CINCINNATI FINANCIAL CORP
Form 10-K
February 27, 2015

United States Securities and Exchange Commission
Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2014.

¨ 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 0-4604

Cincinnati Financial Corporation
(Exact name of registrant as specified in its charter)

Ohio	31-0746871
(State of incorporation)	(I.R.S. Employer Identification No.)

6200 S. Gilmore Road
Fairfield, Ohio 45014-5141
(Address of principal executive offices) (Zip Code)
(513) 870-2000
(Registrant’s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:
None
Securities registered pursuant to Section 12(g) of the Act:
$2.00 par, common stock
(Title of Class)
6.125% Senior Notes due 2034
(Title of Class)
6.9% Senior Debentures due 2028
(Title of Class)
6.92% Senior Debentures due 2028
(Title of Class)

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

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

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 website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 if 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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

Large accelerated filer þ Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

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

The aggregate market value of voting stock held by nonaffiliates of the Registrant was $7,129,857,801 as of June 30, 2014.

As of February 20, 2015, there were 164,166,327 shares of common stock outstanding.

Document Incorporated by Reference

Portions of the definitive Proxy Statement for Cincinnati Financial Corporation's Annual Meeting of Shareholders to be held on May 2, 2015, are incorporated by reference into Part III of this Form 10-K.

2014 ANNUAL REPORT ON FORM 10-K
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Part I

ITEM 1. Business

Cincinnati Financial Corporation – Introduction

We are an Ohio corporation formed in 1968. Our lead subsidiary, The Cincinnati Insurance Company, was founded in 1950. Our main business is property casualty insurance marketed through independent insurance agencies in 39 states. Our headquarters is in Fairfield, Ohio. At year-end 2014, we employed 4,305 associates, including 2,954 headquarters associates who provide support to 1,351 field associates.

Cincinnati Financial Corporation owns 100 percent of three subsidiaries: The Cincinnati Insurance Company, CSU Producer Resources Inc. and CFC Investment Company. In addition, the parent company has an investment portfolio, owns the headquarters property and is responsible for corporate borrowings and shareholder dividends.

The Cincinnati Insurance Company owns 100 percent of our four additional insurance subsidiaries. Our standard market property casualty insurance group includes two of those subsidiaries – The Cincinnati Casualty Company and The Cincinnati Indemnity Company. This group writes a broad range of business, homeowner and auto policies. Other subsidiaries of The Cincinnati Insurance Company include The Cincinnati Life Insurance Company, which provides life insurance, disability income policies and fixed annuities, and The Cincinnati Specialty Underwriters Insurance Company, which offers excess and surplus lines insurance products.

The two noninsurance subsidiaries of Cincinnati Financial Corporation are CSU Producer Resources, which offers insurance brokerage services to our independent agencies so their clients can access our excess and surplus lines insurance products; and CFC Investment Company, which offers commercial leasing and financing services to our agencies, their clients and other customers.

Our filings with the U.S. Securities and Exchange Commission (SEC) are available on our website, cinfin.com/investors, as soon as possible after they have been filed with the SEC. These filings include annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. In the following pages we reference various websites. These websites, including our own, are not incorporated by reference in this Annual Report on Form 10-K.

Periodically, we refer to estimated industry data so that we can give information about our performance versus the overall insurance industry. Unless otherwise noted, the industry data is prepared by A.M. Best Co., a leading insurance industry statistical, analytical and insurer financial strength and credit rating organization. Information from A.M. Best is presented on a statutory accounting basis. When we provide our results on a comparable statutory accounting basis, we label it as such; all other company data is presented in accordance with accounting principles generally accepted in the United States of America (GAAP).

Our Business and Our Strategy

Introduction

The Cincinnati Insurance Company was founded more than 60 years ago by four independent insurance agents. They established the mission that continues to guide all of the companies in the Cincinnati Financial Corporation family – to grow profitably and enhance the ability of local independent insurance agents to deliver quality financial protection to the people and businesses they serve by:

- providing insurance market stability through financial strength
- producing competitive, up-to-date products and services
- developing associates committed to superior service

A select group of independent agencies in 39 states actively markets our property casualty insurance within their communities. At year-end 2014, standard market commercial lines and excess and surplus lines policies were marketed in all of those states, while personal lines policies were marketed in 31 of those states. Within our select group of agencies, we also seek to become the life insurance carrier of choice and to help agents and their clients – our policyholders – by offering leasing and financing services.

Three competitive advantages distinguish our company, positioning us to build shareholder value and to be successful overall:

- Commitment to our professional independent insurance agencies and to their continued success
- Financial strength to fulfill our promises and be a consistent market for our agents' business, supporting stability and confidence
- Operating structure that supports local decision making, showcasing our claims excellence and allowing us to balance growth with underwriting discipline

The primary sources of our company's net income are summarized below. We discuss the contribution to net income from each source in Item 7, Corporate Financial Highlights of Management's Discussion and Analysis.

- Underwriting profit (loss) – Includes revenues from earned premiums from insurance policies sold, reduced by losses and loss expenses from insurance coverages provided by those policies. Those revenues are further reduced by underwriting expenses from marketing policies or related administration of our insurance operation. The net result represents an underwriting profit when revenues exceed losses and expenses.
- Investment income – Is generated primarily from investing the premiums collected from insurance policies, until funds from cash or invested assets are needed to pay losses for insurance claims or other expenses. Interest income from bond investments or dividend income from stock investments are the main categories of our investment income.
- Realized investment gains (losses) – Occur from appreciation or depreciation of invested assets over time. Gains or losses are generally recognized when invested assets are sold or become impaired.

Independent Insurance Agency Marketplace

The U.S. property casualty insurance industry is a highly competitive marketplace with more than 2,000 stock and mutual companies operating independently or in groups. No single company or group dominates across all product lines and states. Standard market insurance companies (carriers) can market a broad array of products nationally or:

- choose to sell a limited product line or only one type of insurance (monoline carrier)
- target a certain segment of the market (for example, personal insurance)
- focus on one or more states or regions (regional carrier)

Standard market property casualty insurers generally offer insurance products through one or more distribution channels:

- independent agents, who represent multiple carriers
- captive agents, who represent one carrier exclusively
- direct marketing to consumers

For the most part, we compete with standard market insurance companies that market through independent insurance agents. Agencies marketing our commercial lines products typically represent six to 12 standard market insurance carriers for commercial lines products, including both national and regional carriers, most of which are mutual companies. Our agencies typically represent four to six standard personal lines carriers. We also compete with carriers that market personal lines products through captive agents and direct writers. Distribution through independent insurance agents or brokers represents nearly 60 percent of overall U.S. property casualty insurance premiums and approximately 80 percent of commercial property casualty insurance premiums, according to studies by the Independent Insurance Agents and Brokers of America.

We are committed exclusively to the independent agency channel. The independent agencies that we choose to market our standard lines insurance products share our philosophies. They do business person to person; offer broad, value-added services; maintain sound balance sheets; and manage their agencies professionally, targeting long-term success. We develop our relationships with agencies that are active in their communities, providing important knowledge of local market trends, opportunities and challenges.

We help our agencies meet the broader needs of their clients and increase and diversify their revenues and profitability by offering insurance solutions beyond our standard market property casualty insurance products. We market life insurance products through the agencies that offer our property casualty products and through other independent life agencies that represent The Cincinnati Life Insurance Company without also representing our other subsidiaries. We operate our own excess and surplus lines insurance brokerage firm and insurance carrier so that we can offer our excess and surplus lines products exclusively to the independent agencies who market our other property casualty insurance products.

The excess and surplus lines market exists due to a regulatory distinction. Generally, excess and surplus lines insurance carriers provide insurance that is unavailable in the standard market due to market conditions or characteristics of the insured persons or organizations that are caused by nature, their claim history or the characteristics of their business. Insurers operating in the excess and surplus lines marketplace generally market business through excess and surplus lines insurance brokers, whether they are small specialty insurers or specialized divisions of larger insurance organizations. We established an excess and surplus lines operation to help meet the needs of agency clients when insurance is unavailable in the standard market. By providing superior service, we can help our agencies grow while also profitably growing our property casualty business.

At year-end 2014, our 1,466 property casualty agency relationships were marketing our standard market insurance products from 1,884 reporting locations. An increasing number of agencies have multiple, separately identifiable locations, reflecting their growth and consolidation of ownership within the independent agency marketplace. The number of reporting agency locations indicates our agents’ regional scope and the extent of our presence within our 39 active states. At year-end 2013, our 1,450 agency relationships had 1,823 reporting locations. At year-end 2012, our 1,408 agency relationships had 1,758 reporting locations.

We made 99, 96 and 140 new agency appointments in 2014, 2013 and 2012, respectively. Of these new appointments, 63, 59 and 109, respectively, were new relationships. The remainder included new branch offices opened by existing Cincinnati agencies and appointment of agencies that merged with a Cincinnati agency. These new appointments and other changes in agency structures or appointment status led to a net increase in agency relationships of 16, 42 and 96 and a net increase in reporting agency locations of 61, 65 and 110 in 2014, 2013 and 2012, respectively.

On average, we have a 12.8 percent share of the standard lines property casualty insurance purchased through our reporting agency locations, according to 2013 data from agency surveys. Our share is 17.6 percent in reporting agency locations that have represented us for more than 10 years; 8.9 percent in agencies that have represented us for six to 10 years; 5.4 percent in agencies that have represented us for two to five years; and 0.9 percent in agencies that have represented us for one year or less.

Our largest single agency relationship accounted for approximately 0.8 percent of our total property casualty earned premiums in 2014. No aggregate locations under a single ownership structure accounted for more than 2.1 percent of our earned premiums in 2014.

Financial Strength

We believe that our financial strength and strong capital and surplus position, reflected in our insurer financial strength ratings, are clear, competitive advantages in the segments of the insurance marketplace that we serve. This strength supports the consistent, predictable performance that our policyholders, agents, associates and shareholders have always expected and received, helping us withstand significant challenges.

While the potential exists for short-term financial performance variability due to our exposures to potential catastrophes or significant capital market losses, the rating agencies consistently have asserted that we have built appropriate financial strength and flexibility to manage that variability. We remain committed to strategies that emphasize being a consistent, stable market for our agents' business rather than seeking short-term benefits that might accrue by quick, opportunistic reaction to changes in market conditions.

We use various principles and practices such as diversification and enterprise risk management to maintain strong capital. For example, we maintain a diversified investment portfolio by reviewing and applying diversification parameters and tolerances.

- Our $9.460 billion fixed-maturity portfolio is diversified and exceeds total insurance reserves. The portfolio had an average rating of A2/A, and its fair value exceeded total insurance reserve liabilities by approximately 35 percent at December 31, 2014. No corporate bond exposure accounted for more than 0.7 percent of our fixed-maturity portfolio, and no municipal exposure accounted for more than 0.3 percent.
- The strength of our fixed-maturity portfolio provides an opportunity to invest for potential capital appreciation by purchasing equity securities. Our $4.858 billion equity portfolio minimizes concentrations in single stocks or industries. At December 31, 2014, no single security accounted for more than 3.3 percent of our portfolio of publicly traded common stocks, and no single sector accounted for more than 17.3 percent.

Strong liquidity increases our flexibility through all periods to maintain our cash dividend and to continue to invest in and expand our insurance operations. At December 31, 2014, we held $1.821 billion of our cash and invested assets at the parent company level, of which $1.639 billion, or 90.0 percent, was invested in common stocks, and $72 million, or 4.0 percent, was cash and cash equivalents.

We minimize reliance on debt as a source of capital, maintaining a debt-to-total-capital ratio below 20 percent. At December 31, 2014, this ratio at 11.3 percent was well below the target limit as capital remained strong while debt levels were reduced by $55 million from year-end 2013. Long-term debt at year-end 2014 totaled $791 million and our short-term debt was $49 million. The long-term debt consists of three nonconvertible, noncallable debentures, two due in 2028 and one in 2034. Ratings for our long-term debt are discussed in Item 7, Liquidity and Capital Resources, Additional Sources of Liquidity.

At year-end 2014 and 2013, risk-based capital (RBC) for our standard market property casualty insurance, excess and surplus lines insurance and life insurance subsidiaries was strong, far exceeding regulatory requirements.

- We ended 2014 with a 0.9-to-1 ratio of property casualty premiums to surplus, a key measure of property casualty insurance company capacity and security. A lower ratio indicates more security for policyholders and greater capacity for growth by an insurer. We believe our ratio provides ample flexibility to diversify risk by expanding our operations into new geographies and product areas. The estimated industry average ratio was 0.7-to-1 at year-end 2014.
- We ended 2014 with an 8.1 percent ratio of life statutory adjusted risk-based surplus to liabilities, a key measure of life insurance company capital strength. The estimated industry average ratio was 12.1 percent at year-end 2014. A

higher ratio indicates an insurer’s stronger security for policyholders and capacity to support business growth.

(Dollars in millions) Statutory Information	At December 31,	
	2014	2013
Standard market property casualty insurance subsidiary		
Statutory capital and surplus	$4,472	$4,326
Risk-based capital (RBC)	4,490	4,343
Authorized control level risk-based capital	563	534
Risk-based capital to authorized control level risk-based capital ratio	8.0	8.1
Written premium to surplus ratio	0.9	0.9
Life insurance subsidiary		
Statutory capital and surplus	$223	$247
Risk-based capital (RBC)	241	264
Authorized control level risk-based capital	33	31
Total liabilities excluding separate account business	2,978	2,807
Risk-based capital to authorized control level risk-based capital ratio	7.3	8.1
Life statutory risk-based adjusted surplus to liabilities ratio	8.1	9.5
Excess and surplus lines insurance subsidiary		
Statutory capital and surplus	$266	$228
Risk-based capital (RBC)	266	228
Authorized control level risk-based capital	32	25
Risk-based capital to authorized control level risk-based capital ratio	8.4	9.2
Written premium to surplus ratio	0.6	0.6

The consolidated property casualty insurance group’s ratio of investments in common stock, at fair value, to statutory capital and surplus was 67.7 percent at year-end 2014 compared with 65.7 percent at year-end 2013.

Cincinnati Financial Corporation’s senior debt is rated by four independent rating firms. In addition, the rating firms award our property casualty and life operations insurance financial strength ratings based on their quantitative and qualitative analyses. These ratings assess an insurer’s ability to meet financial obligations to policyholders and do not necessarily address all of the matters that may be important to shareholders. Ratings may be subject to revision or withdrawal at any time by the ratings agency, and each rating should be evaluated independently of any other rating.

All of our insurance subsidiaries continue to be highly rated. During 2014, three of the four ratings firms affirmed our insurance financial strength ratings. Two of the four continued their stable outlook on the ratings and one revised its outlook to positive from stable.

As of February 25, 2015, our insurance financial strength ratings were:

Rating agency	Insurer Financial Strength Ratings									Date of most recent affirmation or action
	Standard market property casualty insurance subsidiary			Life insurance subsidiary			Excess and surplus lines insurance subsidiary			
			Rating Tier			Rating Tier			Rating Tier	
A. M. Best Co. ambest.com	A+	Superior	2 of 16	A	Excellent	3 of 16	A	Excellent	3 of 16	Stable outlook (12/12/14)
Fitch Ratings fitchratings.com	A+	Strong	5 of 21	A+	Strong	5 of 21	-	-	-	Stable outlook (11/18/14)
Moody's Investors Service moodys.com	A1	Good	5 of 21	-	-	-	-	-	-	Stable outlook (4/30/13)
Standard & Poor's Ratings Services spratings.com	A	Strong	6 of 21	A	Strong	6 of 21	-	-	-	Positive outlook (6/18/14)

On December 12, 2014, A.M. Best affirmed our financial strength ratings that it had assigned in December 2008, continuing its stable outlook. A.M. Best cited our superior risk-adjusted capitalization, conservative loss reserving standards, strong distribution network within our targeted regional markets and historically strong operating performance that has improved in recent years. Concerns noted included variability in earnings, primarily due to significant catastrophe-related losses, and historically elevated common stock leverage. A.M. Best acknowledged several reasons for our strong relationships with independent agencies along with financial flexibility through our holding company.

On June 10, 2014, and on November 18, 2014, Fitch Ratings affirmed the ratings that it had assigned to us in August 2009, continuing its stable outlook. Fitch said our ratings strengths included very strong capitalization, our holding company's sizeable position in cash and marketable securities and our moderate financial leverage ratio. Fitch noted our reserve adequacy and benefits from our implementation of claims and risk management tools in addition to pricing actions. Fitch said its rating could be unfavorably affected by a combined ratio exceeding 105 percent on a sustained basis, evidence of deteriorating profitability on recent growth or by material and sustained deterioration in capitalization.

On June 18, 2014, Standard & Poor’s Ratings Services affirmed the ratings that it had assigned in July 2010, revising its outlook to positive from stable. S&P said its rating reflected our strong competitive position, favorable geographical footprint and extremely strong capital. With the positive outlook, it acknowledged our general underwriting improvement in recent years and our track record of mitigating potential capital and earnings volatility. S&P noted its rating could come under pressure if our overall operating performance or capital adequacy deteriorated significantly or upon perceived adverse changes to our competitive position.

Our debt ratings are discussed in Item 7, Liquidity and Capital Resources, Additional Sources of Liquidity.

Operating Structure

We offer our broad array of insurance products through the independent agency distribution channel. We recognize that locally based independent agencies have relationships in their communities and local marketplace intelligence that can lead to policyholder satisfaction, loyalty and profitable business. Several of our strategic initiatives are intended not only to help us compete but also to enhance support of agencies that represent us, thereby contributing to agency success. We seek to be a consistent and predictable property casualty carrier that agencies can rely on to serve their clients.

In our 10 highest volume states for consolidated property casualty premiums, 1,091 reporting agency locations wrote 62.8 percent of our 2014 consolidated property casualty earned premium volume compared with 1,067 locations and 63.8 percent in 2013. We continue efforts to geographically diversify our property casualty risks.

Our 10 highest premium volume property casualty lines states are shown in the table below.

(Dollars in millions)	Earned premiums	% of total earned	Agency locations	Average premium per location
Year ended December 31, 2014				
Ohio	$715	17.7 %	246	$2.9
Illinois	288	7.1	136	2.1
Indiana	261	6.4	111	2.4
Pennsylvania	222	5.5	99	2.2
Georgia	216	5.3	95	2.3
Michigan	204	5.0	138	1.5
North Carolina	201	5.0	95	2.1
Tennessee	155	3.8	60	2.6
Virginia	146	3.6	65	2.2
Alabama	139	3.4	46	3.0

Field Focus

We rely on our force of 1,351 field associates to provide service and be accountable to our agencies for decisions we make at the local level. These associates live in the communities our agents serve, working from offices in their homes and providing 24/7 availability to our agents and policyholders. Headquarters associates support agencies and field associates with underwriting, accounting, technology assistance, training and other services. Company executives and headquarters associates regularly travel to visit agencies, strengthening the personal relationships we have with these organizations. Agents have opportunities for direct, personal conversations with our senior management team, and headquarters associates have opportunities to refresh their knowledge of marketplace conditions and field activities.

The field team is coordinated by field marketing representatives responsible for underwriting new commercial lines business. They are joined by field representatives specializing in claims, loss control, personal lines, excess and surplus lines, machinery and equipment, bond, premium audit and life insurance. The field team provides many services for agencies and policyholders; for example, our loss control field representatives and others specializing in machinery and equipment risks perform inspections and recommend specific actions to improve the safety of the policyholder’s operations and the quality of the agent’s account.

Agents work with us to carefully select risks and help assure pricing adequacy. They appreciate the time our associates invest in creating solutions for their clients while protecting profitability, whether that means working on an individual case or customizing policy terms and conditions that preserve flexibility, choice and other sales advantages. We seek to develop long-term relationships by understanding the unique needs of their clients, who are also our policyholders.

We also are responsive to agent needs for well-designed property casualty products. Our commercial lines products are structured to allow flexible combinations of property and liability coverages in a single package with a single expiration date and several payment options. This approach brings policyholders convenience, discounts and a reduced risk of coverage gaps or disputes. At the same time, it increases account retention and saves time and expense for the agency and our company.

We employ technology solutions and business process improvements that:

- allow our field and headquarters associates to collaborate with each other and with agencies more efficiently
- provide our agencies the ability to access our systems and data from their agency management systems to process business transactions from their offices

- allow policyholders to directly access, from their systems and mobile devices, pertinent policy information online in order to further improve efficiency for our agencies
- automate our internal processes so our associates can spend more time serving agents and policyholders
- reduce duplicated effort or friction points in technology processes, introducing more efficiency that reduces company and agency costs

Agencies access our systems and other electronic services via their agency management systems or CinciLink®, our agency-only website. CinciLink provides Web-based services and content that makes doing business with us easier, such as commercial and personal lines rating and processing systems, policy loss information, educational courses about our products and services, accounting services, and electronic libraries for property and casualty coverage forms, state rating manuals and marketing materials.

Superior Claims Service
Our claims philosophy reflects our belief that we prosper as a company by responding to claims person to person, paying covered claims promptly, preventing false claims from unfairly adding to overall premiums and building financial strength to meet future obligations.

Our 807 locally based field claims associates work from their homes, assigned to specific agencies. They respond personally to policyholders and claimants, typically within 24 hours of receiving an agency's claim report. We believe we have a competitive advantage because of the person-to-person approach and the resulting high level of service that our field claims representatives provide. We also help our agencies provide prompt service to policyholders by giving most agencies authority to immediately pay most first-party claims under standard market policies up to $2,500. We believe this same local approach to handling claims is a competitive advantage for our agents providing excess and surplus lines coverage in their communities. Handling of these claims includes guidance from headquarters-based excess and surplus lines claims managers.

Our property casualty claims operation uses our claims management system (CMS) to streamline processes and achieve operational efficiencies. CMS allows field and headquarters claims associates to collaborate on reported claims through a virtual claim file. Our field claims representatives use tablet computers to view and enter information into CMS from any location, including a policyholder's home or an agent's office, and to print claim checks using portable printers. Agencies also can access selected CMS information such as activity notes on open claims.

Catastrophe response teams are comprised of volunteers from our experienced field claims staff who have the authority they need to do their jobs. In times of widespread loss, our field claims representatives confidently and quickly resolve claims, often writing checks on the same day they inspect the loss. CMS introduced efficiencies that are especially evident during catastrophes. Electronic claim files allow for fast initial contact with policyholders and easy sharing of information and data by rotating storm teams, headquarters staff and local field claims representatives. When hurricanes or other weather events are predicted, we can identify through mapping technologies the expected number of our policyholders that may be impacted by the event and choose to have catastrophe response team members travel to strategic locations near the expected impact area. They are then in position to quickly get to the affected area, set up temporary offices and start calling on policyholders.

Our claims associates work to control costs where appropriate. They use vendor resources that provide negotiated pricing to our policyholders and claimants. Our field claims representatives also are educated continuously on new techniques and repair trends for vehicles. They can leverage their local knowledge and experience with area body shops, which helps them negotiate the right price with any facility the policyholder chooses.

We staff a Special Investigations Unit (SIU) with former law enforcement and claims professionals whose qualifications make them well suited to gathering facts to uncover potential fraud. While we believe our job is to pay what is due under each policy contract, we also want to prevent false claims from unfairly increasing overall premiums. Our SIU also operates a computer forensics lab, using sophisticated software to recover data and mitigate the cost of computer-related claims for business interruption and loss of records.

Insurance Products

We actively market property casualty insurance in 39 states through a select group of independent insurance agencies. For most agencies that represent us, we believe we offer insurance solutions for approximately 75 percent of the typical insurable risks of their clients. Our standard market commercial lines products and our excess and surplus lines are marketed in all 39 states while our standard market personal lines products are marketed in 31. We offer insurance coverage that includes business property and liability, automobile and homeowner as well as umbrella liability.

The following table shows net written premiums by segment and business line at year-end 2014, 2013 and 2012:

(Dollars in millions)	2014	2013	2012	Percent of total 2014	
Segment:					
Commercial lines insurance	$2,922	$2,760	$2,459	66.5	%
Personal lines insurance	1,068	1,005	918	24.3	
Excess and surplus lines insurance	153	128	105	3.5	
Life insurance	250	241	249	5.7	
Total	$4,393	$4,134	$3,731	100.0	%
Business line:					
Commercial lines insurance					
Commercial casualty	$969	$897	$793	22.0	%
Commercial property	776	673	573	17.7	
Commercial auto	548	507	444	12.5	
Workers' compensation	365	374	341	8.3	
Other commercial	264	309	308	6.0	
Total commercial lines insurance	2,922	2,760	2,459	66.5	
Personal lines insurance					
Personal auto	489	460	425	11.1	
Homeowner	456	428	378	10.4	
Other personal	123	117	115	2.8	
Total personal lines insurance	1,068	1,005	918	24.3	
Excess and surplus lines insurance	153	128	105	3.5	
Life insurance					
Term life insurance	138	129	124	3.2	
Universal life insurance	41	41	45	0.9	
Other life insurance, annuity and disability income products	71	71	80	1.6	
Subtotal	250	241	249	5.7	
Total	$4,393	$4,134	$3,731	100.0	%

We discuss our commercial lines, personal lines and excess and surplus lines insurance operations and products in Commercial Lines Insurance Segment, Personal Lines Insurance Segment, and Excess and Surplus Lines Insurance Segment.

Cincinnati Specialty Underwriters began excess and surplus lines insurance operations in January 2008. We structured this operation to exclusively serve the needs of the independent agencies that currently market our standard market insurance policies. When all or a portion of a current or potential client’s insurance program requires excess and surplus lines coverages, those agencies can write the whole account with Cincinnati, gaining benefits not often found in the broader excess and surplus lines market. Agencies have access to Cincinnati Specialty Underwriters' product line through CSU Producer Resources, the wholly owned insurance brokerage subsidiary of Cincinnati Financial Corporation.

We also support the independent agencies affiliated with our property casualty operations in their efforts to sell life insurance. The life insurance, disability and fixed annuity products offered by our life insurance subsidiary round out and protect accounts and improve account persistency. At the same time, our life operation increases diversification of revenue and profitability sources for both the agency and our company.

Our property casualty agencies make up the main distribution system for our life insurance products. To help build scale, we also develop life insurance business from other independent life insurance agencies in geographic markets underserved through our property casualty agencies. We are careful to solicit business from these other agencies in a manner that does not compete with the life insurance marketing and sales efforts of our property casualty agencies. Our life insurance operation emphasizes up-to-date products, responsive underwriting, high-quality service and competitive pricing.

Other Services to Agencies

We complement our insurance operations by providing products and services that help attract and retain high-quality independent insurance agencies. When we appoint agencies, we look for organizations with knowledgeable, professional staffs. In turn, we make an exceptionally strong commitment to assist them in keeping their knowledge up to date and educating new people they bring on board as they grow. Numerous activities fulfill this commitment at our headquarters, online and in regional and agency locations.

Except for travel-related expenses to classes held at our headquarters, most programs are offered at no cost to our agencies. While that approach may be extraordinary in our industry today, the result is quality service for our policyholders and increased success for our independent agencies.

In addition to broad education and training support, we make available noninsurance financial services. CFC Investment Company offers equipment and vehicle leases and loans for independent insurance agencies, their commercial clients and other businesses. We also provide commercial real estate loans or other financial assistance to help agencies operate, expand and perpetuate their businesses. We believe that providing these services enhances agency relationships with the company and their clients, increasing loyalty while diversifying the agency’s revenues.

Our goal is to support agents with tools and resources that help communicate the value of a Cincinnati policy to their clients and prospective clients. We’ll build on our 2013 and 2014 marketing efforts with a modest national advertising campaign in 2015. Our intent is to increase the visibility of our company, supporting our agents' efforts as they recommend Cincinnati Insurance policies. We also continue to build our social media presence, focusing on providing content that agents can share on their own sites.

Strategic Initiatives

Management has identified strategies that can position us for long-term success. The board of directors and management expect execution of our strategic plan to create significant value for shareholders over time. We broadly group these strategies into two areas of focus – improving insurance profitability and driving premium growth – correlating with important ways we measure progress toward our long-term financial objectives. A primary profitability long-term target is to produce a GAAP combined ratio over any five-year period that consistently averages within the range of 95 percent to 100 percent. A primary premium growth long-term target, established in late 2011, is to profitably grow to reach $5 billion of property casualty and life insurance annual direct written premiums by the end of 2015.

Effective capital management is an important part of creating shareholder value, serving as a foundation to support other strategies focused on profitable growth of our insurance business, with the overall objective of long-term benefit for shareholders. Our capital management philosophy is intended to preserve and build our capital while maintaining appropriate liquidity. A strong capital position provides the capacity to support premium growth, and liquidity provides for our investment in the people and infrastructure needed to implement our other strategic initiatives. Our strong capital and liquidity also provide financial flexibility for shareholder dividends or other capital management actions.

Our strategies seek to position us to compete successfully in the markets we have targeted while optimizing the balance of risk and returns. We believe successful implementation of key initiatives that support our strategies will help us better serve our agent customers, reduce volatility in our financial results and achieve our long-term objectives despite shorter-term effects of difficult economic, market or pricing cycles. We describe our expectations for the results of these initiatives in Item 7, Executive Summary of Management’s Discussion and Analysis.

Improve Insurance Profitability

Implementation of the initiatives described below is intended to enhance underwriting expertise and knowledge for our property casualty business, improving our ability to manage our business while also providing greater efficiency. By improving our capabilities to determine individual insurance policy pricing with better alignment to risk attributes, we can increase our effectiveness in managing profit margins. By improving internal processes and further developing performance metrics, we can continue improving efficiency and effectiveness. These initiatives also support the ability of the agencies that represent us to grow profitably by allowing them to more efficiently serve clients and manage expenses. Important initiatives for 2015 to improve insurance profitability include:

- Enhance underwriting expertise and knowledge – We continue to increase our use of information and develop our skills for better underwriting performance, focusing on areas that will benefit most from additional effort. We also continue to expand our pricing and segmentation capabilities by using predictive analytics, expecting cumulative benefits of these efforts to improve loss ratios over time. Expanded capabilities include streamlining and optimizing data to increase accuracy, timeliness and ease of use. Development and use of additional business data to support more accurate underwriting, more granular pricing and other business decision-making also continues through a multi-year, phased project. Project deliverables include enhancing our data management program in phases, including further developing the data warehouse used in our insurance operations, helping us achieve our strategic objectives.

Initiatives for 2015 include expanding pricing precision by line of business and by state or territory with ongoing enhancement of analytics and predictive modeling tools. These tools better align individual insurance policy pricing to risk attributes, helping us to further segment policies. Our segmentation efforts emphasize identification and retention of policies we believe have relatively stronger pricing, while seeking more aggressive renewal terms and conditions on policies we believe have relatively weaker pricing. We continue to further integrate such tools with policy administration systems to help our underwriting associates better target profitability and discuss pricing impacts with agency personnel.

For commercial autos we insure, pricing precision is an ongoing focus through actions such as improving premium rate classification and using other rating variables in risk selection and pricing, plus further automating collection of key rating variables. For our personal auto line of business, our rate changes for each respective state will continue to apply pricing precision features.

During 2015, we plan to introduce, in select states, predictive modeling for dwelling fire policies. In late 2014, we introduced a by-peril rating plan for homeowners in select states, and plan to expand it to other states in 2015. By-peril rating helps improve pricing precision by separately pricing for the risk of losses from distinct perils, such as wind versus fire.

As part of our ongoing effort to more profitably underwrite property coverages, we'll continue a robust level of inspections of insured property or other loss control activities that provide enhanced underwriting knowledge. We'll also continue to refine our use of deductibles or other policy terms and conditions.

- Improve internal processes – Improved processes support our strategic goals, helping to deploy improved products and pricing more quickly. They also help reduce internal costs and allow us to focus more resources on agency services. Improved workflow tools should increase our efficiency, providing additional operational reporting metrics and making it easier for agencies to do business with us.

During 2015, we'll continue to ramp up operations for our customer care center for small commercial business policies, also making things easier for agents. Our customer care center was piloted and implemented for a small number of select agencies during 2014, and by expanding that we expect nearly 10 percent of our agencies to be taking advantage of it by the end of 2015. Our services include various policy administration functions routinely provided by agencies, allowing agency personnel to focus more on marketing efforts and on providing additional service to their clients as needed. We'll continue to seek other ways to improve policyholder satisfaction through identification and deployment of user-friendly services.

We measure the overall success of our strategy to improve insurance profitability primarily through our GAAP combined ratio for property casualty results, which we believe can consistently average within the range of 95 percent to 100 percent for any five-year period. We also compare our statutory combined ratio to the industry average to gauge our progress.

We expect these initiatives to contribute to our position as the No. 1 or No. 2 carrier based on premium volume in agencies that have represented us for at least five years. We again hit that mark in nearly 75 percent of such agencies based on 2013 premiums. We are working to increase the percentage of agencies where we achieve that rank.

Drive Premium Growth

Implementation of the operational initiatives below is intended to further penetrate each market we serve through our independent agencies. We expect strategies aimed at specific market opportunities, along with service enhancements, to encourage our agents to grow and to increase our share of their business. Our strategy includes evaluating general business statistics, historical profitability trends and historical catastrophe trends to estimate premium growth from existing agencies and to make careful projections about the number of additional agencies needed to achieve premium targets. Our focus remains on the key components of agent satisfaction based on factors that agents tell us are most important. Significant 2015 initiatives to drive premium growth include:

- Expansion of our marketing and service capabilities – We continue to enhance our generalist approach to allow our appointed agencies to better compete in the marketplace by providing services an agent’s clients want and need. During 2015, we will continue to develop and coordinate targeted marketing, including cross-selling opportunities. That includes working to further develop and market programs through our Target Markets department, which offered 17 programs at the end of 2014. We continue to migrate these programs to our enhanced policy administration platform and will make improvements to our programs during this migration. An early 2015 initiative aims to provide a platform for our agents to target group business such as professional and trade associations and franchises. We are also working with risk purchasing groups to provide liability coverages for homogeneous classes of business.

As part of our long-term plans, we expect to significantly expand marketing and enhance our products and services to independent agents serving high net worth personal lines clients. We expect that expansion will include, over the next five years, these states that were not part of our personal lines marketing area at the end of 2014: California, Massachusetts, New Jersey and Texas. Our Executive Classic™ homeowner product offers flexibility and broad coverages. We can also include coverages for automobiles, personal umbrella liability, watercraft and valuable articles sought by these clients. At year-end 2014, our appointed agencies produced for us more than $100 million in annual premiums from high net worth policyholders and we plan to continue to enhance our product line to remain competitive. In the second half of 2015, we plan to offer through agents in the state of New York a new suite of insurance products serving the unique needs of high net worth personal lines clients. Executive Capstone™ will offer higher coverage limits and new options for home, automobile, personal umbrella, watercraft and valuable article products. These improvements will be rolled out to all states over the next several years. While we don't expect expanded high net worth products and services to significantly contribute to growth for our personal lines insurance segment until 2016 and subsequent years, further development of our products and services should position us to be the carrier of choice for this portion of our agent’s accounts.

We will also continue to add field marketing representatives where needed for additional agency support in targeted areas, including some specializing in personal lines or excess and surplus lines. Associates in our life insurance segment plan to increase opportunities for agencies to cross-sell to their clients by providing updated products and services that aim to meet their life insurance needs.

- New agency appointments – We continue to appoint new agencies to develop additional points of distribution, focusing on areas where our property casualty insurance market share is less than 1 percent while also considering economic and catastrophe risk factors. In 2015, we are planning approximately 100 appointments of independent agencies that write in aggregate $1 billion or more in property casualty business annually with various insurance carriers. We generally appoint those agencies in order to have them represent us to sell life insurance, as well as our property casualty insurance, to their clients. We plan to appoint approximately 50 additional independent life agencies to offer only our life insurance products and service. Our excess and surplus lines marketing will focus on selected areas and work to increase penetration with recently appointed agencies.

We seek to build a close, long-term relationship with each agency we appoint. The contribution of new agencies to our property casualty premium growth should occur over several years, as time is required to fully realize the benefits of our agency relationships. We generally earn a 10 percent share of an agency’s business within 10 years of its appointment. We also help our agents grow their business by attracting more clients in their communities through unique Cincinnati-style service. We carefully evaluate the marketing reach of each new appointment to ensure the territory can support both current and new agencies. In counting new agency appointments, we include appointment of new agency relationships with property casualty insurance group subsidiaries of The Cincinnati Insurance Company.

For those that we believe will produce a meaningful amount of new business premiums, we also count appointments of agencies that merge with an existing Cincinnati agency and new branch offices opened by current Cincinnati agencies. We made 99, 96 and 140 new appointments in 2014, 2013 and 2012, respectively, with 63, 59 and 109 representing new relationships.

We measure the overall success of our strategy to drive premium growth primarily through changes in net written premiums. Other important indicators that we are successfully executing initiatives to drive premium growth include tracking our progress toward our year-end 2015 direct written premiums target. We believe we can grow premiums faster than the industry average over any five-year period, while also achieving our long-term objective for underwriting profitability.

Our Segments

Consolidated financial results primarily reflect the results of our five reporting segments. These segments are defined based on financial information we use to evaluate performance and to determine the allocation of assets.

- Commercial lines insurance
- Personal lines insurance
- Excess and surplus lines insurance
- Life insurance
- Investments

We evaluate results for our consolidated property casualty operations, which is the total of our commercial lines, personal lines and excess and surplus lines insurance results.

Revenues, income before income taxes and identifiable assets for each segment are shown in a table in Item 8, Note 18 of the Consolidated Financial Statements. Some of that information is discussed in this section of this report, where we explain the business operations of each segment. The financial performance of each segment is discussed in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

Commercial Lines Insurance Segment

In 2014, the commercial lines insurance segment contributed net earned premiums of $2.856 billion, representing 57.8 percent of consolidated total revenues. This segment reported profit before income taxes of $146 million. Commercial lines net earned premiums rose 8 percent in 2014 and 11 percent in 2013.

Approximately 95 percent of our commercial lines premiums are written to provide accounts with coverages from more than one of our business lines. As a result, we believe that our commercial lines business is best measured and evaluated on a segment basis. However, we provide line of business data to summarize growth and profitability trends separately for our business lines. The five commercial business lines are:

- Commercial casualty – Provides coverage to businesses against third-party liability from accidents occurring on their premises or arising out of their operations, including liability coverage for injuries sustained from products sold as well as coverage for professional services, such as dentistry. Specialized casualty policies may include liability coverage for excess insurance and umbrella liability, including personal umbrella liability written as an endorsement to commercial umbrella coverages, and employment practices liability (EPLI), which protects businesses against claims by employees that their legal rights as employees of the company have been violated, and against other acts or failures to act under specified circumstances. The commercial casualty business line includes liability coverage written as part of commercial package policies.
- Commercial property – Provides coverage for loss or damage to buildings, inventory and equipment caused by covered causes of loss such as fire, wind, hail, water, theft and vandalism, as well as business interruption resulting from a covered loss. Commercial property also includes crime insurance, which provides coverage for losses such as embezzlement or misappropriation of funds by an employee, among others; and inland marine insurance, which provides coverage for builder's risk, cargo, electronic data processing equipment and a variety of mobile equipment, such as contractor's equipment. Various property coverages can be written as stand-alone policies or can be added to a commercial package policy.
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Commercial auto – Protects businesses against liability to others for both bodily injury and property damage, medical payments to insureds and occupants of their vehicles, physical damage to an insured's own vehicle from collision and various other perils, and damages caused by uninsured motorists.

- Workers' compensation – Covers employers for specified benefits payable under state or federal law for workplace injuries to employees. We write workers' compensation coverage in all of our active states except

North Dakota, Ohio, Washington and Wyoming, where coverage is provided solely by the state instead of by private insurers.

- Other commercial lines – This includes the variety of other types of insurance products we offer to businesses. The main coverages offered are summarized below.

Management liability and surety (formerly surety and executive risk) – This includes the following:

Director and officer (D&O) liability insurance, which covers liability for actual or alleged errors in judgment, breaches of duty or other wrongful acts related to activities of for-profit or nonprofit organizations. Our director and officer liability policy can optionally include EPLI coverage, trustee and fiduciary coverage and Internet liability services coverage. We market primarily to nonprofit organizations and they represent approximately half of the premium volume in force for our 2014 director and officer liability business. The for-profit portion includes approximately 250 bank or savings and loan financial institutions, with only 11 having assets of $1 million or more.

Contract and commercial surety bonds, which guarantee a payment or reimbursement for financial losses resulting from dishonesty, failure to perform and other acts.

Fidelity bonds, which cover losses that policyholders incur as a result of fraudulent acts by specified individuals or dishonest acts by employees.

Specialty packages – Includes coverages for property, liability and business interruption tailored to meet the needs of specific industry classes such as artisan contractors, dentists, garage operators, financial institutions, metalworkers, printers, religious institutions or smaller main street businesses. Businessowners policies, which combine property, liability and business interruption coverages for small businesses, are included in specialty packages.

Machinery and equipment – Specialized coverage provides protection for loss or damage to boilers and machinery, including production and computer equipment and business interruption, due to sudden and accidental mechanical breakdown, steam explosion or artificially generated electrical current.

Our emphasis is on products that agents can market to small to midsized businesses in their communities. Of our 1,884 reporting agency locations, 20 market only our management liability and surety products and 33 market only our personal lines products. The remaining 1,831 locations, located in all states in which we actively market, offer some or all of our standard market commercial insurance products.

In 2014, our 10 highest volume commercial lines states generated 60.1 percent of our earned premiums compared with 61.1 percent in 2013 and 62.3 percent in 2012 as we continued efforts to geographically diversify our property casualty risks. Earned premiums in the 10 highest volume states increased 7 percent in 2014 and increased 11 percent in the remaining 29 states. The aggregate number of reporting agency locations in our 10 highest volume states increased to 1,086 in 2014 from 1,064 in 2013.

Our 10 highest premium volume commercial lines states are shown in the table below.

(Dollars in millions)	Earned premiums	% of total earned	Agency locations	Average premium per location
Year ended December 31, 2014				
Ohio	$413	14.5 %	243	$1.7
Illinois	209	7.3	136	1.5
Pennsylvania	191	6.7	99	1.9
Indiana	172	6.0	109	1.6
North Carolina	141	4.9	93	1.5
Michigan	133	4.7	134	1.0
Georgia	122	4.3	89	1.4
Virginia	118	4.1	64	1.8
Tennessee	111	3.9	59	1.9
Wisconsin	105	3.7	60	1.8

For new commercial lines business, case-by-case underwriting and pricing is coordinated by our locally based field marketing representatives. Our agents and our field marketing, claims, loss control, premium audit, bond and machinery and equipment representatives get to know the people and businesses in their communities and can make informed decisions about each risk. Field marketing representatives also are responsible for selecting new independent agencies, coordinating field teams of specialized company representatives and promoting all of the company’s products within the agencies they serve.

Commercial lines policy renewals are managed by headquarters underwriters who are assigned to specific agencies and consult with local field staff as needed. As part of our team approach, headquarters underwriters also help oversee agency growth and profitability. They are responsible for formal issuance of all new business and renewal policies as well as policy endorsements. Further, the headquarters underwriters provide day-to-day customer service to agencies and our field marketing representatives by offering product training, answering underwriting questions, helping to determine underwriting eligibility and assisting with the mechanics of premium determination.

Our emphasis on small to midsized businesses is reflected in the mix of our commercial lines premium volume by policy size. Approximately 80 percent of our commercial in-force policies have annual premiums of $10,000 or less, accounting in total for approximately one-quarter of our 2014 commercial lines premium volume. The remainder of policies have annual premiums greater than $10,000, including in-force policies with annual premiums greater than $100,000 that account for approximately 17 percent of our 2014 commercial lines premium volume.

Our commercial lines packages typically are offered on a three-year policy term for most insurance coverages – a key competitive advantage. In our experience, multi-year packages appeal to the quality-conscious insurance buyers who we believe are typical clients of our independent agents. Customized insurance programs on a three-year term complement the long-term relationships these policyholders typically have with their agents and with the company. By reducing annual administrative efforts, multi-year policies lower expenses for our company and for our agents. The commitment we make to policyholders encourages long-term relationships and reduces their need to annually re-evaluate their insurance carrier or agency. We believe that the advantages of three-year policies in terms of improved policyholder convenience, increased account retention and reduced administrative costs outweigh the potential disadvantage of these policies, even in periods of rising rates.

Although we offer three-year policy terms, premiums for some coverages within those policies are adjustable at anniversary for the next annual period, and policies may be canceled at any time at the discretion of the policyholder. Contract terms often provide that rates for property, general liability, inland marine and crime coverages, as well as policy terms and conditions, are fixed for the term of the policy. However, the exposure we insure is reviewed annually, near the policy anniversary date, and the amount of premiums may be adjusted based on changes to that exposure.

The general liability exposure basis may be audited annually. Commercial auto, workers’ compensation, professional liability and most umbrella liability coverages within multi-year packages are rated at each of the policy's annual anniversaries for the next one-year period. The annual pricing could incorporate rate changes approved by state insurance regulatory authorities between the date the policy was written and its annual anniversary date, as well as changes in risk exposures and premium credits or debits relating to loss experience and other underwriting judgment factors. We estimate that approximately 75 percent of 2014 commercial premiums were subject to annual rating or were written on a one-year policy term.

We believe our commercial lines insurance segment premiums reflect a higher concentration, relative to industry commercial lines premiums, in contractor-related businesses. Since economic activity related to construction, which can heavily influence insured exposures of contractors, may experience cycles that vary significantly with the economy as a whole, our commercial lines premium trends could vary from commercial lines premium trends for the property casualty insurance industry. In 2014, we estimated that policyholders with a contractor-related Insurance Services Office (ISO) general liability code accounted for approximately 36 percent of our general liability premiums, which are included in the commercial casualty line of business, and that policyholders with a contractor-related National Council on Compensation Insurance Inc. (NCCI) workers' compensation code accounted for approximately 50 percent of our workers' compensation premiums.

Understanding evolving market conditions is a critical function for our success, accomplished in both an informal commentary and a formal manner. Informally, our field marketing representatives, underwriters and Target Markets department associates routinely receive market intelligence from a variety of channels, including from the agencies with which they work. This market information helps identify the top competitors by line of business or specialty program and also identifies our market strengths and weaknesses. The information obtained encompasses pricing, breadth of coverage and underwriting/eligibility issues.

In addition to reviewing our competitive position, our product management group and our underwriting audit group review compliance with our underwriting standards as well as the pricing adequacy of our commercial insurance programs and coverages. Further, our Target Markets department analyzes opportunities and develops new products and services, new coverage options and improvements to existing insurance products.

We support our commercial lines operations with a variety of technology tools. At the end of 2014, e-CLAS CPP for commercial package and auto coverages was available to all of our appointed agencies in 36 states, and in 14 states for workers' compensation that represent approximately 75 percent of our workers' compensation premium volume. It is being developed for additional coverages and remaining states that will be deployed over time. In addition to increasing efficiency for our associates, the system allows our agencies options to quote and produce commercial package policies in paper or electronic format from their offices and to bill policies through their agencies or through us. These features increase their ease of doing business with us. The e-CLAS platform also makes use of our real-time agency interface, CinciBridge®, which allows the automated movement of key underwriting data from an agency's management system to e-CLAS. This reduces agents' data entry tasks and allows seamless quoting, rating and issuance capability.

Personal Lines Insurance Segment

The personal lines insurance segment contributed net earned premiums of $1.041 billion to consolidated total revenues, or 21.1 percent of the total, and reported profit before income taxes of $10 million in 2014. Personal lines net earned premiums rose 8 percent in 2014 and 11 percent in 2013.

We prefer to write personal lines coverage in accounts that include both auto and homeowner coverages as well as coverages that are part of our other personal business line. At the end of 2014, for example, 81 percent of our homeowner policies were accompanied by a personal auto policy in the same account. As a result of our account-based approach, we believe that our personal lines business is best measured and evaluated on a segment basis. However, we provide line of business data to summarize growth and profitability trends separately for three business lines:

- Personal auto – Protects against liability to others for both bodily injury and property damage, medical payments to insureds and occupants of their vehicle, physical damage to an insured's own vehicle from collision and various other perils, and damages caused by uninsured motorists. In addition, many states require policies to provide first-party personal injury protection, frequently referred to as no-fault coverage.
- Homeowner – Protects against losses to dwellings and contents from a wide variety of perils, as well as liability arising out of personal activities both on and off the covered premises. We also offer coverage for condominium unit owners and renters.
- Other personal lines – This includes the variety of other types of insurance products we offer to individuals such as dwelling fire, inland marine, personal umbrella liability and watercraft coverages.

At year-end, we marketed personal lines insurance products through 1,391 or approximately 75 percent of our 1,884 reporting agency locations. The 1,391 personal lines agency locations are in 31 of the 39 states in which we offer standard market commercial lines insurance. Those agencies produced over 1.1 million personal lines policies in force for The Cincinnati Insurance companies, representing approximately 450,000 policyholders. We continue to evaluate opportunities to expand our marketing of personal lines to other states. Primary factors considered in the evaluation of a potential new state include market opportunity or potential, weather-related catastrophe history and the legal climate.

As discussed in Strategic Initiatives, we are also expanding the marketing of our personal lines insurance segment through independent agencies to profitably grow our premiums for products and services to their high net worth personal lines clients. At year-end 2014, our appointed agencies produced for us more than $100 million in annual premiums of policyholders with insured home values of $1 million or more. We estimate those policyholders represent approximately 3 percent of our total personal lines policyholders. Our plans to further develop products and services for high net worth policyholders are discussed in Strategic Initiatives.

In 2014, our 10 highest volume personal lines states generated 79.1 percent of our earned premiums compared with 79.6 percent in 2013 and 80.6 percent in 2012. Earned premiums in the four highest volume states increased 4 percent in 2014 while increasing 13 percent in the remaining states, reflecting progress toward our long-term objective of geographic diversification through new states for our personal lines operation. The aggregate number of reporting agency locations in our 10 highest volume states at 875 in 2014 essentially matched the 874 in 2013.

Our 10 highest premium volume personal lines states are shown in the table below.

(Dollars in millions)	Earned premiums	% of total earned	Agency locations	Average premium per location
Year ended December 31, 2014				
Ohio	$288	27.6 %	219	$1.3
Georgia	84	8.1	84	1.0
Indiana	77	7.4	90	0.9
Illinois	69	6.6	97	0.7
Michigan	65	6.2	114	0.6
Alabama	56	5.4	44	1.3
North Carolina	55	5.3	82	0.7
Kentucky	52	5.0	38	1.4
Tennessee	41	3.9	53	0.8
Minnesota	37	3.6	54	0.7

New and renewal personal lines business reflects our risk-specific underwriting philosophy. Each agency selects personal lines business primarily from within the geographic territory that it serves, based in part on agency staff's knowledge of the risks in those communities or familiarity with the policyholder. Personal lines activities are supported by headquarters associates assigned to individual agencies. At year-end 2014, we had nine full-time personal lines field marketing representatives who have underwriting authority and visit agencies on a regular basis. They focus primarily on key states targeted for growth, reinforcing the advantages of our personal lines products and offering training in the use of our processing system.

All of our personal lines policies are written for a one-year term. Competitive advantages of our personal lines operation include broad coverage forms, flexible underwriting, superior claims service and endorsements allowing customization of coverage for both personal auto and homeowner policies. Our personal lines products are processed through Diamond, our Web-based, real-time personal lines policy processing system that supports streamlined processing. Diamond incorporates features frequently requested by our agencies such as prefilling of selected data for improved efficiency, easy-to-use navigation, local and headquarters policy printing options, data transfer to and from popular agency management systems and real-time integration with third-party data such as insurance scores, motor vehicle reports and address verification.

Excess and Surplus Lines Insurance Segment
The excess and surplus lines segment contributed net earned premiums of $148 million to consolidated total revenues, or 3.0 percent of the total, and reported profit before income taxes of $30 million in 2014, its seventh year of operation. Excess and surplus lines net earned premium increased 28 percent in 2014 and 25 percent in 2013.

Our excess and surplus lines policies typically cover business risks with unique characteristics, such as the nature of the business or its claim history, that are difficult to profitably insure in the standard commercial lines market. Excess and surplus lines insurers have more flexibility in coverage terms and rates compared with standard lines companies, generally resulting in policies with higher rates and terms and conditions customized for specific risks, including restricted coverage where appropriate. We target small to midsized risks, seeking to avoid those we consider exotic in nature. Our average excess and surplus lines policy size is approximately $6,000 in annual premiums, and policyholders in many cases also have standard market insurance with one of our other subsidiaries. All of our excess and surplus lines policies are written for a maximum term of one year. Approximately 87 percent of our 2014 premium volume for the excess and surplus lines insurance segment provided commercial casualty coverages and about 13 percent provided commercial property coverages. Those coverages are described below.

- Commercial casualty – Covers businesses for third-party liability from accidents occurring on their premises or arising out of their operations, including products and completed operations. The majority of these policies have coverage limits of $1 million or less. Miscellaneous errors and omissions and professional coverage for liability from actual or alleged errors in judgment, breaches of duty or other wrongful acts related to activities of insured businesses is also available, as is excess liability coverage that adds another layer of protection to the insured's other liability insurance policies. Typical businesses covered include contractors, manufacturers, real estate owners and managers, retail, consultants, and bars or taverns. Policies covering liability at special events are also available.
- Commercial property – Insures buildings, inventory, equipment and business income from loss or damage due to causes such as fire, wind, hail, water, theft and vandalism. Examples of property we commonly insure with excess and surplus lines policies include temporarily vacant buildings, habitational, restaurants and relatively higher-hazard manufacturing classes.

At the end of 2014, we marketed excess and surplus lines insurance products in each of the 39 states in which we offer standard market commercial lines insurance. Offering excess and surplus lines helps agencies representing The Cincinnati Insurance Companies meet the insurance needs of their clients when coverage is unavailable in the standard market. By providing outstanding service, we can help agencies grow and prosper while also profitably growing our property casualty business.

In 2014, our 10 highest volume excess and surplus lines states generated 60.5 percent of our earned premiums compared with 61.9 percent in 2013 and 62.2 percent in 2012.

Our 10 highest premium volume excess and surplus lines states are shown in the table below.

(Dollars in millions)	Earned premiums	% of total earned	
Year ended December 31, 2014			
Ohio	$14	9.5	%
Texas	13	8.7	
Indiana	11	7.5	
Illinois	10	6.8	
Georgia	10	6.6	
Alabama	8	5.2	
Missouri	7	4.6	
Michigan	6	4.1	
North Carolina	6	4.0	

Pennsylvania	5	3.5

Agencies representing The Cincinnati Insurance Companies produce approximately $3 billion in annual premiums for all carriers writing excess and surplus lines policies for their clients. We estimate that approximately half of that premium volume matches the targeted business types and coverages we offer through our excess and surplus lines insurance segment. We structured the operations of this segment to meet the needs of these agencies and to market exclusively through them.

Agencies have access to Cincinnati Specialty Underwriters' product line through CSU Producer Resources, the wholly owned insurance brokerage subsidiary of Cincinnati Financial Corporation. CSU Producer Resources has binding authority on all classes of business written through Cincinnati Specialty Underwriters and maintains appropriate agent and surplus lines licenses to process nonadmitted business.

We seek to earn a share of each agency’s best excess and surplus lines accounts by offering several unique benefits. Agency producers have direct access through CSU Producer Resources to a group of our underwriters who focus exclusively on excess and surplus lines business. Those underwriters can tap into broader Cincinnati services to provide policyholders additional value and help agents build the relationship through experienced and responsive loss control services and claims handling. CSU Producer Resources gives extra support to our independent agency producers by remitting surplus lines taxes and stamping fees and retaining admitted market diligent search affidavits, where required. Agencies marketing through CSU Producer Resources instead of a competing brokerage generally receive a higher commission because use of our internal brokerage subsidiary eliminates some of the intermediary costs. This business is factored in their profit-sharing agreement with The Cincinnati Insurance Companies.

We use a Web-based excess and surplus lines policy administration system to quote, bind, issue and deliver policies electronically to agents. This system provides integration to existing document management and data management systems, allowing for expedited processing of policies and billing. It provides a specimen policy detailing coverages when a policy is quoted and delivers electronic copies of policies to independent agency producers within minutes of underwriting approval and policy issue. In 2014, more than 95 percent of policies were issued within 24 hours of a request to bind a policy.

Life Insurance Segment

The life insurance segment contributed $198 million of net earned premiums, representing 4.0 percent of consolidated total revenues, and negative $5 million of income before income taxes in 2014. Life insurance net earned premiums grew 5 percent in 2014 and 6 percent in 2013.

The Cincinnati Life Insurance Company supports our agency-centered business model. Cincinnati Life helps meet the needs of our agencies, including increasing and diversifying agency revenues. We primarily focus on life products that feature a steady stream of premium payments and that have the potential for generating revenue growth through increasing demand. By diversifying revenue and profitability for both the agency and our company, this strategy enhances the already strong relationship built by the combination of the property casualty and life companies.

Life Insurance Business Lines

Four lines of business – term life insurance, universal life insurance, worksite products and whole life insurance – account for 95.3 percent of the life insurance segment’s revenues:

- Term life insurance – Policies under which a death benefit is payable only if the insured dies during a specific period of time. For policies without a return of premium provision, no benefit is payable if the insured person survives to the end of the term. For policies in force with a return of premium provision, a benefit equal to the sum of all paid base premiums is payable if the insured person survives to the end of the term. Premiums are fixed, and they must be paid as scheduled. The policies are fully underwritten.
- Universal life insurance – Long-duration life insurance policies. Contract premiums are neither fixed nor guaranteed; however, the contract does specify a minimum interest crediting rate and a maximum cost of insurance charge and

expense charge. Premiums may be varied by the contract owner. The cash values, available as a loan collateralized by the cash surrender value, are not guaranteed and depend on the amount and timing of actual premium payments and the amount of actual contract assessments. The policies are fully underwritten.

- Worksite products – Term life insurance, return of premium term life insurance, whole life insurance, universal life and disability insurance offered to employees through their employer. Premiums are collected by the employer using payroll deduction. Policies are issued using a simplified underwriting approach and on a guaranteed issue basis. Worksite insurance products provide our property casualty agency force with excellent cross-serving opportunities for both commercial and personal accounts. Agents report that offering worksite marketing to employees of their commercial accounts provides a benefit to the employees at no cost to the employer. Worksite marketing also connects agents with new customers who may not have previously benefited from receiving the services of a professional independent insurance agent.
- Whole life insurance – Policies that provide life insurance for the entire lifetime of the insured. The death benefit is guaranteed never to decrease and premiums are guaranteed never to increase. While premiums are fixed, they must be paid as scheduled. These policies provide guaranteed cash values that are available as loans collateralized by the cash surrender value. The policies are fully underwritten.

In addition, Cincinnati Life markets:

- Disability income insurance that provides monthly benefits to offset the loss of income when the insured person is unable to work due to accident or illness.
- Deferred annuities that provide regular income payments that commence after the end of a specified period or when the annuitant attains a specified age. During the deferral period, any payments made under the contract accumulate at the crediting rate declared by the company but not less than a contract-specified guaranteed minimum interest rate. A deferred annuity may be surrendered during the deferral period for a cash value equal to the accumulated payments plus interest less the surrender charge, if any.
- Immediate annuities that provide some combination of regular income and lump-sum payments in exchange for a single premium.

Life Insurance Distribution

Our life insurance subsidiary is licensed in 49 states and the District of Columbia. At year-end 2014, almost 88 percent of our 1,844 property casualty agency reporting locations offered Cincinnati Life products to their clients. We also develop life business from approximately 620 other independent life insurance agencies. We are careful to solicit business from these other agencies in a manner that does not conflict with or compete with the marketing and sales efforts of our property casualty agencies.

When marketing through our property casualty agencies, we have specific competitive advantages:

- Because our property casualty operations are held in high regard, property casualty agency management is predisposed to consider selling our life products.
- Marketing efforts for both our property casualty and life insurance businesses are directed by our field marketing department, which assures consistency of communication and operations. Life field marketing representatives are available to meet face-to-face with agency personnel and their clients as well.
- Our life headquarters underwriters and other associates are available to the agents and field team to assist in the placement of business. Fewer and fewer of our competitors provide direct, personal support between the agent and the insurance carrier.

We continue to emphasize the cross-serving opportunities of our life insurance, including term and worksite products, for the property casualty agency's personal and commercial accounts. In both the property casualty and independent life agency distribution systems, we enjoy the advantages of offering competitive, up-to-date products, providing close personal attention in combination with financial strength and stability.

- Term life insurance is our largest life insurance product line. We continue to introduce new term products with features our agents indicate are important, such as a return of premium benefit.
- We also offer products addressing the needs of businesses with key person and buy-sell coverages. We offer quality, personal life insurance coverage to personal and commercial clients of our agencies.

Because of our strong capital position, we can offer a competitive product portfolio including guaranteed products, giving our agents a marketing edge. Our life insurance company maintains strong insurer financial strength ratings: A.M. Best, A (Excellent); Fitch, A+ (Strong); and Standard & Poor's A (Strong); as discussed in Financial Strength. Our life insurance company has chosen not to establish a Moody's rating.

In 2014, our five highest volume states for life insurance premiums, based on information contained in statements filed with state insurance departments, are reflected in the table below.

(Dollars in millions)	Premiums	% of total earned	
Year ended December 31, 2014			
Ohio	$48	18.6	%
Pennsylvania	19	7.2	
Indiana	17	6.5	
Illinois	16	6.4	
Georgia	13	5.1	

Investments Segment

Revenues of the investments segment are primarily from net investment income and from realized investment gains and losses from investment portfolios managed for the holding company and each of the operating subsidiaries.

Our investment department operates under guidelines set forth in our investment policy statement along with oversight of the investment committee of our board of directors. These guidelines set parameters for risk tolerances governing, among other items, the allocation of the portfolio as well as security and sector concentrations. These parameters are part of an integrated corporate risk management program.

The fair value of our investment portfolio was $14.318 billion and $13.496 billion at year-end 2014 and 2013, respectively, as shown in the table below. The overall portfolio remained in an unrealized gain position as equity markets experienced solid returns in 2014, and the gain position for our fixed-maturity investments rose modestly due to a general decline in interest rates.

(Dollars in millions)	At December 31, 2014				At December 31, 2013			
	Cost or amortized cost	Percent of total	Fair value	Percent of total	Cost or amortized cost	Percent of total	Fair value	Percent of total
Taxable fixed maturities	$5,882	50.7 %	$6,330	44.2 %	$5,814	52.1 %	$6,211	46.0 %
Tax-exempt fixed maturities	2,989	25.8	3,130	21.9 %	2,824	25.3	2,910	21.6
Common equity securities	2,583	22.3	4,679	32.7 %	2,396	21.5	4,213	31.2
Nonredeemable preferred equity securities	145	1.2	179	1.2 %	127	1.1	162	1.2
Total	$11,599	100.0 %	$14,318	100.0 %	$11,161	100.0 %	$13,496	100.0 %

The cash we generate from insurance operations historically has been invested in two broad categories of investments:

- Fixed-maturity investments – Includes taxable and tax-exempt bonds and redeemable preferred stocks. During 2014, purchases and market value gains offset sales and calls. During 2013, purchases were largely offset by redemptions and fair value declines.
- Equity investments – Includes common and nonredeemable preferred stocks. During both 2014 and 2013, purchases and fair value gains offset sales by relatively large amounts.

When allocating cash to various asset classes, we consider market-based factors such as risk adjusted after-tax yields as well as internal measures based in part on insurance department regulations and rating agency guidance. During 2014, approximately one-fifth of net purchases were equity securities. We monitor a variety of metrics, including after-tax yields, the ratio of investments in common stocks to statutory capital and surplus for the property casualty insurance operations, and the parent company’s ratio of investment assets to total assets.

At year-end 2014, less than 1 percent of the value of our investment portfolio was made up of securities that are classified as Level 3 assets and that require management’s judgment to develop pricing or valuation techniques. We generally obtain at least two outside valuations for these assets and generally use the more conservative estimate. These investments include private placements, small issues and various thinly traded securities. See Item 7, Critical Accounting Estimates, Fair Value Measurements, and Item 8, Note 3 of the Consolidated Financial Statements, for additional discussion of our valuation techniques.

In addition to securities held in our investment portfolio, at year-end 2014, other invested assets included $31 million of life policy loans and $37 million of private equity investments.

Our investment portfolio is further described below. Additional information about the composition of investments is included in Item 8, Note 2 of the Consolidated Financial Statements. A detailed listing of our portfolio is updated on our website, cinfin.com/investors, each quarter when we report our quarterly financial results.

Fixed-Maturity Securities Investments
By maintaining a well-diversified fixed-maturity portfolio, we attempt to manage overall interest rate, reinvestment, credit and liquidity risk. We pursue a buy-and-hold strategy and do not attempt to make large-scale changes to the portfolio in anticipation of rate movements. By investing new money on a regular basis and analyzing risk-adjusted after-tax yields, we work to achieve a laddering effect to our portfolio that may mitigate some of the effects of adverse interest rate movements.

Fixed-Maturity Portfolio Ratings
At year-end 2014, this portfolio's fair value was 106.6 percent of amortized cost, up from 105.6 percent a year ago as a result of a general decline in interest rates.

The portfolio's fair value rose in 2014 as an interest-rate driven increase in bond prices added to net purchases that were most heavily concentrated in municipal bonds and commercial mortgage backed securities. Our nonrated securities include smaller municipal issues and private placement corporate securities. Many of these, although not rated by Moody's or Standard & Poor's, are rated by the NAIC's Securities' Valuation Office. Also included in this category are smaller public corporate securities, many of which carry a rating by an agency other than Moody's or S&P, such as Fitch or Kroll. Credit ratings at year-end 2014 and 2013 for the fixed-maturity portfolio were:

(Dollars in millions)	At December 31, 2014			At December 31, 2013		
	Fair value	Percent of total		Fair value	Percent of total	
Combined ratings from Moody's and Standard & Poor's:						
Aaa, Aa, A, AAA, AA, A	$5,686	60.1	%	$5,468	59.9	%
Baa, BBB	3,198	33.8		3,197	35.1	
Ba, BB	305	3.2		231	2.5	
B, B	15	0.2		16	0.2	
Caa, CCC	3	0.0		4	0.0	
Nonrated	253	2.7		205	2.3	
Total	$9,460	100.0	%	$9,121	100.0	%

Other selected attributes of the fixed-maturity portfolio are shown in the table below. Additional maturity periods and other information for our fixed-maturity portfolio are shown in Item 8, Note 2 of the Consolidated Financial Statements.

	At December 31,			
	2014		2013	
Weighted average yield-to-amortized cost	4.76	%	4.86	%
Weighted average maturity	6.4	yrs	6.2	yrs
Effective duration	4.4	yrs	4.5	yrs

Taxable Fixed Maturities

The fair values of our taxable fixed-maturity securities portfolio at the end of the last two years were:

(Dollars in millions)	At December 31,	
	2014	2013
Investment-grade corporate	$5,208	$5,293
States, municipalities and political subdivisions	313	301
Below investment-grade corporate	318	240
Commercial mortgage backed	259	143
Government sponsored enterprises	208	200
Foreign government	10	10
Convertibles and bonds with warrants attached	7	17
United States government	7	7
Total	$6,330	$6,211

While our strategy typically is to buy and hold fixed-maturity investments to maturity, we monitor credit profiles and fair value movements when determining holding periods for individual securities. With the exception of U.S. agency issues, no individual issuer's securities accounted for more than 1.0 percent of the taxable fixed-maturity portfolio at year-end 2014. Investment grade corporate bonds had an average rating of Baa1 by Moody’s or BBB+ by Standard & Poor’s and represented 82.3 percent of the taxable fixed-maturity portfolio’s fair value at year end 2014, compared with 85.2 percent in 2013.

The investment-grade corporate bond portfolio is most heavily concentrated in the financial-related sectors, including banking, financial services and insurance. The financial sectors represented 36.9 percent of fair value of this portfolio at year-end 2014, compared with 32.8 percent, at year-end 2013. Although the financial-related sectors make up our largest group of investment-grade corporate bonds, we believe our concentration is below the average for the corporate bond market as a whole. The real estate sector, including commercial mortgage back securities, accounted for 13.5 percent. No other sector exceeded 10 percent of our investment-grade corporate bond portfolio at year-end 2014.

Most of the $313 million of securities issued by states, municipalities and political subdivisions included in our taxable fixed-maturity portfolio at the end of 2014 were Build America Bonds.

Tax-Exempt Fixed Maturities

Our tax-exempt fixed-maturity securities portfolio's fair value was $3.130 billion at December 31, 2014. The portfolio is well diversified among more than 1,500 municipal bond issues. No single municipal issuer accounted for more than 0.8 percent of the tax-exempt fixed-maturity portfolio at year-end 2014. Our largest municipal bond holdings were in these states:

(Dollars in millions) At December 31, 2014	Local issued general obligation bonds	Special revenue bonds	State issued general obligation bonds	Fair value total	Percent of total	
Texas	$368	$71	$—	$439	14.0	%
Indiana	2	244	—	246	7.9	
Ohio	120	78	9	207	6.6	
Michigan	194	8	—	202	6.5	
Washington	127	30	7	164	5.2	
Illinois	146	18	—	164	5.2	
Arizona	78	47	—	125	4.0	
Wisconsin	87	30	2	119	3.8	
Pennsylvania	83	15	10	108	3.5	
Florida	26	74	—	100	3.2	
New York	59	36	4	99	3.2	
New Jersey	55	15	2	72	2.3	
Kansas	51	21	—	72	2.3	
Colorado	44	25	—	69	2.2	
California	40	19	3	62	2.0	
All other states	493	337	52	882	28.1	
Total	$1,973	$1,068	$89	$3,130	100.0	%
At December 31, 2013						
Texas	$385	$66	$—	$451	15.5	%
Michigan	238	9	—	247	8.5	
Indiana	8	232	—	240	8.2	
Ohio	119	87	6	212	7.3	
Illinois	184	19	—	203	7.0	
Washington	150	32	5	187	6.4	
Wisconsin	108	32	2	142	4.9	
Pennsylvania	93	9	9	111	3.8	
Arizona	55	31	—	86	3.0	
Florida	24	62	—	86	3.0	
New York	48	31	4	83	2.9	
Colorado	45	17	—	62	2.1	
New Jersey	44	17	—	61	2.1	
Minnesota	42	7	2	51	1.8	
Utah	31	19	—	50	1.7	
All other states	338	270	30	638	21.8	
Total	$1,912	$940	$58	$2,910	100.0	%

At year-end 2014, our tax-exempt fixed-maturity portfolio had an average rating of Aa2/AA. Over 43 percent or $1.368 billion of the portfolio is insured, and approximately 98 percent of the portfolio has an underlying rating of at least A3 or A- by Moody's or Standard & Poor's at year end. We strongly prefer general obligation or essential services bonds, which we believe provide a superior risk profile. The top three revenue resources of the $1.068 billion in special revenue bonds owned at year-end 2014 were 33 percent from leasing, 25 percent from water and sewer and 8 percent from higher education.

Equity Securities Investments
After covering both our intermediate and long-range insurance obligations with fixed-maturity investments, we historically have used available cash flow to invest in equity securities. Investment in equity securities has played an important role in achieving our portfolio objectives and has contributed to portfolio appreciation. We remain committed to our long-term equity focus, which we believe is key to our company's long-term growth and stability.

Common Stocks
Our cash allocation for common stock purchases is implemented only after we ensure that our insurance reserves are adequately covered by our fixed-maturity investments. We believe our strategy of primarily investing in a diversified selection of larger-capitalization, high-quality, dividend-increasing companies generally results in reduced volatility relative to the broader equity markets.

At year-end 2014 and 2013, no holding had a fair value greater than 3.3 percent of our publicly traded common stock portfolio. Apple Inc. (Nasdaq:AAPL) was our largest single common stock investment at year end 2014, comprising 3.3 percent of the publicly traded common stock portfolio and 1.1 percent of the entire investment portfolio.

At year-end 2014, 35.0 percent of our common stock holdings (measured by fair value) were held at the parent-company level. The distribution of the portfolio among industry sectors is shown in the table below.

Common Stock Portfolio Industry Sector Distribution

	Percent of publicly traded common stock portfolio							
	At December 31, 2014				At December 31, 2013			
	Cincinnati Financial		S&P 500 Industry Weightings		Cincinnati Financial		S&P 500 Industry Weightings	
Sector:								
Information technology	17.3	%	19.8	%	18.7	%	18.6	%
Industrials	14.3		10.3		14.0		10.9	
Financial	13.8		16.3		12.0		16.2	
Healthcare	11.9		14.7		11.5		13.0	
Energy	10.5		8.0		10.5		10.3	
Consumer staples	10.5		10.0		10.5		9.8	
Consumer discretionary	10.2		12.1		9.8		12.5	
Materials	5.5		3.2		5.7		3.5	
Utilities	3.7		3.3		4.2		2.9	
Telecomm services	2.3		2.3		3.1		2.3	
Total	100.0	%	100.0	%	100.0	%	100.0	%

Nonredeemable Preferred Stocks
We evaluate nonredeemable preferred stocks in a manner similar to our evaluation of fixed-maturity investments, seeking attractive relative yields. We generally focus on investment-grade nonredeemable preferred stocks issued by companies with strong histories of paying common dividends, providing us with another layer of protection. When possible, we seek out nonredeemable preferred stocks that offer a dividend received deduction for income tax purposes. We purchased $20 million and sold $2 million in this portfolio in 2014. During 2013, we purchased $48 million and sold $23 million.

Other

We report as Other the noninvestment operations of the parent company and its noninsurer subsidiary CFC Investment Company. This subsidiary offers commercial leasing and financing services to our agencies, their clients and other customers. At year-end 2014, CFC Investment Company had 2,141 accounts and $75 million in receivables, compared with 2,516 accounts and $85 million in receivables at year-end 2013.

Regulation
The business of insurance primarily is regulated by state law. All of our insurance company subsidiaries are domiciled in the state of Ohio except The Cincinnati Specialty Underwriters Insurance Company, which is domiciled in Delaware. Each insurance subsidiary is governed by the insurance laws and regulations in its respective state of domicile. We also are subject to state regulatory authorities of all states in which we write insurance. The state laws and regulations that have the most significant effect on our insurance operations and financial reporting are discussed below.

- Insurance Holding Company Regulation – We are regulated as an insurance holding company system in the respective states of domicile of our primary standard market property casualty company subsidiary and its surplus lines and life insurance subsidiaries. These regulations require that we annually furnish financial and other information about the operations of the individual companies within the holding company system. All transactions within a holding company affecting insurers must be fair and equitable. Notice to the state insurance commissioner is required prior to the consummation of transactions affecting the ownership or control of an insurer and prior to certain material transactions between an insurer and any person or entity in its holding company group. In addition, some of those transactions cannot be consummated without the commissioner's prior approval. Recent amendments to the Model Insurance Holding Company System Regulatory Act and Regulation, adopted by the National Association of Insurance Commissioners (NAIC) and passed by a number of state legislatures, require insurance holding company systems to provide regulators with more information about the risks posed by any noninsurance company subsidiaries in the holding company system.
- Subsidiary Dividends – The Cincinnati Insurance Company is 100 percent owned by Cincinnati Financial Corporation. The dividend-paying capacity of The Cincinnati Insurance Company and its 100 percent owned subsidiaries is regulated by the laws of the applicable state of domicile. Under these laws, our insurance subsidiaries must provide a 10-day advance informational notice to the insurance commissioner for the domiciliary state prior to payment of any dividend or distribution to its shareholders. Generally, the most our insurance subsidiary can pay without prior regulatory approval is the greater of 10 percent of statutory capital and surplus or 100 percent of statutory net income for the prior calendar year.

The insurance company subsidiaries must give 30 days' notice to and obtain prior approval from the state insurance commissioner before the payment of an extraordinary dividend as defined by the state's insurance code. You can find information about the dividends paid by our insurance subsidiary in 2014 in Item 8, Note 9 of the Consolidated Financial Statements.

- Insurance Operations – All of our insurance subsidiaries are subject to licensing and supervision by departments of insurance in the states in which they do business. The nature and extent of such regulations vary, but generally are rooted in statutes that delegate regulatory, supervisory and administrative powers to state insurance departments. Such regulations, supervision and administration of the insurance subsidiaries include, among others, the standards of solvency that must be met and maintained; the licensing of insurers and their agents and brokers; the nature and limitations on investments; deposits of securities for the benefit of policyholders; regulation of standard market policy forms and premium rates; policy cancellations and nonrenewals; periodic examination of the affairs of insurance companies; annual and other reports required to be filed on the financial condition of insurers or for other purposes; requirements regarding reserves for unearned premiums, losses and other matters; the nature of and limitations on dividends to policyholders and shareholders; the nature and extent of required participation in insurance guaranty funds; the involuntary assumption of hard-to-place or high-risk insurance business, primarily workers' compensation insurance; and the collection, remittance and reporting of certain taxes and fees. Our primary insurance regulators have adopted the Model Audit Rule for annual statutory financial reporting. This regulation closely mirrors the Sarbanes-Oxley Act on matters such as auditor independence, corporate governance and internal controls over financial reporting. The regulation permits the audit committee of Cincinnati Financial Corporation's board of directors to also serve as the audit committee of each of our insurance subsidiaries for purposes of this regulation.
- Insurance Guaranty Associations – Each state has insurance guaranty association laws under which the associations may assess life and property casualty insurers doing business in the state for certain obligations of insolvent insurance companies to policyholders and claimants. Typically, states assess each member insurer in an amount related to the

insurer's proportionate share of business written by all member insurers in the state. Our insurance companies received a savings of less than $1 million from guaranty association refunds in both 2014 and 2013. We cannot predict the amount and timing of any future assessments or refunds on our insurance subsidiaries under these laws.

- Shared Market and Joint Underwriting Plans – State insurance regulation requires insurers to participate in assigned risk plans, reinsurance facilities and joint underwriting associations, which are mechanisms that generally provide applicants with various basic insurance coverages when they are not available in voluntary markets. Such mechanisms are most commonly instituted for automobile and workers' compensation insurance, but many states also mandate participation in FAIR Plans or Windstorm Plans, which provide basic property coverages. Participation is based upon the amount of a company's voluntary market share in a particular state for the classes of insurance involved. Underwriting results related to these organizations could be adverse to our company.

- Statutory Accounting – For public reporting, insurance companies prepare financial statements in accordance with GAAP. However, certain data also must be calculated according to statutory accounting rules as defined in the NAIC's Accounting Practices and Procedures Manual. While not a substitute for any GAAP measure of performance, statutory data frequently is used by industry analysts and other recognized reporting sources to facilitate comparisons of the performance of insurance companies.
- Insurance Reserves – State insurance laws require that property casualty and life insurers annually analyze the adequacy of reserves. Our appointed actuaries must submit an opinion that reserves are adequate for policy claims-paying obligations and related expenses.
- Investment Regulation – Insurance company investments must comply with laws and regulations pertaining to the type, quality and concentration of investments. Such laws and regulations permit investments in federal, state and municipal obligations, corporate bonds, preferred and common equity securities, mortgage loans, real estate and certain other investments, subject to specified limits and other qualifications. At December 31, 2014, the company believes it was in compliance with these laws and regulations in all material respects.
- Risk-Based Capital Requirements – The NAIC's risk-based capital (RBC) requirements for property casualty and life insurers serve as an early warning tool for the NAIC and state regulators to identify companies that may be undercapitalized and may merit further regulatory action. The NAIC has a standard formula for annually assessing RBC. The formula for calculating RBC for property casualty companies takes into account asset and credit risks but places more emphasis on underwriting factors for reserving and pricing. The formula for calculating RBC for life insurance companies takes into account factors relating to insurance, business, asset and interest-rate risks.

Although the federal government and its regulatory agencies generally do not directly regulate the business of insurance, federal legislation and administrative rules adopted to implement them do affect our business. Privacy laws, such as the Gramm-Leach-Bliley Act, the Fair Credit Reporting Act and the Health Insurance Portability and Accounting Act (HIPAA) are the federal laws that most affect our day-to-day operations. These apply to us because we gather and use personal nonpublic information to underwrite insurance and process claims. We also are subject to other federal laws, such as the Terrorism Risk Insurance Act (TRIA), anti-money laundering statute (AML), the Nonadmitted and Reinsurance Reform Act (NRRA), and the rules and regulations of the Office of Foreign Assets Control (OFAC).

Title V of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) created the Federal Insurance Office to monitor the insurance industry and gather information to identify issues or gaps in the regulation of insurers that could contribute to a systemic crisis in the insurance industry of the United States financial system, and to recommend to the Financial Stability Oversight Council that it designate an insurer as a systemically significant entity requiring additional supervision by the Federal Reserve Board. We do not expect Dodd-Frank to result in federal oversight of our operations as a systemically significant entity.

We do not expect to have any material effects on our expenditures, earnings or competitive position as a result of compliance with any federal, state or local provisions enacted or adopted relating to the protection of the environment. We currently do not have any material estimated capital expenditures for environmental control facilities.

Enterprise Risk Management

We manage enterprise risk through formal risk management programs overseen by our chief risk officer, an executive officer of the company. Our ERM framework includes an enterprise risk management committee, which is responsible for overseeing risk activities and is comprised of senior executive-level risk owners from across the enterprise. The risk committee's activities are supported by a team of representatives from business areas that focus on identifying, evaluating and developing risk plans for emerging risks. A comprehensive report is provided quarterly to our chairman, our president and chief executive officer, our board of directors and our senior executive team, as appropriate, on the status of risk metrics relative to identified tolerances and limits, risk assessments and risk plans. Our use of operational audits, strategic plans and departmental business plans, as well as our culture of open communications and our fundamental respect for our Code of Conduct, continue to help us manage risks on an ongoing basis.

Our risk management programs include a formalized risk appetite element and a risk identification and quantification process. The overall enterprise objective is to appropriately balance risk and reward to achieve an appropriate return on risk capital. The company's key risks are discussed in Item 1A, Risk Factors, including risks related to natural catastrophes, investments and operations.

We continue to study emerging risks, including climate change risk and its potential financial effects on our results of operation and on those we insure. These effects include deterioration in credit quality of our municipal or corporate bond portfolios and increased losses without sufficient corresponding increases in premiums. As with any risk, we seek to identify the extent of the risk exposure and possible actions to mitigate potential negative effects of risk, at an enterprise level.

ITEM 1A. Risk Factors

Our business involves various risks and uncertainties that may affect achievement of our business objectives. Many of the risks could have ramifications across our organization. For example, while risks related to setting insurance rates and establishing and adjusting loss reserves are insurance activities, errors in these areas could have an impact on our investment activities, growth and overall results.

The following discussion should be viewed as a starting point for understanding the significant risks we face. It is not a definitive summary of their potential impacts or of our strategies to manage and control the risks. Please see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, for a discussion of those strategies.

If any risks or uncertainties discussed here develop into actual events, they could have a material adverse effect on our business, financial condition or results of operations. In that case, the market price of our common stock could decline materially. The failure of our risk management strategies could have a material adverse impact on our financial condition and/or results of operations.

Readers should carefully consider this information together with the other information we have provided in this report and in other reports and materials we file periodically with the Securities and Exchange Commission as well as news releases and other information we disseminate publicly.

We rely exclusively on independent insurance agents to distribute our products.

We market our products through independent, nonexclusive insurance agents. These agents are not obligated to promote our products and can and do sell our competitors' products. We must offer insurance products that meet the needs of these agencies and their clients. We need to maintain good relationships with the agencies that market our products. If we do not, these agencies may market our competitors' products instead of ours, which may lead to us having a less desirable mix of business and could affect our results of operations.

Certain events or conditions could diminish our agents' desire to produce business for us and the competitive advantage that our independent agencies enjoy, including:

- Downgrade of the financial strength ratings of our insurance subsidiaries. We believe our strong insurer financial strength ratings, in particular, the A+ (Superior) ratings from A.M. Best for our standard market property casualty insurance group and each subsidiary in that group, are an important competitive advantage. See Item 1, Our Business and Our Strategy, Financial Strength, for additional discussion of our financial strength ratings.
- Concerns that doing business with us is difficult or not profitable, perceptions that our level of service is no longer a distinguishing characteristic in the marketplace, perceptions that our products do not meet the needs of our agents' clients or perceptions that our business practices are not compatible with agents' business models.
- Mergers and acquisitions could result in a concentration of a significant amount of premium in one agency.
- Delays in the development, implementation, performance and benefits of technology systems and enhancements or independent agent perceptions that our technology solutions do not match their needs.

A reduction in the number of independent agencies marketing our products, the failure of agencies to successfully market our products or pay their accounts to us, changes in the strategy or operations of agencies or the choice of agencies to reduce their writings of our products could affect our results of operations if we were unable to replace them with agencies that produce adequate and profitable premiums.

Further, policyholders may choose a competitor's product rather than our own because of real or perceived differences in price, terms and conditions, coverage or service. If the quality of the independent agencies with which we do business were to decline, that also might cause policyholders to purchase their insurance through different agencies or channels. Consumers, especially in the personal insurance industry segment, may increasingly choose to purchase insurance from distribution channels other than independent insurance agents, such as direct marketers. Increased advertising by insurers, especially direct marketers, could cause consumers to shift their buying habits, bypassing independent agents altogether.

Our credit ratings or financial strength ratings of our insurance subsidiaries could be downgraded.
A downgrade in one or more of our company’s credit or debt ratings could adversely impact our borrowing costs or limit our access to capital. Financial strength ratings reflect a rating agency’s opinion of our insurance subsidiaries’

financial strength, operating performance, strategic position and ability to meet obligations to policyholders. Our ratings are subject to periodic review and there is no assurance that our ratings will not be changed. Ratings agencies could change or expand their requirements or could find that our insurance subsidiaries no longer meet the criteria established for current ratings. If our property casualty insurer financial strength ratings were to be downgraded, our agents might find it more difficult to market our products or might choose to emphasize the products of other carriers. See Item 7, Liquidity and Capital Resources, Additional Sources of Liquidity, for additional discussion of ratings for our long-term debt.

We could experience an unusually high level of losses due to catastrophic, terrorism or pandemic events or risk concentrations.
In the normal course of our business, we provide coverage against perils for which estimates of losses are highly uncertain, in particular catastrophic and terrorism events. Catastrophes can be caused by a number of events, including hurricanes, tornadoes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Due to the nature of these events, we are unable to predict precisely the frequency or potential cost of catastrophe occurrences. Various scientists and other experts believe that changing climate conditions have added to the unpredictability, frequency and severity of such natural disasters in certain parts of the world and have created additional uncertainty as to future trends and exposures. We cannot predict the impact that changing climate conditions may have on our results of operations nor can we predict how any legal, regulatory or social responses to concerns about climate change may impact our business. Additionally, man-made events, such as hydraulic fracturing, could cause damage from earth movement or create environmental and/or health hazards.

The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Our ability to appropriately manage catastrophe risk depends partially on catastrophe models, which may be affected by inaccurate or incomplete data, the uncertainty of the frequency and severity of future events and the uncertain impact of climate change. Additionally, these models are recalibrated and changed over time, with more data availability and changing opinions regarding the effect of current or emerging loss patterns and conditions. Please see Item 7, Liquidity and Capital Resources, 2015 Reinsurance Programs, for a discussion of modeled losses considered in evaluating our reinsurance strategy.

The geographic regions in which we market insurance are exposed to numerous natural catastrophes, such as:
- Hurricanes in the gulf, eastern and southeastern coastal regions.
- Earthquakes in many regions, most particularly in the New Madrid fault zone, which lies within the central Mississippi valley, extending from northeast Arkansas through southeast Missouri, western Tennessee and western Kentucky to southern Illinois, southern Indiana and parts of Ohio.
- Tornado, wind and hail in the Midwest, South, Southeast, Southwest and the mid-Atlantic.
- Wildfires in the West.

The occurrence of terrorist attacks in the geographic areas we serve could result in substantially higher claims under our insurance policies than we have anticipated. While we do insure terrorism risk in all areas we serve, we have identified our major terrorism exposure geographically as general commercial risks in the Tier 1 cities of metropolitan Chicago area, and to a much lesser degree, Washington D.C., Houston and Los Angeles. We have a greater amount of business in less hazardous Tier 2 cities such as Atlanta, Phoenix-Mesa, Minneapolis, Cleveland, St. Louis, Denver, Tampa-St. Petersburg, Pittsburgh and Cincinnati. We have exposure to small co-op utilities, water utilities, wholesale fuel distributors, small shopping malls and small colleges throughout our 39 active states and, because of the number of associates located there, our Fairfield, Ohio, headquarters. Additionally, our life insurance subsidiary could be adversely affected in the event of a terrorist event or an epidemic such as the avian or swine flu, particularly if the epidemic were to affect a broad range of the population beyond just the very young or the very old. Our associate health plan is self-funded and could similarly be affected.

Our results of operations would be adversely affected if the level of losses we experience over a period of time were to exceed our actuarially determined expectations. In addition, our financial condition may be adversely affected if we were required to sell securities prior to maturity or at unfavorable prices to pay an unusually high level of loss and loss expenses. Securities pricing might be even less favorable if a number of insurance or other companies and other investors needed to sell securities during a short period of time because of unusually high losses from catastrophic events.

Our geographic concentration ties our performance to business, economic, environmental and regulatory conditions in certain states. We market our standard market property casualty insurance products in 39 states, but our business is concentrated in the Midwest and Southeast. We also have exposure in states where we do not actively market insurance when clients of our independent agencies have businesses or properties in multiple states.

The Cincinnati Insurance Company also participates in certain assumed reinsurance treaties with reinsurers that spread the risk of very large catastrophe losses among many insurers. At the beginning of 2015, two surplus share treaties were in effect with the largest treaty representing exposure for us of up to $2 million of assumed losses from a single catastrophic event. If there is a high frequency of very large catastrophe events during a coverage period of the treaty, our financial position and results of operations could be materially affected. Please see Item 7, Liquidity and Capital Resources, 2015 Reinsurance Programs, for a discussion of our reinsurance treaties.

In the event of a severe catastrophic event or terrorist attack elsewhere in the world, our insurance losses may be immaterial. However, the companies we invest in might be severely affected, which could affect our financial condition and results of operations. Our reinsurers might experience significant losses, potentially jeopardizing their ability to pay losses we cede to them. It could also reduce the availability of reinsurance. If we cannot obtain adequate coverage at a reasonable cost, it could constrain where we can write business or reduce the amount of business we can write in certain areas. We also may be exposed to state guaranty fund assessments if other carriers in a state cannot meet their obligations to policyholders. A catastrophe or epidemic event also could affect our operations by damaging our headquarters facility, injuring associates and visitors at our Fairfield, Ohio, headquarters or disrupting our associates' ability to perform their assigned tasks.

Our ability to achieve our performance objectives could be affected by changes in the financial, credit and capital markets or the general economy.
We invest premiums received from policyholders and other available cash to generate investment income and capital appreciation, while also maintaining sufficient liquidity to pay covered claims and operating expenses, service our debt obligations and pay dividends. The value of our invested assets is an important component of shareholders' equity, also known as book value. Changes in the valuation of invested assets can significantly affect changes in book value per share, a key performance objective as discussed in Item 7, Executive Summary of Management's Discussion and Analysis.

For fixed-maturity investments such as bonds, which represented 65.8 percent of the fair value of our invested assets at the end of 2014, the inverse relationship between interest rates and bond prices leads to falling bond values during periods of increasing interest rates. A significant increase in the general level of interest rates could have an adverse effect on our shareholders' equity.

Investment income is an important component of our revenues and net income. The ability to increase investment income and generate longer-term growth in book value is affected by factors beyond our control, such as: inflation, economic growth, interest rates, world political conditions, changes in laws and regulations, terrorism attacks or threats, adverse events affecting other companies in our industry or the industries in which we invest, market events leading to credit constriction, and other widespread unpredictable events. These events may adversely affect the economy generally and could cause our investment income or the value of securities we own to decrease. A significant decline in our investment income could have an adverse effect on our net income, and thereby on our shareholders' equity and our statutory capital and surplus. For example, a significant increase in the general level of interest rates could lead to falling bond values. For a more detailed discussion of risks associated with our investments, please refer to Item 7A, Quantitative and Qualitative Disclosures About Market Risk.

We issue life contracts with guaranteed minimum returns, referred to as bank-owned life insurance contracts (BOLIs). BOLI investment assets must meet certain criteria established by the regulatory authorities in the jurisdiction for which the group contract holder is subject. Therefore, sales of investments may be mandated to maintain compliance with these regulations, possibly requiring gains or losses to be recorded. We could experience losses if the assets in the accounts were less than liabilities at the time of maturity or termination.

Our investment performance also could suffer because of the types of investments, industry groups and/or individual securities in which we choose to invest. Market value changes related to these choices could cause a material change in our financial condition or results of operations.

At year-end 2014, common stock holdings made up 32.7 percent of our investment portfolio. Adverse news or events affecting the global or U.S. economy or the equity markets could affect our net income, book value and overall results, as well as our ability to pay our common stock dividend. See Item 7, Investments Results, and Item 7A, Quantitative and Qualitative Disclosures About Market Risk, for a discussion of our investment activities.

Deterioration in the banking sector or in banks with which we have relationships could affect our results of operations. Our ability to maintain or obtain short-term lines of credit could be affected if the banks from which we obtain these lines are acquired, fail or are otherwise negatively affected. We may lose premium revenue if a bank that owns appointed agencies were to change its strategies. We could experience increased losses in our director and officer liability line of business if claims were made against insured financial institutions.

A deterioration of credit and market conditions could also impair our ability to access credit markets and could affect existing or future lending arrangements.

Our overall results could be affected if a significant portion of our commercial lines policyholders, including those purchasing surety bonds, are adversely affected by marked or prolonged economic downturns and events such as a downturn in construction and related sectors, tightening credit markets and higher fuel costs. Such events could make it more difficult for policyholders to finance new projects, complete projects or expand their businesses, leading to lower premiums from reduced payrolls and sales and lower purchases of equipment and vehicles. These events could also cause claims, including surety claims, to increase due to a policyholder's inability to secure necessary financing to complete projects or to collect on underlying lines of credit in the claims process. Such economic downturns and events could have a greater impact in the construction sector where we have a concentration of risks and in geographic areas that are hardest hit by economic downturns.

Deteriorating economic conditions could also increase the degree of credit risk associated with amounts due from independent agents who collect premiums for payment to us and could hamper our ability to recover amounts due from reinsurers.

Our ability to properly underwrite and price risks and increased competition could adversely affect our results.
Our financial condition, cash flow and results of operations depend on our ability to underwrite and set rates accurately for a full spectrum of risks. We establish our pricing based on assumptions about the level of losses that may occur within classes of business, geographic regions and other criteria.

To properly price our products, we must collect, properly analyze and use data to make decisions and take appropriate action; the data must be sufficient, reliable and accessible; we need to develop appropriate rating methodologies and formulae; and we may need to identify and respond to trends quickly. We may overestimate or underestimate loss cost trends or these trends may unexpectedly change, leading to losing business by pricing risks above our competitors or charging rates too low to maintain profitability. Inflation trends, especially outside of historical norms, may make it more difficult to determine adequate pricing. If rates are not accurate, we may not generate enough premiums to offset losses and expenses or we may not be competitive in the marketplace.

Our ability to set appropriate rates could be hampered if a state or states where we write business refuses to allow rate increases that we believe are necessary to cover the risks insured. At least one state requires us to purchase reinsurance from a mandatory reinsurance fund. Such reinsurance funds can create a credit risk for insurers if not adequately funded by the state and, in some cases, the existence of a reinsurance fund could affect the prices charged for our policies. The effect of these and similar arrangements could reduce our profitability in any given period or limit our ability to grow our business.

The insurance industry is cyclical and intensely competitive. From time to time, the insurance industry goes through prolonged periods of intense competition during which it is more difficult to attract new business, retain existing business and maintain profitability. Competition in our insurance business is based on many factors, including:

- Competitiveness of premiums charged
- Relationships among carriers, agents, brokers and policyholders
- Underwriting and pricing methodologies that allow insurers to identify and flexibly price risks
- Compensation provided to agents
- Underwriting discipline

- Terms and conditions of insurance coverage
- Speed with which products are brought to market
- Product and marketing innovations, including advertising
- Technological competence and innovation
- Ability to control expenses
- Adequacy of financial strength ratings by independent ratings agencies such as A.M. Best
- Quality of services and tools provided to agents and policyholders
- Claims satisfaction and reputation

If our pricing were incorrect or we were unable to compete effectively because of one or more of these factors, our premium writings could decline and our results of operations and financial condition could be materially adversely affected. Large competitors could intentionally disrupt the market by targeting certain lines or underpricing the market.

Please see the discussion of our Commercial Lines, Personal Lines, Excess and Surplus Lines and Life Insurance Segments in Item 1, Our Segments, for a discussion of our competitive position in the insurance marketplace.

Our pricing and capital models could be flawed.
We use various predictive pricing models, stochastic models and/or forecasting techniques to help us to understand our business, analyze risk and estimate future trends. The output of these models is used to assist us in making underwriting, pricing, reinsurance, reserving and capital decisions and helps us set our strategic direction. These models contain numerous assumptions, including the assumption that the data used is sufficient and accurate, and are subject to uncertainties and limitations inherent in any statistical analysis. Actual results might differ from modeled output, resulting in pricing our products incorrectly, overestimating or underestimating reserves, or inaccurately forecasting the impact of modeled events on our results. This could materially adversely impact the results of our operations.

Our loss reserves, our largest liability, are based on estimates and could be inadequate to cover our actual losses.
Our consolidated financial statements are prepared using GAAP. These principles require us to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying Notes. Actual results could differ materially from those estimates. For a discussion of the significant accounting policies we use to prepare our financial statements, the material implications of uncertainties associated with the methods, assumptions and estimates underlying our critical accounting policies and the process used to determine our loss reserves, please refer to Item 8, Note 1 of the Consolidated Financial Statements, and Item 7, Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves and Life Insurance Policy Reserves.

Our most critical accounting estimate is loss reserves. Loss reserves are the amounts we expect to pay for covered claims and expenses we incur to settle those claims. The loss reserves we establish in our financial statements represent an estimate of amounts needed to pay and administer claims arising from insured events that have already occurred, including events that have not yet been reported to us. Loss reserves are estimates and are inherently uncertain; they do not and cannot represent an exact measure of liability. Inflationary scenarios, especially scenarios outside of historical norms or regulatory changes that affect the assumptions underlying our critical accounting estimates, may make it more difficult to estimate loss reserves. Accordingly, our loss reserves for past periods could prove to be inadequate to cover our actual losses and related expenses. Any changes in these estimates are reflected in our results of operations during the period in which the changes are made. An increase in our loss reserves would decrease earnings, while a decrease in our loss reserves would increase earnings.

Unforeseen losses, the type and magnitude of which we cannot predict, may emerge in the future. These additional losses could arise from changes in the legal environment, laws and regulations, climate change, catastrophic events, increases in loss severity or frequency, environmental claims, mass torts or other causes. Such future losses could be substantial. Inflationary scenarios may cause the cost of claims, especially medical claims, to rise, impacting reserve adequacy and our results of operations.

Our ability to obtain or collect on our reinsurance protection could affect our business, financial condition, results of operations and cash flows.
We buy property casualty and life reinsurance coverage to mitigate the liquidity risk and earnings volatility risk of an unexpected rise in claims severity or frequency from catastrophic events or a single large loss. The availability, amount and cost of reinsurance depend on market conditions and may vary significantly. If we were unable to obtain reinsurance on acceptable terms and in appropriate amounts, our business and financial condition could be adversely affected.

In addition, we are subject to credit risk with respect to our reinsurers. Although we purchase reinsurance to manage our risks and exposures to losses, this reinsurance does not discharge our direct obligations under the policies we write. We would remain liable to our policyholders even if we were unable to recover what we believe we are entitled to receive under our reinsurance contracts. Reinsurers might refuse or fail to pay losses that we cede to them, or they might delay payment. For long-tail claims, the creditworthiness of our reinsurers may change before we can recover amounts to which we are entitled. A reinsurer’s insolvency, inability or unwillingness to make payments under the terms of its reinsurance agreement with our insurance subsidiaries could have a material adverse effect on our financial position, results of operations and cash flows.

Please see Item 7, Liquidity and Capital Resources, 2015 Reinsurance Programs, for a discussion of selected reinsurance transactions.

Our business depends on the uninterrupted operation of our facilities, systems and business functions.
Our business depends on our associates’ ability to perform necessary business functions, such as processing new and renewal policies and claims. We increasingly rely on technology and systems to accomplish these business functions in an efficient and uninterrupted fashion. Our inability to access our headquarters facilities or a failure of technology, telecommunications or other systems could significantly impair our ability to perform such functions on a timely basis or affect the accuracy of transactions. If sustained or repeated, such a business interruption or system failure could result in a deterioration of our ability to write and process new and renewal business, serve our agents and policyholders, pay claims in a timely manner, collect receivables or perform other necessary business functions. If our disaster recovery and business continuity plans did not sufficiently consider, address or reverse the circumstances of an interruption or failure, this could result in a materially adverse effect on our operating results and financial condition. This risk is exacerbated because approximately 69 percent of our associates work at our Fairfield, Ohio, headquarters.

Our ability to successfully execute business functions also depends on hiring and retaining qualified associates. Competition for high-quality executives and other key associates occurs within the insurance industry and from other industries. We also must effectively develop and manage associates, including providing training and resources. Such tools and information can allow them to effectively perform critical business functions and adapt to changing business needs. If we were unable to attract and retain certain associates, or if we fail to provide adequate training or resources, we could limit the success of executing our strategic plans and vital business functions.

The effects of changes in industry practices, laws and regulations on our business are uncertain.
As industry practices and legal, judicial, legislative, regulatory, political, social and other environmental conditions change, unexpected and unintended issues related to insurance pricing, claims and coverage may emerge. These issues may adversely affect our business by impeding our ability to obtain adequate rates for covered risks, extending coverage beyond our underwriting intent, by increasing the number or size of claims, by varying assumptions underlying our critical accounting estimates or by increasing duties owed to policyholders beyond contractual obligations. In some instances, unforeseeable emerging and latent claim and coverage issues may not become apparent until sometime after we have issued the insurance policies that could be affected by the changes. As a result, the full extent of liability under our insurance contracts may not be known for many years after a policy is issued and our

pricing and reserve estimates may not accurately reflect its effect.

We are required to adopt new or revised accounting standards issued by recognized authoritative organizations, including the Financial Accounting Standards Board (FASB) and the SEC. Future changes required to be adopted could change the current accounting treatment that we apply and could result in material adverse effects on our results of operations and financial condition.

Our investment income benefits from tax rate preferences for municipal bond interest and dividend income from equity securities. Market valuations for these securities also benefit from the tax-preference aspect of current tax laws, affecting the value of our investment portfolio and also shareholders' equity. Future changes in tax laws could result in material adverse effects on our results of operations and financial condition.

The NAIC, state insurance regulators and state legislators continually re-examine existing laws and regulations governing insurance companies and insurance holding companies, specifically focusing on modifications to statutory accounting principles, interpretations of existing laws, regulations relating to product forms and pricing methodologies and the development of new laws and regulations that affect a variety of financial and nonfinancial components of our business. Any proposed or future legislation, regulation or NAIC initiatives, if adopted, may be more restrictive on our ability to conduct business than current regulatory requirements or may result in higher costs. The loss or significant restriction on the use of a particular variable, such as credit, in pricing and underwriting our products could lead to future unprofitability and increased costs.

Federal laws and regulations, including those that may be enacted in the wake of the financial and credit crises, may have adverse effects on our business, potentially including a change from a state-based system of regulation to a system of federal regulation, the repeal of the McCarran Ferguson Act, and/or measures under the Dodd-Frank Act that establish the Federal Insurance Office and provide for a determination that a nonbank financial company presents systemic risk and therefore should be subject to heightened supervision by the Federal Reserve Board. It is not known how this federal office will coordinate and interact with the NAIC and state insurance regulators. Adoption or implementation of any of these measures may restrict our ability to conduct our insurance business, govern our corporate affairs or increase our cost of doing business. Implementation of the Affordable Care Act (ACA) may affect the ability of the company to grow profitably.

The effects of such changes could adversely affect our results of operations. Please see Item 7, Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves and Life Insurance Policy Reserves, for a discussion of our reserving practices.

Managing technology initiatives and meeting data security requirements are significant challenges.
While technology can streamline many business processes and ultimately reduce the cost of operations, technology initiatives present short-term cost, and also have implementation and operational risks. In addition, we may have inaccurate expense projections, implementation schedules or expectations regarding the effectiveness and user acceptance of the end product. These issues could escalate over time. If we were unable to find and retain associates with key technical knowledge, our ability to develop and deploy key technology solutions could be hampered.

We necessarily collect, use and hold data concerning individuals and businesses with whom we have a relationship. Threats to data security, including unauthorized access and cyberattacks, rapidly emerge and change, exposing us to additional costs for protection or remediation and competing time constraints to secure our data in accordance with customer expectations and statutory and regulatory requirements.

While we take commercially reasonable measures to keep our systems and data secure, it is difficult or impossible to defend against every risk being posed by changing technologies as well as criminals' intent on committing cybercrime. Increasing sophistication of cyber criminals and terrorists make keeping up with new threats difficult and could result in a breach. Patching and other measures to protect existing systems and servers could be inadequate, especially on systems that are being retired. Controls employed by our U.S., off-shore and cloud vendors could prove inadequate. We could also experience a breach by intentional or negligent conduct on the part of associates or other internal sources. Our systems and those of our third-party vendors may become vulnerable to damage or disruption due to circumstances beyond our or their control, such as from catastrophic events, power anomalies or outages, natural disasters, network failures, and viruses and malware.

A breach of our security that results in unauthorized access to our data could expose us to a disruption or challenges relating to our daily operations as well as to data loss, litigation, damages, fines and penalties, significant increases in compliance costs and reputational damage.

Our status as an insurance holding company with no direct operations could affect our ability to pay dividends in the future.
Cincinnati Financial Corporation is a holding company that transacts substantially all of its business through its subsidiaries. Our primary assets are the stock in our operating subsidiaries and our investments. Consequently, our cash flow to pay cash dividends and interest on our long-term debt depends on dividends we receive from our operating subsidiaries and income earned on investments held at the parent-company level.

Dividends paid to our parent company by our insurance subsidiary are restricted by the insurance laws of Ohio, its domiciliary state. These laws establish minimum solvency and liquidity thresholds and limits. In 2015, the maximum dividend that may be paid without prior regulatory approval is limited to the greater of 10 percent of statutory capital and surplus or 100 percent of statutory net income for the prior calendar year, up to the amount of statutory unassigned capital and surplus as of the end of the prior calendar year. Dividends exceeding these limitations may be paid only with prior approval of the Ohio Department of Insurance. Consequently, at times, we might not be able to receive dividends from our insurance subsidiary, or we might not receive dividends in the amounts necessary to meet our debt obligations or to pay dividends on our common stock without liquidating securities. This could affect our financial position.

Please see Item 1, Regulation, and Item 8, Note 9 of the Consolidated Financial Statements, for a discussion of insurance holding company dividend regulations.

ITEM 1B. Unresolved Staff Comments
None

ITEM 2. Properties
Cincinnati Financial Corporation owns our headquarters building located on 100 acres of land in Fairfield, Ohio. This building has 1,508,200 square feet of total space. The property, including land, is carried in our financial statements at $137 million as of December 31, 2014, and is classified as land, building and equipment, net, for company use. John J. & Thomas R. Schiff & Co. Inc., a related party, occupies 6,750 square feet (less than 1 percent). This property is used by all segments reported in the Consolidated Financial Statements and accompanying Notes.

Cincinnati Financial Corporation also owns Gilmore Pointe, formerly known as the Fairfield Executive Center, which is located on the northwest corner of our headquarters property. This four-story office building has approximately 124,000 square feet of total space. The property is carried in the financial statements at $7 million as of December 31, 2014, and is classified as land, building and equipment, net, for company use. Unaffiliated tenants occupy 6 percent. This property is used by all segments reported in the Consolidated Financial Statements and accompanying Notes.

The Cincinnati Insurance Company owns the CFC Winton Center used for business continuity, with approximately 48,000 square feet of total space, located approximately six miles from our headquarters. The property, including land, is carried on our financial statements at $10 million as of December 31, 2014, and is classified as land, building and equipment, net, for company use. This property is used by all segments reported in the Consolidated Financial Statements and accompanying Notes.

ITEM 3. Legal Proceedings
Neither the company nor any of our subsidiaries is involved in any material litigation other than ordinary, routine litigation incidental to the nature of its business.

ITEM 4. Mine Safety Disclosures

This item is not applicable to the company.

Part II

ITEM 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Cincinnati Financial Corporation had approximately 70,000 shareholders of record as of December 31, 2014. While approximately 13,000 shareholders are registered, the majority of shareholders are beneficial owners whose shares are held in "street name" by brokers and institutional accounts. We believe many of our independent agent representatives and most of the 4,305 associates of our subsidiaries own the company's common stock.

Our common shares are traded under the symbol CINF on the Nasdaq Global Select Market.

(Source: Nasdaq Global Select Market)	2014				2013			
Quarter:	1st	2nd	3rd	4th	1st	2nd	3rd	4th
High	$52.19	$49.73	$48.86	$55.35	$47.35	$50.60	$50.01	$53.74
Low	44.90	47.00	45.69	45.09	39.60	44.53	43.62	46.61
Period-end close	48.66	48.04	47.05	51.83	47.22	45.92	47.16	52.37
Cash dividends declared	0.44	0.44	0.44	0.44	0.4075	0.4075	0.42	0.42

We discuss the factors that affect our ability to pay cash dividends and repurchase shares in Item 7, Liquidity and Capital Resources. Regulatory restrictions on dividends our insurance subsidiary can pay to the parent company are discussed in Item 8, Note 9 of the Consolidated Financial Statements.

The following summarizes securities authorized for issuance under our equity compensation plans as of December 31, 2014:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights at December 31, 2014	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plan (excluding securities reflected in column (a)) at December 31, 2014
	(a)	(b)	(c)
Equity compensation plans approved by security holders	4,958,191	$39.10	6,199,048
Equity compensation plans not approved by security holders	—	—	—
Total	4,958,191	$39.10	6,199,048

The number of securities remaining available for future issuance includes: 5,503,974 shares available for issuance under the Cincinnati Financial Corporation 2012 Stock Compensation Plan (the 2012 Plan), 517,117 shares available for issuance under the Cincinnati Financial Corporation 2006 Stock Compensation Plan (the 2006 Plan), and 177,957 shares available for issuance of share grants under the Director's Stock Plan of 2009. Both the 2012 Plan and 2006 Plan allow for issuance of stock options, service-based, or performance-based restricted stock units, stock appreciation rights or other equity-based grants. Awards other than stock options and stock appreciation rights granted from the

2012 and 2006 plans are counted as three shares against the plan for each one share of common stock actually issued. Additional information about stock-based associate compensation granted under our equity compensation plans is available in Item 8, Note 17 of the Consolidated Financial Statements.

The following summarizes shares purchased under our repurchase programs:

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs
January 1-31, 2014	—	—	—	5,549,493
February 1-28, 2014	—	—	—	5,549,493
March 1-31, 2014	150,000	$47.69	150,000	5,399,493
April 1-30, 2014	—	—	—	5,399,493
May 1-31, 2014	—	—	—	5,399,493
June 1-30, 2014	—	—	—	5,399,493
July 1-31, 2014	100,000	46.07	100,000	5,299,493
August 1-31, 2014	200,000	46.11	200,000	5,099,493
September 1-30, 2014	—	—	—	5,099,493
October 1-31, 2014	—	—	—	5,099,493
November 1-30, 2014	—	—	—	5,099,493
December 1-31, 2014	—	—	—	5,099,493
Totals	450,000	46.63	450,000	

We did not sell any of our shares that were not registered under the Securities Act during 2014. The board of directors has authorized share repurchases since 1996. Purchases are expected to be made generally through open market transactions. The board gives management discretion to purchase shares at reasonable prices in light of circumstances at the time of purchase, subject to SEC regulations. We have 5,099,493 shares available for purchase under our programs at December 31, 2014.

On October 24, 2007, the board of directors expanded the existing repurchase authorization to approximately 13 million shares. The prior repurchase program for 10 million shares was announced in 2005, replacing a program that had been in effect since 1999. No repurchase program has expired during the period covered by the above table. Neither the 2005 nor 1999 program had an expiration date, but no further repurchases will occur under the 1999 program.

Cumulative Total Return

As depicted in the graph below, the five-year total return on a $100 investment made December 31, 2009, assuming the reinvestment of all dividends, was 146.7 percent for Cincinnati Financial Corporation's common stock compared with 109.3 percent for the Standard & Poor's Composite 1500 Property & Casualty Insurance Index and 105.1 percent for the Standard & Poor's 500 Index.

The Standard & Poor's Composite 1500 Property & Casualty Insurance Index included 26 companies at year-end 2014: Ace Limited, The Allstate Corporation, Amerisafe Inc., Aspen Insurance Holdings Limited, W. R. Berkley Corporation, The Chubb Corporation, Cincinnati Financial Corporation, Employers Holdings Inc., First American Financial Corporation, The Hanover Insurance Group Inc., HCI Group Inc., Infinity Property and Casualty Corporation, Meadowbrook Insurance Group Inc., Mercury General Corporation, The Navigators Group Inc., Old Republic International Corporation, ProAssurance Corporation, The Progressive Corporation, RLI Corp., Safety Insurance Group Inc., Selective Insurance Group Inc., Stewart Information Services Corporation, The Travelers Companies Inc., United Fire & Casualty Company, Universal Insurance Holdings Inc. and XL Group Public Limited Company.

The Standard & Poor's 500 Index includes a representative sample of 500 leading companies in a cross section of industries of the U.S. economy. Although this index focuses on the large capitalization segment of the market, it is widely viewed as a proxy for the total market.

Comparison of Five-Year Cumulative Total Return*

*$100 invested on December 31, 2009, in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

ITEM 6. Selected Financial Data

(In millions except per share data)	Years ended December 31, 2014	2013	2012	2011	2010
Consolidated Income Statement Data					
Earned premiums	$4,243	$3,902	$3,522	$3,194	$3,082
Investment income, net of expenses	549	529	531	525	518
Realized investment gains, net*	133	83	42	70	159
Total revenues	4,945	4,531	4,111	3,803	3,772
Net income	525	517	421	164	375
Net income per common share:					
Basic	$3.21	$3.16	$2.59	$1.01	$2.30
Diluted	3.18	3.12	2.57	1.01	2.30
Cash dividends per common share:					
Declared	1.76	1.655	1.62	1.605	1.59
Paid	1.74	1.6425	1.615	1.6025	1.585
Diluted weighted average shares outstanding	165.1	165.4	163.7	163.3	163.3
Consolidated Balance Sheet Data					
Total investments	$14,386	$13,564	$12,534	$11,801	$11,508
Net unrealized investment gains	2,719	2,335	1,875	1,489	1,250
Deferred policy acquisition costs	578	565	470	477	458
Total assets	18,753	17,662	16,548	15,635	15,065
Gross loss and loss expense reserves	4,485	4,311	4,230	4,339	4,200
Life policy reserves	2,497	2,390	2,295	2,214	2,034
Long-term debt	791	790	790	790	790
Shareholders' equity	6,573	6,070	5,453	5,033	5,012
Book value per share	40.14	37.21	33.48	31.03	30.79
Shares outstanding	163.7	163.1	162.9	162.2	162.8
Value creation ratio	12.6 %	16.1 %	12.6 %	6.0 %	11.1 %
Consolidated Property Casualty Operations Data					
Earned premiums	$4,045	$3,713	$3,344	$3,029	$2,924
Unearned premiums	2,081	1,970	1,790	1,631	1,551
Gross loss and loss expense reserves	4,438	4,241	4,169	4,280	4,137
Investment income, net of expenses	358	348	351	350	348
Loss and loss expense ratio	65.0 %	61.9 %	63.9 %	77.0 %	68.9 %
Underwriting expense ratio	30.6	31.9	32.2	32.3	32.9
Combined ratio	95.6 %	93.8 %	96.1 %	109.3 %	101.8 %

On January 1, 2012, we retrospectively adopted ASU 2010-26, Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts. All prior years' information has been restated.

* Realized investment gains and losses are integral to our financial results over the long term, but our substantial discretion in the timing of investment sales may cause this value to fluctuate substantially. Also, applicable accounting standards require us to recognize gains and losses from certain changes in fair values of securities and embedded derivatives without actual realization of those gains and losses. We discuss realized investment gains for the past three years in Item 7, Investments Results.

ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Introduction

The purpose of Management’s Discussion and Analysis is to provide an understanding of Cincinnati Financial Corporation’s consolidated results of operations and financial condition. Our Management’s Discussion and Analysis should be read in conjunction with Item 6, Selected Financial Data, and Item 8, Consolidated Financial Statements and related Notes. We present per share data on a diluted basis unless otherwise noted, adjusting those amounts for all stock splits and stock dividends.

We begin with an executive summary of our results of operations, followed by other highlights, an overview of our strategy, an outlook for future performance and details on critical accounting estimates. In several instances, we refer to estimated industry data so that we can provide information on our performance within the context of the overall insurance industry. Unless otherwise noted, the industry data is prepared by A.M. Best Co., a leading insurance industry statistical, analytical and financial strength rating organization. Information from A.M. Best is presented on a statutory accounting basis. When we provide our results on a comparable statutory accounting basis, we label it as such; all other company data is presented in accordance with accounting principles generally accepted in the United States of America (GAAP).

Through The Cincinnati Insurance Company, Cincinnati Financial Corporation is one of the 25 largest property casualty insurers in the nation, based on net written premium volume for the first nine months of 2014, among approximately 2,000 U.S. stock and mutual insurer groups. We market our insurance products through a select group of independent insurance agencies in 39 states as discussed in Item 1, Our Business and Our Strategy.

The U.S. economy, the insurance industry and our company continue to face many challenges. Our long-term perspective has allowed us to address immediate challenges while also focusing on the major decisions that best position the company for success through all market cycles. We believe that this forward-looking view consistently benefits our shareholders, agents, policyholders and associates.

To measure our progress, we have defined a measure of value creation that we believe captures the contribution of our insurance operations, the success of our investment strategy and the importance we place on paying cash dividends to shareholders. We refer to this measure as our value creation ratio, or VCR, and it is made up of two primary components: (1) our rate of growth in book value per share plus (2) the ratio of dividends declared per share to beginning book value per share. This measure, intended to be all-inclusive regarding changes in book value per share, uses originally reported book value per share in cases where book value per share has been adjusted, such as after the adoption of Accounting Standards Updates with a cumulative effect of a change in accounting.

Executive Summary

Our value creation ratio, defined above, is our primary performance target. VCR trends are shown in the table below.

	One year		Three-year % average		Five-year % average	
Value creation ratio:						
As of December 31, 2014	12.6	%	13.8	%	11.7	%
As of December 31, 2013	16.1		11.6		13.1	
As of December 31, 2012	12.6		9.9		5.2	

For the period 2013 through 2017, we are targeting an annual value creation ratio averaging 10 percent to 13 percent. We were within that range for 2014, and for the five-year period that ended in 2014. For the period 2009 through 2012, our annual value creation ratio averaged 12.4 percent, within the 12 percent to 15 percent five-year target range established in early 2009, soon after the U.S. credit crisis. For several years following the credit crisis, interest rates generally declined and credit spreads tightened, increasing the contribution of valuation gains from our fixed-maturity securities to the VCR. Those gains contributed between 2 percent and 3 percent annually to VCR during 2010 through 2012. While that contribution is not expected to occur in the subsequent five-year period, as indicated by a significant negative effect in 2013, management believes the company will continue to produce strong underwriting results.

The next two tables show the primary components of our value creation ratio, first on a percentage basis and then on a per-outstanding-share basis. Analysis of the components aids understanding of our financial performance. Our financial results are further analyzed in the Corporate Financial Highlights section below.

	Years ended December 31,		
	2014	2013	2012
Value creation ratio major components:			
Net income before net realized gains	7.2 %	8.5 %	7.7 %
Change in realized and unrealized gains, fixed-maturity securities	1.2	(4.5)	2.7
Change in realized and unrealized gains, equity securities	4.3	10.9	2.8
Other	(0.1)	1.2	(0.6)
Value creation ratio	12.6 %	16.1 %	12.6 %

The 2014 value creation ratio included operating results as its primary contributor, with higher valuation for our equity securities investment portfolio also contributing significantly. A higher valuation for our fixed-maturity securities investment portfolio also contributed, reversing the unfavorable 2013 effect that reflected lower valuation. The 2014 contribution from operating results was 1.3 percentage points lower than in 2013, while the contribution from realized gains plus the change in unrealized gains from our investment portfolios was 0.9 points lower. The 2013 VCR also benefited from other items that affected book value per share, primarily a contribution from updated valuations and related assumptions for our employee benefit pension plan, while the 2014 effect was minimal. The 2012 value creation ratio had contribution amounts fairly similar to 2014.

(Dollars are per share)	Years ended December 31,		
	2014	2013	2012
Book value change per share:			
End of period book value	$40.14	$37.21	$33.48
Less beginning of period book value	37.21	33.48	31.03
Change in book value	$2.93	$3.73	$2.45
Change in book value:			
Net income before realized gains	$2.69	$2.84	$2.41
Change in realized and unrealized gains, fixed-maturity securities	0.43	(1.50)	0.84
Change in realized and unrealized gains, equity securities	1.61	3.64	0.86
Dividend declared to shareholders	(1.76)	(1.66)	(1.62)
Other	(0.04)	0.41	(0.04)
Change in book value	$2.93	$3.73	$2.45

We believe our value creation ratio, a non-GAAP measure, is a useful supplement to GAAP information. With the continuation of economic and market uncertainty in recent years, the long-term nature of this measure provides a meaningful measure of our long-term progress in creating shareholder value. A reconciliation of this non-GAAP measure to comparable GAAP measures is shown in the table below.

(Dollars are per share)	Years ended December 31,		
	2014	2013	2012
Value creation ratio:			
End of year book value	$40.14	$37.21	$33.48
Less beginning of year book value	37.21	33.48	31.16
Change in book value	2.93	3.73	2.32
Dividend declared to shareholders	1.76	1.655	1.62
Total value creation ratio	$4.69	$5.385	$3.94
Value creation ratio from change in book value*	7.9 %	11.1 %	7.4 %
Value creation ratio from dividends declared to shareholders**	4.7	5.0	5.2
Value creation ratio	12.6 %	16.1 %	12.6 %

* Change in book value divided by the beginning of year book value as originally reported
** Dividend declared to shareholders divided by beginning of year book value as originally reported

When looking at our longer-term objectives, we see three primary performance drivers for our value creation ratio:

- Premium growth – We believe over any five-year period our agency relationships and initiatives can lead to a property casualty written premium growth rate that exceeds the industry average. The compound annual growth rate of our net written premiums was 7.3 percent over the five-year period 2010 through 2014, approximately double the 3.4 percent estimated growth rate for the property casualty insurance industry. The industry's growth rate excludes its mortgage and financial guaranty lines of business. Our long-term target for profitable premium growth, established in late 2011 for our property casualty and life insurance segments in aggregate, is to reach $5 billion of annual direct written premiums by the end of 2015. In 2014, our direct written premiums totaled $4.577 billion.
- Combined ratio – We believe our underwriting philosophy and initiatives can drive performance to achieve our underwriting profitability target of a GAAP combined ratio over any five-year period that consistently averages within the range of 95 percent to 100 percent. Our GAAP combined ratio averaged 99.3 percent over the five-year period 2010 through 2014. Performance as measured by the combined ratio is discussed in Consolidated Property Casualty Insurance Results. Our statutory combined ratio averaged 98.8 percent over the five-year period 2010 through 2014 compared with an estimated 100.7 percent for the property casualty industry. The industry's ratio again excludes its mortgage and financial guaranty lines of business.
- Investment contribution – We believe our investment philosophy and initiatives can drive investment income growth and lead to a total return on our equity investment portfolio over a five-year period that exceeds the five-year total return of the Standard & Poor's 500 Index.
  Investment income growth, on a pretax basis, had a compound annual growth rate of 1.8 percent over the five-year period 2010 through 2014. It has grown every year since 2009, except for 2013 with its slight decrease of less than 1 percent.
  Over the five years ended December 31, 2014, our equity portfolio compound annual total return was 14.1 percent compared with a compound annual total return of 15.4 percent for the Index. By design, our equity portfolio is comprised of larger capitalization, high-quality dividend-growing stocks. Therefore we would generally expect its return to lag during the type of extended, lower-quality rally that has occurred since early 2009. For the year 2014, our annual equity portfolio total return was 12.3 percent, compared with 13.7 percent for the Index.

The board of directors is committed to rewarding shareholders directly through cash dividends and share repurchase authorizations. The board also has periodically declared stock dividends and splits. Through 2014, the company has increased the indicated annual cash dividend rate for 54 consecutive years, a record we believe is matched by only nine other publicly traded companies. The board regularly evaluates relevant factors in dividend-related decisions, and the 2014 increase reflects confidence in our strong capital, liquidity and financial flexibility, as well as progress through our initiatives to improve earnings performance while growing insurance premium revenues. We discuss our financial position in more detail in Liquidity and Capital Resources.

Corporate Financial Highlights

In addition to the value creation ratio discussion and analysis in the Executive Summary, we further analyze our financial results in the sections below.

Balance Sheet Data

(Dollars in millions except share data)	At December 31, 2014		At December 31, 2013	
Balance sheet data:				
Total investments	$14,386		$13,564	
Total assets	18,753		17,662	
Short-term debt	49		104	
Long-term debt	791		790	
Shareholders' equity	6,573		6,070	
Book value per share	40.14		37.21	
Debt-to-total-capital ratio	11.3	%	12.8	%

Total investments grew 6 percent during 2014 on a fair value basis, with market gains that added to the 4 percent increase in the cost basis. Entering 2015, we believe the portfolio continues to be well diversified and is well positioned to withstand short-term fluctuations. We discuss our investment strategy in Item 1, Investments Segment, and results for the segment in Investments Results. Total assets rose 6 percent, primarily due to the increase in total investments. Shareholders' equity and book value per share each rose 8 percent, for reasons discussed in the preceding Executive Summary.

The amount of our debt obligations decreased by $54 million in 2014, compared with 2013. Our ratio of debt to total capital (debt plus shareholders' equity) decreased by 1.5 percentage points in 2014 and remains comfortably within our target range.

Income Statement and Per Share Data

(Dollars in millions except per share data)	Years ended December 31, 2014	2013	2012	2014-2013 Change %		2013-2012 Change %
Net income and comprehensive income data:						
Earned premiums	$4,243	$3,902	$3,522	9		11
Investment income, net of expenses (pretax)	549	529	531	4		0
Realized investment gains, net (pretax)	133	83	42	60		98
Total revenues	4,945	4,531	4,111	9		10
Net income	525	517	421	2		23
Comprehensive income	765	892	649	(14	)	37
Net income - diluted	$3.18	$3.12	$2.57	2		21
Cash dividends declared	1.76	1.655	1.62	6		2
Diluted weighted average shares outstanding	165.1	165.4	163.7	0		1

Net income in 2014 rose $8 million or 2 percent compared with 2013, due primarily to the after-tax effects of net realized investment gains that were $31 million higher and investment income that rose by $18 million. Property casualty underwriting results for 2014, on an after-tax basis, were $31 million lower than in 2013, including $21 million from higher natural catastrophe losses and $34 million from higher noncatastrophe weather losses described below in Consolidated Property Casualty Insurance Results.

Net income increased $96 million in 2013, compared with 2012, reflecting the after-tax net effect of two major contributing items: a $62 million improvement in property casualty underwriting results, including $105 million from lower catastrophe losses, and a $26 million increase in net realized investment gains.

As discussed in Investments Results, sales of securities that had appreciated in value led to realized investment gains in all three years. Realized and unrealized investment gains and losses are integral to our financial results over the long term. We have substantial discretion in the timing of investment sales and, therefore, the gains or losses that are recognized in any period. That discretion generally is independent of the insurance underwriting process.

Dividend income rose 13 percent in 2014 while interest income rose 1 percent, driving a net increase in pretax investment income of $20 million, or 4 percent. In addition to a larger common stock portfolio generating more dividend income in both 2014 and 2013, both years also benefited from higher average dividend payment rates. Our investment operation's performance is discussed further in Investments Results.

Contribution from Insurance Operations

(Dollars in millions)	Years ended December 31,			2014-2013	2013-2012
	2014	2013	2012	Change %	Change %
Consolidated property casualty data:					
Net written premiums	$4,143	$3,893	$3,482	6	12
Earned premiums	4,045	3,713	3,344	9	11
Underwriting profit	186	233	137	(20)	70
				Pt. Change	Pt. Change
GAAP combined ratio	95.6 %	93.8 %	96.1 %	1.8	(2.3)
Statutory combined ratio	95.1	92.8	95.4	2.3	(2.6)
Written premium to statutory surplus	0.9	0.9	0.9	0.0	0.0

Property casualty net written premiums grew 6 percent in 2014 and earned premiums grew 9 percent, largely due to higher pricing and premium growth initiatives. That growth lagged the trend experienced in 2013, largely due to pricing increases that were not as strong in 2014. Trends and related factors are discussed in Commercial Lines, Personal Lines and Excess and Surplus Lines Insurance Results, respectively.

Our property casualty insurance operations generated underwriting profits for each of the three years ending in 2014, following underwriting losses for each of the preceding four years. The $47 million decrease in 2014, compared with 2013, included a $32 million increase in losses from natural catastrophe events and $52 million increase in weather-related losses. The $96 million improvement for 2013, compared with 2012, included a $162 million decrease in losses from natural catastrophe events.

We measure property casualty underwriting profitability primarily by the combined ratio. Our combined ratio measures the percentage of each earned premium dollar spent on claims plus all expenses related to our property casualty operations, all on a pretax basis. A lower ratio indicates more favorable results and better underlying performance. A ratio below 100 percent represents an underwriting profit. Initiatives to improve our combined ratio are discussed in Item 1, Our Business and Our Strategy, Strategic Initiatives. In 2014, 2013 and 2012, favorable development on reserves for claims that occurred in prior accident years helped offset other incurred losses and loss expenses. Reserve development is discussed further in Property Casualty Loss and Loss Expense Obligations and Reserves. Losses from weather-related catastrophes are another important item influencing the combined ratio and are discussed along with other factors in Financial Results for our property casualty business and related segments.

Our life insurance segment reported a modest loss in 2014 and a modest profit in 2013, netting to a $4 million profit for both years combined. We discuss results for the segment in Life Insurance Results. Most of this segment's investment income is included in our investments segment results. In addition to investment income, realized investment gains from the life insurance investment portfolio are also included in our investments segment results.

Strategic Initiatives Overview

Management has worked to identify a strategy that can lead to long-term success, with concurrence by the board of directors. Our strategy is intended to position us to compete successfully in the markets we have targeted while appropriately managing risk. We discuss our long-term, proven strategy in Item 1, Our Business and Our Strategy. We believe successful implementation of initiatives that support our strategy will help us better serve our agent customers and reduce volatility in our financial results while we also grow earnings and book value over the long-term, successfully navigating challenging economic, market or industry pricing cycles.

- Improve insurance profitability – Implementation of these initiatives is intended to enhance underwriting expertise and knowledge, thereby increasing our ability to manage our business while also gaining efficiency. Better profit margins can arise from additional information and more focused action on underperforming product lines, plus pricing capabilities we are expanding through the use of technology and analytics. Improved internal processes with additional performance metrics can help us be more efficient and effective. These initiatives also support the ability of the independent agencies that represent us to grow profitably by allowing them to serve clients faster and to more efficiently manage agency expenses.
- Drive premium growth – Implementation of these initiatives is intended to further penetrate each market we serve through our independent agencies. Strategies aimed at specific market opportunities, along with service enhancements, can help our agents grow and increase our share of their business. Diversified growth also may reduce variability of losses from weather-related catastrophes.

We discuss these strategic initiatives, along with related metrics to assess progress, in Item 1, Our Business and Our Strategy, Strategic Initiatives. Detailed discussion of related financial results appears below in Financial Results and Liquidity and Capital Resources.

Factors Influencing Our Future Performance

Our view of the shareholder value we can create over the next five years relies largely on three assumptions – each highly dependent on the external environment. First, we anticipate our average commercial and personal insurance prices will increase in excess of our loss cost trends. Second, we assume that the economy can maintain a growth track during 2015. Third, we assume that valuations of our marketable securities will vary within a typical range, based on historical trends. If those assumptions prove to be inaccurate, we may not be able to achieve our performance targets even if we accomplish our strategic objectives.

Other factors that could influence our ability to achieve our targets include:

- We expect the insurance marketplace to remain competitive, which is likely to cause carriers to pursue strategies that they believe could lead to economies of scale, market share gains or the potential for an improved competitive posture.
- We expect the independent insurance agency system to remain strong, with continued agency consolidation. If soft insurance market conditions return in 2015, it will create additional risk for agencies.
- We expect initiatives that make it easier for agents to do business with us to continue to be a significant factor in agency relationships. Technology is a major driver, with policyholders increasingly demanding online services and access from agents or carriers.

We discuss in our Item 1A, Risk Factors, many potential risks to our business and our ability to achieve our qualitative and quantitative objectives. These are real risks, but their probability of occurring may not be high. We also believe that our risk management programs generally could mitigate their potential effects, in the event they would occur.

For the year 2015, we believe our value creation ratio could be below our long-term target for several reasons.

- The rally in financial markets during recent years had a favorable impact on our value creation ratio, offsetting the unfavorable impact of the sharp decline in financial markets during 2008. Financial markets continued to display volatility during 2014, and some predict more turbulence in 2015 from effects such as changes in government policy, growth challenges for emerging country economies or other geopolitical events that could also affect the U.S. economy and markets. Should financial markets decline during 2015, which could occur as part of typical market volatility patterns, the related book value component of our 2015 value creation ratio could also register a weak or negative result.

- A return of soft insurance market pricing could significantly affect growth rates and earned premium levels into 2015 and for some time into the future, depending on insurance market conditions. After several years of market conditions that weakened loss ratios and hampered near-term profitability, conditions affecting property casualty insurance markets have improved since late 2011. In the future, economic factors, including inflation, may increase our claims and settlement expenses related to medical care, litigation and construction.
- The slowly recovering economy continued to help increase the value of business and personal insurable assets owned by policyholders in 2014. If the economy falters, we may experience low or no premium growth for the property casualty industry. Property casualty written premium growth also may lag as some of our growth initiatives require more time to reach their full contribution.
- We will incur costs for continued investment in our business, including technology, geographic expansion and process initiatives to create long-term value. In addition, we will not see the full advantage of some of these investments for several years.

Critical Accounting Estimates

Cincinnati Financial Corporation's financial statements are prepared using U.S. GAAP. These principles require management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying Notes. Actual results could differ materially from those estimates.

The significant accounting policies used in the preparation of the financial statements are discussed in Item 8, Note 1 of the Consolidated Financial Statements. In conjunction with that discussion, material implications of uncertainties associated with the methods, assumptions and estimates underlying the company's critical accounting policies are discussed below. The audit committee of the board of directors reviews the annual financial statements with management and the independent registered public accounting firm. These discussions cover the quality of earnings, review of reserves and accruals, reconsideration of the suitability of accounting principles, review of highly judgmental areas including critical accounting estimates, audit adjustments and such other inquiries as may be appropriate.

Property Casualty Insurance Loss and Loss Expense Reserves

We establish loss and loss expense reserves for our property casualty insurance business as balance sheet liabilities. These reserves account for unpaid loss and loss expenses as of a financial statement date. Unpaid loss and loss expenses are the estimated amounts necessary to pay for and settle all outstanding insured claims, including incurred but not reported (IBNR) claims, as of that date.

For some lines of business that we write, a considerable and uncertain amount of time can elapse between the occurrence, reporting and payment of insured claims. The amount we will actually have to pay for such claims also can be highly uncertain. This uncertainty, together with the size of our reserves, makes the loss and loss expense reserves our most significant estimate. Gross loss and loss expense reserves were $4.438 billion at year-end 2014 compared with $4.241 billion at year-end 2013.

How Reserves Are Established

Our field claims representatives establish case reserves when claims are reported to the company to provide for our unpaid loss and loss expense obligation associated with individual claims. Field claims managers supervise and review all claims with case reserves less than $100,000. Additionally, a headquarters supervisor and regional manager review all claims under $100,000 if litigation or a certain specialty claim is involved. All claims with case reserves of $100,000 or greater are reviewed and approved by an experienced headquarters supervisor and regional claims manager, and that threshold amount was $35,000 for several years prior to 2015. Upper-level headquarters claims managers also review case reserves of $175,000 or more, a threshold amount that was $100,000 for several years prior to 2015.

Our claims representatives base their case reserve estimates primarily upon case-by-case evaluations that consider:
- type of claim involved
- circumstances surrounding each claim
- policy provisions pertaining to each claim
- potential for subrogation or salvage recoverable
- general insurance reserving practices

Case reserves of all sizes are subject to review on a 90-day cycle, or more frequently if new information about a loss becomes available. As part of the review process, we monitor industry trends, cost trends, relevant court cases, legislative activity and other current events in an effort to ascertain new or additional loss exposures.

We also establish IBNR reserves to provide for all unpaid loss and loss expenses not accounted for by case reserves:
- For events designated as natural catastrophes, we calculate bulk reserves directly as a result of an estimated IBNR claim count and an estimated average claim amount for each event. Once case reserves are established for a catastrophe event, we reduce the bulk reserves. Our claims department management coordinates the assessment of these events and prepares the related bulk reserve estimates. Such an assessment involves a comprehensive analysis of the nature of the event, of policyholder exposures within the affected geographic area and of available claims intelligence. Depending on the nature of the event, available claims intelligence could include surveys of field claims associates within the affected geographic area, feedback from a catastrophe claims team sent into the area, as well as data on claims reported as of the financial statement date. To determine whether an event is designated as a catastrophe, we generally use the catastrophe definition provided by Property Claims Service (PCS), a division of Insurance Services Office (ISO). PCS defines a catastrophe as an event that causes countrywide damage of $25 million or more in insured property losses and affects a significant number of policyholders and insureds.
- For asbestos and environmental claims, we calculate IBNR reserves by deriving an actuarially-based estimate of total unpaid loss and loss expenses. We then reduce the estimate by total case reserves. We discuss the reserve analysis that applies to asbestos and environmental reserves in Liquidity and Capital Resources, Asbestos and Environmental Reserves.
- For loss expenses that pertain primarily to salaries and other costs related to our claims department associates, also referred to as adjusting and other expense or AOE, we calculate reserves based on an analysis of the relationship between paid losses and paid AOE. Reserves for AOE are allocated to company, line of business and accident year based on a claim count algorithm.
- For all other claims and events, IBNR reserves are calculated as the difference between an actuarial estimate of the ultimate cost of total loss and loss expenses incurred reduced by the sum of total loss and loss expense payments and total case reserves estimated for individual claims. We discuss below the development of actuarially based estimates of the ultimate cost of total loss and loss expenses incurred.

Our actuarial staff applies significant judgment in selecting models and estimating model parameters when preparing reserve analyses. Unpaid loss and loss expenses are inherently uncertain as to timing and amount. Uncertainties relating to model appropriateness, parameter estimates and actual loss and loss expense amounts are referred to as model, parameter and process uncertainty, respectively. Our management and actuarial staff address these uncertainties in the reserving process in a variety of ways.

Our actuarial staff bases its IBNR reserve estimates for these losses primarily on the indications of methods and models that analyze accident year data. Accident year is the year in which an insured claim, loss or loss expense occurred. The specific methods and models that our actuaries have used for the past several years are:
- paid and reported loss development methods
- paid and reported loss Bornhuetter-Ferguson methods
- individual and multiple probabilistic trend family models

Our actuarial staff uses diagnostics provided by stochastic reserving software to evaluate the appropriateness of the models and methods listed above. The software's diagnostics have indicated that the appropriateness of these models and methods for estimating IBNR reserves for our lines of business tends to depend on a line's tail. Tail refers to the time interval between a typical claim's occurrence and its settlement. For our long-tail lines such as workers' compensation and commercial casualty, models from the probabilistic trend family tend to provide superior fits and to validate well compared with models underlying the loss development and Bornhuetter-Ferguson methods. The loss development and Bornhuetter-Ferguson methods, particularly the reported loss variations, tend to produce the more appropriate IBNR reserve estimates for our short-tail lines such as homeowner and commercial property. For our mid-tail lines such as personal and commercial auto liability, all models and methods provide useful insights.

Our actuarial staff also devotes significant time and effort to the estimation of model and method parameters. The loss development and Bornhuetter-Ferguson methods require the estimation of numerous loss development factors. The Bornhuetter-Ferguson methods also involve the estimation of numerous ultimate loss ratios by accident year. Models from the probabilistic trend family require the estimation of development trends, calendar year inflation trends and exposure levels. Consequently, our actuarial staff monitors a number of trends and measures to gain key business insights necessary for exercising appropriate judgment when estimating the parameters mentioned, such as:

- company and industry pricing
- company and industry exposure
- company and industry loss frequency and severity
- past large loss events such as hurricanes
- company and industry premium
- company in-force policy count

These trends and measures also support the estimation of ultimate accident year loss ratios needed for applying the Bornhuetter-Ferguson methods and for assessing the reasonability of all IBNR reserve estimates computed. Our actuarial staff reviews these trends and measures quarterly, updating parameters derived from them as necessary.

Quarterly, our actuarial staff summarizes their reserve analysis by preparing an actuarial best estimate and a range of reasonable IBNR reserves intended to reflect the uncertainty of the estimate. An inter-departmental committee that includes our actuarial management team reviews the results of each quarterly reserve analysis. The committee establishes management's best estimate of IBNR reserves, which is the amount that is included in each period's financial statements. In addition to the information provided by actuarial staff, the committee also considers factors such as:

- large loss activity and trends in large losses
- new business activity
- judicial decisions
- general economic trends such as inflation
- trends in litigiousness and legal expenses
- product and underwriting changes
- changes in claims practices

The determination of management's best estimate, like the preparation of the reserve analysis that supports it, involves considerable judgment. Changes in reserving data or the trends and factors that influence reserving data may signal fundamental shifts or may simply reflect single-period anomalies. Even if a change reflects a fundamental shift, the full extent of the change may not become evident until years later. Moreover, since our methods and models do not explicitly relate many of the factors we consider directly to reserve levels, we typically cannot quantify the precise impact of such factors on the adequacy of reserves prospectively or retrospectively.

Due to the uncertainties described above, our ultimate loss experience could prove better or worse than our carried reserves reflect. To the extent that reserves are inadequate and increased, the amount of the increase is a charge in the period that the deficiency is recognized, raising our loss and loss expense ratio and reducing earnings. To the extent that reserves are redundant and released, the amount of the release is a credit in the period that the redundancy is recognized, reducing our loss and loss expense ratio and increasing earnings.

Key Assumptions – Loss Reserving

Our actuarial staff makes a number of key assumptions when using their methods and models to derive IBNR reserve estimates. Appropriate reliance on these key assumptions essentially entails determinations of the likelihood that statistically significant patterns in historical data may extend into the future. The four most significant of the key assumptions used by our actuarial staff and approved by management are:

- Emergence of loss and defense and cost containment expenses, also referred to as DCCE, on an accident year basis. Historical paid loss, reported loss and paid DCCE data for the business lines we analyze contain patterns that reflect how unpaid losses, unreported losses and unpaid DCCE as of a financial statement date will emerge in the future on an accident year basis. Unless our actuarial staff or management identifies reasons or factors that invalidate the extension of historical patterns into the future, these patterns can be used to make projections necessary for estimating IBNR reserves. Our actuaries significantly rely on this assumption in the application of all methods and models mentioned above.
- Calendar year inflation. For long-tail and mid-tail business lines, calendar year inflation trends for future paid losses and paid DCCE do not vary significantly from a stable, long-term average. Our actuaries base reserve estimates derived from probabilistic trend family models on this assumption.
- Exposure levels. Historical earned premiums, when adjusted to reflect common levels of product pricing and loss cost inflation, can serve as a proxy for historical exposures. Our actuaries require this assumption to estimate expected loss ratios and expected DCCE ratios used by the Bornhuetter-Ferguson reserving methods. They may also use this assumption to establish exposure levels for recent accident years, characterized by “green” or immature data, when working with probabilistic trend family models.
- Claims having atypical emergence patterns. Characteristics of certain subsets of claims, such as high frequency, high severity, or mass tort claims, have the potential to distort patterns contained in historical paid loss, reported loss and paid DCCE data. When testing indicates this to be the case for a particular subset of claims, our actuaries segregate these claims from the data and analyze them separately. Subsets of claims that could fall into this category include hurricane claims or claims for other weather events where total losses we incurred were very large, individual large claims and asbestos and environmental claims.

These key assumptions have not changed since 2005, when our actuarial staff began using probabilistic trend family models to estimate IBNR reserves.

Paid losses, reported losses and paid DCCE are subject to random as well as systematic influences. As a result, actual paid losses, reported losses and paid DCCE are virtually certain to differ from projections. Such differences are consistent with what specific models for our business lines predict and with the related patterns in the historical data used to develop these models. As a result, management does not closely monitor statistically insignificant differences between actual and projected data.

Reserve Estimate Variability

Management believes that the standard error of a reserve estimate, a measure of the estimate’s variability, provides the most appropriate measure of the estimate’s sensitivity. The reserves we establish depend on the models we use and the related parameters we estimate in the course of conducting reserve analyses. However, the actual amount required to settle all outstanding insured claims, including IBNR claims, as of a financial statement date depends on stochastic, or random, elements as well as the systematic elements captured by our models and estimated model parameters. For the lines of business we write, process uncertainty – the inherent variability of loss and loss expense payments – typically contributes more to the imprecision of a reserve estimate than parameter uncertainty.

Consequently, a sensitivity measure that ignores process uncertainty would provide an incomplete picture of the reserve estimate’s sensitivity. Since a reserve estimate’s standard error accounts for both process and parameter uncertainty, it reflects the estimate’s full sensitivity to a range of reasonably likely scenarios.

The table below provides standard errors and reserve ranges by major property casualty lines of business and in total for net loss and loss expense reserves as well as the potential effects on our net income, assuming a 35 percent federal tax rate. Standard errors and reserve ranges for assorted groupings of these lines of business cannot be computed by simply adding the standard errors and reserve ranges of the component lines of business, since such an approach would ignore the effects of product diversification. See Liquidity and Capital Resources, Property Casualty Loss and Loss Expense Obligations and Reserves, Range of Reasonable Reserves, for more details on our total reserve range. While the table reflects our assessment of the most likely range within which each line's actual unpaid loss and loss expenses may fall, one or more lines' actual unpaid loss and loss expenses could nonetheless fall outside of the indicated ranges.

(Dollars in millions)	Net loss and loss expense range of reserves				
	Carried reserves	Low point	High point	Standard error	Net income effect
At December 31, 2014					
Total	$4,156	$3,922	$4,296		
Commercial casualty	$1,647	$1,477	$1,779	$151	$98
Commercial property	230	202	244	21	14
Commercial auto	431	411	450	19	12
Workers' compensation	983	873	1,067	97	63
Personal auto	214	204	223	9	6
Homeowners	104	95	112	8	5
At December 31, 2013					
Total	$3,942	$3,727	$4,078		
Commercial casualty	$1,532	$1,368	$1,643	$138	$90
Commercial property	241	223	260	19	12
Commercial auto	371	352	391	19	12
Workers' compensation	966	873	1,059	93	60
Personal auto	198	189	207	9	6
Homeowners	106	98	113	7	5

Life Insurance Policy Reserves

We establish the reserves for traditional life insurance policies based on expected expenses, mortality, morbidity, withdrawal rates and investment yields, including a provision for uncertainty. Once these assumptions are established, they generally are maintained throughout the lives of the contracts. We use both our own experience and industry experience adjusted for historical trends in arriving at our assumptions for expected mortality, morbidity and withdrawal rates. We use our own experience and historical trends for setting our assumptions for expected expenses. We base our assumptions for expected investment income on our own experience adjusted for current economic conditions.

We establish reserves for our universal life, deferred annuity and investment contracts equal to the cumulative account balances, which include premium deposits plus credited interest less charges and withdrawals. Some of our universal life insurance policies contain no-lapse guarantee provisions. For these policies, we establish a reserve in addition to the account balance based on expected no-lapse guarantee benefits and expected policy assessments.

Asset Impairment

Our fixed-maturity and equity investment portfolios are our largest assets. The company's asset impairment committee continually monitors the holdings in these portfolios and all other assets for signs of other-than-temporary or permanent impairment. The committee monitors decreases in the fair value of invested assets; an accumulation of company costs in excess of the amount originally expected to acquire or construct an asset; uncollectability of all receivable assets, or other factors such as bankruptcy, deterioration of creditworthiness, failure to pay interest or dividends; signs indicating that the receivable carrying amount may not be recoverable; and changes in legal factors or in the business climate.

The application of our impairment policy resulted in other-than-temporary impairment (OTTI) charges that reduced our income before income taxes by $24 million in 2014, $2 million in 2013 and $33 million in 2012. Impairment charges are recorded for other-than-temporary declines in value, if, in the asset impairment committee's judgment, the value is not expected to be recouped within a designated recovery period. OTTI losses represent noncash charges to income and are reported as realized investment losses.

Our internal investment portfolio managers monitor their assigned portfolios. If a security is valued below cost or amortized cost, the portfolio managers undertake additional reviews. Such declines often occur in conjunction with events taking place in the overall economy and market, combined with events specific to the industry or operations of the issuing organization. Managers review quantitative measurements such as a declining trend in fair value, the extent of the fair value decline and the length of time the value of the security has been depressed, as well as qualitative measures such as pending events, credit ratings and issuer liquidity. We are even more proactive when these declines in valuation are greater than might be anticipated when viewed in the context of overall economic and market conditions. We provide information about valuations of our invested assets in Item 8, Note 2 of the Consolidated Financial Statements.

All securities valued below 100 percent of cost or amortized cost are reported to the asset impairment committee for evaluation. Securities valued between 95 percent and 100 percent of cost or amortized cost are reviewed but not monitored separately by the committee. When evaluating for OTTI, the committee considers the company's intent and ability to retain a security for a period adequate to recover its cost. Because of the company's financial strength and other factors discussed below, management may not impair certain securities even when they are fair valued below cost or amortized cost.

Securities that have previously been other-than-temporarily impaired are evaluated based on their adjusted cost or amortized cost and further written down, if deemed appropriate. We provide detailed information about securities fair valued in a continuous loss position at year-end 2014 in Item 7A, Application of Asset Impairment Policy.

When determining OTTI charges for our fixed-maturity portfolio, management places significant emphasis on whether issuers of debt are current on contractual payments and whether future contractual amounts are likely to be paid. Our fixed-maturity invested asset impairment policy states that OTTI is considered to have occurred (1) if we intend to sell the impaired fixed-maturity security; (2) if it is more likely than not we will be required to sell the fixed-maturity security before recovery of its amortized cost basis; or (3) if the present value of the expected cash flows is not sufficient to recover the entire amortized cost basis. If we intend to sell or it is more likely than not we will be required to sell, the amortized cost of any such securities is reduced to fair value as the new amortized cost basis, and a realized loss is recorded in the quarter in which it is recognized. When we believe that full collection of interest and/or principal is not likely, we determine the net present value of future cash flows by using the effective interest rate implicit in the security at the date of acquisition as the discount rate and compare that amount to the amortized cost and fair value of the security. The difference between the net present value of the expected future cash flows and amortized cost of the security is considered a credit loss and recognized as a realized loss in the quarter in which it occurs. The difference between the fair value and the net present value of the cash flows of the security, the noncredit loss, is recognized in other comprehensive income as an unrealized loss.

When determining OTTI charges for our equity portfolio, our invested asset impairment policy considers qualitative and quantitative factors, including facts and circumstances specific to individual securities, asset classes, the financial condition of the issuer, changes in dividend payment, the length of time fair value had been less than cost, the severity of the decline in fair value below cost, the volatility of the security and our ability and intent to hold each position until its forecasted recovery.

For each of our equity securities in an unrealized loss position at December 31, 2014, we applied the objective quantitative and qualitative criteria of our invested asset impairment policy for OTTI. Based on the individual qualitative and quantitative factors, as discussed above, we evaluate and determine an expected recovery period for each security. A change in the condition of a security can warrant impairment before the expected recovery period. If the security has not recovered cost within the expected recovery period, the security is other-than-temporarily impaired. Our long-term equity investment philosophy, emphasizing companies with strong indications of paying and growing dividends, combined with our strong statutory capital and surplus, liquidity and cash flow, provide us the ability to hold these investments through what we believe to be slightly longer recovery periods during times of historic levels of market volatility.

Securities considered to have a temporary decline would be expected to recover their cost or amortized cost, which may be at maturity. Under the same accounting treatment as fair value gains, temporary declines (changes in the fair value of these securities) are reflected in shareholders' equity on our Consolidated Balance Sheets in accumulated other comprehensive income (AOCI), net of tax, and have no impact on net income.

Fair Value Measurements

Valuation of Financial Instruments
Valuation of financial instruments, primarily securities held in our investment portfolio, is a critical component of our year-end financial statement preparation. Accounting Standards Codification (ASC) 820-10, Fair Value Measurements and Disclosures, defines fair value as the exit price or the amount that would be (1) received to sell an asset or (2) paid to transfer a liability in an orderly transaction between marketplace participants at the measurement date. When determining an exit price, we must, whenever possible, rely upon observable market data.

We have categorized our financial instruments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level that is significant to the fair value measurement of the instrument. While we consider pricing data from outside services, we ultimately determine whether the data or inputs used by these outside services are observable or unobservable.

Financial assets and liabilities recorded in the Consolidated Balance Sheets are categorized based on the inputs to the valuation techniques as described in Item 8, Note 3 of the Consolidated Financial Statements.

Level 1 and Level 2 Valuation Techniques
Over 99 percent of the $14.318 billion of securities in our investment portfolio, measured at fair value, are classified as Level 1 or Level 2. Financial assets that fall within Level 1 and Level 2 are priced according to observable data from identical or similar securities that have traded in the marketplace. Also within Level 2 are securities that are valued by outside services or brokers where we have evaluated and verified the pricing methodology and determined that the inputs are observable.

Level 3 Valuation Techniques
Financial assets that fall within the Level 3 hierarchy are valued based upon unobservable market inputs, normally because they are not actively traded on a public market. Pricing for each Level 3 security is based upon inputs that are market driven, including third-party reviews provided to the issuer or broker quotes. We placed in the Level 3 hierarchy securities for which we were unable to obtain the pricing methodology or we could not consider the price provided as binding. Pricing for securities classified as Level 3 could not be corroborated by similar securities priced using observable inputs.

Management ultimately determined the pricing for each Level 3 security that we considered to be the best exit price valuation. As of December 31, 2014, total Level 3 assets were less than 1 percent of our investment portfolio measured at fair value. Broker quotes are obtained for thinly traded securities that subsequently fall within the Level 3 hierarchy. We have generally obtained and evaluated two nonbinding quotes from brokers; our investment professionals determine our best estimate of fair value.

Employee Benefit Pension Plan

We have a defined benefit pension plan that was modified during 2008; refer to Item 8, Note 13 of the Consolidated Financial Statements, for additional information. Contributions and pension costs are developed from annual actuarial valuations. These valuations involve key assumptions including discount rates, expected return on plan assets and compensation increase rates, which are updated annually. Any adjustments to these assumptions are based on considerations of current market conditions. Therefore, changes in the related pension costs or credits may occur in the future due to changes in assumptions.

Key assumptions used in developing the 2014 benefit obligation for our qualified plan were a 4.25 percent discount rate and rates of compensation increases ranging from 2.75 percent to 3.25 percent. To determine the discount rate, a theoretical settlement portfolio of high-quality, rated corporate bonds was chosen to provide payments approximately matching the plan's projected benefit payments. A single interest rate was determined, resulting in a discounted value of the plan's benefit payments that equates to the market value of the selected bonds. The discount rate is reflective of current market interest rate conditions and our plan's liability characteristics.

Key assumptions used in developing the 2014 net pension expense for our qualified plan were a 5.15 percent discount rate, a 7.25 percent expected return on plan assets and rates of compensation increases ranging from 2.75 percent to 3.25 percent.

In 2014, the net pension expense was $13 million. In 2015, we expect the net pension expense to be approximately $14 million.

Holding all other assumptions constant, a 0.5 percentage-point decrease in the discount rate would decrease our 2015 income before income taxes by $1 million. A 0.5 percentage point decrease in the expected return on plan assets would decrease our 2015 income before income taxes by $1 million.

The fair value of the plan assets exceeded the accumulated benefit obligation by $4 million and $23 million at year-end 2014 and 2013, respectively. The fair value of the plan assets was $31 million less than the projected plan benefit obligation at year-end 2014 and $4 million less at year-end 2013. Market conditions and interest rates significantly affect future assets and liabilities of the pension plan. During the first quarter of 2015, we contributed $5 million to our qualified plan.

Deferred Policy Acquisition Costs

We establish a deferred asset for expenses associated with successfully acquiring property casualty and life insurance policies, primarily commissions, premium taxes and underwriting costs. Underlying assumptions are updated periodically to reflect actual experience, and we evaluate our deferred acquisition cost recoverability.

For property casualty insurance policies, deferred acquisition costs are amortized over the terms of the policies. These costs are principally agent commissions, premium taxes and certain underwriting costs related to successful contract acquisition, which are deferred and amortized into net income as premiums are earned. We assess recoverability of deferred acquisition costs at the segment level, consistent with the ways we acquire, service, manage and measure profitability. Deferred acquisition costs track with the change in premiums. Our property casualty insurance operations consist of three segments, commercial lines insurance, personal lines insurance and excess and surplus lines insurance.

For life insurance policies, acquisition costs are amortized into income either over the premium-paying period of the policies or the life of the policy, depending on the policy type. These costs are principally agent commissions and underwriting costs related to successful contract acquisition. We analyze our acquisition cost assumptions periodically to reflect actual experience; we evaluate our deferred acquisition cost for recoverability; and we regularly conduct reviews for potential premium deficiencies or loss recognition. Changes in the amounts or timing of estimated future profits could result in adjustments to the accumulated amortization of these costs.

Recent Accounting Pronouncements

Information about recent accounting pronouncements is provided in Item 8, Note 1 of the Consolidated Financial Statements. We have determined that recent accounting pronouncements have not had, nor are they expected to have, any material impact on our consolidated financial statements.

Financial Results

Consolidated financial results primarily reflect the results of our five reporting segments. These segments are defined based on financial information we use to evaluate performance and to determine the allocation of assets.

- Commercial lines insurance
- Personal lines insurance
- Excess and surplus lines insurance
- Life insurance
- Investments

We report as Other the noninvestment operations of the parent company and its noninsurer subsidiary, CFC Investment Company.

We measure profit or loss for our commercial lines, personal lines and excess and surplus lines and life insurance segments based upon underwriting results (profit or loss), which represent net earned premium less loss and loss expenses and underwriting expenses on a pretax basis. We also frequently evaluate results for our consolidated property casualty insurance operations, which is the total of our commercial, personal, and excess and surplus lines insurance results. Underwriting results and segment pretax operating income are not substitutes for net income determined in accordance with GAAP.

For our consolidated property casualty insurance operations as well as the insurance segments, statutory accounting data and ratios are key performance indicators that we use to assess business trends and to make comparisons to industry results, since GAAP-based industry data generally is not as readily available.

Investments held by the parent company and the investment portfolios for the insurance subsidiaries are managed and reported as the investments segment, separate from the underwriting businesses. Net investment income and net realized investment gains and losses for our investment portfolios are discussed in the Investments Results.

The calculations of segment data are described in more detail in Item 8, Note 18, of the Consolidated Financial Statements. The following sections provide analysis and discussion of results of operations for each of the five segments.

Consolidated Property Casualty Insurance Results

Earned and net written premiums for our consolidated property casualty operations grew in 2014, reflecting higher pricing and strategic initiatives for targeted growth. A key measure of property casualty profitability is underwriting profit or loss. Our 2014 underwriting profit of $186 million was $47 million less than in 2013. The decrease included a $32 million increase in natural catastrophe losses, mostly from severe weather. It also included a $52 million increase from weather-related losses not identified as part of designated catastrophe events for the property casualty industry, typically referred to as noncatastrophe weather losses. The unfavorable effects of those higher weather-related losses in aggregate during 2014 offset the benefits of higher pricing and our ongoing initiatives to improve pricing precision and loss experience related to claims and loss control practices. Prior accident year loss experience before catastrophes during 2014 was favorable but less so than in 2013. The less favorable experience was primarily due to re-estimates of losses and loss expenses incurred but not reported (IBNR), particularly for our commercial casualty line of business, as discussed in Commercial Lines Insurance Results.

The table below highlights property casualty results, with analysis and discussion in the sections that follow.

Overview – Three-Year Highlights

(Dollars in millions)	Years ended December 31,			2014-2013	2013-2012
	2014	2013	2012	Change %	Change %
Earned premiums	$4,045	$3,713	$3,344	9	11
Fee revenues	6	4	6	50	(33)
Total revenues	4,051	3,717	3,350	9	11
Loss and loss expenses from:					
Current accident year before catastrophe losses	2,495	2,249	2,160	11	4
Current accident year catastrophe losses	230	199	373	16	(47)
Prior accident years before catastrophe losses	(72)	(120)	(357)	40	66
Prior accident years catastrophe losses	(26)	(27)	(39)	4	31
Total loss and loss expenses	2,627	2,301	2,137	14	8
Underwriting expenses	1,238	1,183	1,076	5	10
Underwriting profit	$186	$233	$137	(20)	70
Ratios as a percent of earned premiums:				Pt. Change	Pt. Change
Current accident year before catastrophe losses	61.7 %	60.6 %	64.6 %	1.1	(4.0)
Current accident year catastrophe losses	5.7	5.4	11.1	0.3	(5.7)
Prior accident years before catastrophe losses	(1.8)	(3.3)	(10.7)	1.5	7.4
Prior accident years catastrophe losses	(0.6)	(0.8)	(1.1)	0.2	0.3
Total loss and loss expense	65.0	61.9	63.9	3.1	(2.0)
Underwriting expense	30.6	31.9	32.2	(1.3)	(0.3)
Combined ratio	95.6 %	93.8 %	96.1 %	1.8	(2.3)
Combined ratio:	95.6 %	93.8 %	96.1 %	1.8	(2.3)
Contribution from catastrophe losses and prior years reserve development	3.3	1.3	(0.7)	2.0	2.0
Combined ratio before catastrophe losses and prior years reserve development	92.3 %	92.5 %	96.8 %	(0.2)	(4.3)

Performance highlights for consolidated property casualty operations include:

- Premiums – Strong growth in renewal written premiums drove increases in earned premiums and net written premiums for both 2014 and 2013, rising in each of our property casualty segments. Higher and more precise pricing continues to benefit operating results and is further discussed by segment in the results sections below. New business written premiums in 2014 were down $40 million, compared with the record-high amount we reported in 2013. The year 2013 also represented the sixth straight year of higher new business premiums, reflecting our premium growth initiatives from recent years. Those initiatives also favorably affect growth in subsequent years, particularly as newer agency relationships mature over time. Agents appointed during 2014 or

2013 produced an increase in standard lines new business of $20 million during 2014, compared with 2013. A higher level of insured exposures, reflecting improvement in some areas of the economy, also favorably affected growth in net written premiums, primarily in our commercial lines insurance segment. The contributions to commercial lines premiums from audits, which are significantly affected by economic trends, are further discussed in Commercial Lines Insurance Results.

Other written premiums – primarily premiums ceded to our reinsurers as part of our reinsurance program – in total reduced 2014 net written premiums by $11 million more than in 2013. A decrease in ceded premiums contributed $22 million to net written premium growth for 2014, compared with 2013. Other written premiums also included a less favorable adjustment for 2014, compared with 2013, for estimated direct written premiums of policies in effect but not yet processed in our commercial lines insurance segment. This written premium adjustment has an immaterial effect on earned premiums.

The table below analyzes premium revenue components and trends. Premium trends by segment are further discussed for the respective property casualty segments.

(Dollars in millions)	Years ended December 31,			2014-2013	2013-2012
	2014	2013	2012	Change %	Change %
Agency renewal written premiums	$3,794	$3,493	$3,138	9	11
Agency new business written premiums	503	543	501	(7)	8
Other written premiums	(154)	(143)	(157)	(8)	9
Net written premiums	4,143	3,893	3,482	6	12
Unearned premium change	(98)	(180)	(138)	46	(30)
Earned premiums	$4,045	$3,713	$3,344	9	11

- Combined ratio – The 2014 combined ratio rose 1.8 percentage points compared with 2013, as higher weather-related losses largely offset our recent-year initiatives to improve pricing precision and loss experience related to claims and loss control practices. Compared with 2013, the 2014 ratio for natural catastrophe losses rose 0.5 points while the ratio for noncatastrophe weather losses rose 1.0 points. In addition, higher estimates of incurred but not reported (IBNR) losses and loss expenses for our commercial casualty line of business increased our 2014 consolidated property casualty combined ratio by 1.5 points, compared with 2013. We further discuss those ratios and ones related to reserve development in the sections that follow our discussion below in Catastrophe Losses Incurred.

Our statutory combined ratio was 95.1 percent in 2014 compared with 92.7 percent in 2013 and 95.4 percent in 2012. The estimated statutory combined ratio for the property casualty industry, with the industry's ratio excluding its mortgage and financial guaranty lines of business, was 97.2 percent in 2014, 96.4 percent in 2013 and 102.5 percent in 2012. The contribution of catastrophe losses to our statutory combined ratio was 5.1 percentage points in 2014, 4.6 percentage points in 2013 and 10.0 percentage points in 2012, compared with an industry estimate of 4.4, 3.9 and 8.0 percentage points, respectively. Components of the combined ratio are discussed below, followed by additional discussion by segment.

Catastrophe loss trends are an important factor in assessing trends for overall underwriting results. Our 10-year historical annual average contribution of catastrophe losses to the combined ratio was 6.0 percentage points at December 31, 2014. Our five-year average was 7.4 percentage points.

The following table shows catastrophe losses incurred, net of reinsurance, for the past three years, as well as the effect of loss development on prior period catastrophe reserves. We individually list declared catastrophe events for which our incurred losses reached or exceeded $10 million.

Catastrophe Losses Incurred
(Dollars in millions, net of reinsurance)

Dates	Events	Regions	Commercial lines	Personal lines	Excess and surplus lines	Total
2014						
Jan. 5-8	Freezing, ice, snow, wind	Midwest, Northeast, South	$45	$24	$1	$70
Apr. 27-May 1	Flood, hail, wind	Midwest, Northeast, South	4	9	—	13
May 10-13	Flood, hail, wind	Midwest	6	7	—	13
May 18-19	Flood, hail, wind	Midwest, South, West	23	19	1	43
Jun. 3-4	Flood, hail, wind	Midwest	9	1	—	10
All other 2014 catastrophes			48	32	1	81
Development on 2013 and prior catastrophes			(15)	(11)	—	(26)
Calendar year incurred total			$120	$81	$3	$204
2013						
Mar. 18-19	Hail, wind	South	$4	$7	$—	$11
Apr. 7-11	Hail, lightning, wind	Midwest, West	12	10	—	22
Apr. 16-19	Hail, lightning, wind	Midwest	5	6	—	11
May. 18-20	Hail, lightning, wind	Midwest, Northeast, South	9	1	—	10
May. 28-29	Hail, lightning, wind	South	8	2	1	11
Jun. 24-26	Hail, lightning, wind	Midwest, Northeast	5	6	—	11
Jul. 9-11	Hail, lightning, wind	Midwest, Northeast	5	6	—	11
Jul. 23-24	Hail, lightning, wind	Midwest, South	14	4	—	18
Aug. 6-7	Hail, lightning, wind	Midwest	6	9	—	15
Nov. 17-18	Hail, lightning, wind	Midwest, South	18	17	—	35
All other 2013 catastrophes			28	16	—	44
Development on 2012 and prior catastrophes			(17)	(10)	—	(27)
Calendar year incurred total			$97	$74	$1	$172
2012						
Feb. 28-29	Hail, tornado, wind	Midwest	$19	$6	$—	$25
Mar. 2-3	Hail, tornado, wind	Midwest, South	30	48	—	78
Apr. 28-29	Hail, lightning, wind	Midwest, South	53	26	1	80
Jun. 28-Jul. 2	Hail, lightning, wind	Midwest, Northeast, South	39	42	—	81
Jul. 2-4	Hail, lightning, wind	Midwest, Northeast	7	5	—	12
Oct. 28-31	Sandy	Midwest, Northeast, South	20	10	—	30
All other 2012 catastrophes			43	23	1	67
Development on 2011 and prior catastrophes			(17)	(22)	—	(39)

Calendar year incurred total	$ 194	$ 138	$ 2	$ 334

Consolidated Property Casualty Insurance Loss and Loss Expenses

Loss and loss expenses include both net paid losses and reserve changes for unpaid losses as well as the associated loss expenses. Most of the incurred losses and loss expenses shown in the consolidated property casualty insurance results three-year highlights table are for the respective current accident years, with reserve development on prior accident years shown separately. Since less than half of our consolidated property casualty current accident year incurred losses and loss expenses represents net paid amounts, the majority represents reserves for our estimate of ultimate losses and loss expenses. These reserves develop over time, and we re-estimate previously reported reserves as we learn more about the development of the related claims. The table below illustrates that development. For example, the 66.0 percent accident year 2013 loss and loss expense ratio reported as of December 31, 2013, developed favorably by 1.6 percentage points to 64.4 percent due to claims settling for less than previously estimated, or due to updated reserve estimates for unpaid claims, as of December 31, 2014. Accident years 2013 and 2012 have both developed favorably, as indicated by the progression over time for the ratios in the table.

(Dollars in millions)

Accident year loss and loss expenses incurred and ratios to earned premiums:									
Accident year:	2014	2013	2012	2014		2013		2012	
as of December 31, 2014	$2,725	$2,391	$2,416	67.4	%	64.4	%	72.3	%
as of December 31, 2013		2,448	2,431			66.0		72.7	
as of December 31, 2012			2,533					75.7	

Catastrophe loss trends, discussed above, account for much of the movement in current accident year loss and loss expense ratios for years 2012 to 2013, while noncatastrophe weather and higher commercial casualty IBNR, noted above, account for most of the change between 2013 to 2014. Catastrophe losses added 5.7 percentage points in 2014, 5.4 points in 2013 and 11.1 points in 2012 to the respective consolidated property casualty current accident year loss and loss expense ratios in the table above.

The 61.7 percent ratio for current accident year loss and loss expenses before catastrophe losses for 2014 rose 1.1 percentage points compared with the 60.6 percent accident year 2013 ratio measured as of December 31, 2013. Noncatastrophe weather losses and higher commercial casualty IBNR, noted above, largely accounted for the increase and offset favorable effects from initiatives to improve pricing precision and loss experience related to claims and loss control practices.

Reserve development on prior accident years continued to net to a favorable amount in 2014. We recognized $98 million in favorable development in 2014, less benefit than $147 million in 2013 and $396 million in 2012. Of the $49 million decrease in 2014, compared with 2013, $74 million was attributable to our commercial casualty line of business. Approximately 87 percent of our net favorable reserve development on prior accident years recognized during 2014 occurred in our workers’ compensation and commercial property lines of business. In 2013, our commercial casualty and workers' compensation lines of business were responsible for approximately 57 percent of the favorable reserve development. As discussed in Liquidity and Capital Resources, Property Casualty Loss and Loss Expense Obligations and Reserves, Property Casualty Insurance Development of Estimated Reserves by Accident Year, commercial casualty and workers' compensation are considered long-tail lines with potential for revisions inherent in estimating reserves. Favorable development recognized during 2012 was also primarily from our commercial casualty and workers’ compensation lines of business. Development by line of business is further analyzed in Property Casualty Insurance Development of Estimated Reserves by Accident Year.

Consolidated Property Casualty Insurance Losses by Size

(Dollars in millions, net of reinsurance)	Years ended December 31, 2014	2013	2012	2014-2013 Change %	2013-2012 Change %
Current accident year losses greater than $5,000,000	$30	$23	$22	30	5
Current accident year losses $1,000,000-$5,000,000	172	167	150	3	11
Large loss prior accident year reserve development	7	44	9	(84)	nm
Total large losses incurred	209	234	181	(11)	29
Losses incurred but not reported	133	123	(14)	8	nm
Other losses excluding catastrophe losses	1,660	1,412	1,311	18	8
Catastrophe losses	197	166	321	19	(48)
Total losses incurred	$2,199	$1,935	$1,799	14	8
Ratios as a percent of earned premiums:				Pt. Change	Pt. Change
Current accident year losses greater than $5,000,000	0.7 %	0.6 %	0.7 %	0.1	(0.1)
Current accident year losses $1,000,000-$5,000,000	4.3	4.5	4.5	(0.2)	—
Large loss prior accident year reserve development	0.2	1.2	0.3	(1.0)	0.9
Total large loss ratio	5.2	6.3	5.5	(1.1)	0.8
Losses incurred but not reported	3.3	3.3	(0.4)	—	3.7
Other losses excluding catastrophe losses	41.0	38.0	39.1	3.0	(1.1)
Catastrophe losses	4.9	4.5	9.6	0.4	(5.1)
Total loss ratio	54.4 %	52.1 %	53.8 %	2.3	(1.7)

In 2014, total large losses incurred decreased by $25 million or 11 percent, net of reinsurance. The corresponding ratio decreased 1.1 percentage points. Large loss trends are further analyzed in the segment discussion and analysis that follows discussion of consolidated property casualty results. Our analysis of large losses incurred indicated no unexpected concentration of these losses and reserve increases by geographic region, policy inception, agency or field marketing territory. We believe the inherent volatility of aggregate loss experience for our portfolio of larger policies is greater than that of our portfolio of smaller policies, and we continue to monitor the volatility in addition to general inflationary trends in loss costs.

Consolidated Property Casualty Insurance Underwriting Expenses

(Dollars in millions)	Years ended December 31, 2014	2013	2012	2014-2013 Change %	2013-2012 Change %
Commission expenses	$744	$705	$635	6	11
Other underwriting expenses	478	462	425	3	9
Policyholder dividends	16	16	16	0	0
Total underwriting expenses	$1,238	$1,183	$1,076	5	10
Ratios as a percent of earned premiums:				Pt. Change	Pt. Change
Commission expense	18.4 %				