PROGRESSIVE CORP/OH/
Form 10-Q
August 02, 2012

# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 1O-Q

**(Mark One)**

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the quarterly period ended June 30, 2012**

**or**

¨ **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: 1-9518**

# THE PROGRESSIVE CORPORATION

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Ohio** | **34-0963169** |
| **(State or other jurisdiction of** | **(I.R.S. Employer** |
| **incorporation or organization)** | **Identification No.)** |
| **6300 Wilson Mills Road, Mayfield Village, Ohio** | **44143** |
| **(Address of principal executive offices)** | **(Zip Code)** |

**(440) 461-5000**

**(Registrant s telephone number, including area code)**

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 þ 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 þ No ¨

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 Exchange Act. (Check one):

| | |
|---|---|
| Large accelerated filer þ | Accelerated filer ¨ |
| Non-accelerated filer ¨ (Do not check if a smaller reporting company) | Smaller reporting company ¨ |

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Common Shares, $1.00 par value: 609,158,487 outstanding at June 30, 2012

**PART I FINANCIAL INFORMATION**

**Item 1. Financial Statements.**

The Progressive Corporation and Subsidiaries

**Consolidated Statements of Comprehensive Income**

(unaudited)

| | Three Months | | | Six Months | | |
|---|---|---|---|---|---|---|
| **Periods Ended June 30,** **(millions except per share amounts)** | **2012** | **2011** | **% Change** | **2012** | **2011** | **% Change** |
| **Revenues** | | | | | | |
| Net premiums earned | $ 3,996.1 | $ 3,719.9 | 7 | $ 7,857.6 | $ 7,385.2 | 6 |
| Investment income | 112.5 | 120.8 | (7) | 227.2 | 244.1 | (7) |
| Net realized gains (losses) on securities: | | | | | | |
| Other-than-temporary impairment (OTTI) losses: | | | | | | |
| Total OTTI losses | (5.1) | (3.1) | 65 | (5.6) | (4.5) | 24 |
| Non-credit losses, net of credit losses recognized on previously recorded non-credit OTTI losses | (.3) | .9 | NM | (.7) | .9 | NM |
| Net impairment losses recognized in earnings | (5.4) | (2.2) | 145 | (6.3) | (3.6) | 75 |
| Net realized gains (losses) on securities | .7 | 28.2 | (98) | 79.1 | 129.3 | (39) |
| Total net realized gains (losses) on securities | (4.7) | 26.0 | NM | 72.8 | 125.7 | (42) |
| Service revenues | 10.2 | 6.0 | 70 | 18.4 | 11.2 | 64 |
| Gains (losses) on extinguishment of debt | (1.0) | 0 | NM | (1.7) | 0 | NM |
| Total revenues | 4,113.1 | 3,872.7 | 6 | 8,174.3 | 7,766.2 | 5 |
| **Expenses** | | | | | | |
| Losses and loss adjustment expenses | 3,043.7 | 2,660.9 | 14 | 5,806.1 | 5,169.0 | 12 |
| Policy acquisition costs | 364.5 | 348.3 | 5 | 724.1 | 695.0 | 4 |
| Other underwriting expenses | 492.8 | 466.0 | 6 | 1,003.6 | 920.7 | 9 |
| Investment expenses | 3.8 | 3.5 | 9 | 8.0 | 6.6 | 21 |
| Service expenses | 9.9 | 4.8 | 106 | 18.1 | 8.8 | 106 |
| Interest expense | 30.7 | 31.5 | (3) | 62.6 | 63.0 | (1) |
| Total expenses | 3,945.4 | 3,515.0 | 12 | 7,622.5 | 6,863.1 | 11 |
| **Net Income** | | | | | | |
| Income before income taxes | 167.7 | 357.7 | (53) | 551.8 | 903.1 | (39) |
| Provision for income taxes | 49.1 | 112.5 | (56) | 175.6 | 295.0 | (40) |
| Net income | 118.6 | 245.2 | (52) | 376.2 | 608.1 | (38) |
| **Other Comprehensive Income (Loss), Net of Tax** | | | | | | |
| Net unrealized gains (losses) on securities: | | | | | | |
| Net non-credit related OTTI losses, adjusted for valuation changes | .1 | (2.2) | NM | 3.1 | (3.1) | NM |
| Other net unrealized gains (losses) on securities | (51.0) | 53.5 | NM | 148.4 | 84.0 | 77 |
| Total net unrealized gains (losses) on securities | (50.9) | 51.3 | NM | 151.5 | 80.9 | 87 |
| Net unrealized gains on forecasted transactions | (.6) | (.8) | (25) | (1.2) | (1.6) | (25) |

| | | | | | | |
|---|---|---|---|---|---|---|
| Foreign currency translation adjustment | (.6) | .3 | NM | (.1) | .5 | NM |
| Other comprehensive income (loss) | (52.1) | 50.8 | NM | 150.2 | 79.8 | 88 |
| Comprehensive income | $ 66.5 | $ 296.0 | (78) | $ 526.4 | $ 687.9 | (23) |
| **Computation of Net Income Per Share** | | | | | | |
| Average shares outstanding Basic | 604.8 | 643.6 | (6) | 605.5 | 647.6 | (7) |
| Net effect of dilutive stock-based compensation | 4.1 | 4.3 | (5) | 4.0 | 4.1 | (2) |
| Total equivalent shares Diluted | 608.9 | 647.9 | (6) | 609.5 | 651.7 | (6) |
| Basic: Net income per share | $ .20 | $ .38 | (49) | $ .62 | $ .94 | (34) |
| Diluted: Net income per share | $ .19 | $ .38 | (49) | $ .62 | $ .93 | (34) |
| **Dividends declared per share**[1] | $ 0 | $ 0 | | $ 0 | $ 0 | |

NM = Not Meaningful

[1] Progressive maintains an annual dividend program. See *Note 8 Dividends* for further discussion.

See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries

**Consolidated Balance Sheets**

(unaudited)

| (millions) | June 30, 2012 | June 30, 2011 | December 31, 2011 |
|---|---|---|---|
| **Assets** | | | |
| Investments Available-for-sale, at fair value: | | | |
| Fixed maturities (amortized cost: $11,723.6, $11,499.5, and $11,455.7) | $ 12,075.9 | $ 11,788.5 | $ 11,759.3 |
| Equity securities: | | | |
| Nonredeemable preferred stocks (cost: $425.4, $495.5, and $473.7) | 799.3 | 1,029.7 | 806.3 |
| Common equities (cost: $1,494.9, $1,379.8, and $1,431.0) | 2,055.1 | 1,867.9 | 1,845.6 |
| Short-term investments (amortized cost: $1,679.2, $1,343.5, and $1,551.8) | 1,679.2 | 1,343.5 | 1,551.8 |
| Total investments | 16,609.5 | 16,029.6 | 15,963.0 |
| Cash | 165.5 | 149.7 | 155.7 |
| Accrued investment income | 96.4 | 104.3 | 105.7 |
| Premiums receivable, net of allowance for doubtful accounts of $118.8, $109.5, and $124.2 | 3,222.1 | 2,982.6 | 2,929.8 |
| Reinsurance recoverables, including $30.4, $34.3, and $32.3 on paid losses and loss adjustment expenses | 844.7 | 775.7 | 818.0 |
| Prepaid reinsurance premiums | 71.1 | 86.7 | 69.8 |
| Deferred acquisition costs | 452.4 | 451.6 | 433.6 |
| Income taxes | 147.8 | 111.4 | 208.0 |
| Property and equipment, net of accumulated depreciation of $606.6, $596.4, and $573.8 | 914.3 | 917.1 | 911.3 |
| Other assets | 195.2 | 198.9 | 249.9 |
| Total assets | $ 22,719.0 | $ 21,807.6 | $ 21,844.8 |
| **Liabilities and Shareholders Equity** | | | |
| Unearned premiums | $ 5,014.6 | $ 4,704.3 | $ 4,579.4 |
| Loss and loss adjustment expense reserves | 7,573.2 | 7,142.6 | 7,245.8 |
| Accounts payable, accrued expenses, and other liabilities | 1,781.8 | 1,652.1 | 1,770.8 |
| Debt[1] | 2,062.8 | 1,959.1 | 2,442.1 |
| Total liabilities | 16,432.4 | 15,458.1 | 16,038.1 |
| Common Shares, $1.00 par value (authorized 900.0; issued 797.7, including treasury shares of 188.5, 155.0, and 184.7) | 609.2 | 642.7 | 613.0 |
| Paid-in capital | 1,040.4 | 1,007.7 | 1,006.2 |
| Retained earnings | 3,794.3 | 3,835.6 | 3,495.0 |
| Accumulated other comprehensive income, net of tax: | | | |
| Net non-credit related OTTI losses, adjusted for valuation changes | (2.3) | (4.9) | (5.4) |
| Other net unrealized gains (losses) on securities | 836.6 | 853.1 | 688.2 |
| Total net unrealized gains (losses) on securities | 834.3 | 848.2 | 682.8 |
| Net unrealized gains on forecasted transactions | 6.7 | 13.1 | 7.9 |
| Foreign currency translation adjustment | 1.7 | 2.2 | 1.8 |
| Total accumulated other comprehensive income | 842.7 | 863.5 | 692.5 |
| Total shareholders equity | 6,286.6 | 6,349.5 | 5,806.7 |
| Total liabilities and shareholders equity | $ 22,719.0 | $ 21,807.6 | $ 21,844.8 |

[1] Consists of long-term debt. See *Note 4 Debt.*

See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries

**Consolidated Statements of Cash Flows**

(unaudited)

| **Six months ended June 30,**<br>**(millions)** | **2012** | **2011** |
|---|---|---|
| **Cash Flows From Operating Activities** | | |
| Net income | $ 376.2 | $ 608.1 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 45.5 | 42.6 |
| Amortization of fixed-income securities | 98.3 | 116.4 |
| Amortization of stock-based compensation | 31.5 | 24.5 |
| Net realized (gains) losses on securities | (72.8) | (125.7) |
| Net (gains) losses on disposition of property and equipment | 3.5 | 7.3 |
| (Gains) losses on extinguishment of debt | 1.7 | 0 |
| Changes in: | | |
| Premiums receivable | (292.3) | (244.2) |
| Reinsurance recoverables | (26.7) | (34.2) |
| Prepaid reinsurance premiums | (1.3) | 1.4 |
| Deferred acquisition costs | (18.8) | (34.4) |
| Income taxes | (21.1) | 34.1 |
| Unearned premiums | 435.2 | 350.4 |
| Loss and loss adjustment expense reserves | 327.4 | 71.5 |
| Accounts payable, accrued expenses, and other liabilities | 230.6 | 194.4 |
| Other, net | 18.2 | 18.9 |
| Net cash provided by operating activities | 1,135.1 | 1,031.1 |
| **Cash Flows From Investing Activities** | | |
| Purchases: | | |
| Fixed maturities | (2,628.7) | (4,265.9) |
| Equity securities | (79.4) | (397.5) |
| Sales: | | |
| Fixed maturities | 1,689.4 | 3,570.6 |
| Equity securities | 101.6 | 240.9 |
| Maturities, paydowns, calls, and other: | | |
| Fixed maturities | 616.6 | 735.4 |
| Equity securities | 3.9 | 0 |
| Net purchases of short-term investments - other | (128.0) | (252.3) |
| Net unsettled security transactions | 62.4 | 39.2 |
| Purchases of property and equipment | (53.5) | (35.6) |
| Sales of property and equipment | 1.5 | 1.2 |
| Net cash used in investing activities | (414.2) | (364.0) |
| **Cash Flows From Financing Activities** | | |
| Proceeds from exercise of stock options | .5 | 5.4 |
| Tax benefit from exercise/vesting of stock-based compensation | 4.1 | 2.4 |
| Payment of debt | (350.0) | 0 |
| Reacquisition of debt | (31.9) | 0 |
| Dividends paid to shareholders[1] | (251.0) | (263.6) |
| Acquisition of treasury shares | (83.0) | (420.9) |
| Net cash used in financing activities | (711.3) | (676.7) |

| | | | | |
|---|---|---|---|---|
| Effect of exchange rate changes on cash | | .2 | | .4 |
| Increase (decrease) in cash | | 9.8 | | (9.2) |
| Cash, January 1 | | 155.7 | | 158.9 |
| Cash, June 30 | $ | 165.5 | $ | 149.7 |

[1] Progressive maintains an annual dividend program. See *Note 8 Dividends* for further discussion.

See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries

**Notes to Consolidated Financial Statements**

(unaudited)

**Note 1** ***Basis of Presentation*** The consolidated financial statements include the accounts of The Progressive Corporation, its subsidiaries, and a mutual company affiliate. All of the subsidiaries and the mutual company affiliate are wholly owned or controlled. The consolidated financial statements reflect all normal recurring adjustments that, in the opinion of management, were necessary for a fair statement of the results for the interim periods presented. The results of operations for the period ended June 30, 2012, are not necessarily indicative of the results expected for the full year. These consolidated financial statements and the notes thereto should be read in conjunction with Progressive s audited financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2011.

On January 1, 2012, we adopted, on a prospective basis, the accounting standard update related to the accounting for the deferral of costs associated with the successful acquisition or renewal of insurance contracts. As a result, $23 million of deferred acquisition costs that no longer met the criteria for deferral upon adoption were recognized as a reduction to income primarily over the first six months of 2012, consistent with our insurance policy terms.

**Note 2** ***Investments*** The following tables present the composition of our investment portfolio by major security type, consistent with our internal classification of how we manage, monitor, and measure the portfolio:

| **($ in millions)** | **Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Net Realized Gains (Losses)**[1] | **Fair Value** | **% of Total Fair Value** |
|---|---|---|---|---|---|---|
| June 30, 2012 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | $ 2,833.0 | $ 105.6 | $ 0 | $ 0 | $ 2,938.6 | 17.7% |
| State and local government obligations | 1,926.9 | 51.2 | (.5) | 0 | 1,977.6 | 11.9 |
| Corporate debt securities | 2,893.6 | 114.4 | (5.6) | 4.8 | 3,007.2 | 18.1 |
| Residential mortgage-backed securities | 429.2 | 14.7 | (22.3) | 0 | 421.6 | 2.5 |
| Commercial mortgage-backed securities | 2,020.2 | 74.7 | (1.4) | 0 | 2,093.5 | 12.6 |
| Other asset-backed securities | 1,250.8 | 13.7 | (.2) | (.3) | 1,264.0 | 7.6 |
| Redeemable preferred stocks | 369.9 | 21.0 | (17.5) | 0 | 373.4 | 2.3 |
| Total fixed maturities | 11,723.6 | 395.3 | (47.5) | 4.5 | 12,075.9 | 72.7 |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 425.4 | 376.5 | (1.0) | (1.6) | 799.3 | 4.8 |
| Common equities | 1,494.9 | 591.1 | (30.9) | 0 | 2,055.1 | 12.4 |
| Short-term investments: | | | | | | |
| Other short-term investments | 1,679.2 | 0 | 0 | 0 | 1,679.2 | 10.1 |
| Total portfolio[2,3] | $ 15,323.1 | $ 1,362.9 | $ (79.4) | $ 2.9 | $ 16,609.5 | 100.0% |

| ($ in millions) | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Net Realized Gains (Losses)[1] | Fair Value | % of Total Fair Value |
|---|---|---|---|---|---|---|
| June 30, 2011 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | $ 2,881.1 | $ 80.3 | $ (.8) | $ 0 | $ 2,960.6 | 18.5% |
| State and local government obligations | 1,812.7 | 46.0 | (1.3) | 0 | 1,857.4 | 11.6 |
| Corporate debt securities | 2,765.1 | 89.5 | (5.1) | 5.9 | 2,855.4 | 17.8 |
| Residential mortgage-backed securities | 537.0 | 12.7 | (29.8) | 0 | 519.9 | 3.2 |
| Commercial mortgage-backed securities | 1,755.6 | 60.4 | (3.6) | 0 | 1,812.4 | 11.3 |
| Other asset-backed securities | 1,312.4 | 15.0 | (.8) | 1.1 | 1,327.7 | 8.3 |
| Redeemable preferred stocks | 435.6 | 28.0 | (8.5) | 0 | 455.1 | 2.8 |
| Total fixed maturities | 11,499.5 | 331.9 | (49.9) | 7.0 | 11,788.5 | 73.5 |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 495.5 | 534.8 | 0 | (.6) | 1,029.7 | 6.4 |
| Common equities | 1,379.8 | 494.7 | (6.6) | 0 | 1,867.9 | 11.7 |
| Short-term investments: | | | | | | |
| Other short-term investments | 1,343.5 | 0 | 0 | 0 | 1,343.5 | 8.4 |
| Total portfolio[2,3] | $ 14,718.3 | $ 1,361.4 | $ (56.5) | $ 6.4 | $ 16,029.6 | 100.0 % |

| ($ in millions) | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Net Realized Gains (Losses)[1] | Fair Value | % of Total Fair Value |
|---|---|---|---|---|---|---|
| December 31, 2011 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | $ 2,842.7 | $ 120.3 | $ 0 | $ 0 | $ 2,963.0 | 18.6 % |
| State and local government obligations | 1,938.6 | 64.1 | (.6) | 0 | 2,002.1 | 12.5 |
| Corporate debt securities | 2,801.5 | 94.3 | (6.5) | 6.9 | 2,896.2 | 18.1 |
| Residential mortgage-backed securities | 452.9 | 9.3 | (35.3) | 0 | 426.9 | 2.7 |
| Commercial mortgage-backed securities | 1,829.8 | 52.3 | (5.5) | 0 | 1,876.6 | 11.8 |
| Other asset-backed securities | 1,210.9 | 11.3 | (1.3) | (.3) | 1,220.6 | 7.6 |
| Redeemable preferred stocks | 379.3 | 18.6 | (24.0) | 0 | 373.9 | 2.3 |
| Total fixed maturities | 11,455.7 | 370.2 | (73.2) | 6.6 | 11,759.3 | 73.6 |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 473.7 | 342.6 | (3.7) | (6.3) | 806.3 | 5.1 |
| Common equities | 1,431.0 | 440.0 | (25.4) | 0 | 1,845.6 | 11.6 |
| Short-term investments: | | | | | | |
| Other short-term investments | 1,551.8 | 0 | 0 | 0 | 1,551.8 | 9.7 |
| Total portfolio[2,3] | $ 14,912.2 | $ 1,152.8 | $ (102.3) | $ .3 | $ 15,963.0 | 100.0 % |

1 Represents net holding period gains (losses) on certain hybrid securities (discussed below).

2 At June 30, 2012, we had $15.5 million of net unsettled security transactions included in other liabilities, compared to $7.1 million and $46.9 million included in other assets at June 30, 2011 and December 31, 2011, respectively.

3 The total fair value of the portfolio at June 30, 2012 and 2011, and December 31, 2011 included $1.4 billion, $1.6 billion, and $2.0 billion, respectively, of securities held in a consolidated, non-insurance subsidiary of the holding company, net of any unsettled security transactions.

Our other short-term investments include Eurodollar deposits, commercial paper, reverse repurchase transactions, and other investments that are expected to mature within one year.

Included in our fixed-maturity and equity securities are hybrid securities, which are reported at fair value:

| (millions) | June 30, 2012 | 2011 | December 31, 2011 |
|---|---|---|---|
| Fixed maturities: | | | |
| Corporate debt securities | $ 166.8 | $ 230.5 | $ 234.9 |
| Other asset-backed securities | 15.9 | 16.5 | 15.5 |
| Total fixed maturities | 182.7 | 247.0 | 250.4 |
| Equity securities: | | | |
| Nonredeemable preferred stocks | 18.9 | 22.9 | 14.2 |
| Total hybrid securities | $ 201.6 | $ 269.9 | $ 264.6 |

Certain corporate debt securities are accounted for as hybrid securities since they were acquired at a substantial premium and contain a change-in-control put option (derivative) that permits the investor, at its sole option if and when a change in control is triggered, to put the security back to the issuer at a 1% premium to par. Due to this change-in-control put option and the substantial market premium paid to acquire these securities, there is the potential that the election to put, upon the change in control, could result in an acceleration of the remaining premium paid on these securities, which would result in a loss of $11.6 million as of June 30, 2012, if all of the bonds experienced a simultaneous change in control and we elected to exercise all of our put options. The put feature limits the potential loss in value that could be experienced in the event a corporate action occurs that results in a change in control which materially diminishes the credit quality of the issuer. We are under no obligation to exercise the put option we hold if a change in control occurs.

The other asset-backed security in the table above represents one hybrid security that was acquired at a deep discount to par due to a failing auction, and contains a put option that allows the investor to put that security back to the auction at par if the auction is restored. This embedded derivative has the potential to more than double our initial investment yield.

The hybrid securities in our nonredeemable preferred stock portfolio are perpetual preferred stocks that have call features with fixed-rate coupons, whereby the change in value of the call features is a component of the overall change in value of the preferred stocks.

Our securities are reported at fair value, with the changes in fair value of these securities (other than hybrid securities and derivative instruments) reported as a component of accumulated other comprehensive income, net of deferred income taxes. The changes in fair value of the hybrid securities and derivative instruments are recorded as a component of net realized gains (losses) on securities.

***Fixed Maturities*** The composition of fixed maturities by maturity at June 30, 2012, was:

| (millions) | Cost | Fair Value |
|---|---|---|
| Less than one year | $ 1,491.3 | $ 1,514.0 |
| One to five years | 8,722.4 | 8,995.8 |
| Five to ten years | 1,424.2 | 1,479.3 |
| Ten years or greater | 85.0 | 86.1 |
| Total[1] | $ 11,722.9 | $ 12,075.2 |

1 Excludes $0.7 million of gains on the open credit default swap position.

Asset-backed securities are classified in the maturity distribution table based upon their projected cash flows. All other securities which do not have a single maturity date are reported at expected average maturity. Contractual maturities may differ from expected maturities because the issuers of the securities may have the right to call or prepay obligations.

***Gross Unrealized Losses*** As of June 30, 2012, we had $48.5 million of gross unrealized losses in our fixed-income securities (i.e., fixed-maturity securities, nonredeemable preferred stocks, and short-term investments) and $30.9 million in our common equities. We currently do not intend to sell the fixed-income securities and determined that it is more likely than not that we will not be required to sell these securities during the periods of time necessary to recover their respective cost bases. A review of our fixed-income securities indicated that the issuers were current with respect to their interest obligations and that there was no evidence of any deterioration of the current cash flow projections that would indicate we would not receive the remaining principal at maturity. In addition, 94% of our common stock portfolio was indexed to the Russell 1000; as such, this portfolio may contain securities in a loss position for an extended period of time, subject to possible write-downs, as described below. We may retain these securities as long as the portfolio and index correlation remain similar. To the extent there is issuer specific deterioration, we may write-down the securities. The remaining 6% of our common stocks are part of a managed equity strategy selected and administered by an external investment advisor. If our strategy were to change and these securities were determined to be other-than-temporarily impaired, we would recognize a write-down in accordance with our stated policy.

The following tables show the composition of gross unrealized losses by major security type and by the length of time that individual securities have been in a continuous unrealized loss position:

| (millions) | Total Fair Value | Gross Unrealized Losses | Less than 12 Months Fair Value | Less than 12 Months Unrealized Losses | 12 Months or Greater Fair Value | 12 Months or Greater Unrealized Losses |
|---|---|---|---|---|---|---|
| June 30, 2012 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 |
| State and local government obligations | 118.3 | (.5) | 95.3 | (.3) | 23.0 | (.2) |
| Corporate debt securities | 170.0 | (5.6) | 111.4 | (.4) | 58.6 | (5.2) |
| Residential mortgage-backed securities | 271.3 | (22.3) | 32.3 | (1.1) | 239.0 | (21.2) |
| Commercial mortgage-backed securities | 73.5 | (1.4) | 39.9 | (.1) | 33.6 | (1.3) |
| Other asset-backed securities | 35.0 | (.2) | 20.0 | 0 | 15.0 | (.2) |
| Redeemable preferred stocks | 169.4 | (17.5) | 43.5 | (1.5) | 125.9 | (16.0) |
| Total fixed maturities | 837.5 | (47.5) | 342.4 | (3.4) | 495.1 | (44.1) |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 22.3 | (1.0) | 0 | 0 | 22.3 | (1.0) |
| Common equities | 229.0 | (30.9) | 173.4 | (17.8) | 55.6 | (13.1) |
| Total equity securities | 251.3 | (31.9) | 173.4 | (17.8) | 77.9 | (14.1) |
| Total portfolio | $ 1,088.8 | $ (79.4) | $ 515.8 | $ (21.2) | $ 573.0 | $ (58.2) |

| (millions) | Total Fair Value | Gross Unrealized Losses | Less than 12 Months Fair Value | Less than 12 Months Unrealized Losses | 12 Months or Greater Fair Value | 12 Months or Greater Unrealized Losses |
|---|---|---|---|---|---|---|
| June 30, 2011 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | $ 33.4 | $ (.8) | $ 33.4 | $ (.8) | $ 0 | $ 0 |
| State and local government obligations | 163.3 | (1.3) | 121.1 | (.6) | 42.2 | (.7) |
| Corporate debt securities | 354.7 | (5.1) | 330.3 | (4.7) | 24.4 | (.4) |
| Residential mortgage-backed securities | 402.1 | (29.8) | 185.4 | (3.0) | 216.7 | (26.8) |
| Commercial mortgage-backed securities | 220.9 | (3.6) | 138.6 | (2.1) | 82.3 | (1.5) |
| Other asset-backed securities | 120.0 | (.8) | 115.5 | (.3) | 4.5 | (.5) |
| Redeemable preferred stocks | 161.7 | (8.5) | 0 | 0 | 161.7 | (8.5) |
| Total fixed maturities | 1,456.1 | (49.9) | 924.3 | (11.5) | 531.8 | (38.4) |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 0 | 0 | 0 | 0 | 0 | 0 |
| Common equities | 95.0 | (6.6) | 94.7 | (6.5) | .3 | (.1) |
| Total equity securities | 95.0 | (6.6) | 94.7 | (6.5) | .3 | (.1) |
| Total portfolio | $ 1,551.1 | $ (56.5) | $ 1,019.0 | $ (18.0) | $ 532.1 | $ (38.5) |

| (millions) | Total Fair Value | Gross Unrealized Losses | Less than 12 Months Fair Value | Less than 12 Months Unrealized Losses | 12 Months or Greater Fair Value | 12 Months or Greater Unrealized Losses |
|---|---|---|---|---|---|---|
| December 31, 2011 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 |
| State and local government obligations | 93.6 | (.6) | 79.5 | (.5) | 14.1 | (.1) |
| Corporate debt securities | 262.7 | (6.5) | 137.3 | (4.6) | 125.4 | (1.9) |
| Residential mortgage-backed securities | 308.7 | (35.3) | 34.4 | (2.0) | 274.3 | (33.3) |
| Commercial mortgage-backed securities | 203.7 | (5.5) | 161.4 | (3.5) | 42.3 | (2.0) |
| Other asset-backed securities | 284.2 | (1.3) | 259.7 | (1.0) | 24.5 | (.3) |
| Redeemable preferred stocks | 191.4 | (24.0) | 43.5 | (1.5) | 147.9 | (22.5) |
| Total fixed maturities | 1,344.3 | (73.2) | 715.8 | (13.1) | 628.5 | (60.1) |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 19.5 | (3.7) | 19.5 | (3.7) | 0 | 0 |
| Common equities | 214.6 | (25.4) | 196.7 | (23.1) | 17.9 | (2.3) |
| Total equity securities | 234.1 | (29.1) | 216.2 | (26.8) | 17.9 | (2.3) |
| Total portfolio | $ 1,578.4 | $ (102.3) | $ 932.0 | $ (39.9) | $ 646.4 | $ (62.4) |

***Other-Than-Temporary Impairment (OTTI)*** The following table shows the total non-credit portion of the OTTI recorded in accumulated other comprehensive income, reflecting the original non-credit loss at the time the credit impairment was determined:

| (millions) | June 30, 2012 | June 30, 2011 | December 31, 2011 |
|---|---|---|---|
| Fixed maturities: | | | |
| Residential mortgage-backed securities | $ (44.2) | $ (45.2) | $ (44.8) |
| Commercial mortgage-backed securities | (.9) | (1.0) | (1.0) |
| Total fixed maturities | $ (45.1) | $ (46.2) | $ (45.8) |

The following tables provide rollforwards of the amounts related to credit losses recognized in earnings for the periods ended June 30, 2012 and 2011, for which portions of the OTTI losses were also recognized in accumulated other comprehensive income at the time the credit impairments were determined and recognized:

| | Three Months Ended June 30, 2012 | | | |
|---|---|---|---|---|
| | Mortgage-Backed | | Corporate | |
| **(millions)** | **Residential** | **Commercial** | **Debt** | **Total** |
| Beginning balance at April 1, 2012 | $ 28.3 | $ .8 | $ 0 | $ 29.1 |
| Credit losses for which an OTTI was previously recognized | .2 | 0 | 0 | .2 |
| Credit losses for which an OTTI was not previously recognized | 0 | 0 | 0 | 0 |
| Reductions for securities sold/matured | 0 | 0 | 0 | 0 |
| Change in recoveries of future cash flows expected to be collected[1] | (.4) | (.1) | 0 | (.5) |
| Reductions for previously recognized credit impairments written-down to fair value[2] | 0 | 0 | 0 | 0 |
| Ending balance at June 30, 2012 | $ 28.1 | $ .7 | $ 0 | $ 28.8 |

| | Six Months Ended June 30, 2012 | | | |
|---|---|---|---|---|
| | Mortgage-Backed | | Corporate | |
| **(millions)** | **Residential** | **Commercial** | **Debt** | **Total** |
| Beginning balance at January 1, 2012 | $ 34.5 | $ 1.3 | $ 0 | $ 35.8 |
| Credit losses for which an OTTI was previously recognized | .1 | 0 | 0 | .1 |
| Credit losses for which an OTTI was not previously recognized | .2 | 0 | 0 | .2 |
| Reductions for securities sold/matured | 0 | (.2) | 0 | (.2) |
| Change in recoveries of future cash flows expected to be collected[1] | (2.7) | (.1) | 0 | (2.8) |
| Reductions for previously recognized credit impairments written-down to fair value[2] | (4.0) | (.3) | 0 | (4.3) |
| Ending balance at June 30, 2012 | $ 28.1 | $ .7 | $ 0 | $ 28.8 |

| | Three Months Ended June 30, 2011 | | | |
|---|---|---|---|---|
| | Mortgage-Backed | | Corporate | |
| **(millions)** | **Residential** | **Commercial** | **Debt** | **Total** |
| Beginning balance at April 1, 2011 | $ 34.5 | $ 1.0 | $ 6.5 | $ 42.0 |
| Credit losses for which an OTTI was previously recognized | 1.0 | .2 | 0 | 1.2 |
| Credit losses for which an OTTI was not previously recognized | 1.0 | 0 | 0 | 1.0 |
| Reductions for securities sold/matured | 0 | 0 | 0 | 0 |
| Change in recoveries of future cash flows expected to be collected[1] | (.3) | (.3) | 0 | (.6) |
| Reductions for previously recognized credit impairments written-down to fair value[2] | 0 | 0 | 0 | 0 |
| Ending balance at June 30, 2011 | $ 36.2 | $ .9 | $ 6.5 | $ 43.6 |

| | Six Months Ended June 30, 2011 | | | |
|---|---|---|---|---|
| | Mortgage-Backed | | Corporate | |
| **(millions)** | **Residential** | **Commercial** | **Debt** | **Total** |
| Beginning balance at January 1, 2011 | $ 32.3 | $ 1.0 | $ 6.5 | $ 39.8 |
| Credit losses for which an OTTI was previously recognized | 1.0 | 0 | 0 | 1.0 |
| Credit losses for which an OTTI was not previously recognized | 1.1 | .4 | 0 | 1.5 |
| Reductions for securities sold/matured | 0 | 0 | 0 | 0 |
| Change in recoveries of future cash flows expected to be collected[1] | 2.9 | (.1) | 0 | 2.8 |
| Reductions for previously recognized credit impairments written-down to fair value[2] | (1.1) | (.4) | 0 | (1.5) |

| | | | | |
|---|---|---|---|---|
| Ending balance at June 30, 2011 | $ 36.2 | $ .9 | $ 6.5 | $ 43.6 |

[1] Reflects expected recovery of prior period impairments that will be accreted into income over the remaining life of the security, net of any current quarter decreases in expected cash flows on previously recorded reductions.

[2] Reflects reductions of prior credit impairments where the current credit impairment requires writing securities down to fair value (i.e., no remaining non-credit loss).

Although we determined that it is more likely than not that we will not be required to sell the securities prior to the recovery of their respective cost bases (which could be maturity), we are required to measure the amount of credit losses on the securities that were determined to be other-than-temporarily impaired. In that process, we considered a number of factors and inputs related to the individual securities. The methodology and significant inputs used to measure the amount of credit losses in our portfolio included: current performance indicators on the underlying assets (e.g., delinquency rates, foreclosure rates, and default rates), credit support (via current levels of subordination), and historical credit ratings. Updated cash flow expectations were also generated by our portfolio managers based upon these performance indicators. In order to determine the amount of credit loss, if any, the net present value of the cash flows expected (i.e., expected recovery value) was calculated using the current book yield for each security, and was compared to its current amortized value. In the event that the net present value was below the amortized value, a credit loss was deemed to exist, and the security was written down.

***Trading Securities*** At June 30, 2012 and 2011, and December 31, 2011, we did not hold any trading securities and did not have any net realized gains (losses) on trading securities for the three and six months ended June 30, 2012 and 2011.

***Derivative Instruments*** We have invested in the following derivative exposures at various times: interest rate swaps, asset-backed credit default swaps, U.S. corporate debt credit default swaps, cash flow hedges, and equity options.

For all derivative positions discussed below, realized holding period gains and losses are netted with any upfront cash that may be exchanged under the contract to determine if the net position should be classified either as an asset or liability. To be reported as an asset and a component of the available-for-sale portfolio, the inception-to-date realized gain on the derivative position at period end would have to exceed any upfront cash received (net derivative asset). On the other hand, a net derivative liability would include any inception-to-date realized loss plus the amount of upfront cash received (or netted, if upfront cash was paid) and would be reported as a component of other liabilities. These net derivative assets/liabilities are not separately disclosed on the balance sheet due to their immaterial effect on our financial condition, cash flows, and results of operations.

The following table shows the status of our derivative instruments at June 30, 2012 and 2011, and December 31, 2011, and for the three and six months ended June 30, 2012 and 2011; amounts are on a pretax basis:

| **(millions)** | | | | | | **Balance Sheet** | | | **Comprehensive Income Statement** | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Notional Value[1]** | | | | | **Assets (Liabilities) Fair Value** | | | **Net Realized Gains (Losses) on Securities** | | | |
| | | | | | | | | | **Three months ended** | | **Six months ended** | |
| | **June 30,** | | **Dec. 31,** | | | **June 30,** | | **Dec. 31,** | **June 30,** | | **June 30,** | |
| **Derivatives designated as:** | **2012** | **2011** | **2011** | **Purpose** | **Classification** | **2012** | **2011** | **2011** | **2012** | **2011** | **2012** | **2011** |
| **<u>Hedging instruments</u>** | | | | | | | | | | | | |
| Closed: | | | | | | | | | | | | |
| Ineffective cash flow hedge | $ 30 | $ 0 | $ 15 | Manage interest rate risk | NA | $ 0 | $ 0 | $ 0 | $ .3 | $ 0 | $ .6 | $ 0 |
| **<u>Non-hedging instruments</u>** | | | | | | | | | | | | |
| <u>Assets:</u> | | | | | | | | | | | | |
| Corporate credit default swaps | 25 | 35 | 25 | Manage credit risk | Investments - fixed maturities | .7 | .9 | .7 | .1 | .5 | (.3) | (.2) |
| <u>Liabilities:</u> | | | | | | | | | | | | |
| Interest rate swaps | 1,263 | 1,013 | 1,263 | Manage portfolio duration | Other liabilities | (91.5) | (45.8) | (76.1) | (24.5) | (24.0) | (26.8) | (21.4) |
| <u>Closed:</u> | | | | | | | | | | | | |
| Interest rate swaps | 0 | 100 | 350 | Manage portfolio duration | NA | 0 | 0 | 0 | 0 | 0 | 0 | .5 |
| Total | NA | NA | NA | | | $ (90.8) | $ (44.9) | $ (75.4) | $ (24.1) | $ (23.5) | $ (26.5) | $ (21.1) |

NA= Not Applicable

[1] The amounts represent the value held at quarter and year end for open positions and the maximum amount held during the year for closed positions.

*CASH FLOW HEDGES*

During the second quarter and first six months of 2012, and the second half of 2011, we repurchased, in the open market, $17.8 million, $30.4 million, and $15.0 million, respectively, in aggregate principal amount of our 6.70% Fixed-to-Floating Rate Junior Subordinated Debentures due 2067 (the 6.70% Debentures ). For the portion of the 6.70% Debentures we repurchased, we reclassified $0.3 million, $0.6 million, and $0.3 million, in the respective periods, on a pretax basis, of the unrealized gain on forecasted transactions from accumulated other comprehensive income on the balance sheet to net realized gains on securities on the comprehensive income statement.

*INTEREST RATE SWAPS*

During the periods ended June 30, 2012 and 2011, and December 31, 2011, we invested in interest rate swap positions, primarily to manage the fixed-income portfolio duration. At June 30, 2012, we held a 9-year interest rate swap position (opened in 2009) and two 5-year interest rate swap positions (opened in 2011); in each case, we are paying a fixed rate and receiving a variable rate, effectively shortening the duration of our fixed-income portfolio. We closed a portion of the 9-year position during the first quarter 2011. The combined open positions have generated an aggregate realized loss, as interest rates have fallen since the inception of these positions. As of June 30, 2012 and 2011, and December 31, 2011, we delivered $101.3 million, $63.4 million, and $81.7 million, respectively, in cash collateral to the applicable counterparty on these positions.

*CORPORATE CREDIT DEFAULT SWAPS*

*Financial Services Sector* During the periods ended June 30, 2012 and 2011, and December 31, 2011, we held a position, which was opened during the third quarter 2008, on one corporate issuer within the financial services sector for which we bought credit default protection in the form of a credit default swap for a 5-year time horizon. We hold this protection to reduce some of our exposure to additional valuation declines on a preferred stock position of the same issuer. As of June 30, 2012 and December 31, 2011, we received $0.7 million in cash collateral from the counterparty on this position; we received $0.2 million in cash collateral as of June 30, 2011.

*Automotive Sector* We held no credit default swaps in this sector at June 30, 2012 or December 31, 2011. During the period ended June 30, 2011, we held a position, which was opened during 2010 and closed during the third quarter 2011, where we sold credit protection in the form of a corporate credit default swap on one issuer in the automotive sector for a 5-year time horizon. We would have been required to cover a $10 million notional value if a credit event had been triggered, including failure to pay or bankruptcy by the issuer. We acquired an equal par value amount of U.S. Treasury Notes with a similar maturity to cover the credit default swap s notional exposure. As of June 30, 2011, the credit worthiness of the issuer was favorable and we received $1.0 million in cash collateral from the counterparty on this position.

**Note 3** ***Fair Value*** We have categorized our financial instruments, based on the degree of subjectivity inherent in the method by which they are valued, into a fair value hierarchy of three levels, as follows:

*Level 1*: Inputs are unadjusted quoted prices in active markets for identical instruments at the measurement date (e.g., U.S. government obligations, active exchange-traded equity securities, and certain short-term securities).

*Level 2*: Inputs (other than quoted prices included within Level 1) that are observable for the instrument either directly or indirectly (e.g., certain corporate and municipal bonds and certain preferred stocks). This includes: (i) quoted prices for similar instruments in active markets, (ii) quoted prices for identical or similar instruments in markets that are not active, (iii) inputs other than quoted prices that are observable for the instruments, and (iv) inputs that are derived principally from or corroborated by observable market data by correlation or other means.

*Level 3*: Inputs that are unobservable. Unobservable inputs reflect our subjective evaluation about the assumptions market participants would use in pricing the financial instrument (e.g., certain structured securities and privately held investments).

Determining the fair value of the investment portfolio is the responsibility of management. As part of our responsibility, we evaluate whether a market is distressed or inactive in determining the fair value of our portfolio. We review certain market level inputs to evaluate whether sufficient activity, volume, and new issuances exist to create an active market. Based on this evaluation, we concluded that there was sufficient activity related to the sectors and securities for which we obtained valuations.

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The composition of the investment portfolio by major security type was:

| | Fair Value | | | | |
|---|---|---|---|---|---|
| **(millions)** | **Level 1** | **Level 2** | **Level 3** | **Total** | **Cost** |
| June 30, 2012 | | | | | |
| Fixed maturities: | | | | | |
| U.S. government obligations | $ 2,938.6 | $ 0 | $ 0 | $ 2,938.6 | $ 2,833.0 |
| State and local government obligations | 0 | 1,977.6 | 0 | 1,977.6 | 1,926.9 |
| Corporate debt securities | 0 | 3,007.2 | 0 | 3,007.2 | 2,893.6 |
| Subtotal | 2,938.6 | 4,984.8 | 0 | 7,923.4 | 7,653.5 |
| Asset-backed securities: | | | | | |
| Residential mortgage-backed | 0 | 367.1 | 54.5 | 421.6 | 429.2 |
| Commercial mortgage-backed | 0 | 2,070.3 | 23.2 | 2,093.5 | 2,020.2 |
| Other asset-backed | 0 | 1,262.9 | 1.1 | 1,264.0 | 1,250.8 |
| Subtotal asset-backed securities | 0 | 3,700.3 | 78.8 | 3,779.1 | 3,700.2 |
| Redeemable preferred stocks: | | | | | |
| Financials | 0 | 130.3 | 0 | 130.3 | 120.7 |
| Utilities | 0 | 64.9 | 0 | 64.9 | 65.9 |
| Industrials | 0 | 178.2 | 0 | 178.2 | 183.3 |
| Subtotal redeemable preferred stocks | 0 | 373.4 | 0 | 373.4 | 369.9 |
| Total fixed maturities | 2,938.6 | 9,058.5 | 78.8 | 12,075.9 | 11,723.6 |
| Equity securities: | | | | | |
| Nonredeemable preferred stocks: | | | | | |
| Financials | 259.8 | 498.4 | 0 | 758.2 | 394.0 |
| Utilities | 0 | 41.1 | 0 | 41.1 | 31.4 |
| Industrials | 0 | 0 | 0 | 0 | 0 |
| Subtotal nonredeemable preferred stocks | 259.8 | 539.5 | 0 | 799.3 | 425.4 |
| Common equities: | | | | | |
| Common stocks | 2,042.9 | 0 | 0 | 2,042.9 | 1,491.5 |
| Other equity-like investments | 0 | 0 | 12.2 | 12.2 | 3.4 |
| Subtotal common equities | 2,042.9 | 0 | 12.2 | 2,055.1 | 1,494.9 |
| Total fixed maturities and equity securities | 5,241.3 | 9,598.0 | 91.0 | 14,930.3 | 13,643.9 |
| Short-term investments: | | | | | |
| Other short-term investments | 1,330.3 | 348.9 | 0 | 1,679.2 | 1,679.2 |
| Total portfolio | $ 6,571.6 | $ 9,946.9 | $ 91.0 | $ 16,609.5 | $ 15,323.1 |
| Debt | $ 0 | $ 2,342.2 | $ 0 | $ 2,342.2 | $ 2,062.8 |

| (millions) | Fair Value Level 1 | Level 2 | Level 3 | Total | Cost |
|---|---|---|---|---|---|
| June 30, 2011 | | | | | |
| Fixed maturities: | | | | | |
| U.S. government obligations | $ 2,960.6 | $ 0 | $ 0 | $ 2,960.6 | $ 2,881.1 |
| State and local government obligations | 0 | 1,857.4 | 0 | 1,857.4 | 1,812.7 |
| Corporate debt securities | 0 | 2,825.6 | 29.8 | 2,855.4 | 2,765.1 |
| Subtotal | 2,960.6 | 4,683.0 | 29.8 | 7,673.4 | 7,458.9 |
| Asset-backed securities: | | | | | |
| Residential mortgage-backed | 0 | 448.4 | 71.5 | 519.9 | 537.0 |
| Commercial mortgage-backed | 0 | 1,785.9 | 26.5 | 1,812.4 | 1,755.6 |
| Other asset-backed | 0 | 1,323.2 | 4.5 | 1,327.7 | 1,312.4 |
| Subtotal asset-backed securities | 0 | 3,557.5 | 102.5 | 3,660.0 | 3,605.0 |
| Redeemable preferred stocks: | | | | | |
| Financials | 24.5 | 129.8 | 0 | 154.3 | 136.7 |
| Utilities | 0 | 71.9 | 0 | 71.9 | 70.6 |
| Industrials | 0 | 228.9 | 0 | 228.9 | 228.3 |
| Subtotal redeemable preferred stocks | 24.5 | 430.6 | 0 | 455.1 | 435.6 |
| Total fixed maturities | 2,985.1 | 8,671.1 | 132.3 | 11,788.5 | 11,499.5 |
| Equity securities: | | | | | |
| Nonredeemable preferred stocks: | | | | | |
| Financials | 430.8 | 541.9 | 0 | 972.7 | 451.8 |
| Utilities | 0 | 54.1 | 0 | 54.1 | 40.7 |
| Industrials | 0 | 2.9 | 0 | 2.9 | 3.0 |
| Subtotal nonredeemable preferred stocks | 430.8 | 598.9 | 0 | 1,029.7 | 495.5 |
| Common equities: | | | | | |
| Common stocks | 1,856.0 | 0 | 0 | 1,856.0 | 1,375.7 |
| Other equity-like investments | 0 | 0 | 11.9 | 11.9 | 4.1 |
| Subtotal common equities | 1,856.0 | 0 | 11.9 | 1,867.9 | 1,379.8 |
| Total fixed maturities and equity securities | $ 5,271.9 | $ 9,270.0 | $ 144.2 | 14,686.1 | 13,374.8 |
| Short-term investments: | | | | | |
| Other short-term investments[1] | | | | 1,343.5 | 1,343.5 |
| Total portfolio | | | | $ 16,029.6 | $ 14,718.3 |
| Debt[1] | | | | $ 2,129.9 | $ 1,959.1 |

| | Fair Value | | | | |
|---|---|---|---|---|---|
| **(millions)** | **Level 1** | **Level 2** | **Level 3** | **Total** | **Cost** |
| December 31, 2011 | | | | | |
| Fixed maturities: | | | | | |
| U.S. government obligations | $ 2,963.0 | $ 0 | $ 0 | $ 2,963.0 | $ 2,842.7 |
| State and local government obligations | 0 | 2,002.1 | 0 | 2,002.1 | 1,938.6 |
| Corporate debt securities | 0 | 2,896.2 | 0 | 2,896.2 | 2,801.5 |
| Subtotal | 2,963.0 | 4,898.3 | 0 | 7,861.3 | 7,582.8 |
| Asset-backed securities: | | | | | |
| Residential mortgage-backed | 0 | 364.6 | 62.3 | 426.9 | 452.9 |
| Commercial mortgage-backed | 0 | 1,855.3 | 21.3 | 1,876.6 | 1,829.8 |
| Other asset-backed | 0 | 1,218.0 | 2.6 | 1,220.6 | 1,210.9 |
| Subtotal asset-backed securities | 0 | 3,437.9 | 86.2 | 3,524.1 | 3,493.6 |
| Redeemable preferred stocks: | | | | | |
| Financials | 24.1 | 107.2 | 0 | 131.3 | 124.3 |
| Utilities | 0 | 68.1 | 0 | 68.1 | 70.8 |
| Industrials | 0 | 174.5 | 0 | 174.5 | 184.2 |
| Subtotal redeemable preferred stocks | 24.1 | 349.8 | 0 | 373.9 | 379.3 |
| Total fixed maturities | 2,987.1 | 8,686.0 | 86.2 | 11,759.3 | 11,455.7 |
| Equity securities: | | | | | |
| Nonredeemable preferred stocks: | | | | | |
| Financials | 227.9 | 525.4 | 0 | 753.3 | 433.7 |
| Utilities | 0 | 53.0 | 0 | 53.0 | 40.0 |
| Industrials | 0 | 0 | 0 | 0 | 0 |
| Subtotal nonredeemable preferred stocks | 227.9 | 578.4 | 0 | 806.3 | 473.7 |
| Common equities: | | | | | |
| Common stocks | 1,834.1 | 0 | 0 | 1,834.1 | 1,427.3 |
| Other equity-like investments | 0 | 0 | 11.5 | 11.5 | 3.7 |
| Subtotal common equities | 1,834.1 | 0 | 11.5 | 1,845.6 | 1,431.0 |
| Total fixed maturities and equity securities | $ 5,049.1 | $ 9,264.4 | $ 97.7 | 14,411.2 | 13,360.4 |
| Short-term investments: | | | | | |
| Other short-term investments[1] | | | | 1,551.8 | 1,551.8 |
| Total portfolio | | | | $ 15,963.0 | $ 14,912.2 |
| Debt[1] | | | | $ 2,664.7 | $ 2,442.1 |

[1] Under the prior accounting guidance, fair value hierarchies were not required.

Our portfolio valuations classified as either Level 1 or Level 2 in the above tables are priced exclusively by external sources, including: pricing vendors, dealers/market makers, and exchange-quoted prices. During the second quarter 2012, we had one redeemable preferred security with a value of $25.0 million that was transferred from Level 1 to Level 2 as it is no longer traded on an exchange. During the second quarter 2011, we had two nonredeemable preferred securities with an aggregate value of $74.9 million that were transferred from Level 1 to Level 2 due to inconsistent exchange-trading volume. At December 31, 2011, we had one nonredeemable preferred security with a value of $44.2 million that was transferred from Level 1 to Level 2 due to the lack of an exchange-quoted price at year-end. The exchange price was not available due to illiquidity in the market place. A consistent exchange-quoted price was previously available for this security, and we will continue to monitor the security for future exchange trading volume. We recognize transfers between levels at the end of the reporting period.

Our short-term security holdings classified as Level 1 are considered highly liquid, actively marketed, and have a very short duration, primarily seven days or less to redemption. These securities are held at their original cost, adjusted for any amortization of discount or premium, since that value very closely approximates what an active market participant would be willing to pay for such securities. The remainder of our short-term securities are classified as Level 2 and are not priced externally since these securities continually trade at par value. These securities are classified as Level 2 since they are primarily longer-dated auction securities issued by municipalities that contain a redemption put feature back to the auction pool with a redemption period of less than seven days. The auction pool is created by a liquidity provider and if the auction is not available at the end of the seven days, we are able to put the security back to the state of issuance at par.

At June 30, 2012 and 2011, vendor-quoted prices represented 56% of our Level 1 classifications (excluding short-term investments), compared to 59% at December 31, 2011. The securities quoted by vendors in Level 1 represent our holdings in U.S. Treasury Notes, which are frequently traded and the quotes are considered similar to exchange-traded quotes. The balance of our Level 1 pricing comes from quotes obtained directly from trades made on active exchanges.

At June 30, 2012, vendor-quoted prices comprised 97% of our Level 2 classifications (excluding short-term investments), while dealer-quoted prices represented 3%, compared to 98% and 2% and 96% and 4%, at June 30, 2011 and December 31, 2011, respectively. In our process for selecting a source (e.g., dealer, pricing service) to provide pricing for securities in our portfolio, we reviewed documentation from the sources that detailed the pricing techniques and methodologies used by these sources and determined if their policies adequately considered market activity, either based on specific transactions for the particular security type or based on modeling of securities with similar credit quality, duration, yield, and structure that were recently transacted. Once a source is chosen, we continue to monitor any changes or modifications to their processes by reviewing their documentation on internal controls for pricing and market reviews.

As part of our pricing procedures, we obtain quotes from more than one source to help us fully evaluate the market price of securities. However, our internal pricing policy is to use a consistent source for individual securities in order to maintain the integrity of our valuation process. Under our policy, when a review of the valuation received from our selected source appears outside what is considered market level activity (which is defined as trading at spreads or yields significantly different than comparable securities or outside the general sector level movement without a reasonable explanation), we may use an alternate source s price. To the extent we determine that it is prudent to substitute one source s price for another, we will contact the initial source to obtain an understanding of the factors that may be contributing to the significant price variance, which often leads the source to adjust their pricing input data for future pricing.

To allow us to determine if our initial source is providing a price that is outside of a reasonable range, we review our portfolio pricing on a weekly basis. We frequently challenge prices from our sources when a price provided does not match our expectations based on our evaluation of market trends/activity. Initially, we perform a global review of our portfolio by sector to identify securities whose prices appear outside of a reasonable range. We refine our review to analyze prices by specific criteria, such as whether the security is investment or non-investment-grade, prime or sub-prime, or a consumer product (e.g., auto, credit card). Through this review, we try to determine what contributed to the price variances among sources by analyzing spread movement, comparable security trades, if available, or industry or specific issuer fundamentals. We review quality control measures of our sources as they become available to determine if any significant changes have occurred from period to period that might indicate issues/concerns regarding their evaluation or market coverage. We also review data assumptions as supplied by our sources to determine if that data is relevant to current market conditions. In addition, we independently review each sector for transaction volumes, new issuances, and changes in spreads, as well as the overall movement of interest rates along the yield curve to determine if sufficient activity and liquidity exists to provide a credible source for our market valuations.

During each valuation period, we create internal estimations of portfolio valuation (performance returns), based on current market-related activity (i.e., interest rate and credit spread movements and other credit-related factors) within each major sector of our portfolio. We compare our internally generated portfolio results with those generated based on quotes we received externally and research material valuation differences. We compare our results to index returns for each major sector adjusting for duration and credit quality differences to better understand our portfolio s results. Additionally, we review on a monthly basis our external sales transactions and compare the actual final market sales price to a previous market valuation price. This review provides us further validation that our pricing sources are providing market level prices, since we are able to explain significant price changes (i.e., greater than 2%) as known events occur in the market place and affect a particular security s price at sale.

This analysis provides us additional comfort regarding the source s process, the quality of its review, and its willingness to improve its analysis based on feedback from clients. We believe this effort helps ensure that we are reporting the most representative fair values of our securities.

With limited exceptions, our Level 3 securities are also priced externally; however, due to several factors (e.g., nature of the securities, level of activity, and lack of similar securities trading to obtain observable market level inputs), these valuations are more subjective in nature. Certain private equity investments and fixed-income investments included in the Level 3 category are valued using external pricing supplemented by internal review and analysis.

After all the valuations are received and our review is complete, if the inputs used by vendors are determined to not contain sufficient observable market information, we will reclassify the affected security valuations to Level 3. At June 30, 2012 and 2011, and December 31, 2011, securities in our fixed-maturity portfolio listed as Level 3 were comprised substantially of securities that were either: (i) private placement deals, (ii) thinly held and/or traded securities, or (iii) non-investment-grade securities with little liquidity. Based on these factors, it was difficult to independently verify observable market inputs that were used to generate the external valuations we received. At June 30, 2012, we had one private common equity security with a value of $11.2 million that was priced internally. The same security had a value of $10.2 million at both June 30, 2011 and December 31, 2011. At June 30, 2012, we did not have any securities in our fixed-maturity portfolio that were priced internally. At June 30, 2011 and December 31, 2011, we had two fixed-maturity securities with aggregate values of $0.6 million and $0.5 million, respectively, that were priced internally. Despite the lack of sufficient observable market information, we believe the valuations received in conjunction with our procedures for evaluating third-party prices support the fair values as reported in the financial statements.

We review the prices from our external sources for reasonableness using internally developed assumptions to derive a price for the security, which is then compared to the price we received. Based on our review, all of the prices received from external sources remained unadjusted.

The following tables provide a summary of changes in fair value associated with Level 3 assets for the three and six months ended June 30, 2012 and 2011:

| | Level 3 Fair Value Three months ended June 30, 2012 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| (millions) | Fair Value at March 31, 2012 | Calls/ Maturities/ Paydowns | Purchases | Sales | Net Realized (gain)/loss | Change in Valuation | Net Transfers in (out) | Fair value at June 30, 2012 |
| Fixed maturities: | | | | | | | | |
| Asset-backed securities: | | | | | | | | |
| Residential mortgage-backed | $ 58.7 | $ (4.1) | $ 0 | $ 0 | $ 0 | $ (.1) | $ 0 | $ 54.5 |
| Commercial mortgage-backed | 22.8 | (.1) | 0 | 0 | 0 | .5 | 0 | 23.2 |
| Other asset-backed | 1.8 | (.7) | 0 | 0 | 0 | 0 | 0 | 1.1 |
| Total asset-backed securities | 83.3 | (4.9) | 0 | 0 | 0 | .4 | 0 | 78.8 |
| Corporate debt securities | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Total fixed maturities | 83.3 | (4.9) | 0 | 0 | 0 | .4 | 0 | 78.8 |
| Equity securities: | | | | | | | | |
| Common equities: | | | | | | | | |
| Other equity-like investments | 11.1 | 0 | 0 | 0 | 0 | 1.1 | 0 | 12.2 |
| Total Level 3 securities | $ 94.4 | $ (4.9) | $ 0 | $ 0 | $ 0 | $ 1.5 | $ 0 | $ 91.0 |

| | Level 3 Fair Value Six months ended June 30, 2012 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| (millions) | Fair Value at Dec. 31, 2011 | Calls/ Maturities/ Paydowns | Purchases | Sales | Net Realized (gain)/loss | Change in Valuation | Net Transfers in (out) | Fair value at June 30, 2012 |
| Fixed maturities: | | | | | | | | |
| Asset-backed securities: | | | | | | | | |
| Residential mortgage-backed | $ 62.3 | $ (7.8) | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 54.5 |
| Commercial mortgage-backed | 21.3 | (.1) | 0 | 0 | 0 | 2.0 | 0 | 23.2 |
| Other asset-backed | 2.6 | (1.5) | 0 | 0 | 0 | 0 | 0 | 1.1 |
| Total asset-backed securities | 86.2 | (9.4) | 0 | 0 | 0 | 2.0 | 0 | 78.8 |
| Corporate debt securities | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Total fixed maturities | 86.2 | (9.4) | 0 | 0 | 0 | 2.0 | 0 | 78.8 |
| Equity securities: | | | | | | | | |
| Common equities: | | | | | | | | |
| Other equity-like investments | 11.5 | 0 | 0 | 0 | 0 | .7 | 0 | 12.2 |
| Total Level 3 securities | $ 97.7 | $ (9.4) | $ 0 | $ 0 | $ 0 | $ 2.7 | $ 0 | $ 91.0 |

| (millions) | Fair Value at March 31, 2011 | Calls/ Maturities/ Paydowns | Purchases | Sales | Net Realized (gain)/loss | Change in Valuation | Net Transfers in (out) | Fair value at June 30, 2011 |
|---|---|---|---|---|---|---|---|---|
| | Level 3 Fair Value Three months ended June 30, 2011 | | | | | | | |
| Fixed maturities: | | | | | | | | |
| Asset-backed securities: | | | | | | | | |
| Residential mortgage-backed | $ 76.3 | $ (4.8) | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 71.5 |
| Commercial mortgage-backed | 27.1 | (.1) | 0 | 0 | 0 | (.5) | 0 | 26.5 |
| Other asset-backed | 5.1 | (.5) | 0 | 0 | 0 | (.1) | 0 | 4.5 |
| Total asset-backed securities | 108.5 | (5.4) | 0 | 0 | 0 | (.6) | 0 | 102.5 |
| Corporate debt securities | 29.6 | 0 | 0 | 0 | 0 | .2 | 0 | 29.8 |
| Total fixed maturities | 138.1 | (5.4) | 0 | 0 | 0 | (.4) | 0 | 132.3 |
| Equity securities: | | | | | | | | |
| Common equities: | | | | | | | | |
| Other equity-like investments | 11.8 | 0 | 0 | 0 | 0 | .1 | 0 | 11.9 |
| Total Level 3 securities | $ 149.9 | $ (5.4) | $ 0 | $ 0 | $ 0 | $ (.3) | $ 0 | $ 144.2 |

| (millions) | Fair Value at Dec. 31, 2010 | Calls/ Maturities/ Paydowns | Purchases | Sales | Net Realized (gain)/loss | Change in Valuation | Net Transfers in (out)[1] | Fair value at June 30, 2011 |
|---|---|---|---|---|---|---|---|---|
| | Level 3 Fair Value Six months ended June 30, 2011 | | | | | | | |
| Fixed maturities: | | | | | | | | |
| Asset-backed securities: | | | | | | | | |
| Residential mortgage-backed | $ 96.7 | $ (9.8) | $ 0 | $ 0 | $ 0 | $ 0 | $ (15.4) | $ 71.5 |
| Commercial mortgage-backed | 27.5 | (.1) | 0 | 0 | 0 | (.9) | 0 | 26.5 |
| Other asset-backed | 5.0 | (.9) | 0 | 0 | 0 | .4 | 0 | 4.5 |
| Total asset-backed securities | 129.2 | (10.8) | 0 | 0 | 0 | (.5) | (15.4) | 102.5 |
| Corporate debt securities | 29.5 | 0 | 0 | 0 | 0 | .3 | 0 | 29.8 |
| Total fixed maturities | 158.7 | (10.8) | 0 | 0 | 0 | (.2) | (15.4) | 132.3 |
| Equity securities: | | | | | | | | |
| Common equities: | | | | | | | | |
| Other equity-like investments | 11.8 | 0 | 0 | 0 | 0 | .1 | 0 | 11.9 |
| Total Level 3 securities | $ 170.5 | $ (10.8) | $ 0 | $ 0 | $ 0 | $ (.1) | $ (15.4) | $ 144.2 |

1 The $(15.4) million was transferred out of Level 3 into Level 2 due to the availability of vendor pricing on a residential mortgage-backed security.

The following table provides a summary of the quantitative information about Level 3 fair value measurements for our applicable securities at June 30, 2012:

| | | Quantitative Information about Level 3 Fair Value Measurements | | |
|---|---|---|---|---|
| (millions) | Fair Value at June 30, 2012 | Valuation Technique | Unobservable Input | Unobservable Input Assumption |
| Fixed maturities: | | | | |
| Asset-backed securities: | | | | |
| Residential mortgage-backed | $ .2 | External vendor | Prepayment rate[1] | 16 |
| Total fixed maturities | .2 | | | |
| Equity securities: | | | | |
| Common equities: | | | | |
| Other equity-like investments | 11.2 | Discounted consolidated equity | Discount for lack of marketability | 20% |
| Total | $ 11.4 | | | |

1 The 16 constant prepayment rate (CPR) assumes that 16% of the principal amount of the underlying loans will be paid off prematurely in each year.

The residential mortgage-backed security in the table above was previously priced internally; however, as of June 30, 2012, we began using an external vendor to price the security. The unobservable input assumption above was obtained from the vendor and the price we received at June 30, 2012 was consistent with our expectations. The quantitative table does not include securities whose Level 3 fair values are obtained from non-binding external sources where unobservable inputs are not reasonably available to us. Due to the relative size of the securities fair values compared to the total portfolio s fair value, any changes in pricing methodology would not have a significant change in valuation that would materially impact other comprehensive income.

**Note 4 *Debt*** Debt consisted of:

| | June 30, 2012 | | June 30, 2011 | | December 31, 2011 | |
|---|---|---|---|---|---|---|
| (millions) | Carrying Value | Fair Value | Carrying Value | Fair Value | Carrying Value | Fair Value |
| 6.375% Senior Notes due 2012 | $ 0 | $ 0 | $ 349.8 | $ 360.9 | $ 350.0 | $ 350.5 |
| 7% Notes due 2013 | 149.8 | 160.7 | 149.7 | 167.6 | 149.7 | 162.4 |
| 3.75% Senior Notes due 2021 | 497.2 | 540.1 | 0 | 0 | 497.0 | 525.3 |
| 6 5/8% Senior Notes due 2029 | 295.1 | 378.3 | 294.9 | 349.1 | 295.0 | 364.4 |
| 6.25% Senior Notes due 2032 | 394.4 | 502.2 | 394.3 | 444.1 | 394.4 | 492.4 |
| 6.70% Fixed-to-Floating Rate Junior Subordinated Debentures due 2067 | 726.3 | 760.9 | 770.4 | 808.2 | 756.0 | 769.7 |
| Total | $ 2,062.8 | $ 2,342.2 | $ 1,959.1 | $ 2,129.9 | $ 2,442.1 | $ 2,664.7 |