "construction defect" claims).

While the majority of general liability coverages are written on an "occurrence" basis, certain general liability coverages (such as those covering directors and officers or professional liability) are typically insured on a "claims-made" basis.

General liability reserves are generally analyzed as two components: primary and excess/umbrella, with the primary component generally analyzed separately for bodily injury and property damage. Bodily injury liability payments reimburse the claimant for damages pertaining to physical injury as a result of the policyholder's legal obligation arising from non-intentional acts such as negligence, subject to the insurance policy provisions. In some cases the damages can include future wage loss (which is a

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function of future earnings power and wage inflation) and future medical treatment costs. Property damage liability payments result from damages to the claimant's private property arising from the policyholder's legal obligation for non-intentional acts. In most cases, property damage losses are a function of costs as of the loss date, or soon thereafter.

In addition, sizable or unique exposures are reviewed separately. These exposures include asbestos, environmental, other mass torts, construction defect and large unique accounts that would otherwise distort the analysis. These unique categories often require a very high degree of judgment and require reserve analyses that do not rely on conventional actuarial methods.

Defense costs are also a part of the insured costs covered by liability policies and can be significant, sometimes greater than the cost of the actual paid claims. For some products this risk is mitigated by policy language such that the insured portion of defense costs erodes the amount of policy limit available to pay the claim. Such "defense within the limits" policies are most common for "claims-made" products. When defense costs are outside of the limits, amounts paid for defense costs do not erode the policy limits.

This line is typically the largest source of reserve estimate uncertainty in the United States (excluding assumed reinsurance contracts covering the same risk). Major contributors to this reserve estimate uncertainty include the reporting lag (i.e., the length of time between the event triggering coverage and the actual reporting of the claim), the number of parties involved in the underlying tort action, whether the "event" triggering coverage is confined to only one time period or is spread over multiple time periods, the potential dollars involved (in the individual claim actions), whether such claims were reasonably foreseeable and intended to be covered at the time the contracts were written (i.e., coverage dispute potential), and the potential for mass claim actions. Claims with longer reporting lags result in greater inherent risk. This is especially true for alleged claims with a latency feature, particularly where courts have ruled that coverage is spread over multiple policy years, hence involving multiple defendants (and their insurers and reinsurers) and multiple policies (thereby increasing the potential dollars involved and the underlying settlement complexity). Claims with long latencies also increase the potential recognition lag (i.e., the lag between writing a type of policy in a certain market and the recognition that such policies have potential mass tort and/or latent claim exposure).

The amount of reserve estimate uncertainty also varies significantly by component for the general liability product line. The components in this product line with the longest latency, longest reporting lags, largest potential dollars involved and greatest claim settlement complexity are asbestos and environmental. Components that include latency, reporting lag and/or complexity issues, but to a materially lesser extent than asbestos and environmental, include construction defect and other mass tort actions. Many components of general liability are not subject to material latency or claim complexity risks and hence have materially less uncertainty than the previously mentioned components. In general, policies providing coverage with shorter reporting lags, fewer parties involved in settlement negotiations, only one policy potentially triggered per claim, fewer potential settlement dollars, reasonably foreseeable (and stable) potential hazards/claims and no mass tort potential result in much less reserve estimate uncertainty than policies without those characteristics.

In addition to the conventional actuarial methods mentioned in the general discussion section, the company utilizes various report year development and S-curve methods for the construction defect components of this product line. The Construction Defect report year development analysis is supplemented with projected claim counts and average values for IBNR claim counts. For components with greater lags in claim reporting, such as excess and umbrella components of this product line, the company relies more heavily on the BF method than on the paid and case incurred development methods.

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Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required general liability reserves (beyond those included in the general discussion section) include:

General liability risk factors

- Changes in claim handling philosophies
- Changes in policy provisions or court interpretation of such provisions
- New or expanded theories of liability
- Trends in jury awards
- Changes in the propensity to sue, in general with specificity to particular issues
- Changes in the propensity to litigate rather than settle a claim
- Changes in statutes of limitations
- Changes in the underlying court system
- Distortions from losses resulting from large single accounts or single issues
- Changes in tort law
- Shifts in lawsuit mix between federal and state courts
- Changes in claim adjuster office structure (causing distortions in the data)
- The potential impact of inflation on loss costs
- Changes in settlement patterns

General liability book of business risk factors

- Changes in policy provisions (e.g., deductibles, policy limits, endorsements)
- Changes in underwriting standards

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Product mix (e.g., size of account, industries insured, jurisdiction mix)

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for general liability (excluding asbestos and environmental), a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.5% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line, excluding estimated asbestos and environmental amounts, over the last nine years has varied from -8% to 4% (averaging -3%) for the Company and from -5% to 5% (averaging -2%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. General liability reserves (excluding asbestos and environmental) represent approximately 22% of the Company's total claims and claim adjustment expense reserves.

The Company's change in reserve estimate for this product line, excluding estimated asbestos and environmental amounts, was -4% for 2013, -3% for 2012 and -8% for 2011. The 2013 change was primarily concentrated in accident years 2010 and prior and reflected what the Company believes are more favorable legal and judicial environments than what the Company previously expected. The 2012 change was primarily concentrated in excess coverages for accident years 2009 and prior and reflected what the Company believes are more favorable legal and judicial environments than what the Company



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previously expected. Also contributing to the 2012 change was better than expected results for management liability business, primarily for the errors & omissions and fiduciary products for accident years 2007 and prior. The 2011 change was concentrated in excess coverages for accident years 2005-2008 and reflected what the Company believes are more favorable legal and judicial environments than what the Company previously expected.

**Commercial Property**

Commercial property is generally considered a short tail line with a simpler and faster claim reporting and adjustment process than liability coverages, and less uncertainty in the reserve setting process (except for more complex business interruption claims). It is generally viewed as a moderate frequency, low to moderate severity line, except for catastrophes and coverage related to large properties. The claim reporting and settlement process for property coverage claim reserves is generally restricted to the insured and the insurer. Overall, the claim liabilities for this line create a low estimation risk, except possibly for catastrophes and business interruption claims.

Commercial property reserves are typically analyzed in two components, one for catastrophic or other large single events, and another for all other events. Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required property reserves (beyond those included in the general discussion section) include:

Commercial property risk factors

Physical concentration of policyholders

Availability and cost of local contractors

For the more severe catastrophic events, "demand surge" inflation, which refers to significant short-term increases in building material and labor costs due to a sharp increase in demand for those materials and services

Local building codes

Amount of time to return property to full usage (for business interruption claims)

Frequency of claim re-openings on claims previously closed

Court interpretation of policy provisions (such as occurrence definition, or wind versus flooding)

Lags in reporting claims (e.g., winter damage to summer homes, hidden damage after an earthquake, hail damage to roofs and/or equipment on roofs)

Court or legislative changes to the statute of limitations

Commercial property book of business risk factors

Policy provisions mix (e.g., deductibles, policy limits, endorsements)

Changes in underwriting standards

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Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for property, a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.1% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line over the last nine years has varied from -34% to -5% (averaging -18%) for the Company, and from -14% to -5% (averaging -10%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes

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is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Commercial property reserves represent approximately 3% of the Company's total claims and claim adjustment expense reserves.

Since commercial property is considered a short tail coverage, the one year change for commercial property can be more volatile than that for the longer tail product lines. This is due to the fact that the majority of the reserve for commercial property relates to the most recent accident year, which is subject to the most uncertainty for all product lines. This recent accident year uncertainty is relevant to commercial property because of weather-related events which, notwithstanding 2010 and 2011 experience, tend to be concentrated in the second half of the year, and generally are not completely resolved until the following year. Reserve estimates associated with major catastrophes may take even longer to resolve. The reserve estimates for this product line are also potentially subject to material changes due to uncertainty in measuring ultimate losses for significant catastrophes such as the events of September 11, 2001, Hurricane Katrina and Storm Sandy.

The Company's change in reserve estimate for this product line was -17% for 2013, -22% for 2012 and -5% for 2011. The 2013 change primarily reflected better than expected loss experience for accident years 2010 through 2012, driven by favorable loss development related to both catastrophe and non-catastrophe losses. The 2012 change primarily reflected better than expected development for accident years 2009 through 2011, driven by favorable loss development related to catastrophe losses incurred in 2011, and by higher subrogation and salvage recoveries for accident years 2009 through 2011. The 2011 change primarily reflected better than expected development in the 2008 and 2009 accident years for certain large national property and ocean marine exposures.

**Commercial Multi-Peril**

Commercial multi-peril provides a combination of property and liability coverage typically for small businesses and, therefore, includes both short and long tail coverages. For property coverage, it generally takes a relatively short period of time to close claims, while for the other coverages, generally for the liability coverages, it takes a longer period of time to close claims.

The reserving risk for this line is dominated by the liability coverage portion of this product, except occasionally in the event of catastrophic or large single losses. The reserving risk for this line differs from that of the general liability product line and the property product line due to the nature of the customer. Commercial multi-peril is generally sold to smaller-sized accounts, while the customer profile for general liability and commercial property includes larger customers.

See "Commercial property risk factors" and "General liability risk factors," discussed above, with regard to reserving risk for commercial multi-peril.

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for commercial multi-peril (excluding asbestos and environmental), a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.2% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line over the last nine years has varied from -19% to 5% (averaging -5%) for the Company, and from -6% to 2% (averaging -3%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Commercial multi-peril reserves (excluding asbestos and environmental reserves) represent approximately 7% of the Company's total claims and claim adjustment expense reserves.

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As discussed above, this line combines general liability and commercial property coverages and it has been impacted in the past by many of the same events as those two lines.

The Company's change in reserve estimate for this product line was 2% for 2013, -1% for 2012 and 5% for 2011. The 2013 change primarily reflected unfavorable loss experience for the liability coverage for accident years 2008 through 2011, driven by higher than expected severity and defense costs. The 2011 change reflected unfavorable loss development driven by late reporting of hail claims incurred in 2010.

**Commercial Automobile**

The commercial automobile product line is a mix of property and liability coverages and, therefore, includes both short and long tail coverages. The payments that are made quickly typically pertain to auto physical damage (property) claims and property damage (liability) claims. The payments that take longer to finalize and are more difficult to estimate relate to bodily injury claims. In general, claim reporting lags are minor, claim complexity is not a major issue, and the line is viewed as high frequency, low to moderate severity. Overall, the claim liabilities for this line create a moderate estimation risk.

Commercial automobile reserves are typically analyzed in four components: bodily injury liability; property damage liability; collision claims; and comprehensive claims. These last two components have minimum reserve risk and fast payouts and, accordingly, separate risk factors are not presented.

The Company utilizes the conventional actuarial methods mentioned in the general discussion above in estimating claim liabilities for this line. This is supplemented with detailed custom analyses where needed.

Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required commercial automobile reserves (beyond those included in the general discussion section) include:

Bodily injury and property damage liability risk factors

Trends in jury awards

Changes in the underlying court system

Changes in case law

Litigation trends

Frequency of claims with payment capped by policy limits

Change in average severity of accidents, or proportion of severe accidents

Changes in auto safety technology

Subrogation opportunities

Changes in claim handling philosophies

Frequency of visits to health providers

Number of medical procedures given during visits to health providers

Types of health providers used

Types of medical treatments received

Changes in cost of medical treatments

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Degree of patient responsiveness to treatment

Commercial automobile book of business risk factors

Changes in policy provisions (e.g., deductibles, policy limits, endorsements, etc.)

Changes in mix of insured vehicles (e.g., long haul trucks versus local and smaller vehicles, fleet risks versus non-fleets)

Changes in underwriting standards

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for commercial automobile, a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.2% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line over the last nine years has varied from -10% to 7% (averaging -3%) for the Company, and from -3% to 2% (averaging -1%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Commercial automobile reserves represent approximately 7% of the Company's total claims and claim adjustment expense reserves.

The Company's change in reserve estimate for this product line was 1% for 2013, 7% for 2012 and 5% for 2011. The 2012 change reflected higher than expected severity in the bodily injury coverage primarily for accident years 2010 and 2011. The 2011 change reflected higher than expected severity for the 2009 and 2010 accident years.

Workers' Compensation

Workers' compensation is generally considered a long tail coverage, as it takes a relatively long period of time to finalize claims from a given accident year. While certain payments such as initial medical treatment or temporary wage replacement for the injured worker are made quickly, some other payments are made over the course of several years, such as awards for permanent partial injuries. In addition, some payments can run as long as the injured worker's life, such as permanent disability benefits and on-going medical care. Despite the possibility of long payment tails, the reporting lags are generally short, settlements are generally not complex, and most of the liability can be considered high frequency with moderate severity. The largest reserve risk generally comes from the low frequency, high severity claims providing lifetime coverage for medical expense arising from a worker's injury, as such claims are subject to greater inflation risk. Overall, the claim liabilities for this line create a somewhat greater than moderate estimation risk.

Workers' compensation reserves are typically analyzed in three components: indemnity losses, medical losses and claim adjustment expenses.

Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required workers' compensation reserves (beyond those included in the general discussion section) include:

Indemnity risk factors

Time required to recover from the injury

Degree of available transitional jobs

Degree of legal involvement



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Changes in the interpretations and processes of the administrative bodies that oversee workers' compensation claims

Future wage inflation for states that index benefits

Changes in the administrative policies of second injury funds

Medical risk factors

Changes in the cost of medical treatments (including prescription drugs) and underlying fee schedules ("inflation")

Frequency of visits to health providers

Number of medical procedures given during visits to health providers

Types of health providers used

Type of medical treatments received

Use of preferred provider networks and other medical cost containment practices

Availability of new medical processes and equipment

Changes in the use of pharmaceutical drugs

Degree of patient responsiveness to treatment

General workers' compensation risk factors

Frequency of claim reopenings on claims previously closed

Mortality trends of injured workers with lifetime benefits and medical treatment

Degree of cost shifting between workers' compensation and health insurance, including Medicare, and the impact, if any, of the Affordable Care Act.

Workers' compensation book of business risk factors

Product mix



Injury type mix

Changes in underwriting standards

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for workers' compensation, a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.3% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line over the last nine years has varied from -2% to 1% (averaging 0%) for the Company, and from -1% to 2% (averaging 0%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Workers' compensation reserves represent approximately 35% of the Company's total claims and claim adjustment expense reserves.

The Company's change in reserve estimate for this product line was -1% in 2013, -2% in 2012 and 0% for 2011. The 2012 change was primarily driven by better than expected frequency and severity related to lifetime medical claims for accident years 2008 and prior.

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**Fidelity and Surety**

Fidelity is generally considered a short tail coverage. It takes a relatively short period of time to finalize and settle fidelity claims. The volatility of fidelity reserves is generally related to the type of business of the insured, the size and complexity of the insured's business operations, amount of policy limit and attachment point of coverage. The uncertainty surrounding reserves for small, commercial insureds is typically less than the uncertainty for large commercial or financial institutions. The high frequency, low severity nature of small commercial fidelity losses provides for stability in loss estimates, whereas the low frequency, high severity nature of losses for large insureds results in a wider range of ultimate loss outcomes. Actuarial techniques that rely on a stable pattern of loss development are generally not applicable to low frequency, high severity policies.

Surety has certain components that are generally considered short tail coverages with short reporting lags, although large individual construction and commercial surety contracts can result in a long settlement tail, based on the length and complexity of the construction project or commercial transaction being insured. (Large construction projects can take many years to complete.) The frequency of losses in surety generally correlates with economic cycles as the primary cause of surety loss is the inability of an insured contractor to fulfill its contractual obligations. The Company actively seeks to mitigate this exposure to loss through disciplined risk selection and adherence to underwriting standards. The volatility of surety losses is generally related to the type of business performed by the insured, the type of bonded obligation, the amount of limit exposed to loss and the amount of assets available to the insurer to mitigate losses, such as unbilled contract funds, collateral, first and third party indemnity, and other security positions of an insured's assets. Certain classes of surety claims are very high severity, low frequency in nature. These can include large construction contractors involved with one or multiple large, complex projects as well as certain large commercial surety exposures. Other claim factors affecting reserve variability of surety include litigation related to amounts owed by and due the insured (e.g., salvage and subrogation efforts) and the results of financial restructuring of an insured.

Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required fidelity and surety reserves (beyond those included in the general discussion section) include:

Fidelity risk factors

Type of business of insured

Policy limit and attachment points

Third-party claims

Coverage litigation

Complexity of claims

Growth in insureds' operations

Surety risk factors

Economic trends, including the general level of construction activity

Concentration of reserves in a relatively few large claims

Type of business insured

Type of obligation insured

Cumulative limits of liability for insured

Assets available to mitigate loss

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Defective workmanship/latent defects

Financial strategy of insured

Changes in statutory obligations

Geographic spread of business

Fidelity and Surety book of business risk factors

Changes in policy provisions (e.g., deductibles, limits, endorsements)

Changes in underwriting standards

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for fidelity and surety, a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.3% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line over the last nine years has varied from -21% to 0% (averaging -8%) for the Company, and from -13% to 24% (averaging -1%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Fidelity and surety reserves represent approximately 2% of the Company's total claims and claim adjustment expense reserves.

In general, developments on single large claims (both adverse and favorable) are a primary source of changes in reserve estimates for this product line.

The Company's change in reserve estimate for this product line was -21% for 2013, -8% for 2012 and -11% for 2011. The 2013 change reflected better than expected results primarily for the contract surety line of business for accident years 2010 and prior. The 2012 change reflected better than expected results primarily for the contract surety line of business for accident years 2008 and prior. The 2011 change primarily reflected better than expected development for accident years 2008 and prior for the contract surety business.

**Personal Automobile**

Personal automobile includes both short and long tail coverages. The payments that are made quickly typically pertain to auto physical damage (property) claims and property damage (liability) claims. The payments that take longer to finalize and are more difficult to estimate relate to bodily injury claims. Reporting lags are relatively short and the claim settlement process for personal automobile liability generally is the least complex of the liability products. It is generally viewed as a high frequency, low to moderate severity product line. Overall, the claim liabilities for this line create a moderate estimation risk.

Personal automobile reserves are typically analyzed in five components: bodily injury liability, property damage liability, no-fault losses, collision claims and comprehensive claims. These last two components have minimum reserve risk and fast payouts and, accordingly, separate factors are not presented.

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Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required personal automobile reserves (beyond those included in the general reserve discussion section) include:

Bodily injury and property damage liability risk factors

Trends in jury awards

Changes in the underlying court system and its philosophy

Changes in case law

Litigation trends

Frequency of claims with payment capped by policy limits

Change in average severity of accidents, or proportion of severe accidents

Subrogation opportunities

Degree of patient responsiveness to treatment

Changes in claim handling philosophies

No-fault risk factors (for selected states and time periods)

Effectiveness of no-fault laws

Frequency of visits to health providers

Number of medical procedures given during visits to health providers

Types of health providers used

Types of medical treatments received

Changes in cost of medical treatments

Degree of patient responsiveness to treatment

Personal automobile book of business risk factors

Changes in policy provisions (e.g., deductibles, policy limits, endorsements, etc.)

Changes in underwriting standards

Changes in the use of credit data for rating and underwriting

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for personal automobile, a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.1% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line over the last nine years has varied from -9% to 3% (averaging -2%) for the Company, and from -4% to -1% (averaging -3%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Personal automobile reserves represent approximately 5% of the Company's total claims and claim adjustment expense reserves.

The Company's change in reserve estimate for this product line was 1% for 2013, 2% for 2012 and 3% for 2011. The 2012 change was primarily driven by higher than expected bodily injury severity for

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accident year 2011. The 2011 change reflected worse than expected severity for the 2007-2010 accident years.

**Homeowners and Personal Lines Other**

Homeowners is generally considered a short tail coverage. Most payments are related to the property portion of the policy, where the claim reporting and settlement process is generally restricted to the insured and the insurer. Claims on property coverage are typically reported soon after the actual damage occurs, although delays of several months are not unusual. The resulting settlement process is typically fairly short term, although exceptions do exist.

The liability portion of the homeowners policy generates claims which take longer to pay due to the involvement of litigation and negotiation, but with generally small reporting lags.

Overall, the line is generally high frequency, low to moderate severity (except for catastrophes), with simple to moderate claim complexity.

Homeowners reserves are typically analyzed in two components: non-catastrophe related losses and catastrophe loss payments.

Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required homeowners reserves (beyond those included in the general discussion section) include:

Non-catastrophe risk factors

Salvage opportunities

Amount of time to return property to residential use

Changes in weather patterns

Local building codes

Litigation trends

Trends in jury awards

Court interpretation of policy provisions (such as occurrence definition, or wind versus flooding)

Lags in reporting claims (e.g., winter damage to summer homes, hidden damage after an earthquake, hail damage to roofs and/or equipment on roofs)

Court or legislative changes to the statute of limitations

Catastrophe risk factors

Physical concentration of policyholders

Availability and cost of local contractors

Local building codes

Quality of construction of damaged homes

Amount of time to return property to residential use

For the more severe catastrophic events, "demand surge" inflation, which refers to significant short-term increases in building material and labor costs due to a sharp increase in demand for those materials and services

Homeowners book of business risk factors

Policy provisions mix (e.g., deductibles, policy limits, endorsements, etc.)



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Degree of concentration of policyholders

Changes in underwriting standards

Changes in the use of credit data for rating and underwriting

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for homeowners and personal lines other, a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.0% increase (decrease) in claims and claim adjustment expense reserves.

Historically, the one-year change in the reserve estimate for this product line (excluding the umbrella line of business, which for statutory reporting purposes is included with the general liability line of business) over the last nine years has varied from -22% to 3% (averaging -9%) for the Company, and from -8% to -2% (averaging -5%) for the industry overall. The Company's year-to-year changes are driven by, and are based on, observed events during the year. The Company believes that its range of historical outcomes is illustrative of reasonably possible one-year changes in reserve estimates for this product line. Homeowners and personal lines other reserves represent approximately 2% of the Company's total claims and claim adjustment expense reserves.

This line combines both liability and property coverages; however, the majority of the reserves relate to property. While property is considered a short tail coverage, the one year change for property can be more volatile than that for the longer tail product lines. This is due to the fact that the majority of the reserve for property relates to the most recent accident year, which is subject to the most uncertainty for all product lines. This recent accident year uncertainty is relevant to property because of weather related events which, notwithstanding 2010 and 2011 experience, tend to be concentrated in the second half of the year, and generally are not completely resolved until the following year. Reserve estimates associated with major catastrophes may take even longer to resolve.

The Company's change in reserve estimate for this product line (excluding the umbrella line of business) was -17% for 2013, -11% for 2012 and -7% for 2011. The 2013 change was primarily driven by better than expected loss experience for catastrophe losses incurred in 2012 and non-catastrophe weather-related losses and non-weather-related losses for accident years 2012 and 2011. The 2012 change reflected better than expected loss development related to catastrophe losses incurred in 2011 and non-catastrophe losses incurred in accident years 2010 and 2011. The 2011 change reflected better than expected loss development related to catastrophe losses incurred in the first half of 2010.

**International and other**

International and other includes products written by the Company's international operations, as well as all other products not explicitly discussed above. The principal component of "other" claim reserves is assumed reinsurance written on an excess-of-loss basis, which may include reinsurance of non-U.S. exposures, and is runoff business.

International and other claim liabilities result from a mix of coverages, currencies and jurisdictions/countries. The common characteristic is the need to customize the analysis to the individual component, and the inability to rely on data characterizations and reporting requirements in the U.S. statutory reporting framework.

Due to changes in the business mix for this line over time, including the recent acquisition of Dominion, the recently incurred claim liabilities are relatively shorter tail (due to both the products and the jurisdictions involved, e.g., Canada, the Republic of Ireland and the United Kingdom), while the older liabilities include some from runoff operations that are extremely long tail (e.g., U.S. excess liabilities reinsured through the London market, and several underwriting pools in runoff). The speed

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of claim reporting and claim settlement is a function of the specific coverage provided, the jurisdiction, the distribution system (e.g., underwriting pool versus direct) and the proximity of the insurance sale to the insured hazard (e.g., insured and insurer located in different countries). In particular, liabilities arising from the underwriting pools in runoff may result in significant reporting lags, settlement lags and claim complexity, due to the need to coordinate with other pool members or co-insurers through a broker or lead-insurer for claim settlement purposes.

International reserves are generally analyzed by country and general coverage category (e.g. General Liability in Canada, Commercial Property in the United Kingdom, etc.). The business is also generally split by direct versus assumed reinsurance for a given coverage. Where the underlying insured hazard is outside the United States, the underlying coverages are generally similar to those described under the Homeowners, Personal Automobile, Commercial Automobile, General Liability, Commercial Property and Surety discussions above, taking into account differences in the legal environment and differences in terms and conditions. For example, in some jurisdictions there are no aggregate policy limits on certain liability coverages.

Other reserves, primarily assumed reinsurance in runoff, are generally analyzed by program/pool, treaty type, and general coverage category (e.g. General Liability excess of loss reinsurance). Excess exposure requires the insured to "prove" not only claims under the policy, but also the prior payment of claims reaching up to the excess policy's attachment point.

Examples of common risk factors, or perceptions thereof, that could change and, thus, affect the required International and other reserves (beyond those included in the general discussion section, and in the Personal Automobile, Homeowners, General Liability, Commercial Property, Commercial Automobile and Surety discussions above) include:

International and other risk factors

Changes in claim handling procedures, including those of the primary carriers

Changes in policy provisions or court interpretation of such provision

New theories of liability

Trends in jury awards

Changes in the propensity to sue

Changes in statutes of limitations

Changes in the underlying court system

Distortions from losses resulting from large single accounts or single issues

Changes in tort law

Changes in claim adjuster office structure (causing distortions in the data)

International and other book of business risk factors

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Changes in policy provisions (e.g., deductibles, policy limits, endorsements, "claims-made" language)

Changes in underwriting standards

Product mix (e.g., size of account, industries insured, jurisdiction mix)

Unanticipated changes in risk factors can affect reserves. As an indicator of the causal effect that a change in one or more risk factors could have on reserves for International and other (excluding asbestos and environmental), a 1% increase (decrease) in incremental paid loss development for each future calendar year could result in a 1.2% increase (decrease) in claims and claim adjustment expense reserves. International and other reserves (excluding asbestos and environmental) represent approximately 11% of the Company's total claims and claim adjustment expense reserves.

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International and other represents a combination of different product lines, some of which are in runoff. Comparative historical information is not available for international product lines as insurers domiciled outside of the U.S. do not file U.S. statutory reports. Comparative historical information on runoff business is not indicative of reasonably possible one-year changes in the reserve estimate for this mix of runoff business. Accordingly, the Company has not included comparative analyses for International and other.

**Reinsurance Recoverables**

Amounts recoverable from reinsurers are estimated in a manner consistent with the associated claim liability. 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. In addition, in the ordinary course of business, the Company becomes involved in coverage disputes with its reinsurers. Some of these disputes could result in lawsuits and arbitrations brought by or against the reinsurers to determine the Company's rights and obligations under the various reinsurance agreements. The Company employs dedicated specialists and aggressive strategies to manage reinsurance collections and disputes.

The Company has entered into two reinsurance contracts in connection with catastrophe bonds issued by Long Point Re III. Both of these contracts meet the requirements to be accounted for as reinsurance in accordance with guidance for accounting for reinsurance contracts. The catastrophe bonds are described in more detail in "Item 1 Business Catastrophe Reinsurance."

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, disputes, applicable coverage defenses 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. From time to time, as a result of the long-tailed nature of the underlying liabilities, coverage complexities and potential for disputes, the Company considers the commutation of reinsurance contracts. Changes in estimated reinsurance recoverables and commutation activity could result in additional income statement charges.

Recoverables attributable to structured settlements relate primarily to personal injury claims, of which workers' compensation claims comprise a significant portion, for which the Company has purchased annuities and remains contingently liable in the event of a default by the companies issuing the annuities. Recoverables attributable to mandatory pools and associations relate primarily to workers' compensation service business. These recoverables are supported by the participating insurance companies' obligation to pay a pro rata share based on each company's voluntary market share of written premium in each state in which it is a pool participant. In the event a member of a mandatory pool or association defaults on its share of the pool's or association's obligations, the other members' share of such obligation increases proportionally.

For a discussion of a pending reinsurance dispute pertaining to a portion of the Company's reinsurance recoverable from the Munich Re Group, see note 16 of notes to the consolidated financial statements.

**Investment Valuation and Impairments**

*Fair Value Measurements*

The Company's estimates of fair value for financial assets and financial liabilities are based on the framework established in the fair value accounting guidance. The framework is based on the inputs used in valuation, gives the highest priority to quoted prices in active markets and requires that

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observable inputs be used in the valuations when available. The disclosure of fair value estimates in the fair value accounting guidance hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions. The level in the fair value hierarchy within which the fair value measurement is reported is based on the lowest level input that is significant to the measurement in its entirety. The three levels of the hierarchy are as follows:

Level 1 Unadjusted quoted market prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; or valuations based on models where the significant inputs are observable (e.g., interest rates, yield curves, prepayment speeds, default rates, loss severities, etc.) or can be corroborated by observable market data.

Level 3 Valuations based on models where significant inputs are not observable. The unobservable inputs reflect the Company's own assumptions about the inputs that market participants would use.

***Valuation of Investments Reported at Fair Value in Financial Statements***

The fair value of a financial instrument is the estimated amount at which the instrument could be exchanged in an orderly transaction between knowledgeable, unrelated, willing parties, i.e., not in a forced transaction. The estimated fair value of a financial instrument may differ from the amount that could be realized if the security was sold in an immediate sale, e.g., a forced transaction. Additionally, the valuation of investments is more subjective when markets are less liquid due to the lack of market based inputs, which may increase the potential that the estimated fair value of an investment is not reflective of the price at which an actual transaction would occur.

For investments that have quoted market prices in active markets, the Company uses the unadjusted quoted market prices as fair value and includes these prices in the amounts disclosed in Level 1 of the hierarchy. The Company receives the quoted market prices from a third party, nationally recognized pricing service (pricing service). When quoted market prices are unavailable, the Company utilizes a pricing service to determine an estimate of fair value, which is mainly used for its fixed maturity investments. The fair value estimates provided from this pricing service are included in the amount disclosed in Level 2 of the hierarchy. If quoted market prices and an estimate from a pricing service are unavailable, the Company produces an estimate of fair value based on internally developed valuation techniques, which, depending on the level of observable market inputs, will render the fair value estimate as Level 2 or Level 3. The Company bases all of its estimates of fair value for assets on the bid price as it represents what a third-party market participant would be willing to pay in an arm's length transaction.

***Fixed Maturities***

The Company utilized a pricing service to estimate fair value measurements for approximately 98% of its fixed maturities at both December 31, 2013 and 2012. The pricing service utilizes market quotations for fixed maturity securities that have quoted prices in active markets. Since fixed maturities other than U.S. Treasury securities generally do not trade on a daily basis, the pricing service prepares estimates of fair value measurements for these securities using its proprietary pricing applications, which include available relevant market information, benchmark curves, benchmarking of like securities, sector groupings and matrix pricing. Additionally, the pricing service uses an Option Adjusted Spread model to develop prepayment and interest rate scenarios.

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The pricing service evaluates each asset class based on relevant market information, relevant credit information, perceived market movements and sector news. The market inputs utilized in the pricing evaluation, listed in the approximate order of priority, include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data, and industry and economic events. The extent of the use of each market input depends on the asset class and the market conditions. Depending on the security, the priority of the use of inputs may change or some market inputs may not be relevant. For some securities, additional inputs may be necessary.

The pricing service utilized by the Company has indicated that it will only produce an estimate of fair value if there is objectively verifiable information to produce a valuation. If the pricing service discontinues pricing an investment, the Company would be required to produce an estimate of fair value using some of the same methodologies as the pricing service but would have to make assumptions for market-based inputs that are unavailable due to market conditions.

The fair value estimates of most fixed maturity investments are based on observable market information rather than market quotes. Accordingly, the estimates of fair value for such fixed maturities, other than U.S. Treasury securities, provided by the pricing service are included in the amount disclosed in Level 2 of the hierarchy. The estimated fair value of U.S. Treasury securities is included in the amount disclosed in Level 1 as the estimates are based on unadjusted market prices.

The Company reviews the estimates of fair value provided by the pricing service and compares the estimates to the Company's knowledge of the market to determine if the estimates obtained are representative of the prices in the market. In addition, the Company has periodic discussions with the pricing service to discuss any changes in their process and reactions to overall markets. The Company produces a report monthly that lists all price changes from the previous month in excess of 10%. The Company reviews the report and will challenge any prices deemed not to be representative of fair value. In addition, the Company has implemented various other processes including randomly selecting purchased or sold securities and comparing execution prices to the estimates from the pricing service as well as reviewing reports that contain securities whose valuation did not change from their previous valuation (stale price review). The Company also uses an additional independent pricing service to further test the primary pricing service's valuation of the Company's fixed maturity portfolio. These processes have not highlighted any significant issues with the fair value estimates received from the pricing service.

The Company also holds certain fixed maturity investments which are not priced by the pricing service and, accordingly, estimates the fair value of such fixed maturities using an internal matrix that is based on market information regarding interest rates, credit spreads and liquidity. The underlying source data for calculating the matrix of credit spreads relative to the U.S. Treasury curve are the BofA Merrill Lynch U.S. Corporate Index and the BofA Merrill Lynch High Yield BB Rated Index. The Company includes the fair value estimates of these corporate bonds in Level 2, since all significant inputs are market observable.

While the vast majority of the Company's municipal bonds and corporate bonds are included in Level 2, the Company holds a number of municipal bonds and corporate bonds which are not valued by the pricing service and estimates the fair value of these bonds using an internal pricing matrix with some unobservable inputs that are significant to the valuation. Due to the limited amount of observable market information, the Company includes the fair value estimates for these particular bonds in Level 3. The fair value of the fixed maturities for which the Company used an internal pricing matrix was \$94 million and \$102 million at December 31, 2013 and 2012, respectively. Additionally, the Company holds a small amount of other fixed maturity investments that have characteristics that make them unsuitable for matrix pricing. For these fixed maturities, the Company obtains a quote from a broker (primarily the market maker). The fair value of the fixed maturities for which the Company

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received a broker quote was \$161 million and \$128 million at December 31, 2013 and 2012, respectively. Due to the disclaimers on the quotes that indicate that the price is indicative only, the Company includes these fair value estimates in Level 3.

*Non-Fixed Maturities and Other Investments Not Reported at Fair Value*

See note 4 of notes to the Company's consolidated financial statements for a discussion of the determination of fair value of non-fixed maturities and valuation of investments not reported at fair value in the financial statements.

**Investment Impairments**

The Company conducts a periodic review to identify and evaluate invested assets having other-than-temporary impairments. Some of the factors considered in identifying other-than-temporary impairments include: (1) for fixed maturity investments, whether the Company intends to sell the investment or whether it is more likely than not that the Company will be required to sell the investment prior to an anticipated recovery in value; (2) for non-fixed maturity investments, the Company's ability and intent to retain the investment for a reasonable period of time sufficient to allow for an anticipated recovery in value; (3) the likelihood of the recoverability of principal and interest for fixed maturity securities (i.e., whether there is a credit loss) or cost for equity securities; (4) the length of time and extent to which the fair value has been less than amortized cost for fixed maturity securities or cost for equity securities; and (5) the financial condition, near-term and long-term prospects for the issuer, including the relevant industry conditions and trends, and implications of rating agency actions and offering prices.

*Other-Than-Temporary Impairments of Fixed Maturities and Equity Securities*

For fixed maturity investments 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 the credit loss component of the impairment from the amount related to all other factors and reports the credit loss component in net realized investment gains (losses). The impairment related to all other factors is reported in other comprehensive income.

For equity securities (including public common and non-redeemable preferred stock) and for fixed maturity investments the Company intends to sell or for which it is more likely than not that the Company will be required to sell before an anticipated recovery in value, the full amount of the impairment is included in net realized investment gains (losses).

Upon recognizing an other-than-temporary impairment, the new cost basis of the investment is the previous amortized cost basis less the other-than-temporary impairment recognized in net realized investment gains (losses). The new cost basis is not adjusted for any subsequent recoveries in fair value; however, for fixed maturity investments the difference between the new cost basis and the expected cash flows is accreted on a quarterly basis to net investment income over the remaining expected life of the investment.

Due to the subjective nature of the Company's analysis and estimates of future cash flows, along with the judgment that must be applied in the analysis, it is possible that the Company could reach a different conclusion whether or not to impair a security if it had access to additional information about the issuer. Additionally, it is possible that the issuer's actual ability to meet contractual obligations may be different than what the Company determined during its analysis, which may lead to a different impairment conclusion in future periods.

See note 1 of notes to the Company's consolidated financial statements for a further discussion of investment impairments.

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**Goodwill and Other Intangible Assets Impairments**

See note 1 of notes to the Company's consolidated financial statements for a discussion of impairments of goodwill and other intangible assets.

**OTHER UNCERTAINTIES**

For a discussion of other risks and uncertainties that could impact the Company's results of operations or financial position, see note 16 of notes to the Company's consolidated financial statements and "Item 1A Risk Factors."

**FUTURE APPLICATION OF ACCOUNTING STANDARDS**

See note 1 of notes to the Company's consolidated financial statements for a discussion of recently issued accounting standards updates.

The Company is currently required to prepare its financial statements in accordance with U.S. Generally Accepted Accounting Principles (GAAP), as promulgated by the Financial Accounting Standards Board (FASB). During the last several years, the Securities and Exchange Commission (SEC) has been evaluating whether, when and how International Financial Reporting Standards (IFRS) should be incorporated into the U.S. financial reporting system. Before making a decision, the SEC set forth a work plan to evaluate the remaining differences between GAAP and IFRS, determine whether IFRS represented high quality standards, consider how the International Accounting Standards Board is funded and its governance structure, and examine the variations in the way IFRS was applied by various foreign companies that file financial statements with the SEC. In July 2012, the SEC staff issued a final report on the SEC work plan which concluded that IFRS provide high quality accounting standards, but also indicated concerns with funding, consistency of application and enforcement of IFRS globally. The report did not give a recommendation to the SEC on whether, when and how IFRS should be incorporated into the U.S. financial reporting system. Additionally, the SEC has not indicated a timeline for further consideration of incorporating IFRS.

The International Accounting Standards Board (IASB) and the FASB have a convergence program with the intent of developing global standards for several significant areas of accounting, including the accounting for insurance contracts. In June 2012, the FASB issued a statement that indicated that based on the nature and totality of differences between the FASB's and IASB's views, it is not likely that the two boards will achieve convergence on this project. The FASB further noted that the FASB and IASB have very different perspectives on the project, given that the U.S. has existing guidance on insurance contracts whereas there is currently no comprehensive IFRS accounting standard for insurance contracts. In June 2013, each board issued for comment an exposure draft of the accounting for insurance contracts that has significant differences from the other board's draft as well as from current GAAP. Both exposure drafts propose changes that, if ultimately adopted, could significantly impact the accounting by insurers, including the Company, for premiums and unearned premium reserves, the liability for claims and claims adjustment expenses, reinsurance, and deferred acquisition costs. The Boards are reviewing the comments received on the exposure drafts and are expected to begin re-deliberations in the first quarter of 2014. As a result of this, it is currently unclear what changes, if any, may be made to the accounting for insurance contracts under GAAP as a result of this project. Additionally, any new standards issued by the Boards regarding insurance contracts may involve methodologies for valuing insurance contract liabilities that may be significantly different from the methodologies required by current U.S. GAAP. It is also possible that the Boards could issue different final standards that could result in the Company having to apply an accounting standard for its consolidated financial statements that is different from the accounting standard used for local reporting in foreign jurisdictions.



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The FASB and the IASB also continue to deliberate the three remaining projects intended to bring convergence between GAAP and IFRS for revenue recognition, accounting for financial instruments, and leasing. The revenue recognition project is largely converged and the Boards are expected to issue final guidance in the first half of 2014, while the Boards currently have different positions on certain key aspects of the financial instrument project (the classification and measurement and impairment). Both Boards intend to complete their financial instrument project during the first half of 2014. The timing of the leasing project is not known at this time.

The Company is not able to predict whether it will choose to, or be required to, adopt IFRS or how the adoption of IFRS (or the potential convergence of GAAP and IFRS, including the joint project for valuing insurance contract liabilities) may impact the Company's financial statements in the future.

**FORWARD-LOOKING STATEMENTS**

This report contains, and management may make, certain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, may be forward-looking statements. Words such as "may," "will," "should," "likely," "anticipates," "expects," "intends," "plans," "projects," "believes," "estimates" and similar expressions are used to identify these forward-looking statements. Specifically, statements about the Company's share repurchase plans, expected margin improvement, potential returns, future pension plan contributions and the potential impact of investment markets and other economic conditions on the Company's investment portfolio and underwriting results, among others, are forward looking, and the Company may also make forward-looking statements about, among other things:

its results of operations and financial condition (including, among other things, premium volume, premium rates, net and operating income, investment income and performance, loss costs, return on equity, and expected current returns and combined ratios);

the sufficiency of the Company's asbestos and other reserves;

the impact of emerging claims issues as well as other insurance and non-insurance litigation;

the cost and availability of reinsurance coverage;

catastrophe losses;

the impact of investment, economic and underwriting market conditions;

strategic initiatives, including initiatives, such as in Personal Insurance, to improve profitability and competitiveness; and

the impact of its merger and acquisition transactions, including the acquisition of Dominion.

The Company cautions investors that such statements are subject to risks and uncertainties, many of which are difficult to predict and generally beyond the Company's control, that could cause actual results to differ materially from those expressed in, or implied or projected by, the forward-looking information and statements.

For a discussion of some of the factors that could cause actual results to differ, see "Item 1A Risk Factors" and "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates."

The Company's forward-looking statements speak only as of the date of this report or as of the date they are made, and the Company undertakes no obligation to update its forward-looking statements.



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**Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

**MARKET RISK**

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates (inclusive of credit spreads), foreign currency exchange rates and other relevant market rate or price changes. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying assets are traded. The following is a discussion of the Company's primary market risk exposures and how those exposures are managed as of December 31, 2013. The Company's market risk sensitive instruments, including derivatives, are primarily entered into for purposes other than trading.

The carrying value of the Company's investment portfolio at December 31, 2013 and 2012 was \$73.16 billion and \$73.84 billion, respectively, of which 87% and 89% was invested in fixed maturity securities, respectively. At December 31, 2013 and 2012, approximately 9.3% and 6.2%, respectively, of the Company's invested assets were denominated in foreign currencies. The increase at December 31, 2013 primarily reflected the impact of the Company's acquisition of Dominion. The Company's exposure to equity price risk is not significant. The Company has no direct commodity risk and is not a party to any credit default swaps.

The primary market risks to the investment portfolio are interest rate risk and credit risk associated with investments in fixed maturity securities. The portfolio duration is primarily managed through cash market transactions and treasury futures transactions. In 2013, the estimated average effective duration of the Company's portfolio of fixed maturity and short-term security investments increased, primarily reflecting the impact of an increase in interest rates during the year. By the end of the second quarter of 2013, based upon the outlook for interest rates, the Company closed all of its short positions in U.S. Treasury futures contracts, which it had used to reduce the Company's exposure to a decrease in its book value resulting from an increase in interest rates. During the second half of 2013, the Company did not enter into any U.S. Treasury futures contracts. The Company may once again enter into positions in U.S. Treasury futures in future periods to help manage the duration of its investment portfolio. For additional information regarding the Company's investments, see notes 3 and 4 of notes to the Company's consolidated financial statements as well as the "Investment Portfolio" and "Outlook" sections of "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations."

The primary market risk for all of the Company's debt is interest rate risk at the time of refinancing. The Company monitors the interest rate environment and evaluates refinancing opportunities as maturity dates approach. For additional information regarding the Company's debt see note 8 of notes to the Company's consolidated financial statements as well as the "Liquidity and Capital Resources" section of "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations."

The Company's foreign exchange market risk exposure is concentrated in the Company's invested assets, insurance reserves and shareholders' equity denominated in foreign currencies. Cash flows from the Company's foreign operations are the primary source of funds for the purchase of investments denominated in foreign currencies. The Company purchases these investments primarily to fund insurance reserves and other liabilities denominated in the same currency, effectively reducing its foreign currency exchange rate exposure. Invested assets denominated in the Canadian dollar comprised approximately 5.5% and 2.3% of the total invested assets at December 31, 2013 and 2012, respectively. The increase at December 31, 2013 primarily reflected the impact of the Company's acquisition of Dominion. Invested assets denominated in the British Pound Sterling comprised approximately 2.4% of the total invested assets at both December 31, 2013 and 2012. Invested assets denominated in other currencies at December 31, 2013 and 2012 were not material.

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There were no other significant changes in the Company's primary market risk exposures or in how those exposures were managed for the year ended December 31, 2013 compared to the year ended December 31, 2012. The Company does not currently anticipate significant changes in its primary market risk exposures or in how those exposures are managed in future reporting periods based upon what is known or expected to be in effect in future reporting periods.

**SENSITIVITY ANALYSIS**

Sensitivity analysis is defined as the measurement of potential loss in future earnings, fair values or cash flows of market sensitive instruments resulting from one or more selected hypothetical changes in interest rates and other market rates or prices over a selected period of time. In the Company's sensitivity analysis model, a hypothetical change in market rates is selected that is expected to reflect reasonably possible near-term changes in those rates. "Near-term" means a period of time going forward up to one year from the date of the consolidated financial statements. Actual results may differ from the hypothetical change in market rates assumed in this disclosure, especially since this sensitivity analysis does not reflect the results of any actions that would be taken by the Company to mitigate such hypothetical losses in fair value.

**Interest Rate Risk**

In this sensitivity analysis model, the Company uses fair values to measure its potential loss. The sensitivity analysis model includes the following financial instruments entered into for purposes other than trading: fixed maturities, non-redeemable preferred stocks, mortgage loans, short-term securities, debt and derivative financial instruments. The primary market risk to the Company's market sensitive instruments is interest rate risk (inclusive of credit spreads). The sensitivity analysis model uses various basis point changes in interest rates to measure the hypothetical change in fair value of financial instruments included in the model.

For invested assets with primary exposure to interest rate risk, estimates of portfolio duration and convexity are used to model the loss of fair value that would be expected to result from a parallel increase in interest rates. Durations on invested assets are adjusted for call, put and interest rate reset features. Durations on tax-exempt securities are adjusted for the fact that the yields on such securities do not normally move in lockstep with changes in the U.S. Treasury curve. Fixed maturity portfolio durations are calculated on a market value weighted basis, including accrued interest, using holdings as of December 31, 2013 and 2012.

For debt, the change in fair value is determined by calculating hypothetical December 31, 2013 and 2012 ending prices based on yields adjusted to reflect a 100 basis point change, comparing such hypothetical ending prices to actual ending prices, and multiplying the difference by the par or securities outstanding.

The sensitivity analysis model used by the Company produces a loss in fair value of market sensitive instruments of approximately \$1.90 billion and \$1.64 billion based on a 100 basis point increase in interest rates at December 31, 2013 and 2012, respectively.

The loss estimates do not take into account the impact of possible interventions that the Company might reasonably undertake in order to mitigate or avoid losses that would result from emerging interest rate trends. In addition, the loss value only reflects the impact of an interest rate increase on the fair value of the Company's financial instruments.

**Foreign Currency Exchange Rate Risk**

The Company uses fair values of investment securities to measure its potential loss from foreign denominated investments. A hypothetical 10% reduction in value of foreign denominated investments is

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used to estimate the impact on the market value of the foreign denominated holdings. The Company's analysis indicates that a hypothetical 10% reduction in the value of foreign denominated investments would be expected to produce a loss in fair value of approximately \$681 million and \$459 million at December 31, 2013 and 2012, respectively. This increase in the projected loss at December 31, 2013 primarily reflected the impact of the Company's acquisition of Dominion.

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**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

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**Report Of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
The Travelers Companies, Inc.:

We have audited the accompanying consolidated balance sheet of The Travelers Companies, Inc. and subsidiaries (the Company) as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Travelers Companies, Inc. and subsidiaries as of December 31, 2013 and 2012, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), The Travelers Companies, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control Integrated Framework* (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 13, 2014 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

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KPMG LLP  
New York, New York  
February 13, 2014

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF INCOME**

(in millions, except per share amounts)

For the year ended December 31,	2013	2012	2011
<b>Revenues</b>			
Premiums	\$ 22,637	\$ 22,357	\$ 22,090
Net investment income	2,716	2,889	2,879
Fee income	395	323	296
Net realized investment gains(1)	166	51	55
Other revenues	277	120	126
<b>Total revenues</b>	<b>26,191</b>	<b>25,740</b>	<b>25,446</b>
<b>Claims and expenses</b>			
Claims and claim adjustment expenses	13,307	14,676	16,276
Amortization of deferred acquisition costs	3,821	3,910	3,876
General and administrative expenses	3,757	3,610	3,556
Interest expense	361	378	386
<b>Total claims and expenses</b>	<b>21,246</b>	<b>22,574</b>	<b>24,094</b>
<b>Income before income taxes</b>	<b>4,945</b>	<b>3,166</b>	<b>1,352</b>
Income tax expense (benefit)	1,272	693	(74)
<b>Net income</b>	<b>\$ 3,673</b>	<b>\$ 2,473</b>	<b>\$ 1,426</b>
<b>Net income per share</b>			
Basic	\$ 9.84	\$ 6.35	\$ 3.40
Diluted	\$ 9.74	\$ 6.30	\$ 3.36
<b>Weighted average number of common shares outstanding</b>			
Basic	370.3	386.2	415.8



Diluted	<b>374.3</b>	389.8	420.5
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(1) Total other-than-temporary impairment (OTTI) gains (losses) were \$(10) million, \$27 million and \$30 million for the years ended December 31, 2013, 2012 and 2011, respectively. Of total OTTI, credit losses of \$(15) million, \$(15) million and \$(25) million for the years ended December 31, 2013, 2012 and 2011, respectively, were recognized in net realized investment gains. In addition, unrealized gains from other changes in total OTTI of \$5 million, \$42 million and \$55 million for the years ended December 31, 2013, 2012 and 2011, respectively, were recognized in other comprehensive income (loss) as part of changes in net unrealized gains on investment securities having credit losses recognized in the consolidated statement of income.

The accompanying notes are an integral part of the consolidated financial statements.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**

(in millions)

For the year ended December 31,	2013	2012	2011
<b>Net income</b>	<b>\$ 3,673</b>	<b>\$ 2,473</b>	<b>\$ 1,426</b>
<b>Other comprehensive income (loss):</b>			
Changes in net unrealized gains on investment securities:			
Having no credit losses recognized in the consolidated statement of income	(2,734)	281	1,570
Having credit losses recognized in the consolidated statement of income	3	81	4
Net changes in benefit plan assets and obligations	647	(69)	(307)
Net changes in unrealized foreign currency translation	(112)	43	(90)
<b>Other comprehensive income (loss) before income taxes</b>	<b>(2,196)</b>	<b>336</b>	<b>1,177</b>
Income tax expense (benefit)	(770)	105	427
<b>Other comprehensive income (loss), net of taxes</b>	<b>(1,426)</b>	<b>231</b>	<b>750</b>
<b>Comprehensive income</b>	<b>\$ 2,247</b>	<b>\$ 2,704</b>	<b>\$ 2,176</b>

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEET**

(in millions)

At December 31,	2013	2012
<b>Assets</b>		
Fixed maturities, available for sale, at fair value (amortized cost \$62,196 and \$60,829)	\$ 63,956	\$ 65,393
Equity securities, available for sale, at fair value (cost \$686 and \$462)	943	645
Real estate investments	938	883
Short-term securities	3,882	3,483
Other investments	3,441	3,434
<b>Total investments</b>	<b>73,160</b>	<b>73,838</b>
Cash	294	330
Investment income accrued	734	752
Premiums receivable	6,125	5,872
Reinsurance recoverables	9,713	10,712
Ceded unearned premiums	801	856
Deferred acquisition costs	1,804	1,792
Deferred taxes	303	
Contractholder receivables	4,328	4,806
Goodwill	3,634	3,365
Other intangible assets	351	381
Other assets	2,565	2,234
<b>Total assets</b>	<b>\$ 103,812</b>	<b>\$ 104,938</b>
<b>Liabilities</b>		
Claims and claim adjustment expense reserves	\$ 50,895	\$ 50,922
Unearned premium reserves	11,850	11,241
Contractholder payables	4,328	4,806
Payables for reinsurance premiums	298	346
Deferred taxes		338
Debt	6,346	6,350
Other liabilities	5,299	5,530
<b>Total liabilities</b>	<b>79,016</b>	<b>79,533</b>
<b>Shareholders' equity</b>		
Common stock (1,750.0 shares authorized; 353.5 and 377.4 shares issued and outstanding)	21,500	21,161
Retained earnings	24,291	21,352
Accumulated other comprehensive income	810	2,236
Treasury stock, at cost (401.5 and 372.3 shares)	(21,805)	(19,344)

<b>Total shareholders' equity</b>	<b>24,796</b>	25,405
<b>Total liabilities and shareholders' equity</b>	<b>\$ 103,812</b>	<b>\$ 104,938</b>

The accompanying notes are an integral part of the consolidated financial statements.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**

(in millions)

For the year ended December 31,	2013	2012	2011
<b>Convertible preferred stock savings plan</b>			
Balance, beginning of year	\$	\$	\$ 68
Redemptions			(5)
Conversion to common stock			(63)
Balance, end of year			
<b>Common stock</b>			
Balance, beginning of year	21,161	20,732	20,162
Employee share-based compensation	158	261	328
Common shares issued conversion of preferred stock			93
Compensation amortization under share-based plans and other changes	181	168	149
Balance, end of year	21,500	21,161	20,732
<b>Retained earnings</b>			
Balance, beginning of year	21,352	19,579	18,847
Net income	3,673	2,473	1,426
Dividends	(734)	(700)	(669)
Premium on preferred stock converted to common stock			(30)
Other			5
Balance, end of year	24,291	21,352	19,579
<b>Accumulated other comprehensive income, net of tax</b>			
Balance, beginning of year	2,236	2,005	1,255
Other comprehensive income (loss)	(1,426)	231	750
Balance, end of year	810	2,236	2,005
<b>Treasury stock (at cost)</b>			
Balance, beginning of year	(19,344)	(17,839)	(14,857)
Treasury stock acquired share repurchase authorization	(2,400)	(1,450)	(2,900)
Net shares acquired related to employee share-based compensation plans	(61)	(55)	(82)
Balance, end of year	(21,805)	(19,344)	(17,839)

**Total shareholders' equity** \$ **24,796** \$ 25,405 \$ 24,477

<b>Common shares outstanding</b>			
Balance, beginning of year	<b>377.4</b>	392.8	434.6
Treasury stock acquired share repurchase authorization	<b>(28.4)</b>	(22.4)	(51.0)
Net shares issued under employee share-based compensation plans	<b>4.5</b>	7.0	7.7
Common shares issued conversion of preferred stock			1.5
Balance, end of year	<b>353.5</b>	377.4	392.8

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF CASH FLOWS**

(in millions)

For the year ended December 31,	2013	2012	2011
<b>Cash flows from operating activities</b>			
Net income	\$ 3,673	\$ 2,473	\$ 1,426
Adjustments to reconcile net income to net cash provided by operating activities:			
Net realized investment gains	(166)	(51)	(55)
Depreciation and amortization	867	827	802
Deferred federal income tax expense	167	223	63
Amortization of deferred acquisition costs	3,821	3,910	3,876
Equity in income from other investments	(357)	(342)	(281)
Premiums receivable	54	(138)	(237)
Reinsurance recoverables	1,284	453	809
Deferred acquisition costs	(3,759)	(3,914)	(3,881)
Claims and claim adjustment expense reserves	(2,057)	(540)	(154)
Unearned premium reserves	27	123	188
Other	262	206	(387)
<b>Net cash provided by operating activities</b>	<b>3,816</b>	<b>3,230</b>	<b>2,169</b>
<b>Cash flows from investing activities</b>			
Proceeds from maturities of fixed maturities	7,904	8,369	7,404
Proceeds from sales of investments:			
Fixed maturities	1,635	1,087	1,161
Equity securities	86	37	135
Real estate investments	18	53	1
Other investments	762	835	594
Purchases of investments:			
Fixed maturities	(9,467)	(10,447)	(8,704)
Equity securities	(57)	(48)	(131)
Real estate investments	(107)	(95)	(66)
Other investments	(446)	(534)	(889)
Net sales of short-term securities	111	117	2,018
Securities transactions in course of settlement	21	(23)	
Acquisition, net of cash acquired	(997)		
Other	(373)	(323)	(371)
<b>Net cash provided by (used in) investing activities</b>	<b>(910)</b>	<b>(972)</b>	<b>1,152</b>
<b>Cash flows from financing activities</b>			
Payment of debt	(500)	(258)	(8)
Issuance of debt	494		
Dividends paid to shareholders	(729)	(694)	(665)
Issuance of common stock employee share options	206	295	314
Treasury stock acquired share repurchase authorization	(2,400)	(1,474)	(2,919)
Treasury stock acquired net employee share-based compensation	(61)	(53)	(46)
Excess tax benefits from share-based payment arrangements	51	38	18
<b>Net cash used in financing activities</b>	<b>(2,939)</b>	<b>(2,146)</b>	<b>(3,306)</b>

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Effect of exchange rate changes on cash	(3)	4	(1)
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Net increase (decrease) in cash	(36)	116	14
Cash at beginning of year	330	214	200

<b>Cash at end of year</b>	<b>\$ 294</b>	<b>\$ 330</b>	<b>\$ 214</b>
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**Supplemental disclosure of cash flow information**

Income taxes paid	\$ 1,057	\$ 188	\$ 218
Interest paid	\$ 355	\$ 375	\$ 382

The accompanying notes are an integral part of the consolidated financial statements.



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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation**

The consolidated financial statements include the accounts of The Travelers Companies, Inc. (together with its subsidiaries, the Company). The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles (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 consolidated financial statements and the reported amounts of revenues and claims and expenses during the reporting period. Actual results could differ from those estimates. Certain reclassifications have been made to the 2012 and 2011 financial statements to conform to the 2013 presentation. All material intercompany transactions and balances have been eliminated.

On November 1, 2013, the Company acquired all of the issued and outstanding shares of Dominion for an aggregate purchase price of approximately \$1.034 billion. Dominion primarily markets personal lines and small commercial insurance business in Canada. At the acquisition date, the Company recorded at fair value \$3.91 billion of assets acquired and \$2.88 billion of liabilities assumed as part of purchase accounting, including \$16 million of identifiable intangible assets and \$273 million of goodwill. The operating income and the amount of assets acquired from Dominion were included in the Company's Financial, Professional & International Insurance segment effective at the acquisition date. The unearned premium reserve related to the acquired insurance and reinsurance contracts was carried over and included in the Company's unearned premium reserve. Premium revenue from the acquired business will be recognized on a pro rata basis beginning with the acquisition date over the remaining policy terms in accordance with the Company's accounting policy. The Company recognized an intangible asset for the value of business acquired (VOBA) of \$76 million at the acquisition date. VOBA represents the present value of future gross profits of the business acquired from Dominion, is reported as part of the Company's deferred acquisition costs, and will be amortized in proportion to the premium revenue recognized from the acquired business.

**Adoption of Accounting Standards Updates**

*Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*

In February 2013, the Financial Accounting Standards Board (FASB) issued updated guidance to improve the reporting of reclassifications out of accumulated other comprehensive income. The guidance requires an entity to present, either on the face of the statement of income or in the notes, separately for each component of comprehensive income, the current period reclassifications out of accumulated other comprehensive income by the respective line items of net income affected by the reclassification.

The updated guidance was effective prospectively for reporting periods beginning after December 15, 2012. The Company adopted the updated guidance effective March 31, 2013, and such adoption did not have any effect on the Company's results of operations, financial position or liquidity.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Accounting Standards Not Yet Adopted**

*Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date*

In February 2013, the FASB issued updated guidance to resolve diversity in practice concerning the recognition, measurement, and disclosure of obligations resulting from certain joint and several liability arrangements for which the total amount under the arrangement is fixed at the reporting date. The guidance requires that the reporting entity measure joint and several liability arrangements within the scope of the guidance as the amount the reporting entity agreed to pay on the basis of its arrangement among the co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The updated guidance is effective for the quarter ending March 31, 2014. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

*Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity*

In March 2013, the FASB issued updated guidance to resolve diversity in practice concerning the release of the cumulative foreign currency translation adjustment into net income when a parent sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets within a foreign entity. When a company ceases to have a controlling financial interest in a subsidiary within a foreign entity, the company should recognize any related cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary had resided. Upon the partial sale of an equity method investment that is a foreign entity, the company should release into earnings a pro rata portion of the cumulative translation adjustment. Upon the partial sale of an equity method investment that is not a foreign entity, the company should release into earnings the cumulative translation adjustment if the partial sale represents a complete or substantially complete liquidation of the foreign entity that holds the equity method investment. The updated guidance is effective for the quarter ending March 31, 2014. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

**Accounting Policies**

**Investments**

*Fixed Maturity and Equity Securities*

Fixed maturities include bonds, notes and redeemable preferred stocks. Fixed maturities, including instruments subject to securities lending agreements, are classified as available for sale and are reported at fair value, with unrealized investment gains and losses, net of income taxes, charged or credited directly to other comprehensive income. Equity securities, which include public common and non-redeemable preferred stocks, are classified as available for sale with changes in fair value, net of income taxes, charged or credited directly to other comprehensive income.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

*Real Estate Investments*

The Company's real estate investments include warehouses, office buildings and other commercial land and properties that are directly owned. Real estate is recorded on the purchase date at the purchase price, which generally represents fair value, and is supported by internal analysis or external appraisals that use discounted cash flow analyses and other acceptable valuation techniques. Real estate held for investment purposes is subsequently carried at cost less accumulated depreciation.

Buildings are depreciated on a straight-line basis over the shorter of the expected useful life of the building or 39 years. Real estate held for sale is carried at lower of cost or fair value, less estimated costs to sell.

*Short-term Securities*

Short-term securities have an original maturity of less than one year and are carried at amortized cost, which approximates fair value.

*Other Investments*

Investments in Private Equity Limited Partnerships, Hedge Funds and Real Estate Partnerships

The Company uses the equity method of accounting for private equity limited partnerships, hedge funds and real estate partnerships. The partnerships and the hedge funds generally report investments on their balance sheet at fair value. The financial statements prepared by the investee are received by the Company on a lag basis, with the lag period generally dependent upon the type of underlying investments. The private equity and real estate partnerships provide financial information quarterly which is generally available to investors, including the Company, within three to six months following the date of the reporting period. The hedge funds provide financial information monthly, which is generally available to investors within one month following the date of the reporting period. The Company regularly requests financial information from the partnerships prior to the receipt of the partnerships' financial statements and records any material information obtained from these requests in its consolidated financial statements.

*Other*

Also included in other investments are non-public common and preferred equities, trading securities and derivatives. Non-public common and preferred equities are reported at fair value with changes in fair value, net of income taxes, charged or credited directly to other comprehensive income. Trading securities are marked to market with the change in fair value recognized in net investment income during the current period. The Company sold all of its remaining trading securities during 2013. The Company's derivative financial instruments are carried at fair value, with the changes in fair value reflected in the consolidated statement of income in net realized investment gains (losses). For a further discussion of the derivatives used by the Company, see note 3.

**Net Investment Income**

Investment income from fixed maturities is recognized based on the constant effective yield method which includes an adjustment for estimated principal repayments, if any. The effective yield used to determine amortization for fixed maturities subject to prepayment risk (e.g., asset-backed,

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

loan-backed and structured securities) is recalculated and adjusted periodically based upon actual historical and/or projected future cash flows, which are obtained from a widely-accepted securities data provider. The adjustments to the yield for highly rated prepayable fixed maturities are accounted for using the retrospective method. The adjustments to the yield for non-highly rated prepayable fixed maturities are accounted for using the prospective method. Dividends on equity securities (including those with transfer restrictions) are recognized in income when declared. Rental income on real estate is recognized on a straight-line basis over the lease term. See note 3 for further discussion. Investments in private equity limited partnerships, hedge funds, real estate partnerships and joint ventures are accounted for using the equity method of accounting, whereby the Company's share of the investee's earnings or losses in the fund is reported in net investment income. Trading securities were marked to market with the change in fair value recognized in net investment income during the current period. The Company sold all of its remaining trading securities in 2013.

Accrual of income is suspended on non-securitized fixed maturities that are in default, or on which it is likely that future payments will not be made as scheduled. Interest income on investments in default is recognized only when payments are received. Investments included in the consolidated balance sheet that were not income-producing for the preceding 12 months were not material.

For fixed maturities where the Company records an other-than-temporary impairment, a determination is made as to the cause of the impairment and whether the Company expects a recovery in the value. For fixed maturities where the Company expects a recovery in value, not necessarily to par, the constant effective yield method is utilized, and the investment is amortized to the expected recovery amount.

**Investment Gains and Losses**

Net realized investment gains and losses are included as a component of pretax revenues based upon specific identification of the investments sold on the trade date. Included in net realized investment gains (losses) are other-than-temporary impairment losses on invested assets other than those investments accounted for using the equity method of accounting as described in the "Investment Impairments" section that follows.

**Investment Impairments**

The Company conducts a periodic review to identify and evaluate invested assets having other-than-temporary impairments. Some of the factors considered in identifying other-than-temporary impairments include: (1) for fixed maturity investments, whether the Company intends to sell the investment or whether it is more likely than not that the Company will be required to sell the investment prior to an anticipated recovery in value; (2) for non-fixed maturity investments, the Company's ability and intent to retain the investment for a reasonable period of time sufficient to allow for an anticipated recovery in value; (3) the likelihood of the recoverability of principal and interest for fixed maturity securities (i.e., whether there is a credit loss) or cost for equity securities; (4) the length of time and extent to which the fair value has been less than amortized cost for fixed maturity securities or cost for equity securities; and (5) the financial condition, near-term and long-term prospects for the issuer, including the relevant industry conditions and trends, and implications of rating agency actions and offering prices.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Other-Than-Temporary Impairments of Fixed Maturities and Equity Securities**

For fixed maturity investments 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 the credit loss component of the impairment from the amount related to all other factors and reports the credit loss component in net realized investment gains (losses). The impairment related to all other factors is reported in other comprehensive income.

For equity securities (including public common and non-redeemable preferred stock) and for fixed maturity investments the Company intends to sell or for which it is more likely than not that the Company will be required to sell before an anticipated recovery in value, the full amount of the impairment is included in net realized investment gains (losses).

Upon recognizing an other-than-temporary impairment, the new cost basis of the investment is the previous amortized cost basis less the other-than-temporary impairment recognized in net realized investment gains (losses). The new cost basis is not adjusted for any subsequent recoveries in fair value; however, for fixed maturity investments the difference between the new cost basis and the expected cash flows is accreted on a quarterly basis to net investment income over the remaining expected life of the investment.

*Determination of Credit Loss - Fixed Maturities*

The Company determines the credit loss component of fixed maturity investments by utilizing discounted cash flow modeling to determine the present value of the security and comparing the present value with the amortized cost of the security. If the amortized cost is greater than the present value of the expected cash flows, the difference is considered a credit loss and recognized in net realized investment gains (losses).

For non-structured fixed maturities (U.S. Treasury securities, obligations of U.S. government and government agencies and authorities, obligations of states, municipalities and political subdivisions, debt securities issued by foreign governments, and certain corporate debt), the estimate of expected cash flows is determined by projecting a recovery value and a recovery time frame and assessing whether further principal and interest will be received. The determination of recovery value incorporates an issuer valuation assumption utilizing one or a combination of valuation methods as deemed appropriate by the Company. The Company determines the undiscounted recovery value by allocating the estimated value of the issuer to the Company's assessment of the priority of claims. The present value of the cash flows is determined by applying the effective yield of the security at the date of acquisition (or the most recent implied rate used to accrete the security if the implied rate has changed as a result of a previous impairment) and an estimated recovery time frame. Generally, that time frame for securities for which the issuer is in bankruptcy is 12 months. For securities for which the issuer is financially troubled but not in bankruptcy, that time frame is generally 24 months. Included in the present value calculation are expected principal and interest payments; however, for securities for which the issuer is classified as bankrupt or in default, the present value calculation assumes no interest payments and a single recovery amount.

In estimating the recovery value, significant judgment is involved in the development of assumptions relating to a myriad of factors related to the issuer including, but not limited to, revenue, margin and earnings projections, the likely market or liquidation values of assets, potential additional

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

debt to be incurred pre- or post-bankruptcy/restructuring, the ability to shift existing or new debt to different priority layers, the amount of restructuring/bankruptcy expenses, the size and priority of unfunded pension obligations, litigation or other contingent claims, the treatment of intercompany claims and the likely outcome with respect to inter-creditor conflicts.

For structured fixed maturity securities (primarily residential and commercial mortgage-backed securities and asset-backed securities), the Company estimates the present value of the security by projecting future cash flows of the assets underlying the securitization, allocating the flows to the various tranches based on the structure of the securitization and determining the present value of the cash flows using the effective yield of the security at the date of acquisition (or the most recent implied rate used to accrete the security if the implied rate has changed as a result of a previous impairment or changes in expected cash flows). The Company incorporates levels of delinquencies, defaults and severities as well as credit attributes of the remaining assets in the securitization, along with other economic data, to arrive at its best estimate of the parameters applied to the assets underlying the securitization. In order to project cash flows, the following assumptions are applied to the assets underlying the securitization: (1) voluntary prepayment rates, (2) default rates and (3) loss severity. The key assumptions made for the Prime, Alt-A and first-lien Sub-Prime mortgage-backed securities at December 31, 2013 were as follows:

(at December 31, 2013)	Prime	Alt-A	Sub-Prime
Voluntary prepayment rates	4% - 34%	0% - 15%	1% - 9%
Percentage of remaining pool liquidated due to defaults	1% - 45%	19% - 69%	23% - 74%
Loss severity	30% - 60%	50% - 75%	65% - 100%

## Real Estate Investments

On at least an annual basis, the Company obtains independent appraisals for substantially all of its real estate investments. In addition, the carrying value of all real estate investments is reviewed for impairment on a quarterly basis or when events or changes in circumstances indicate that the carrying amount may not be recoverable. The review for impairment considers the valuation from the independent appraisal, when applicable, and incorporates an estimate of the undiscounted cash flows expected to result from the use and eventual disposition of the real estate property. An impairment loss is recognized if the expected future undiscounted cash flows are less than the carrying value of the real estate property. The impairment loss is the amount by which the carrying amount exceeds fair value.

## Other Investments

*Investments in Private Equity Limited Partnerships, Hedge Funds and Real Estate Partnerships*

The Company reviews its investments in private equity limited partnerships, hedge funds and real estate partnerships for impairment no less frequently than quarterly and monitors the performance throughout the year through discussions with the managers/general partners. If the Company becomes aware of an impairment of a partnership's investments at the balance sheet date prior to receiving the partnership's financial statements, it will recognize an impairment by recording a reduction in the carrying value of the partnership with a corresponding charge to net investment income.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Changes in Intent to Sell Temporarily Impaired Assets**

The Company may, from time to time, sell invested assets subsequent to the balance sheet date that it did not intend to sell at the balance sheet date. Conversely, the Company may not sell invested assets that it asserted that it intended to sell at the balance sheet date. Such changes in intent are due to events occurring subsequent to the balance sheet date. The types of events that may result in a change in intent include, but are not limited to, significant changes in the economic facts and circumstances related to the invested asset (e.g., a downgrade or upgrade from a rating agency), significant unforeseen changes in liquidity needs, or changes in tax laws or the regulatory environment.

**Securities Lending**

The Company has engaged in securities lending activities from which it generates net investment income by lending certain of its investments to other institutions for short periods of time. Borrowers of these securities provide collateral equal to at least 102% of the market value of the loaned securities plus accrued interest. This collateral is held by a third-party custodian, and the Company has the right to access the collateral only in the event that the institution borrowing the Company's securities is in default under the lending agreement. Therefore, the Company does not recognize the receipt of the collateral held by the third-party custodian or the obligation to return the collateral. The loaned securities remain a recorded asset of the Company. The Company accepts only cash as collateral for securities on loan and restricts the manner in which that cash is invested.

**Reinsurance Recoverables**

Amounts recoverable from reinsurers are estimated in a manner consistent with the associated claim liability. 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, disputes, applicable coverage defenses and other relevant factors. Amounts deemed to be uncollectible, including amounts due from known insolvent reinsurers, are written off against the allowance for estimated uncollectible reinsurance recoverables. Any subsequent collections of amounts previously written off are reported as part of claims and claim adjustment expenses. 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.

**Deferred Acquisition Costs**

Incremental direct costs of acquired new and renewal insurance contracts, consisting of commissions (other than contingent commissions) and premium-related taxes, are capitalized and charged to expense pro rata over the contract periods in which the related premiums are earned. Deferred acquisition costs are reviewed to determine if they are recoverable from future income and, if not, are charged to expense. Future investment income attributable to related premiums is taken into account in measuring the recoverability of the carrying value of this asset. All other acquisition expenses are charged to operations as incurred.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Contractholder Receivables and Payables**

Under certain workers' compensation insurance contracts with deductible features, the Company is obligated to pay the claimant for the full amount of the claim. The Company is subsequently reimbursed by the policyholder for the deductible amount. These amounts are included on a gross basis in the consolidated balance sheet in contractholder payables and contractholder receivables, respectively.

**Goodwill and Other Intangible Assets**

The Company performs a review, on at least an annual basis, of goodwill held by the reporting units which are the Company's three operating and reportable segments: Business Insurance; Financial, Professional & International Insurance; and Personal Insurance. The Company estimates the fair value of its reporting units and compares it to their carrying value, including goodwill. If the carrying values of the reporting units were to exceed their fair value, the amount of the impairment would be calculated and goodwill adjusted accordingly.

The Company uses a discounted cash flow model to estimate the fair value of its reporting units. The discounted cash flow model is an income approach to valuation that is based on a detailed cash flow analysis for deriving a current fair value of reporting units and is representative of the Company's reporting units' current and expected future financial performance. The discount rate assumptions reflect the Company's assessment of the risks inherent in the projected future cash flows and the Company's weighted-average cost of capital, and are compared against available market data for reasonableness.

Other indefinite-lived intangible assets held by the Company are also reviewed for impairment on at least an annual basis. The classification of the asset as indefinite-lived is reassessed and an impairment is recognized if the carrying amount of the asset exceeds its fair value.

Intangible assets that are deemed to have a finite useful life are amortized over their useful lives. The carrying amount of intangible assets with a finite useful life is regularly reviewed for indicators of impairment in value. Impairment is recognized only if the carrying amount of the intangible asset is not recoverable from its undiscounted cash flows and is measured as the difference between the carrying amount and the fair value of the asset.

As a result of the reviews performed for the years ended December 31, 2013, 2012 and 2011, the Company determined that the estimated fair value significantly exceeded the respective carrying value of its reporting units for those years and that goodwill was not impaired. The Company also determined during its reviews for each year that its other indefinite-lived intangible assets and finite-lived intangible assets were not impaired.

**Claims and Claim Adjustment Expense Reserves**

Claims and claim adjustment expense reserves represent estimates for the ultimate cost of unpaid reported and unreported claims incurred and related expenses. The reserves are adjusted regularly based upon experience. Included in the claims and claim adjustment expense reserves in the consolidated balance sheet are certain reserves discounted to the present value of estimated future payments. The liabilities for losses for most long-term disability and annuity claim payments, primarily arising from workers' compensation insurance and workers' compensation excess insurance policies,



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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

were discounted using a rate of 5% at both December 31, 2013 and 2012. These discounted reserves totaled \$2.21 billion and \$2.01 billion at December 31, 2013 and 2012, respectively.

The Company performs a continuing review of its claims and claim adjustment expense reserves, including its reserving techniques and its reinsurance. The reserves are also reviewed regularly by qualified actuaries employed by the Company. Since the reserves are based on estimates, the ultimate liability may be more or less than such reserves. The effects of changes in such estimated reserves are included in the results of operations in the period in which the estimates are changed. Such changes in estimates could occur in a future period and may be material to the Company's results of operations and financial position in such period.

**Other Liabilities**

Included in other liabilities in the consolidated balance sheet is the Company's estimate of its liability for guaranty fund and other insurance-related assessments. The liability for expected state guaranty fund and other premium-based assessments is recognized as the Company writes or becomes obligated to write or renew the premiums on which the assessments are expected to be based. The liability for loss-based assessments is recognized as the related losses are incurred. At December 31, 2013 and 2012, the Company had a liability of \$261 million and \$297 million, respectively, for guaranty fund and other insurance-related assessments and related recoverables of \$14 million and \$15 million, respectively. The liability for such assessments and the related recoverables are not discounted for the time value of money. The loss-based assessments are expected to be paid over a period ranging from one year to the life expectancy of certain workers' compensation claimants and the recoveries are expected to occur over the same period of time.

Also included in other liabilities is an accrual for policyholder dividends. Certain insurance contracts, primarily workers' compensation, are participating whereby dividends are paid to policyholders in accordance with contract provisions. Net written premiums for participating dividend policies were approximately 1%, 2% and 1% of total net written premiums for the year ended December 31, 2013, 2012 and 2011, respectively. Policyholder dividends are accrued against earnings using best available estimates of amounts to be paid. The liability accrued for policyholder dividends totaled \$53 million and \$59 million at December 31, 2013 and 2012, respectively.

**Treasury Stock**

The cost of common stock repurchased by the Company is reported as treasury stock and represents authorized and unissued shares of the Company under the Minnesota Business Corporation Act.

**Statutory Accounting Practices**

The Company's U.S. insurance subsidiaries, domiciled principally in the state of Connecticut, prepare statutory financial statements in accordance with the accounting practices prescribed or permitted by the insurance departments of the states of domicile. Prescribed statutory accounting practices are those practices that are incorporated directly or by reference in state laws, regulations, and general administrative rules applicable to all insurance enterprises domiciled in a particular state. Permitted statutory accounting practices include practices not prescribed by the domiciliary state, but

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

allowed by the domiciliary state regulatory authority. The impact of any permitted accounting practices on policyholders' surplus of the Company is not material.

The Company's non-U.S. insurance subsidiaries file financial statements prepared in accordance with the regulatory reporting requirements of their respective local jurisdiction.

**Premiums and Unearned Premium Reserves**

Premiums are recognized as revenues pro rata over the policy period. Unearned premium reserves represent the unexpired portion of policy premiums. Accrued retrospective premiums are included in premium balances receivable. Premium balances receivable are reported net of an allowance for estimated uncollectible premium amounts.

Ceded premiums are charged to income over the applicable term of the various reinsurance contracts with third party reinsurers. Prepaid reinsurance premiums represent the unexpired portion of premiums ceded to reinsurers and are reported as part of other assets.

**Fee Income**

Fee income includes servicing fees from carriers and revenues from large deductible policies and service contracts and is recognized pro rata over the contract or policy periods.

**Other Revenues**

Other revenues include revenues from premium installment charges, which are recognized as collected, revenues of noninsurance subsidiaries other than fee income and gains and losses on dispositions of assets and redemption of debt, and other miscellaneous revenues.

**Income Taxes**

The Company recognizes deferred income tax assets and liabilities for the expected future tax effects attributable to temporary differences between the financial statement and tax return bases of assets and liabilities, based on enacted tax rates and other provisions of the tax law. The effect of a change in tax laws or rates on deferred tax assets and liabilities is recognized in income in the period in which such change is enacted. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that all or some portion of the deferred tax assets will not be realized.

**Foreign Currency Translation**

The Company assigns functional currencies to its foreign operations, which are generally the currencies of the local operating environment. Foreign currency amounts are remeasured to the functional currency, and the resulting foreign exchange gains or losses are reflected in earnings. Functional currency amounts are then translated into U.S. dollars. The foreign currency remeasurement and translation are calculated using current exchange rates for items reported in the balance sheets and average exchange rates for items recorded in earnings. The change in unrealized foreign currency translation gain or loss during the year, net of tax, is a component of other comprehensive income.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Share-Based Compensation**

The Company has an employee stock incentive compensation plan that permits grants of nonqualified stock options, incentive stock options, stock appreciation rights, restricted stock, deferred stock, stock units, performance awards and other stock-based or stock-denominated awards with respect to the Company's common stock.

Compensation cost is measured based on the grant-date fair value of an award, utilizing the assumptions discussed in note 13. Compensation cost is recognized for financial reporting purposes over the period in which the employee is required to provide service in exchange for the award (generally the vesting period). In connection with certain share-based awards, participants are entitled to receive dividends during the vesting period, either in cash or dividend equivalent shares, commensurate with the dividends paid to common shareholders. Dividends and dividend equivalent shares on awards that are expected to vest are recorded in retained earnings. Dividends paid on awards that are not expected to vest as part of the Company's forfeiture estimate are recorded as compensation expense.

**Nature of Operations**

The Company is organized into three reportable business segments: Business Insurance; Financial, Professional & International Insurance; and Personal Insurance. These segments reflect the manner in which the Company's businesses are currently managed and represent an aggregation of products and services based on type of customer, how the business is marketed and the manner in which risks are underwritten. The specific business segments are as follows:

**Business Insurance**

The Business Insurance segment offers a broad array of property and casualty insurance and insurance-related services to its clients primarily in the United States. Business Insurance is organized into the following six groups, which collectively comprise Business Insurance Core operations:

*Select Accounts* provides small businesses with property and casualty products, including commercial multi-peril, commercial property, general liability, commercial auto and workers' compensation insurance.

*Commercial Accounts* provides mid-sized businesses with property and casualty products, including commercial multi-peril, commercial property, general liability, commercial auto and workers' compensation insurance.

*National Accounts* provides large companies with casualty products and services, including workers' compensation, general liability and automobile liability, generally utilizing loss-sensitive products, on both a bundled and unbundled basis. National Accounts also includes the Company's commercial residual market business, which primarily offers workers' compensation products and services to the involuntary market.

*Industry-Focused Underwriting.* The following units provide targeted industries with differentiated combinations of insurance coverage, risk management, claims handling and other services:

*Construction* serves a broad range of construction businesses, offering guaranteed cost products and loss sensitive programs structured to meet customer needs. Products offered



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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

include workers' compensation, general liability and commercial auto coverages, and other risk management solutions.

*Technology* serves small to large companies involved in telecommunications, information technology, medical technology and electronics manufacturing, offering a comprehensive portfolio of products and services. Products offered include commercial property, commercial auto, general liability, workers' compensation, internet liability, technology errors and omissions coverages and global companion products.

*Public Sector Services* provides insurance products and services to public entities including municipalities, counties, Indian Nation gaming organizations and selected special government districts such as water and sewer utilities. Products offered by this unit typically cover commercial property, commercial auto, general liability, professional liability and workers' compensation exposures.

*Oil & Gas* provides specialized property and liability products and services for customers involved in the exploration and production of oil and natural gas, including operators, drilling and well servicing contractors, supply companies and manufacturers that support upstream operations. Products offered include workers' compensation, general liability, commercial auto, commercial property, control of well and other risk management solutions.

*Agribusiness* serves small to medium-sized agricultural businesses, including farms, ranches, wineries and related operations. Products offered include property and liability coverages other than workers' compensation.

*Target Risk Underwriting.* The following units serve commercial businesses requiring specialized product underwriting, claims handling and risk management services:

*National Property* provides traditional and customized property insurance programs to large and mid-sized customers, including office building owners, manufacturers, municipalities and schools, retailers, and service businesses.

*Inland Marine* provides insurance for goods in transit and movable objects for customers such as jewelers, museums, contractors and the transportation industry. Builders' risk insurance is also offered to customers during the construction, renovation or repair of buildings and other structures.

*Ocean Marine* serves the marine transportation industry and related services, as well as other businesses involved in international trade. The Company's product offerings in this unit fall under six main coverage categories: marine liability, cargo, hull and machinery, protection and indemnity, pleasure craft, and marine property and liability.

*Excess Casualty* serves small to mid-sized commercial businesses, offering mono-line umbrella and excess coverage where the Company typically does not write the primary casualty coverage or where other business units within the Company prefer to access the underwriting expertise and/or limit capacity of the Excess Casualty business unit.

*Boiler & Machinery* serves small to large companies, offering comprehensive breakdown coverages for equipment, including property and business interruption coverages. Through the BoilerRe unit, Boiler & Machinery also serves other property and casualty carriers that

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

do not have in-house expertise with reinsurance, underwriting, engineering, claim handling and risk management services for this type of coverage.

*Global Partner Services* provides insurance to foreign organizations with property and liability exposures located in the United States (reverse-flow), as part of a global program.

*Specialized Distribution.* The following units market and underwrite their products to customers predominantly through licensed wholesale agents and program managers that manage customers' unique insurance requirements.

*Northland* provides insurance coverage for the commercial transportation industry, as well as commercial liability and commercial property policies for small, difficult to place specialty classes of commercial business, primarily on an excess and surplus lines basis.

*National Programs* offers tailored property and casualty programs on an admitted basis for customers with common risk characteristics or coverage requirements. Programs available include, but are not limited to, those for entertainment, architects and engineers, equipment rental, golf services and owners of franchised businesses.

Business Insurance also includes the Special Liability Group (which manages the Company's asbestos and environmental liabilities) and the assumed reinsurance and certain other runoff operations, which collectively are referred to as Business Insurance Other.

**Financial, Professional & International Insurance**

The Financial, Professional & International Insurance segment includes surety and financial liability coverages, which primarily use credit-based underwriting processes, as well as property and casualty products that are primarily marketed on a domestic basis in Canada, the United Kingdom and the Republic of Ireland, and on an international basis through Lloyd's. The segment includes the following groups:

*Bond & Financial Products* provides a wide range of customers with bond and insurance products and risk management services. The range of coverages includes performance, payment and commercial surety and fidelity bonds for construction and general commercial enterprises; management liability coverages for losses caused by the actual or alleged negligence or misconduct of directors and officers or employee dishonesty; employment practices liability coverages and fiduciary coverages for public corporations, private companies and not-for-profit organizations; professional liability coverage for actual or alleged errors and omissions committed in the course of professional conduct or practice for a variety of professionals including, among others, lawyers and design professionals; and professional and management liability, property, workers' compensation, auto and general liability and fidelity insurance for financial institutions.

*International*, through its operations in Canada, the United Kingdom and the Republic of Ireland, offers specialized insurance and risk management services to several customer groups, including, among others, those in the technology, public services, and financial and professional services industry sectors. In addition, International markets personal lines and small commercial insurance business in Canada through Dominion, which the Company acquired on November 1, 2013. International, through its Lloyd's syndicate (Syndicate 5000), for which the Company

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

provides 100% of the capital, underwrites through five principal business units marine, global property, accident & special risks, power & utilities and aviation.

In addition, the Company owns 49.5% of the common stock of J. Malucelli Participações em Seguros e Resseguros S.A. (JMalucelli), its joint venture in Brazil. JMalucelli is currently the market leader in surety in Brazil based on market share, and commenced writing other property and casualty insurance business in 2012. The Company's investment in JMalucelli is accounted for using the equity method and is included in "other investments" on the consolidated balance sheet.

**Personal Insurance**

The Personal Insurance segment writes a broad range of property and casualty insurance covering individuals' personal risks. The primary products of automobile and homeowners insurance are complemented by a broad suite of related coverages.

Automobile policies provide coverage for liability to others for both bodily injury and property damage, uninsured motorist protection, and for physical damage to an insured's own vehicle from collision, fire, flood, hail and theft. In addition, many states require policies to provide first-party personal injury protection, frequently referred to as no-fault coverage.

Homeowners policies provide protection against losses to dwellings and contents from a variety of perils (excluding flooding) as well as coverage for personal liability. The Company writes homeowners insurance for dwellings, condominiums and tenants, and rental properties. The Company also writes coverage for boats and yachts and valuable personal items such as jewelry, and also writes coverages for umbrella liability, identity fraud, and weddings and special events.

**2. SEGMENT INFORMATION**

The accounting policies used to prepare the segment reporting data for the Company's three reportable business segments are the same as those described in the Summary of Significant Accounting Policies in note 1.

Except as described below for certain legal entities, the Company allocates its invested assets and the related net investment income to its reportable business segments. Pretax net investment income is allocated based upon an investable funds concept, which takes into account liabilities (net of non-invested assets) and appropriate capital considerations for each segment. For investable funds, a benchmark investment yield is developed that reflects the estimated duration of the loss reserves' future cash flows, the interest rate environment at the time the losses were incurred and A+ rated corporate debt instrument yields. For capital, a benchmark investment yield is developed that reflects the average yield on the total investment portfolio. The benchmark investment yields are applied to each segment's investable funds and capital, respectively, to produce a total notional investment income by segment. The Company's actual net investment income is allocated to each segment in proportion to the respective segment's notional investment income to total notional investment income. There are certain legal entities within the Company that are dedicated to specific reportable business segments. The invested assets and related net investment income from these legal entities are reported in the applicable business segment and are not allocated among the other business segments.

The cost of the Company's catastrophe treaty program is included in the Company's ceded premiums and is allocated among reportable business segments based on an estimate of actual market reinsurance pricing using expected losses calculated by the Company's catastrophe model, adjusted for any experience adjustments.



Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2. SEGMENT INFORMATION (Continued)**

The following tables summarize the components of the Company's revenues, operating income (loss), net written premiums and total assets by reportable business segments:

(for the year ended December 31, in millions)	Business Insurance	Financial, Professional & International Insurance	Personal Insurance	Total Reportable Segments
<b>2013</b>				
Premiums	\$ 12,084	\$ 3,229	\$ 7,324	\$ 22,637
Net investment income	1,975	372	369	2,716
Fee income	393	2		395
Other revenues	158	22	103	283
Total operating revenues(1)	\$ 14,610	\$ 3,625	\$ 7,796	\$ 26,031
Amortization and depreciation	\$ 2,445	\$ 779	\$ 1,461	\$ 4,685
Income tax expense	740	245	366	1,351
Operating income(1)	2,329	648	838	3,815
<b>2012</b>				
Premiums	\$ 11,691	\$ 3,045	\$ 7,621	\$ 22,357
Net investment income	2,090	395	404	2,889
Fee income	322	1		323
Other revenues	40	26	66	132
Total operating revenues(1)	\$ 14,143	\$ 3,467	\$ 8,091	\$ 25,701
Amortization and depreciation	\$ 2,393	\$ 731	\$ 1,602	\$ 4,726
Income tax expense	539	255	32	826
Operating income(1)	1,843	642	217	2,702
<b>2011</b>				
Premiums	\$ 11,327	\$ 3,174	\$ 7,589	\$ 22,090
Net investment income	2,041	414	424	2,879
Fee income	295	1		296
Other revenues	31	26	70	127
Total operating revenues(1)	\$ 13,694	\$ 3,615	\$ 8,083	\$ 25,392

Amortization and depreciation	\$ 2,313	\$ 740	\$ 1,615	\$ 4,668
Income tax expense (benefit)	134	230	(293)	71
Operating income (loss)(1)	1,354	647	(332)	1,669

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(1)

Operating revenues for reportable business segments exclude net realized investment gains (losses). Operating income (loss) for reportable business segments equals net income (loss) excluding the after-tax impact of net realized investment gains (losses).

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Net written premiums by market were as follows:

<b>(for the year ended December 31, in millions)</b>	<b>2013</b>	<b>2012</b>	<b>2011</b>
<b>Business Insurance:</b>			
Select Accounts	\$ 2,724	\$ 2,775	\$ 2,784
Commercial Accounts	3,197	3,101	2,890
National Accounts	1,010	907	782
Industry-Focused Underwriting	2,645	2,554	2,407
Target Risk Underwriting	1,799	1,666	1,587
Specialized Distribution	858	870	880
Total Business Insurance Core	12,233	11,873	11,330
Business Insurance Other		(1)	10
Total Business Insurance	12,233	11,872	11,340
<b>Financial, Professional &amp; International Insurance:</b>			
Bond & Financial Products	2,030	1,924	1,953
International	1,279	1,057	1,149
Total Financial, Professional & International Insurance	3,309	2,981	3,102
<b>Personal Insurance:</b>			
Automobile	3,370	3,642	3,788
Homeowners and Other	3,855	3,952	3,957
Total Personal Insurance	7,225	7,594	7,745
Total consolidated net written premiums	\$ 22,767	\$ 22,447	\$ 22,187

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## 2. SEGMENT INFORMATION (Continued)

## Business Segment Reconciliations

(for the year ended December 31, in millions)	2013	2012	2011
<b>Revenue reconciliation</b>			
Earned premiums			
Business Insurance:			
Workers' compensation	\$ 3,560	\$ 3,222	\$ 2,899
Commercial automobile	1,904	1,943	1,940
Commercial property	1,698	1,621	1,607
General liability	1,790	1,757	1,738
Commercial multi-peril	3,093	3,113	3,126
Other	39	35	17
Total Business Insurance	12,084	11,691	11,327
Financial, Professional & International Insurance:			
Fidelity and surety	913	939	970
General liability	891	850	832
International	1,248	1,088	1,218
Other	177	168	154
Total Financial, Professional & International Insurance	3,229	3,045	3,174
Personal Insurance:			
Automobile	3,431	3,665	3,720
Homeowners and Other	3,893	3,956	3,869
Total Personal Insurance	7,324	7,621	7,589
Total earned premiums	22,637	22,357	22,090
Net investment income	2,716	2,889	2,879
Fee income	395	323	296
Other revenues	283	132	127
Total operating revenues for reportable segments	26,031	25,701	25,392
Other revenues	(6)	(12)	(1)
Net realized investment gains	166	51	55
Total consolidated revenues	\$ 26,191	\$ 25,740	\$ 25,446

**Income reconciliation, net of tax**

Total operating income for reportable segments	\$	<b>3,815</b>	\$	2,702	\$	1,669
Interest Expense and Other(1)		<b>(248)</b>		(261)		(279)
Total operating income		<b>3,567</b>		2,441		1,390
Net realized investment gains		<b>106</b>		32		36
Total consolidated net income	\$	<b>3,673</b>	\$	2,473	\$	1,426

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- (1) The primary component of Interest Expense and Other was after-tax interest expense of \$235 million, \$246 million and \$251 million in 2013, 2012 and 2011, respectively.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2. SEGMENT INFORMATION (Continued)**

(at December 31, in millions)	2013	2012
<b>Asset reconciliation:</b>		
Business Insurance	\$ 73,746	\$ 76,972
Financial, Professional & International Insurance	16,691	13,452
Personal Insurance	12,870	14,195
Total assets for reportable segments	103,307	104,619
Other assets(1)	505	319
Total consolidated assets	\$ 103,812	\$ 104,938

(1)

The primary components of other assets at December 31, 2013 were other intangible assets and accrued over-funded benefit plan assets related to the Company's qualified domestic pension plan. The primary component of other assets at December 31, 2012 was other intangible assets.

**Enterprise-Wide Disclosures**

The Company does not have revenue from transactions with a single customer amounting to 10 percent or more of its revenues.

The following table presents revenues of the Company's operations based on location:

(for the year ended December 31, in millions)	2013	2012	2011
U.S.	\$ 25,138	\$ 24,827	\$ 24,408
Non-U.S.	1,053	913	1,038
Total revenues	\$ 26,191	\$ 25,740	\$ 25,446

[Table of Contents](#)**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. INVESTMENTS****Fixed Maturities**

The amortized cost and fair value of investments in fixed maturities classified as available for sale were as follows:

(at December 31, 2013, in millions)	Amortized Cost	Gross Unrealized Gains	Losses	Fair Value
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,288	\$ 39	\$ 12	\$ 2,315
Obligations of states, municipalities and political subdivisions:				
Pre-refunded	9,074	445	1	9,518
All other	25,414	991	361	26,044
Total obligations of states, municipalities and political subdivisions	34,488	1,436	362	35,562
Debt securities issued by foreign governments	2,552	33	8	2,577
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2,263	179	18	2,424
All other corporate bonds	20,472	767	299	20,940
Redeemable preferred stock	133	6	1	138
Total	\$ 62,196	\$ 2,460	\$ 700	\$ 63,956

(at December 31, 2012, in millions)	Amortized Cost	Gross Unrealized Gains	Losses	Fair Value
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,148	\$ 75	\$ 1	\$ 2,222
Obligations of states, municipalities and political subdivisions:				
Pre-refunded	8,458	567		9,025
All other	27,405	2,262	11	29,656
Total obligations of states, municipalities and political subdivisions	35,863	2,829	11	38,681
Debt securities issued by foreign governments	2,185	72		2,257
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2,744	255	2	2,997
All other corporate bonds	17,863	1,360	20	19,203
Redeemable preferred stock	26	7		33
Total	\$ 60,829	\$ 4,598	\$ 34	\$ 65,393





Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. INVESTMENTS (Continued)**

The amortized cost and fair value of fixed maturities by contractual maturity follow. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(at December 31, 2013, in millions)	Amortized Cost	Fair Value
Due in one year or less	\$ 8,386	\$ 8,525
Due after 1 year through 5 years	20,359	21,407
Due after 5 years through 10 years	17,225	17,579
Due after 10 years	13,963	14,021
	<b>59,933</b>	<b>61,532</b>
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2,263	2,424
<b>Total</b>	<b>\$ 62,196</b>	<b>\$ 63,956</b>

Pre-refunded bonds of \$9.52 billion and \$9.03 billion at December 31, 2013 and 2012, respectively, were bonds for which states or municipalities have established irrevocable trusts, almost exclusively comprised of U.S. Treasury securities, which were created to satisfy their responsibility for payments of principal and interest.

The Company's fixed maturity investment portfolio at December 31, 2013 and 2012 included \$2.42 billion and \$3.00 billion, respectively, of residential mortgage-backed securities, which include pass-through securities and collateralized mortgage obligations (CMO). Included in the totals at December 31, 2013 and 2012 were \$1.06 billion and \$1.44 billion, respectively, of GNMA, FNMA and FHLMC (excluding FHA project loans) guaranteed residential mortgage-backed pass-through securities classified as available for sale. Also included in those totals were residential CMOs classified as available for sale with a fair value of \$1.36 billion and \$1.56 billion, respectively. Approximately 42% and 43% of the Company's CMO holdings were guaranteed by or fully collateralized by securities issued by GNMA, FNMA or FHLMC at December 31, 2013 and 2012, respectively. The average credit rating of the \$790 million and \$893 million of non-guaranteed CMO holdings at December 31, 2013 and 2012, respectively, was "Ba3" and "B2," respectively. The average credit rating of all of the above securities was "A1" at both December 31, 2013 and 2012.

At December 31, 2013 and 2012, the Company held commercial mortgage-backed securities (CMBS, including FHA project loans) of \$475 million and \$453 million, respectively, which are included in "All other corporate bonds" in the tables above. At December 31, 2013 and 2012, approximately \$59 million and \$64 million of these securities, respectively, or the loans backing such securities, contained guarantees by the U.S. government or a government-sponsored enterprise, and \$7 million and \$4 million at December 31, 2013 and 2012, respectively, were comprised of Canadian non-guaranteed securities. The average credit rating of the \$416 million and \$389 million of non-guaranteed securities at December 31, 2013 and 2012, respectively, was "Aaa" at both dates. The CMBS portfolio is supported by loans that are diversified across economic sectors and geographical areas. The average credit rating of the CMBS portfolio was "Aaa" at both December 31, 2013 and 2012.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. INVESTMENTS (Continued)**

At December 31, 2013 and 2012, the Company had \$131 million and \$403 million, respectively, of securities on loan as part of a tri-party lending agreement.

Proceeds from sales of fixed maturities classified as available for sale were \$1.64 billion, \$1.09 billion and \$1.16 billion in 2013, 2012 and 2011, respectively. Gross gains of \$66 million, \$70 million and \$63 million and gross losses of \$25 million, \$9 million and \$10 million were realized on sales and other fixed maturity-related transactions (excluding impairments) in 2013, 2012 and 2011, respectively.

At December 31, 2013 and 2012, the Company's insurance subsidiaries had \$4.77 billion and \$4.94 billion, respectively, of securities on deposit at financial institutions in certain states pursuant to the respective states' insurance regulatory requirements. Funds deposited with third parties to be used as collateral to secure various liabilities on behalf of insureds, cedants and other creditors had a fair value of \$59 million and \$68 million at December 31, 2013 and 2012, respectively. Other investments pledged as collateral securing outstanding letters of credit had a fair value of \$42 million and \$56 million at December 31, 2013 and 2012, respectively. In addition, the Company utilized a Lloyd's trust deposit at December 31, 2013, whereby owned securities with a fair value of approximately \$181 million held by an insurance subsidiary were pledged into a Lloyd's trust account to support capital requirements for the Company's operations at Lloyd's.

**Equity Securities**

The cost and fair value of investments in equity securities were as follows:

(at December 31, 2013, in millions)	Cost	Gross Unrealized		Fair Value
		Gains	Losses	
Common stock	\$ 385	\$ 226	\$ 1	\$ 610
Non-redeemable preferred stock	301	34	2	333
<b>Total</b>	<b>\$ 686</b>	<b>\$ 260</b>	<b>\$ 3</b>	<b>\$ 943</b>

(at December 31, 2012, in millions)	Cost	Gross Unrealized		Fair Value
		Gains	Losses	
Common stock	\$ 366	\$ 148	\$ 4	\$ 510
Non-redeemable preferred stock	96	39		135
<b>Total</b>	<b>\$ 462</b>	<b>\$ 187</b>	<b>\$ 4</b>	<b>\$ 645</b>

Proceeds from sales of equity securities were \$86 million, \$37 million and \$135 million in 2013, 2012 and 2011, respectively. Gross gains of \$16 million, \$8 million and \$48 million and gross losses of \$1 million, less than \$1 million and \$2 million were realized on those sales

(excluding impairments) in 2013, 2012 and 2011, respectively.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**3. INVESTMENTS (Continued)**

**Real Estate**

The Company's real estate investments include warehouses, office buildings and other commercial land and properties that are directly owned. The Company negotiates commercial leases with individual tenants through unrelated, licensed real estate brokers. Negotiated terms and conditions include, among others, rental rates, length of lease period and improvements to the premises to be provided by the landlord.

Proceeds from the sale of real estate investments were \$18 million and \$53 million in 2013 and 2012, respectively. Gross gains of \$7 million and \$19 million were realized on those sales in 2013 and 2012, respectively, and there were no gross losses. In 2011, there were no sales of real estate investments. The Company had no real estate held for sale at December 31, 2013 and 2012. Accumulated depreciation on real estate held for investment purposes was \$264 million and \$242 million at December 31, 2013 and 2012, respectively.

Future minimum rental income on operating leases relating to the Company's real estate properties is expected to be \$84 million, \$75 million, \$58 million, \$41 million and \$30 million for 2014, 2015, 2016, 2017 and 2018, respectively, and \$48 million for 2019 and thereafter.

**Short-term Securities**

The Company's short-term securities consist of Aaa-rated registered money market funds, U.S. Treasury securities, high-quality commercial paper (primarily A1/P1) and high-quality corporate securities purchased within a year to their maturity with a combined average of 80 days to maturity at December 31, 2013. The amortized cost of these securities, which totaled \$3.88 billion and \$3.48 billion at December 31, 2013 and 2012, respectively, approximated their fair value.

**Variable Interest Entities**

Entities which do not have sufficient equity at risk to allow the entity to finance its activities without additional financial support or in which the equity investors, as a group, do not have the characteristic of a controlling financial interest are referred to as variable interest entities (VIE). A VIE is consolidated by the variable interest holder that is determined to have the controlling financial interest (primary beneficiary) as a result of having both the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and the obligation to absorb losses or right to receive benefits from the VIE that could potentially be significant to the VIE. The Company determines whether it is the primary beneficiary of an entity subject to consolidation based on a qualitative assessment of the VIE's capital structure, contractual terms, nature of the VIE's operations and purpose and the Company's relative exposure to the related risks of the VIE on the date it becomes initially involved in the VIE. The Company reassesses its VIE determination with respect to an entity on an ongoing basis.

The Company is a passive investor in limited partner equity interests issued by third party VIEs. These include certain of the Company's investments in private equity limited partnerships, hedge funds and real estate partnerships where the Company is not related to the general partner. These investments are generally accounted for under the equity method and reported in the Company's consolidated balance sheet as other investments unless the Company is deemed the primary beneficiary. These equity interests generally cannot be redeemed. Distributions from these investments are received

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## 3. INVESTMENTS (Continued)

by the Company as a result of liquidation of the underlying investments of the funds and/or as income distribution. The Company's maximum exposure to loss with respect to these investments is limited to the investment carrying amounts reported in the Company's consolidated balance sheet and any unfunded commitment. Neither the carrying amounts nor the unfunded commitments related to these VIEs are material.

**Unrealized Investment Losses**

The following tables summarize, for all investments in an unrealized loss position at December 31, 2013 and 2012, the aggregate fair value and gross unrealized loss by length of time those securities have been continuously in an unrealized loss position. The fair value amounts reported in the tables are estimates that are prepared using the process described in note 4. The Company also relies upon estimates of several factors in its review and evaluation of individual investments, using the process described in note 1, in determining whether such investments are other-than-temporarily impaired.

(at December 31, 2013, in millions)	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>Fixed maturities</b>						
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 433	\$ 12	\$	\$	\$ 433	\$ 12
Obligations of states, municipalities and political subdivisions	4,785	298	432	64	5,217	362
Debt securities issued by foreign governments	907	8	1		908	8
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	542	17	21	1	563	18
All other corporate bonds	6,887	253	421	46	7,308	299
Redeemable preferred stock	82	1			82	1
<b>Total fixed maturities</b>	<b>13,636</b>	<b>589</b>	<b>875</b>	<b>111</b>	<b>14,511</b>	<b>700</b>
<b>Equity securities</b>						
Common stock	53	1			53	1
Non-redeemable preferred stock	147	2			147	2
<b>Total equity securities</b>	<b>200</b>	<b>3</b>			<b>200</b>	<b>3</b>
<b>Total</b>	<b>\$ 13,836</b>	<b>\$ 592</b>	<b>\$ 875</b>	<b>\$ 111</b>	<b>\$ 14,711</b>	<b>\$ 703</b>

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## 3. INVESTMENTS (Continued)

(at December 31, 2012, in millions)	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>Fixed maturities</b>						
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 589	\$ 1	\$	\$	\$ 589	\$ 1
Obligations of states, municipalities and political subdivisions	611	9	45	2	656	11
Debt securities issued by foreign governments	186		2		188	
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	70		36	2	106	2
All other corporate bonds	1,097	13	89	7	1,186	20
<b>Total fixed maturities</b>	<b>2,553</b>	<b>23</b>	<b>172</b>	<b>11</b>	<b>2,725</b>	<b>34</b>
<b>Equity securities</b>						
Common stock	40	4			40	4
Non-redeemable preferred stock	13				13	
<b>Total equity securities</b>	<b>53</b>	<b>4</b>			<b>53</b>	<b>4</b>
<b>Total</b>	<b>\$ 2,606</b>	<b>\$ 27</b>	<b>\$ 172</b>	<b>\$ 11</b>	<b>\$ 2,778</b>	<b>\$ 38</b>

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. INVESTMENTS (Continued)**

The following table summarizes, for all fixed maturities and equity securities reported at fair value for which fair value is less than 80% of amortized cost at December 31, 2013, the gross unrealized investment loss by length of time those securities have continuously been in an unrealized loss position of greater than 20% of amortized cost:

(in millions)	Period For Which Fair Value Is Less Than 80% of Amortized Cost				Total
	3 Months or Less	Greater Than 3 Months, 6 Months, or Less	Greater Than 6 Months, 12 Months, or Less	Greater Than 12 Months	
<b>Fixed maturities</b>					
Mortgage-backed securities	\$	\$	\$	\$	\$
Other	7	3	1	3	14
Total fixed maturities	7	3	1	3	14
<b>Equity securities</b>					
Total	\$ 7	\$ 3	\$ 1	\$ 3	\$ 14

These unrealized losses at December 31, 2013 represented less than 1% of the combined fixed maturity and equity security portfolios on a pretax basis and less than 1% of shareholders' equity on an after-tax basis.

**Impairment Charges**

Impairment charges included in net realized investment gains in the consolidated statement of income were as follows:

(for the year ended December 31, in millions)	2013	2012	2011
<b>Fixed maturities</b>			
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$	\$	\$
Obligations of states, municipalities and political subdivisions			
Debt securities issued by foreign governments			
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2	4	13
All other corporate bonds	3	4	5
Redeemable preferred stock			
Total fixed maturities	5	8	18
<b>Equity securities</b>			
Common stock	5	3	6
Non-redeemable preferred stock		1	

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Total equity securities	5	4	6
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<b>Other investments</b>	<b>5</b>	<b>3</b>	<b>1</b>
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Total	\$ 15	\$ 15	\$ 25
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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## 3. INVESTMENTS (Continued)

The following tables present a roll-forward of the credit component of OTTI on fixed maturities recognized in the consolidated statement of income for which a portion of the OTTI was recognized in other comprehensive income for the years ended December 31, 2013 and 2012:

	Cumulative OTTI Credit Losses Recognized for Securities Held, Beginning of Period	Additions for OTTI Securities Where No Credit Losses Were Previously Recognized	Additions for OTTI Securities Where Credit Losses Have Been Previously Recognized	Reductions Due to Sales/Defaults of Credit- Impaired Securities	Adjustments to Book Value of Credit- Impaired Securities due to Changes in Cash Flows	Cumulative OTTI Credit Losses Recognized for Securities Still Held, End of Period
<b>Year ended December 31, 2013</b> (in millions)						
<b>Fixed maturities</b>						
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	\$ 63	\$	\$ 2	\$	\$ 4	\$ 69
All other corporate bonds	102	3		(7)	3	101
Total fixed maturities	\$ 165	\$ 3	\$ 2	\$ (7)	\$ 7	\$ 170

	Cumulative OTTI Credit Losses Recognized for Securities Held, Beginning of Period	Additions for OTTI Securities Where No Credit Losses Were Previously Recognized	Additions for OTTI Securities Where Credit Losses Have Been Previously Recognized	Reductions Due to Sales/Defaults of Credit- Impaired Securities	Adjustments to Book Value of Credit- Impaired Securities due to Changes in Cash Flows	Cumulative OTTI Credit Losses Recognized for Securities Still Held, End of Period
<b>Year ended December 31, 2012</b> (in millions)						
<b>Fixed maturities</b>						
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	\$ 58	\$	\$ 4	\$ (1)	\$ 2	\$ 63
All other corporate bonds	94		4		4	102
Total fixed maturities	\$ 152	\$	\$ 8	\$ (1)	\$ 6	\$ 165

**Concentrations and Credit Quality**

Concentrations of credit risk arise from exposure to counterparties that are engaged in similar activities and have similar economic characteristics that could cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The Company seeks to mitigate credit risk by actively monitoring the creditworthiness of counterparties, obtaining collateral as deemed appropriate and applying controls that include credit approvals, limits of credit exposure and other monitoring procedures.

At December 31, 2013, other than U.S. Treasury securities, obligations of U.S. government and government agencies and authorities, and obligations of the Canadian government, the Company was not exposed to any concentration of credit risk of a single issuer greater than 5% of the Company's shareholders' equity. At December 31, 2012, other than U.S. Treasury securities and obligations of U.S. government and government agencies and authorities, the Company was not exposed to any concentration of credit risk of a single issuer greater than 5% of the Company's shareholders' equity.

Included in fixed maturities are below investment grade securities totaling \$1.93 billion and \$2.05 billion at December 31, 2013 and 2012, respectively. The Company defines its below investment grade securities as those securities rated below investment grade by external rating agencies, or the equivalent by the Company when a public rating does not exist. Such securities include below

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## 3. INVESTMENTS (Continued)

investment grade bonds that are publicly traded and certain other privately issued bonds that are classified as below investment grade loans.

## Net Investment Income

(for the year ended December 31, in millions)	2013	2012	2011
<b>Gross investment income</b>			
Fixed maturities	\$ 2,310	\$ 2,439	\$ 2,543
Equity securities	31	28	29
Short-term securities	11	10	12
Real estate	37	34	34
Other investments	364	414	292
Gross investment income	2,753	2,925	2,910
Investment expenses	37	36	31
Net investment income	\$ 2,716	\$ 2,889	\$ 2,879

Changes in net unrealized gains on investment securities that are included as a separate component of other comprehensive income (loss) were as follows:

(at and for the year ended December 31, in millions)	2013	2012	2011
<b>Changes in net unrealized investment gains</b>			
Fixed maturities	\$ (2,804)	\$ 326	\$ 1,588
Equity securities	74	38	(2)
Other investments	(1)	(2)	(14)
Change in net pretax unrealized gains on investment securities	(2,731)	362	1,572
Related tax expense (benefit)	(950)	130	560
Change in net unrealized gains on investment securities	(1,781)	232	1,012
Balance, beginning of year	3,103	2,871	1,859
Balance, end of year	\$ 1,322	\$ 3,103	\$ 2,871

## Derivative Financial Instruments

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From time to time, the Company enters into U.S. Treasury note futures contracts to modify the effective duration of specific assets within the investment portfolio. U.S. Treasury futures contracts require a daily mark-to-market and settlement with the broker. At December 31, 2013 and 2012, the Company had \$0 and \$800 million notional value of open U.S. Treasury futures contracts, respectively. Net realized investment gains in 2013, 2012 and 2011 included net gains of \$115 million, net losses of \$14 million and net losses of \$62 million, respectively, related to U.S. Treasury futures contracts.

The Company purchases investments that have embedded derivatives, primarily convertible debt securities. These embedded derivatives are carried at fair value with changes in value reflected in net realized investment gains. Derivatives embedded in convertible debt securities are reported on a combined basis with their host instrument and are classified as fixed maturity securities. The Company

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**3. INVESTMENTS (Continued)**

recorded net realized investment gains of less than \$1 million in 2013, net realized investment losses of less than \$1 million in 2012 and net realized investment losses of \$2 million in 2011 related to these embedded derivatives.

**4. FAIR VALUE MEASUREMENTS**

The Company's estimates of fair value for financial assets and financial liabilities are based on the framework established in the fair value accounting guidance. The framework is based on the inputs used in valuation, gives the highest priority to quoted prices in active markets and requires that observable inputs be used in the valuations when available. The disclosure of fair value estimates in the fair value accounting guidance hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions. The level in the fair value hierarchy within which the fair value measurement is reported is based on the lowest level input that is significant to the measurement in its entirety. The three levels of the hierarchy are as follows:

Level 1 Unadjusted quoted market prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; or valuations based on models where the significant inputs are observable (e.g., interest rates, yield curves, prepayment speeds, default rates, loss severities, etc.) or can be corroborated by observable market data.

Level 3 Valuations based on models where significant inputs are not observable. The unobservable inputs reflect the Company's own assumptions about the inputs that market participants would use.

***Valuation of Investments Reported at Fair Value in Financial Statements***

The fair value of a financial instrument is the estimated amount at which the instrument could be exchanged in an orderly transaction between knowledgeable, unrelated, willing parties, i.e., not in a forced transaction. The estimated fair value of a financial instrument may differ from the amount that could be realized if the security was sold in an immediate sale, e.g., a forced transaction. Additionally, the valuation of investments is more subjective when markets are less liquid due to the lack of market based inputs, which may increase the potential that the estimated fair value of an investment is not reflective of the price at which an actual transaction would occur.

For investments that have quoted market prices in active markets, the Company uses the unadjusted quoted market prices as fair value and includes these prices in the amounts disclosed in Level 1 of the hierarchy. The Company receives the quoted market prices from a third party, nationally recognized pricing service (pricing service). When quoted market prices are unavailable, the Company utilizes a pricing service to determine an estimate of fair value, which is mainly used for its fixed maturity investments. The fair value estimates provided from this pricing service are included in the amount disclosed in Level 2 of the hierarchy. If quoted market prices and an estimate from a pricing service are unavailable, the Company produces an estimate of fair value based on internally developed valuation techniques, which, depending on the level of observable market inputs, will render the fair

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**4. FAIR VALUE MEASUREMENTS (Continued)**

value estimate as Level 2 or Level 3. The Company bases all of its estimates of fair value for assets on the bid price as it represents what a third-party market participant would be willing to pay in an arm's length transaction.

*Fixed Maturities*

The Company utilized a pricing service to estimate fair value measurements for approximately 98% of its fixed maturities at both December 31, 2013 and 2012. The pricing service utilizes market quotations for fixed maturity securities that have quoted prices in active markets. Since fixed maturities other than U.S. Treasury securities generally do not trade on a daily basis, the pricing service prepares estimates of fair value measurements for these securities using its proprietary pricing applications, which include available relevant market information, benchmark curves, benchmarking of like securities, sector groupings and matrix pricing. Additionally, the pricing service uses an Option Adjusted Spread model to develop prepayment and interest rate scenarios.

The pricing service evaluates each asset class based on relevant market information, relevant credit information, perceived market movements and sector news. The market inputs utilized in the pricing evaluation, listed in the approximate order of priority, include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data, and industry and economic events. The extent of the use of each market input depends on the asset class and the market conditions. Depending on the security, the priority of the use of inputs may change or some market inputs may not be relevant. For some securities, additional inputs may be necessary.

The pricing service utilized by the Company has indicated that it will only produce an estimate of fair value if there is objectively verifiable information to produce a valuation. If the pricing service discontinues pricing an investment, the Company would be required to produce an estimate of fair value using some of the same methodologies as the pricing service but would have to make assumptions for market-based inputs that are unavailable due to market conditions.

The fair value estimates of most fixed maturity investments are based on observable market information rather than market quotes. Accordingly, the estimates of fair value for such fixed maturities, other than U.S. Treasury securities, provided by the pricing service are included in the amount disclosed in Level 2 of the hierarchy. The estimated fair value of U.S. Treasury securities is included in the amount disclosed in Level 1 as the estimates are based on unadjusted market prices.

The Company also holds certain fixed maturity investments which are not priced by the pricing service and, accordingly, estimates the fair value of such fixed maturities using an internal matrix that is based on market information regarding interest rates, credit spreads and liquidity. The underlying source data for calculating the matrix of credit spreads relative to the U.S. Treasury curve are the BofA Merrill Lynch U.S. Corporate Index and the BofA Merrill Lynch High Yield BB Rated Index. The Company includes the fair value estimates of these corporate bonds in Level 2, since all significant inputs are market observable.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**4. FAIR VALUE MEASUREMENTS (Continued)**

While the vast majority of the Company's municipal bonds and corporate bonds are included in Level 2, the Company holds a number of municipal bonds and corporate bonds which are not valued by the pricing service and estimates the fair value of these bonds using an internal pricing matrix with some unobservable inputs that are significant to the valuation. Due to the limited amount of observable market information, the Company includes the fair value estimates for these particular bonds in Level 3. The fair value of the fixed maturities for which the Company used an internal pricing matrix was \$94 million and \$102 million at December 31, 2013 and 2012, respectively. Additionally, the Company holds a small amount of other fixed maturity investments that have characteristics that make them unsuitable for matrix pricing. For these fixed maturities, the Company obtains a quote from a broker (primarily the market maker). The fair value of the fixed maturities for which the Company received a broker quote was \$161 million and \$128 million at December 31, 2013 and 2012, respectively. Due to the disclaimers on the quotes that indicate that the price is indicative only, the Company includes these fair value estimates in Level 3.

*Equities Public Common and Preferred*

For public common and preferred stocks, the Company receives prices from a nationally recognized pricing service that are based on observable market transactions and includes these estimates in the amount disclosed in Level 1. When current market quotes in active markets are unavailable for certain non-redeemable preferred stocks held by the Company, the Company receives an estimate of fair value from the pricing service that provides fair value estimates for the Company's fixed maturities. The service utilizes some of the same methodologies to price the non-redeemable preferred stocks as it does for the fixed maturities. The Company includes the fair value estimate for these non-redeemable preferred stocks in the amount disclosed in Level 2.

*Other Investments*

The Company holds investments in various publicly-traded securities which are reported in other investments. These investments include securities in the Company's trading portfolio, mutual funds and other small holdings. The \$19 million and \$46 million fair value of these investments at December 31, 2013 and 2012, respectively, was disclosed in Level 1. At December 31, 2013 and 2012, the Company held investments in non-public common and preferred equity securities, with fair value estimates of \$34 million and \$54 million, respectively, reported in other investments, where the fair value estimate is determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth and other business and market sector fundamentals. Due to the significant unobservable inputs in these valuations, the Company includes the total fair value estimate for all of these investments at December 31, 2013 and 2012 in the amount disclosed in Level 3.

*Derivatives*

At December 31, 2013 and 2012, the Company held \$8 million and \$21 million, respectively, of convertible bonds containing embedded conversion options that are valued separately from the host bond contract in the amount disclosed in Level 2 fixed maturities.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****4. FAIR VALUE MEASUREMENTS (Continued)****Fair Value Hierarchy**

The following tables present the level within the fair value hierarchy at which the Company's financial assets and financial liabilities are measured on a recurring basis at December 31, 2013 and 2012. An investment transferred between levels during a period is transferred at its fair value as of the beginning of that period.

(at December 31, 2013, in millions)	Total	Level 1	Level 2	Level 3
<b>Invested assets:</b>				
<b>Fixed maturities</b>				
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,315	\$ 2,298	\$ 17	\$
Obligations of states, municipalities and political subdivisions	35,562	1	35,538	23
Debt securities issued by foreign governments	2,577		2,577	
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2,424		2,415	9
All other corporate bonds	20,940		20,726	214
Redeemable preferred stock	138		129	9
<b>Total fixed maturities</b>	<b>63,956</b>	<b>2,299</b>	<b>61,402</b>	<b>255</b>
<b>Equity securities</b>				
Common stock	610	610		
Non-redeemable preferred stock	333	138	195	
<b>Total equity securities</b>	<b>943</b>	<b>748</b>	<b>195</b>	
<b>Other investments</b>	<b>53</b>	<b>19</b>		<b>34</b>
<b>Total</b>	<b>\$ 64,952</b>	<b>\$ 3,066</b>	<b>\$ 61,597</b>	<b>\$ 289</b>



Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****4. FAIR VALUE MEASUREMENTS (Continued)**

During the year ended December 31, 2013, the Company had transfers of \$31 million of redeemable preferred stock and \$54 million of non-redeemable preferred stock from Level 1 to Level 2.

(at December 31, 2012, in millions)	Total	Level 1	Level 2	Level 3
<b>Invested assets:</b>				
<b>Fixed maturities</b>				
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,222	\$ 2,205	\$ 17	\$
Obligations of states, municipalities and political subdivisions	38,681		38,653	28
Debt securities issued by foreign governments	2,257		2,257	
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2,997		2,992	5
All other corporate bonds	19,203		19,006	197
Redeemable preferred stock	33	32	1	
<b>Total fixed maturities</b>	<b>65,393</b>	<b>2,237</b>	<b>62,926</b>	<b>230</b>
<b>Equity securities</b>				
Common stock	510	510		
Non-redeemable preferred stock	135	92	43	
<b>Total equity securities</b>	<b>645</b>	<b>602</b>	<b>43</b>	
<b>Other investments</b>	<b>100</b>	<b>46</b>		<b>54</b>
<b>Total</b>	<b>\$ 66,138</b>	<b>\$ 2,885</b>	<b>\$ 62,969</b>	<b>\$ 284</b>

During the year ended December 31, 2012, the Company had transfers of \$4 million of non-redeemable preferred stock from Level 1 to Level 2.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****4. FAIR VALUE MEASUREMENTS (Continued)**

The following tables present the changes in the Level 3 fair value category for the years ended December 31, 2013 and 2012.

(in millions)	Fixed Maturities	Other Investments	Total
Balance at December 31, 2012	\$ 230	\$ 54	\$ 284
Total realized and unrealized investment gains (losses):			
Reported in net realized investment gains(1)	4	12	16
Reported in increases (decreases) in other comprehensive income	(2)	1	(1)
Purchases, sales and settlements/maturities:			
Purchases	180		180
Sales	(25)	(33)	(58)
Settlements/maturities	(83)		(83)
Gross transfers into Level 3	15		15
Gross transfers out of Level 3	(64)		(64)
Balance at December 31, 2013	\$ 255	\$ 34	\$ 289

Amount of total realized investment gains (losses) for the period included in the consolidated statement of income attributable to changes in the fair value of assets still held at the reporting date	\$	\$	\$
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(1) Includes impairments on investments held at the end of the period as well as amortization on fixed maturities.

(in millions)	Fixed Maturities	Other Investments	Total
Balance at December 31, 2011	\$ 250	\$ 44	\$ 294
Total realized and unrealized investment gains (losses):			
Reported in net realized investment gains(1)	4		