

PROGRESSIVE CORP/OH/
Form 10-Q
August 10, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2009

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)

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Ohio
(State or other jurisdiction of
incorporation or organization)

34-0963169
(I.R.S. Employer
Identification No.)

6300 Wilson Mills Road, Mayfield Village, Ohio
(Address of principal executive offices)

44143
(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 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 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

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

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: 678,600,888 outstanding at July 31, 2009

PART I - FINANCIAL INFORMATION**Item 1. Financial Statements.**

The Progressive Corporation and Subsidiaries

Consolidated Statements of Income

(unaudited)

Periods Ended June 30, (millions - except per share amounts)	Three Months			Six Months		
	2009	2008	% Change	2009	2008	% Change
Revenues						
Net premiums earned	\$ 3,441.4	\$ 3,411.2	1	\$ 6,848.0	\$ 6,801.2	1
Investment income	122.1	165.8	(26)	253.6	325.1	(22)
Net realized gains (losses) on securities:						
Other-than-temporary impairment (OTI) losses:						
Total OTI losses	(53.8)			(53.8)		
Less: portion of OTI losses recognized in other comprehensive income	23.8			23.8		
Net impairment losses recognized in earnings	(30.0)			(30.0)		
Net realized gains (losses) on securities	45.9	(44.6)		(27.5)	(12.4)	
Total net realized gains (losses) on securities	15.9	(44.6)	NM	(57.5)	(12.4)	364
Service revenues	4.1	4.2	(2)	7.6	8.6	(12)
Total revenues	3,583.5	3,536.6	1	7,051.7	7,122.5	(1)
Expenses						
Losses and loss adjustment expenses	2,462.6	2,471.3		4,799.6	4,955.3	(3)
Policy acquisition costs	334.1	340.7	(2)	670.3	680.2	(1)
Other underwriting expenses	390.9	379.5	3	768.3	763.8	1
Investment expenses	2.6	2.9	(10)	5.2	4.4	18
Service expenses	4.7	5.4	(13)	9.3	10.5	(11)
Interest expense	34.7	34.3	1	68.4	68.6	
Total expenses	3,229.6	3,234.1		6,321.1	6,482.8	(2)
Net Income						
Income before income taxes	353.9	302.5	17	730.6	639.7	14
Provision for income taxes	103.8	87.0	19	248.0	184.8	34
Net income	\$ 250.1	\$ 215.5	16	\$ 482.6	\$ 454.9	6
Computation of Earnings Per Share						
Basic:						
Average shares outstanding	669.2	667.4		668.9	669.5	
Per share	\$.37	\$.32	16	\$.72	\$.68	6

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Diluted:						
Average shares outstanding	669.2	667.4		668.9	669.5	
Net effect of dilutive stock-based compensation	5.4	6.3	(14)	4.4	6.0	(27)
Total equivalent shares	674.6	673.7		673.3	675.5	
Per share	\$.37	\$.32	16	\$.72	\$.67	6
Dividends declared per share¹	\$	\$		\$	\$	

NM = Not Meaningful

¹ Progressive maintains an annual dividend program. See *Note 9 - Dividends* for further discussion. See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries

Consolidated Balance Sheets

(unaudited)

(millions)	June 30, 2009	2008	December 31, 2008
Assets			
Investments - Available-for-sale, at fair value:			
Fixed maturities (amortized cost: \$11,453.9, \$9,406.2, and \$10,295.3)	\$ 10,935.3	\$ 9,212.9	\$ 9,946.7
Equity securities:			
Nonredeemable preferred stocks (cost: \$810.4, \$2,741.8, and \$1,131.3)	1,130.1	2,210.5	1,150.0
Common equities (cost: \$292.4, \$1,310.8, and \$553.6)	408.7	2,039.4	727.8
Short-term investments (amortized cost: \$1,137.2, \$513.2, and \$1,153.6)	1,137.2	513.2	1,153.6
Total investments	13,611.3	13,976.0	12,978.1
Cash	160.7	9.9	2.9
Accrued investment income	113.7	123.1	125.7
Premiums receivable, net of allowance for doubtful accounts of \$103.5, \$99.0, and \$113.7	2,545.0	2,515.5	2,408.6
Reinsurance recoverables, including \$40.9, \$42.5, and \$44.0 on paid losses	288.7	308.6	288.5
Prepaid reinsurance premiums	62.6	63.1	62.4
Deferred acquisition costs	436.3	446.2	414.0
Income taxes	727.6	291.2	821.6
Property and equipment, net of accumulated depreciation of \$591.4, \$636.0, and \$653.6	989.9	1,002.7	997.1
Other assets	151.8	178.1	151.6
Total assets	\$ 19,087.6	\$ 18,914.4	\$ 18,250.5
Liabilities and Shareholders' Equity			
Unearned premiums	\$ 4,379.6	\$ 4,403.6	\$ 4,175.9
Loss and loss adjustment expense reserves	6,198.9	6,000.6	6,177.4
Accounts payable, accrued expenses, and other liabilities	1,407.7	1,530.0	1,506.4
Debt ¹	2,176.4	2,174.7	2,175.5
Total liabilities	14,162.6	14,108.9	14,035.2
Common Shares, \$1.00 par value (authorized 900.0; issued 797.8, 797.9, and 797.9, including treasury shares of 117.8, 122.5, and 121.4)			
	680.0	675.4	676.5
Paid-in capital	914.2	863.6	892.9
Accumulated other comprehensive income (loss):			
Net unrealized gains (losses) on securities	(30.9)	15.4	(76.8)
Portion of OTI losses recognized in other comprehensive income	(15.5)		
Total net unrealized gains (losses) on securities	(46.4)	15.4	(76.8)
Net unrealized gains on forecasted transactions	23.9	26.3	24.9
Retained earnings	3,353.3	3,224.8	2,697.8
Total shareholders' equity	4,925.0	4,805.5	4,215.3
Total liabilities and shareholders' equity	\$ 19,087.6	\$ 18,914.4	\$ 18,250.5

¹ Consists of long-term debt. See *Note 4 - Debt*.
See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries

Consolidated Statements of Changes in Shareholders' Equity

(unaudited)

Six months ended June 30, (millions)	2009		2008	
Retained Earnings				
Balance, Beginning of year	\$ 2,697.8		\$ 2,927.7	
Cumulative effect of change in accounting principle ¹	189.6			
Balance, Beginning of year, as adjusted	2,887.4		2,927.7	
Net income	482.6	\$ 482.6	454.9	\$ 454.9
Treasury shares purchased	(16.9)		(155.6)	
Other, net ²	.2		(2.2)	
Balance, End of period	\$ 3,353.3		\$ 3,224.8	
Accumulated Other Comprehensive Income (Loss), Net of Tax				
Balance, Beginning of year	\$ (51.9)		\$ 492.8	
Cumulative effect of change in accounting principle ¹	(189.6)			
Balance, Beginning of year, as adjusted	(241.5)		492.8	
Changes in:				
Net unrealized gains (losses) on securities		235.5		(449.6)
Portion of OTI losses recognized in other comprehensive income (loss)		(15.5)		
Total net unrealized gains (losses) on securities		220.0		(449.6)
Net unrealized gains on forecasted transactions		(1.0)		(1.5)
Other comprehensive income (loss)	219.0	219.0	(451.1)	(451.1)
Balance, End of period	\$ (22.5)		\$ 41.7	
Comprehensive Income		\$ 701.6		\$ 3.8
Common Shares, \$1.00 Par Value				
Balance, Beginning of year	\$ 676.5		\$ 680.2	
Stock options exercised	1.2		2.3	
Treasury shares purchased	(1.3)		(9.8)	
Restricted stock issued, net of forfeitures	3.6		2.7	
Balance, End of period	\$ 680.0		\$ 675.4	
Paid-In Capital				
Balance, Beginning of year	\$ 892.9		\$ 834.8	
Stock options exercised	6.2		16.5	
Tax benefits from exercise/vesting of stock-based compensation	.2		8.0	
Treasury shares purchased	(1.8)		(12.1)	
Restricted stock issued, net of forfeitures	(3.6)		(2.7)	
Amortization of stock-based compensation	19.0		15.7	

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Other ²	1.3	3.4
Balance, End of period	\$ 914.2	\$ 863.6
Total Shareholders Equity	\$ 4,925.0	\$ 4,805.5

¹ Pursuant to FASB Staff Position (FSP) FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments. See *Note 11 - New Accounting Standards* for further discussion.

² Primarily reflects activity associated with our deferred compensation and incentive plans. There are 20.0 million Serial Preferred Shares authorized; no such shares are issued or outstanding.

There are 5.0 million Voting Preference Shares authorized; no such shares have been issued.

See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries

Consolidated Statements of Cash Flows

(unaudited)

Six months ended June 30, (millions)	2009	2008
Cash Flows From Operating Activities		
Net income	\$ 482.6	\$ 454.9
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	43.2	48.0
Amortization of fixed-income securities	118.3	126.2
Amortization of stock-based compensation	19.3	16.0
Net realized (gains) losses on securities	57.5	12.4
Net loss on disposition of property and equipment	1.5	1.0
Changes in:		
Premiums receivable	(136.4)	(120.4)
Reinsurance recoverables	(.2)	26.5
Prepaid reinsurance premiums	(.2)	6.7
Deferred acquisition costs	(22.3)	(19.9)
Income taxes	(24.6)	56.9
Unearned premiums	203.7	193.2
Loss and loss adjustment expense reserves	21.5	57.9
Accounts payable, accrued expenses, and other liabilities	146.4	41.7
Other, net	17.8	38.6
Net cash provided by operating activities	928.1	939.7
Cash Flows From Investing Activities		
Purchases:		
Fixed maturities	(6,119.8)	(2,663.5)
Equity securities	(25.8)	(546.6)
Short-term investments - auction rate securities		(479.5)
Sales:		
Fixed maturities	4,850.5	2,188.7
Equity securities	456.3	278.6
Short-term investments - auction rate securities		479.5
Maturities, paydowns, calls, and other:		
Fixed maturities	361.1	227.9
Equity securities		34.9
Net sales (purchases) of short-term investments - other	16.3	(130.5)
Net unsettled security transactions	(259.0)	(24.8)
Purchases of property and equipment	(38.3)	(51.3)
Sales of property and equipment	.8	
Net cash used in investing activities	(757.9)	(686.6)
Cash Flows From Financing Activities		
Proceeds from exercise of stock options	7.4	18.8
Tax benefit from exercise/vesting of stock-based compensation	.2	8.0
Dividends paid to shareholders ¹		(98.3)
Acquisition of treasury shares	(20.0)	(177.5)
Net cash used in financing activities	(12.4)	(249.0)

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Increase in cash	157.8	4.1
Cash, January 1	2.9	5.8
Cash, June 30	\$ 160.7	\$ 9.9

¹ Progressive maintains an annual dividend program. See *Note 9 - 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 These 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, 2008.

The consolidated financial statements reflect all normal recurring adjustments which, 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, 2009, are not necessarily indicative of the results expected for the full year.

Subsequent events have been evaluated through August 10, 2009, the date the financial statements were issued via filing this Quarterly Report on Form 10-Q with the Securities and Exchange Commission.

Note 2 Investments During the second quarter 2009, we adopted the new accounting guidance relating to the recognition and presentation of other-than-temporary impairments (see *Note 11- New Accounting Standards* for further information).

The following table presents 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, 2009						
Fixed maturities:						
U.S. government obligations	\$ 5,362.6	\$ 9.3	\$ (144.6)	\$	\$ 5,227.3	38.4 %
State and local government obligations	2,383.7	56.1	(36.8)		2,403.0	17.7
Corporate debt securities	803.4	19.1	(25.8)		796.7	5.8
Residential mortgage-backed securities	561.7	.7	(121.8)		440.6	3.2
Commercial mortgage-backed securities	1,491.7	5.9	(111.6)		1,386.0	10.2
Other asset-backed securities	200.5	3.3	(3.0)		200.8	1.5
Redeemable preferred stocks	648.2	9.0	(179.3)		477.9	3.5
Other debt obligations	2.1	.9			3.0	
Total fixed maturities	11,453.9	104.3	(622.9)		10,935.3	80.3
Equity securities:						
Nonredeemable preferred stocks	810.4	334.2	(3.3)	(11.2)	1,130.1	8.3
Common equities	292.4	123.7	(7.4)		408.7	3.0
Short-term investments:						
Other short-term investments	1,137.2				1,137.2	8.4
Total portfolio^{2,3}	\$ 13,693.9	\$ 562.2	\$ (633.6)	\$ (11.2)	\$ 13,611.3	100.0 %

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(\$ in millions)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Net Realized Gains (Losses) ¹	Fair Value	% of Total Fair Value
June 30, 2008						
Fixed maturities:						
U.S. government obligations ⁴	\$ 1,636.9	\$ 9.0	\$ (5.6)	\$	\$ 1,640.3	11.7 %
State and local government obligations	3,178.4	23.3	(38.8)		3,162.9	22.7
Foreign government obligations	30.0	.4			30.4	.2
Corporate debt securities	969.0	2.2	(28.9)		942.3	6.7
Residential mortgage-backed securities	853.9	3.8	(34.9)		822.8	5.9
Commercial mortgage-backed securities	1,856.2	12.5	(42.1)		1,826.6	13.1
Other asset-backed securities	167.1	.8	(2.0)		165.9	1.2
Redeemable preferred stocks	712.6	1.8	(95.7)		618.7	4.4
Other debt obligations	2.1	.9			3.0	
Total fixed maturities	9,406.2	54.7	(248.0)		9,212.9	65.9
Equity securities:						
Nonredeemable preferred stocks	2,741.8	3.4	(515.0)	(19.7)	2,210.5	15.8
Common equities	1,310.8	770.0	(41.4)		2,039.4	14.6
Short-term investments:						
Other short-term investments	513.2				513.2	3.7
Total portfolio^{2,3}	\$ 13,972.0	\$ 828.1	\$ (804.4)	\$ (19.7)	\$ 13,976.0	100.0 %

(\$ in millions)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Net Realized Gains (Losses) ¹	Fair Value	% of Total Fair Value
December 31, 2008						
Fixed maturities:						
U.S. government obligations	\$ 3,565.7	\$ 129.0	\$ (1.1)	\$	\$ 3,693.6	28.5 %
State and local government obligations	3,041.4	53.1	(90.1)		3,004.4	23.1
Foreign government obligations	16.2	.2			16.4	.1
Corporate debt securities	692.1	1.6	(54.4)		639.3	4.9
Residential mortgage-backed securities	758.7	1.4	(137.1)		623.0	4.8
Commercial mortgage-backed securities	1,692.7	1.0	(243.7)		1,450.0	11.2
Other asset-backed securities	139.2		(10.1)		129.1	1.0
Redeemable preferred stocks	387.2	8.7	(8.0)		387.9	3.0
Other debt obligations	2.1	.9			3.0	
Total fixed maturities	10,295.3	195.9	(544.5)		9,946.7	76.6
Equity securities:						
Nonredeemable preferred stocks	1,131.3	73.5	(17.3)	(37.5)	1,150.0	8.9
Common equities	553.6	203.5	(29.3)		727.8	5.6
Short-term investments:						
Other short-term investments	1,153.6				1,153.6	8.9
Total portfolio^{2,3}	\$ 13,133.8	\$ 472.9	\$ (591.1)	\$ (37.5)	\$ 12,978.1	100.0 %

¹ Represents net holding period gains (losses) on certain hybrid securities (discussed below) and on common equity options (see the *Derivative Instruments* section below for further discussion).

² June 30, 2009 total excludes \$4.8 million of unsettled security transactions offset in other assets. At June 30, 2008 and December 31, 2008, we had \$52.2 million and \$254.2 million, respectively, of unsettled security transactions offset in other liabilities.

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June 30, 2009, June 30, 2008, and December 31, 2008 totals include \$.9 billion, \$1.7 billion, and \$1.0 billion, respectively, of securities in the portfolio of a consolidated, non-insurance subsidiary of the holding company, net of any unsettled security transactions.

⁴ Balance at June 30, 2008 includes \$49.6 million of collateral in the form of Treasury Notes delivered to a counterparty on a derivative position; the position was closed in the fourth quarter 2008. See the *Derivative Instruments* section below for further discussion.

Our fixed-maturity securities include debt securities and redeemable preferred stocks. At June 30, 2009, June 30, 2008, and December 31, 2008, the nonredeemable preferred stock portfolio included \$17.3 million, \$116.8 million, and \$53.0 million, respectively, of hybrid securities (i.e., 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). Common equities include common stocks and other risk investments (i.e., private equity investments and limited partnership interests in private equity and mezzanine funds). Our other short-term investments include Eurodollar deposits, commercial paper, and other investments which are expected to mature within one year.

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 change in fair value of the hybrid securities and derivative instruments is recorded as a component of net realized gains (losses) on securities.

Other-than-Temporary Impairment (OTI) In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-than-Temporary Impairments. The new accounting position provides guidance in determining whether impairments in debt securities are other-than-temporary and requires additional disclosures relating to OTI and unrealized losses on investments; the new standard did not change the impairment model for equity securities. Pursuant to the new standard, we analyze our debt securities to determine if we intend to sell, or if it is more likely than not that we will be required to sell, the security prior to recovery and, if so, we will write down the security to its current fair value with the entire amount of the write-down recorded to earnings. To the extent that it is more likely than not that we will hold the debt security until recovery (which could be maturity), we need to determine if any of the decline in value is due to a credit loss (i.e., where the present value of cash flows expected to be collected is lower than the amortized cost basis of the security) and, if so, we will recognize that portion of the impairment in earnings, with the balance (i.e., non-credit related impairment) recognized as part of our net unrealized gains (losses) in other comprehensive income.

In addition, the new guidance requires that, during the initial period of adoption, we record a cumulative effect of change in accounting principle to reclassify the non-credit component of a previously recognized OTI from retained earnings to other comprehensive income. Based on our review of OTI losses on securities held at March 31, 2009, we reclassified \$189.6 million (or \$291.8 million on a pretax basis) from retained earnings to accumulated other comprehensive income (loss).

Under the new accounting guidance, we are required to separate our OTI losses between those related to a credit loss and the portion that was a non-credit related impairment. The following table shows our OTI losses for the second quarter 2009 under this guidance:

(millions)	Total OTI	Credit Related and Other OTI (Income Statement)	Non-Credit Related (Balance Sheet)
Fixed maturities:			
Residential mortgage-backed securities:			
Bifurcated	\$ 38.3	\$ 14.5	\$ 23.8
Non-bifurcated ¹	14.2	14.2	
Total fixed maturities	52.5	28.7	23.8
Common stocks	1.3	1.3	NA
Total	\$ 53.8	\$ 30.0	\$ 23.8

NA = Not Applicable

¹ Represents securities where our total OTI was credit related; no unrealized losses are recorded as a component of accumulated other comprehensive income.

The following table provides a rollforward of the amounts related to credit losses recognized in earnings for which a portion of the OTI loss was recognized in accumulated other comprehensive income:

(millions)	Corporate Debt	Residential Mortgage- Backed	Total
Beginning balance at April 1, 2009 ¹	\$ 6.5	\$ 24.2	\$ 30.7
Credit losses for which an OTI was previously recognized ²		1.4	1.4
Credit losses for which an OTI was not previously recognized ²		13.1	13.1
Ending balance at June 30, 2009	\$ 6.5	\$ 38.7	\$ 45.2

¹ Represents the credit loss taken on securities held and in an unrealized loss position as of the date the new accounting guidance was adopted.

² Amounts reflect credit losses taken during the period on securities held and in an unrealized loss position at June 30, 2009.

At June 30, 2009, we did not intend to sell the fixed maturity securities on which a credit loss was recognized, and determined that it is more likely than not that we will not be required to sell the securities prior to the recovery (which could be maturity) of their respective cost bases.

In order to measure the amount of credit losses on the securities that were determined to be other-than-temporarily impaired during the second quarter 2009, we considered a number of factors and inputs related to the individual securities. During the second quarter 2009, all of the securities that comprise the \$28.7 million in credit losses were within the residential mortgage-backed portfolio. The methodology and significant inputs used to measure the amount of credit losses in this portfolio included: current performance indicators on the underlying assets (i.e., 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 losses, if any, the net present value of the cash flows expected (i.e., expected recovery value) was calculated using the current implied 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 to its net present value level.

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Gross Unrealized Losses As of June 30, 2009, we had \$626.2 million of gross unrealized losses in our fixed-income securities (i.e., fixed-maturity securities and nonredeemable preferred stocks) and \$7.4 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 for the period of time necessary to recover their new cost basis. In addition, we may retain the common stocks to maintain correlation to the Russell 1000 Index as long as the portfolio and index correlation remain similar. 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 by the length of time that individual securities have been in a continuous unrealized loss position:

(millions)	Total		Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses ¹
June 30, 2009						
Fixed maturities:						
U.S. government obligations	\$ 4,683.3	\$ (144.6)	\$ 4,683.3	\$ (144.6)	\$	\$
State and local government obligations	838.1	(36.8)	58.1	(.8)	780.0	(36.0)
Corporate debt securities	369.5	(25.8)	93.8	(3.1)	275.7	(22.7)
Residential mortgage-backed securities	404.6	(121.8)	8.5	(.3)	396.1	(121.5)
Commercial mortgage-backed securities	1,034.6	(111.6)	65.1	(3.7)	969.5	(107.9)
Other asset-backed securities	68.7	(3.0)	57.0	(.1)	11.7	(2.9)
Redeemable preferred stocks	447.0	(179.3)	39.8	(5.1)	407.2	(174.2)
Total fixed maturities	7,845.8	(622.9)	5,005.6	(157.7)	2,840.2	(465.2)
Equity securities:						
Nonredeemable preferred stocks	112.2	(3.3)			112.2	(3.3)
Common equities	61.1	(7.4)	49.0	(5.6)	12.1	(1.8)
Total equity securities	173.3	(10.7)	49.0	(5.6)	124.3	(5.1)
Total portfolio	\$ 8,019.1	\$ (633.6)	\$ 5,054.6	\$ (163.3)	\$ 2,964.5	\$ (470.3)

(millions)	Total		Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2008						
Fixed maturities:						
U.S. government obligations	\$ 997.4	\$ (5.6)	\$ 997.4	\$ (5.6)	\$	\$
State and local government obligations	1,511.5	(38.8)	1,209.2	(30.9)	302.3	(7.9)
Corporate debt securities	672.0	(28.9)	438.1	(10.7)	233.9	(18.2)
Residential mortgage-backed securities	675.5	(34.9)	541.3	(30.5)	134.2	(4.4)
Commercial mortgage-backed securities	1,275.5	(42.1)	886.3	(23.2)	389.2	(18.9)
Other asset-backed securities	32.5	(2.0)	3.9	(.1)	28.6	(1.9)
Redeemable preferred stocks	550.0	(95.7)	195.7	(7.1)	354.3	(88.6)
Total fixed maturities	5,714.4	(248.0)	4,271.9	(108.1)	1,442.5	(139.9)
Equity securities:						
Nonredeemable preferred stocks	1,993.3	(515.0)	948.4	(161.5)	1,044.9	(353.5)
Common equities	287.8	(41.4)	285.3	(41.3)	2.5	(.1)
Total equity securities	2,281.1	(556.4)	1,233.7	(202.8)	1,047.4	(353.6)
Total portfolio	\$ 7,995.5	\$ (804.4)	\$ 5,505.6	\$ (310.9)	\$ 2,489.9	\$ (493.5)

(millions)	Total		Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2008						
Fixed maturities:						
U.S. government obligations	\$ 232.5	\$ (1.1)	\$ 232.5	\$ (1.1)	\$	\$
State and local government obligations	1,100.6	(90.1)	274.8	(17.9)	825.8	(72.2)
Corporate debt securities	493.1	(54.4)	278.3	(27.4)	214.8	(27.0)
Residential mortgage-backed securities	592.8	(137.1)	219.1	(41.4)	373.7	(95.7)
Commercial mortgage-backed securities	1,422.1	(243.7)	842.9	(116.7)	579.2	(127.0)
Other asset-backed securities	128.8	(10.1)	117.7	(7.4)	11.1	(2.7)
Redeemable preferred stocks	60.6	(8.0)	60.6	(8.0)		
Total fixed maturities	4,030.5	(544.5)	2,025.9	(219.9)	2,004.6	(324.6)
Equity securities:						
Nonredeemable preferred stocks	437.6	(17.3)	305.4	(13.2)	132.2	(4.1)
Common equities	123.2	(29.3)	110.5	(26.5)	12.7	(2.8)
Total equity securities	560.8	(46.6)	415.9	(39.7)	144.9	(6.9)
Total portfolio	\$ 4,591.3	\$ (591.1)	\$ 2,441.8	\$ (259.6)	\$ 2,149.5	\$ (331.5)

¹ Includes \$291.8 million related to the cumulative effect of change in accounting principle (discussed above).

Included in gross unrealized losses at June 30, 2009, was \$30.4 million related to securities for which a portion of the OTI loss was recorded in earnings as a credit loss (\$6.6 million of corporate debt securities as part of the cumulative effect adjustment discussed above, and \$23.8 million of residential mortgage-backed securities recorded in the second quarter 2009). The fair value and gross unrealized losses for these securities were comprised of the following:

(millions)	Total		Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Fixed maturities:						
Corporate debt securities	\$ 19.9	\$ (6.6)	\$ 19.9	\$ (6.6)	\$	\$
Residential mortgage-backed securities	53.4	(23.8)			53.4	(23.8)
Total fixed maturities	\$ 73.3	\$ (30.4)	\$ 19.9	\$ (6.6)	\$ 53.4	\$ (23.8)

Trading Securities At June 30, 2009, June 30, 2008, and December 31, 2008, 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, 2009 and 2008.

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; and cash flow hedges. In addition, during 2009, we invested in equity options as an economic, forecasted forward sale.

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 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.

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The following table shows the status of our derivative instruments at June 30, 2009, June 30, 2008, and December 31, 2008 and for the three and six months ended June 30, 2009 and 2008:

(millions)	Notional Value			Purpose	Classification	Balance Sheet			Income Statement			
	June 30,		Dec. 31,			Fair Value			Net Realized			
	2009	2008	2008			2009	2008	Dec. 31,	Gains (Losses) on Securities		Three months ended	
Derivatives designated as:	2009	2008	2008	Purpose	Classification	2009	2008	2008	2009	2008	2009	2008
Hedging instruments												
Foreign currency cash flow hedge	\$ 8	\$	\$ 8	Forecasted transaction	Accumulated other comprehensive income	\$ 1.1	\$	\$.2	\$	\$	\$	\$
Non-hedging instruments												
Assets:												
Interest rate swaps		1,275	1,800	Manage portfolio duration	Investments - fixed maturities		9.2	96.3		10.1		10.1
Equity options (32,190 contracts) ¹	(a)			Manage price risk	Investments - common equities	4.2						
Liabilities:												
Interest rate swaps	668			Manage portfolio duration	Other liabilities	(9.8)			(8.8)		(8.8)	
Corporate credit default swaps	32		25	Manage credit risk	Other liabilities	(.3)		(.5)	(1.1)		(.6)	
Equity options (7,500 contracts)	(a)			Manage price risk	Other liabilities	(.1)			.3		.4	
Asset-backed credit default swaps		140		General portfolio investing	Other liabilities	(83.8)			(13.1)		(26.2)	
Closed:												
Interest rate swaps	3,518	1,550	NA	Manage portfolio duration					5.8	3.5	57.1	
Equity options (137,500 contracts)	(a)		NA	Manage price risk					(14.5)		(11.0)	
Total	NA	NA	NA			\$ (4.9)	\$ (74.6)	\$ 96.0	\$ (24.1)	\$ 2.8	\$ (16.5)	\$ 41.0

- (a) Each contract is equivalent to 100 shares of common stock of the issuer.
NA = Not Applicable

¹ The realized gain (loss) for the three and six months ended June 30, 2009 is less than \$.1 million.

CASH FLOW HEDGES

During the fourth quarter 2008, we entered into a cash flow hedge of forecasted foreign currency transactions. The hedge was designated as, and qualified for, cash flow hedge accounting treatment. We will defer the pretax gain or loss on this hedge and report the amount in accumulated other comprehensive income. The gain or loss on the contract will be amortized over the period during which foreign denominated expenses occur, which is expected to begin in the second half of 2009.

INTEREST RATE SWAPS

During the periods ended June 30, 2009, June 30, 2008, and December 31, 2008, we invested in interest rate swap positions primarily to manage the fixed-income portfolio duration. As of June 30, 2009, we delivered \$7.6 million in cash collateral to the counterparties on our open interest rate swap positions. As of December 31, 2008, we had received \$79.6 million in cash collateral from the counterparties on our then open interest rate swap positions, which was invested in short-term securities. We did not have any outstanding cash collateral at June 30, 2008.

CORPORATE CREDIT DEFAULT SWAPS

During the periods ended June 30, 2009 and December 31, 2008, we held a position on one corporate issuer within the financial services sector where we bought credit default protection in the form of credit default swaps for a 5-year time horizon. Additionally, during the second quarter 2009, we bought credit default protection in the form of credit default swaps for a 2-year time horizon on one corporate issuer within the industrial sector. We paid \$.6 million in upfront cash when we entered the 2-year exposure position, which is offset against our current exposure. We hold this protection to reduce our exposure to additional valuation declines on our preferred stock due to potential credit impairment of the issuer. We held no corporate credit default swap positions during the first six months of 2008.

EQUITY OPTIONS

During the period ended June 30, 2009, we simultaneously sold and purchased a substantially equivalent amount of call and put options, respectively, on Citigroup common stock, one of our preferred stock holdings. The purpose of this transaction was to effect a forward sale of a portion of the common stock we expected to receive from Citigroup resulting from the planned conversion of our preferred stock into common stock pursuant to Citigroup's intended exchange. This was achieved through matching the strike price and term of the option contracts and was meant to offset the downside price risk of the common stock during the time period pending the exchange. As of June 30, 2009, we delivered \$5.4 million in the form of cash to a counterparty as collateral to cover potential assignments of outstanding call options.

ASSET-BACKED CREDIT DEFAULT SWAPS

We held no asset-backed credit default swap positions during the first six months of 2009. During the first six months of 2008, we held a position for which we sold credit protection in the form of a credit default swap comprised of a basket of 20 asset-backed bonds supported by sub-prime mortgage loans. We covered the credit default swap's notional exposure by acquiring U.S. Treasury Notes of equal maturity and principal amount and reducing our overall exposure with any upfront cash received. During the fourth quarter 2008, we closed our entire asset-backed credit default swap position. As a result, we did not have any collateral deliveries related to this position outstanding at June 30, 2009 or December 31, 2008, compared to \$49.6 million of delivered U.S. Treasury Notes collateral at June 30, 2008; we did not have any cash collateral outstanding at June 30, 2008.

Note 3 Fair Value We have categorized our financial instruments, based on the degree of subjectivity inherent in the valuation technique, 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 and active exchange-traded equity 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 the reporting entity's subjective evaluation about the assumptions market participants would use in pricing the financial instrument (e.g., certain structured securities and privately held investments). During the second quarter 2009, we adopted the new fair value guidance (see *Note 11 - New Accounting Standards* for further information) that requires us to evaluate whether a market is distressed or inactive in determining the fair value for our portfolio. Based on this new guidance, we added to our review certain additional market level inputs to evaluate whether sufficient activity, volume, and new issuances existed 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:

(millions)	Fair Value			Total	Cost
	Level 1	Level 2	Level 3		
June 30, 2009					
Fixed maturities:					
U.S. government obligations	\$ 5,227.3	\$	\$	\$ 5,227.3	\$ 5,362.6
State and local government obligations		2,403.0		2,403.0	2,383.7
Corporate and other debt securities		772.3	27.4	799.7	805.5
Asset-backed securities:					
Residential mortgage-backed		440.3	.3	440.6	561.7
Commercial mortgage-backed obligations		968.2	18.2	986.4	1,060.4
Commercial mortgage-backed obligations: interest only		394.8	4.8	399.6	431.3
Other asset-backed		181.0	19.8	200.8	200.5
Total asset-backed securities		1,984.3	43.1	2,027.4	2,253.9
Redeemable preferred stocks:					
Financials	15.2	188.7		203.9	277.2
Utilities		56.9		56.9	70.9
Industrials		168.1	49.0	217.1	300.1
Total redeemable preferred stocks	15.2	413.7	49.0	477.9	648.2
Total fixed maturities	5,242.5	5,573.3	119.5	10,935.3	11,453.9
Equity securities:					
Nonredeemable preferred stocks:					
Agencies	2.0			2.0	.8
Financials	455.8	506.7		962.5	643.3
Utilities		53.4		53.4	50.8
Industrials			112.2	112.2	115.5
Total nonredeemable preferred stocks	457.8	560.1	112.2	1,130.1	810.4
Common equities:					
Common stock	395.6			395.6	286.8
Other risk investments			13.1	13.1	5.6
Total common equities	395.6		13.1	408.7	292.4
	\$ 6,095.9	\$ 6,133.4	\$ 244.8	12,474.1	12,556.7
Other short-term investments ¹				1,137.2	1,137.2
Total portfolio				\$ 13,611.3	\$ 13,693.9
Debt ²				\$ 1,859.0	\$ 2,176.4

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(millions)	Fair Value			Total	Cost
	Level 1	Level 2	Level 3		
June 30, 2008					
Fixed maturities:					
U.S. government obligations	\$ 1,640.3	\$	\$	\$ 1,640.3	\$ 1,636.9
State and local government obligations		3,162.9		3,162.9	3,178.4
Foreign government obligations		30.4		30.4	30.0
Corporate and other debt securities		915.3	30.0	945.3	971.1
Asset-backed securities:					
Residential mortgage-backed		780.6	42.2	822.8	853.9
Commercial mortgage-backed obligations		1,161.3	40.7	1,202.0	1,209.6
Commercial mortgage-backed obligations: interest only		616.8	7.8	624.6	646.6
Other asset-backed		137.3	28.6	165.9	167.1
Total asset-backed securities		2,696.0	119.3	2,815.3	2,877.2
Redeemable preferred stocks:					
Financials	18.7	238.3		257.0	320.5
Utilities		66.9		66.9	70.6
Industrials		294.8		294.8	321.5
Total redeemable preferred stocks	18.7	600.0		618.7	712.6
Total fixed maturities	1,659.0	7,404.6	149.3	9,212.9	9,406.2
Equity securities:					
Nonredeemable preferred stocks:					
Agencies	422.8			422.8	499.3
Financials	705.9	901.4		1,607.3	2,058.8
Utilities		65.9		65.9	68.2
Industrials		114.5		114.5	115.5
Total nonredeemable preferred stocks	1,128.7	1,081.8		2,210.5	2,741.8
Common equities:					
Common stock	2,025.6			2,025.6	1,304.7
Other risk investments			13.8	13.8	6.1
Total common equities	2,025.6		13.8	2,039.4	1,310.8
	\$ 4,813.3	\$ 8,486.4	\$ 163.1	13,462.8	13,458.8
Other short-term investments ¹				513.2	513.2
Total portfolio				\$ 13,976.0	\$ 13,972.0
Debt ²				\$ 2,052.6	\$ 2,174.7

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(millions)	Fair Value			Total	Cost
	Level 1	Level 2	Level 3		
<u>December 31, 2008</u>					
Fixed maturities:					
U.S. government obligations	\$ 3,693.6	\$	\$	\$ 3,693.6	\$ 3,565.7
State and local government obligations		3,004.4		3,004.4	3,041.4
Foreign government obligations		16.4	&nbs		