UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Fiscal Year Ended December 31, 2013 **Commission File No. 1-13653**

AMERICAN FINANCIAL GROUP, INC.

Incorporated under the Laws of Ohio **IRS Employer I.D. No. 31-1544320**

301 East Fourth Street, Cincinnati, Ohio 45202
(513) 579-2121

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock	New York Stock Exchange and Nasdaq Global Select Market
6-3/8% Senior Notes due June 12, 2042	New York Stock Exchange
5-3/4% Senior Notes due August 25, 2042	New York Stock Exchange
7% Senior Notes due September 30, 2050	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act: None

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months. Yes ☑ No ☐

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

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

Large accelerated filer ☑ 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 ☑

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the Registrant's most recently completed second fiscal quarter: $3.9 billion.

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date: 89,560,038 shares (excluding 14.9 million shares owned by subsidiaries) as of February 1, 2014.

Documents Incorporated by Reference:

Proxy Statement for 2014 Annual Meeting of Stockholders (portions of which are incorporated by reference into Part III hereof).

AMERICAN FINANCIAL GROUP, INC.

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FORWARD-LOOKING STATEMENTS

The disclosures in this Form 10-K contain certain forward-looking statements that are subject to numerous assumptions, risks or uncertainties. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Some of the forward-looking statements can be identified by the use of words such as "anticipates", "believes", "expects", "projects", "estimates", "intends", "plans", "seeks", "could", "may", "should", "will" or the negative version of those words or other comparable terminology. Such forward-looking statements include statements relating to: expectations concerning market and other conditions and their effect on future premiums, revenues, earnings and investment activities; recoverability of asset values; expected losses and the adequacy of reserves for long-term care, asbestos, environmental pollution and mass tort claims; rate changes; and improved loss experience.

Actual results and/or financial condition could differ materially from those contained in or implied by such forward-looking statements for a variety of reasons including but not limited to the following and those discussed in Item 1A — Risk Factors.

- *changes in financial, political and economic conditions, including changes in interest and inflation rates, currency fluctuations and extended economic recessions or expansions in the U.S. and/or abroad;*
- *performance of securities markets;*
- *AFG's ability to estimate accurately the likelihood, magnitude and timing of any losses in connection with investments in the non-agency residential mortgage market;*
- *new legislation or declines in credit quality or credit ratings that could have a material impact on the valuation of securities in AFG's investment portfolio;*
- *the availability of capital;*
- *regulatory actions (including changes in statutory accounting rules);*
- *changes in the legal environment affecting AFG or its customers;*
- *tax law and accounting changes;*
- *levels of natural catastrophes and severe weather, terrorist activities (including any nuclear, biological, chemical or radiological events), incidents of war or losses resulting from civil unrest and other major losses;*
- *development of insurance loss reserves and establishment of other reserves, particularly with respect to amounts associated with asbestos and environmental claims and AFG's run-off long-term care business;*
- *availability of reinsurance and ability of reinsurers to pay their obligations;*
- *trends in persistency, mortality and morbidity;*
- *competitive pressures, including those in the annuity distribution channels;*
- *the ability to obtain adequate rates and policy terms; and*
- *changes in AFG's credit ratings or the financial strength ratings assigned by major ratings agencies to AFG's operating subsidiaries.*

The forward-looking statements herein are made only as of the date of this report. The Company assumes no obligation to publicly update any forward-looking statements.

PART I

ITEM 1

Business

Introduction

American Financial Group, Inc. (“AFG” or the “Company”) is a holding company that, through the operations of Great American Insurance Group, is engaged primarily in property and casualty insurance, focusing on specialized commercial products for businesses, and in the sale of fixed and fixed-indexed annuities in the retail, financial institutions and education markets. Its address is 301 East Fourth Street, Cincinnati, Ohio 45202; its phone number is (513) 579-2121. SEC filings, news releases, AFG’s Code of Ethics applicable to directors, officers and employees and other information may be accessed free of charge through AFG’s Internet site at: www.AFGinc.com. (Information on AFG’s Internet site is not part of this Form 10-K.)

Property and Casualty Insurance Segment

General

AFG’s property and casualty operations provide a wide range of commercial coverages through the approximately 30 niche insurance businesses that make up the Great American Insurance Group. AFG’s property and casualty insurance operations ultimately report to a single senior executive and operate under a business model that allows local decision-making for underwriting, claims and policy servicing in each of the niche operations. Each business is managed by experienced professionals in particular lines or customer groups and operates autonomously but with certain central controls and accountability. The decentralized approach allows each unit the autonomy necessary to respond to local and specialty market conditions while capitalizing on the efficiencies of centralized investment and administrative support functions. AFG’s property and casualty insurance operations employed approximately 5,300 people as of December 31, 2013. These operations are conducted through the subsidiaries listed in the following table, which includes independent ratings and 2013 net written premiums (in millions) for each major subsidiary. Ratings are generally based on concerns for policyholders and agents and are not directed toward the protection of investors. AFG believes that maintaining a rating in the “A” category by A.M. Best is important to compete successfully in most lines of business.

	Ratings		Net Written
Company	AM Best	S&P	Premiums
Great American Insurance Pool (*)	A+	A+	$ 2,135
National Interstate	A	not rated	538
Republic Indemnity	A	A+	216
Marketform Lloyd’s Syndicate	A	A+	166
Mid-Continent Casualty	A+	A+	147
American Empire Surplus Lines	A+	A+	80
Other			59
			$ 3,341

(*) The Great American Insurance Pool represents Great American Insurance Company (“GAI”) and 10 subsidiaries.

The primary objectives of AFG’s property and casualty insurance operations are to achieve solid underwriting profitability and provide excellent service to its policyholders and agents. Underwriting profitability is measured by the combined ratio, which is a sum of the ratios of losses, loss adjustment expenses (“LAE”), underwriting expenses and policyholder dividends to premiums. A combined ratio under 100% indicates an underwriting profit. The combined ratio does not reflect investment income, other income or federal income taxes.

While many costs included in underwriting are readily determined (commissions, administrative expenses and many of the losses on claims reported), the process of determining overall underwriting results is highly dependent upon the use of estimates in the case of losses incurred or expected but not yet reported or developed. Actuarial procedures and projections are used to obtain “point estimates” of ultimate losses. While the process is imprecise and develops amounts which are subject to change over time, management believes that the liabilities for unpaid losses and loss adjustment expenses are adequate.

AFG's statutory combined ratio averaged 94.1% for the period 2011 to 2013 as compared to 102.2% for the property and casualty industry over the same period (Source: "A.M. Best's U.S. Property/Casualty Review & Preview" — February 2014 Edition). AFG believes that its specialty niche focus, product line diversification and underwriting discipline have contributed to the Company's ability to consistently outperform the industry's underwriting results. Management's philosophy is to refrain from writing business that is not expected to produce an underwriting profit even if it is necessary to limit premium growth to do so.

Financial data is reported in accordance with U.S. generally accepted accounting principles ("GAAP") for shareholder and other investment purposes and reported on a statutory basis for insurance regulatory purposes. Major differences for statutory accounting include charging policy acquisition costs to expense as incurred rather than spreading the costs over the periods covered by the policies; reporting investment grade bonds and redeemable preferred stocks at amortized cost rather than fair value; netting of reinsurance recoverables and prepaid reinsurance premiums against the corresponding liabilities rather than reporting such items separately; and charging to surplus certain GAAP assets, such as furniture and fixtures and agents' balances over 90 days old.

Unless indicated otherwise, the financial information presented for the property and casualty insurance operations herein is presented based on GAAP. Statutory information is provided for industry comparisons or where comparable GAAP information is not readily available.

Property and Casualty Results

Performance measures such as underwriting profit or loss and related combined ratios are often used by property and casualty insurers to help users of their financial statements better understand the company's performance. See *Note C — "Segments of Operations"* to the financial statements for the reconciliation of AFG's operating profit by significant business segment to the Statement of Earnings.

The following table shows the performance of AFG's property and casualty insurance operations (dollars in millions):

	2013	2012	2011
Gross written premiums	$ 4,805	$ 4,321	$ 4,106
Ceded reinsurance	(1,464)	(1,372)	(1,336)
Net written premiums	$ 3,341	$ 2,949	$ 2,770
Net earned premiums	$ 3,204	$ 2,847	$ 2,759
Loss and LAE	1,986	1,842	1,694
Special asbestos and environmental ("A&E") charges	54	31	50
Underwriting expenses	1,019	887	835
Underwriting gain	$ 145	$ 87	$ 180
GAAP ratios:			
Loss and LAE ratio	63.7%	65.8%	63.2%
Underwriting expense ratio	31.8%	31.1%	30.2%
Combined ratio	95.5%	96.9%	93.4%
Statutory ratios:			
Loss and LAE ratio	62.2%	63.2%	60.4%
Underwriting expense ratio	31.9%	32.4%	32.3%
Combined ratio	94.1%	95.6%	92.7%
Industry statutory combined ratio (a)			
All lines	97.6%	102.2%	106.7%
Commercial lines	98.3%	104.4%	106.7%

(a) The source of the industry ratios is "A.M. Best's U.S. Property/Casualty — Review & Preview" (February 2014 Edition).

As with other property and casualty insurers, AFG's operating results can be adversely affected by unpredictable catastrophe losses. Certain natural disasters (hurricanes, severe storms, earthquakes, tornadoes, floods, etc.) and other incidents of major loss (explosions, civil disorder, terrorist events, fires, etc.) are classified as catastrophes by industry associations. Losses from these incidents are usually tracked separately from other business of insurers because of their sizable effects on overall operations. Total net losses to AFG's insurance operations from current accident year catastrophes were $31 million in 2013, $46 million in 2012 and $43 million in 2011 and are included in the table above.

AFG generally seeks to reduce its exposure to catastrophes through individual risk selection, including minimizing coastal and known fault-line exposures, and the purchase of reinsurance. AFG's exposure to a catastrophic earthquake or windstorm that industry models indicate could occur once in every 500 years (a "500-year event") is expected to be less than 2.5% of AFG's shareholders' equity.

Property and Casualty Insurance Products

AFG is focused on growth opportunities in what it believes to be more profitable specialty businesses where AFG personnel are experts in particular lines of business or customer groups. The following are examples of AFG's specialty businesses:

Property and Transportation	
Inland and Ocean Marine	Provides coverage primarily for builders' risk, contractors' equipment, property, motor truck cargo, marine cargo, boat dealers, marina operators/dealers and excursion vessels.
Agricultural-related	Provides federally reinsured multi-peril crop (allied lines) insurance covering most perils as well as crop-hail, equine mortality and other coverages for full-time operating farms/ranches and agribusiness operations on a nationwide basis.
Commercial Automobile	Provides coverage for vehicles (such as buses and trucks) in a broad range of businesses including the moving and storage and transportation industries, and a specialized physical damage product for the trucking industry.
Specialty Casualty	
Executive and Professional Liability	Markets coverage for directors and officers of businesses and non-profit organizations; errors and omissions; and provides non-U.S. medical malpractice insurance.
Umbrella and Excess Liability	Provides liability coverage in excess of primary layers.
Excess and Surplus	Provides liability, umbrella and excess coverage for unique, volatile or hard to place risks, using rates and forms that generally do not have to be approved by state insurance regulators.
General Liability	Provides coverage for contractor-related businesses, energy development and production risks, and environmental liability risks.
Targeted Programs	Includes coverage (primarily liability and property) for social service agencies, leisure, entertainment and non-profit organizations, customized solutions for other targeted markets and alternative risk programs using agency captives.
Workers' Compensation	Provides coverage for prescribed benefits payable to employees who are injured on the job.
Specialty Financial	
Fidelity and Surety	Provides fidelity and crime coverage for government, mercantile and financial institutions and surety coverage for various types of contractors and public and private corporations.
Lease and Loan Services	Provides coverage for insurance risk management programs for lending and leasing institutions, including equipment leasing and collateral and lender-placed mortgage property insurance.

Management believes specialization is the key element to the underwriting success of these business units. These specialty businesses are opportunistic and their premium volume will vary based on prevailing market conditions. AFG continually evaluates expansion in existing markets and opportunities in new specialty markets that meet its profitability objectives. For example, in January 2014, AFG announced that it had reached a definitive agreement to acquire Summit Holdings Southeast, Inc. and its related companies. Summit is a leading provider of workers' compensation solutions in the southeastern United

States, with over $500 million in net written premiums in 2013. Likewise, AFG will withdraw from markets that do not meet its profit objectives or business strategy, such as the withdrawal from certain program business in 2010 and 2011.

Premium Distribution

The following table shows the net written premiums by sub-segment for AFG's property and casualty insurance operations for 2013, 2012 and 2011 (dollars in millions):

	2013	2012	2011
Property and transportation	$ 1,547	$ 1,473	$ 1,436
Specialty casualty	1,224	992	867
Specialty financial	486	411	398
Other	84	73	69
	$ 3,341	$ 2,949	$ 2,770

The geographic distribution of statutory direct written premiums by AFG's U.S.-based insurers for 2013, 2012 and 2011 is shown below. Approximately 5% of AFG's direct written premiums in 2013 were derived from non U.S.-based insurers, primarily Marketform, a United Kingdom-based Lloyd's insurer.

	2013	2012	2011		2013	2012	2011
California	13.8%	12.6%	12.0%	Georgia	2.3%	2.4%	2.4%
Illinois	6.8%	7.1%	8.0%	Indiana	2.3%	2.6%	2.9%
Texas	6.8%	6.9%	6.8%	New Jersey	2.3%	2.1%	2.1%
New York	6.6%	5.9%	4.8%	Pennsylvania	2.3%	2.6%	2.6%
Florida	4.3%	4.4%	4.5%	Ohio	2.1%	2.3%	2.4%
Iowa	3.4%	3.7%	3.8%	Oklahoma	2.1%	2.2%	2.0%
Kansas	3.2%	3.7%	4.1%	Nebraska	2.1%	2.2%	2.3%
Missouri	3.1%	2.9%	3.2%	North Dakota	2.1%	2.1%	2.2%
South Dakota	2.7%	2.5%	2.7%	Minnesota	2.0%	2.1%	2.1%
Michigan	2.4%	2.4%	1.8%	Other	24.9%	25.0%	25.1%
North Carolina	2.4%	2.3%	2.2%		100.0%	100.0%	100.0%

Reinsurance

Consistent with standard practice of most insurance companies, AFG reinsures a portion of its property and casualty business with other insurance companies and assumes a relatively small amount of business from other insurers. AFG uses reinsurance for two primary purposes: (i) to provide higher limits of coverage than it would otherwise be willing to provide (i.e. large line capacity) and (ii) to protect its business by reducing the impact of catastrophes. The availability and cost of reinsurance are subject to prevailing market conditions, which may affect the volume and profitability of business that is written. AFG is subject to credit risk with respect to its reinsurers, as the ceding of risk to reinsurers does not relieve AFG of its liability to its insureds until claims are fully settled.

The commercial marketplace requires large policy limits ($25 million or more) in several of AFG's lines of business, including certain executive and professional liability, umbrella and excess liability, and fidelity and surety coverages. Since these limits exceed management's desired exposure to an individual risk, AFG generally enters into reinsurance agreements to reduce its net exposure under such policies to an acceptable level. Reinsurance continues to be available for this large line capacity exposure with satisfactory pricing and terms.

AFG has taken steps to limit its exposure to wind and earthquake losses by purchasing catastrophe reinsurance. In addition, AFG purchases catastrophe reinsurance for its workers' compensation businesses. Although the cost of catastrophe reinsurance varies depending on exposure and the level of worldwide loss activity, AFG continues to obtain reinsurance coverage in adequate amounts at acceptable rates due to management's decision to limit overall exposure to catastrophe losses through individual risk selection (including minimizing coastal and known fault-line exposures).

In addition to the large line capacity and catastrophe reinsurance programs discussed above, AFG purchases reinsurance on a product-by-product basis. AFG regularly reviews the financial strength of its current and potential reinsurers. These reviews include consideration of credit ratings, available capital, claims paying history and expertise. This process periodically results in the transfer of risks to more financially secure reinsurers. Substantially all reinsurance is ceded to companies with investment grade S&P ratings or is secured by “funds withheld” or other collateral. Under “funds withheld” arrangements, AFG retains ceded premiums to fund ceded losses as they become due from the reinsurer. Recoverables from the following companies were individually between 5% and 11% of AFG’s total property and casualty reinsurance recoverable (net of payables to reinsurers) at December 31, 2013: Hannover Reinsurance Co. Ltd, Munich Reinsurance America, Inc. and Swiss Reinsurance America Corporation. In addition, AFG has a reinsurance recoverable from Ohio Casualty Insurance Company of $191 million related to that company’s purchase of AFG’s commercial lines business in 1998. No other reinsurers exceeded 5% of AFG’s property and casualty reinsurance recoverable.

Reinsurance is provided on one of two bases, facultative or treaty. Facultative reinsurance is generally provided on a risk by risk basis. Individual risks are ceded and assumed based on an offer and acceptance of risk by each party to the transaction. AFG purchases facultative reinsurance, both pro rata and excess of loss, depending on the risk and available reinsurance markets. Treaty reinsurance provides for risks meeting prescribed criteria to be automatically ceded and assumed according to contract provisions.

The following table presents (by type of coverage) the amount of each loss above the specified retention maximum generally covered by treaty reinsurance programs (in millions) as of January 1, 2014:

Coverage	Retention Maximum	Reinsurance Coverage (a)
California Workers’ Compensation	$ 2	$ 148
Other Workers’ Compensation	2	48
Commercial Umbrella	4	46
Property — General	5	45
Property — Catastrophe	19	81

(a) Reinsurance covers substantial portions of losses in excess of retention. However, in general, losses resulting from terrorism are not covered.

In addition to the coverage shown above, AFG reinsures a portion of its crop insurance business through the Federal Crop Insurance Corporation (“FCIC”). The FCIC offers both proportional (or “quota share”) and non-proportional coverages. The proportional coverage provides that a fixed percentage of risk is assumed by the FCIC. The non-proportional coverage allows AFG to select desired retention of risk on a state-by-state, county, crop or plan basis. AFG typically reinsures 15% to 25% of gross written premium with the FCIC. AFG also purchases quota share reinsurance in the private market. This quota share provides for a ceding commission to AFG and a profit sharing provision. During both 2013 and 2012, AFG reinsured 52.5% of premiums not reinsured by the FCIC in the private market and purchased stop loss protection coverage for the remaining portion of the business. AFG expects to utilize similar levels of reinsurance in 2014.

The Balance Sheet caption “recoverables from reinsurers” included approximately $82 million on paid losses and LAE and $2.12 billion on unpaid losses and LAE at December 31, 2013. These amounts are net of allowances of approximately $27 million for doubtful collection of reinsurance recoverables. The collectibility of a reinsurance balance is based upon the financial condition of a reinsurer as well as individual claim considerations.

Reinsurance premiums ceded and assumed are presented in the following table (in millions):

	2013	2012	2011
Reinsurance ceded	$ 1,464	$ 1,372	$ 1,336
Reinsurance ceded, excluding crop	802	743	652
Reinsurance assumed — including involuntary pools and associations	61	38	45

Loss and Loss Adjustment Expense Reserves

The consolidated financial statements include the estimated liability for unpaid losses and LAE of AFG's insurance subsidiaries. This liability represents estimates of the ultimate net cost of all unpaid losses and LAE and is determined by using case-basis evaluations, actuarial projections and management's judgment. These estimates are subject to the effects of changes in claim amounts and frequency and are periodically reviewed and adjusted as additional information becomes known. In accordance with industry practices, such adjustments are reflected in current year operations. Generally, reserves for reinsurance assumed and involuntary pools and associations are reflected in AFG's results at the amounts reported by those entities.

The following table presents the development of AFG's liability for losses and LAE, net of reinsurance, on a GAAP basis for the last ten years. The top line of the table shows the estimated liability (in millions) for unpaid losses and LAE recorded at the balance sheet date for the indicated years. The second line shows the re-estimated liability as of December 31, 2013. The remainder of the table presents intervening development as percentages of the initially estimated liability. The development results from additional information and experience in subsequent years, particularly with regard to A&E charges, settlements and reallocations as detailed below. The middle line shows a cumulative deficiency (redundancy), which represents the aggregate percentage increase (decrease) in the liability initially estimated. The lower portion of the table indicates the cumulative amounts paid as of successive periods as a percentage of the original loss reserve liability. For purposes of this table, reserves of businesses sold are considered paid at the date of sale. See *Note O — "Insurance — Property and Casualty Insurance Reserves"* to the financial statements for an analysis of changes in AFG's estimated liability for losses and LAE, net and gross of reinsurance, over the past three years on a GAAP basis.

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Liability for unpaid losses and loss adjustment expenses:											
As originally estimated	$ 2,901	$ 3,155	$ 3,619	$ 3,791	$ 3,868	$ 4,154	$ 3,899	$ 4,164	$ 4,282	$ 4,129	$ 4,288
As re-estimated at December 31, 2013	$ 3,527	$ 3,383	$ 3,391	$ 3,317	$ 3,295	$ 3,784	$ 3,664	$ 4,041	$ 4,252	$ 4,114	N/A
Liability re-estimated:											
One year later	104.9%	106.3%	98.4%	97.4%	93.6%	95.2%	96.0%	98.3%	99.3%	99.6%	
Two years later	114.0%	106.1%	98.8%	92.3%	89.7%	91.6%	94.2%	97.2%	99.3%		
Three years later	114.7%	107.7%	95.2%	89.5%	85.8%	90.4%	93.9%	97.0%			
Four years later	118.0%	106.0%	93.6%	87.0%	84.5%	90.8%	94.0%				
Five years later	118.5%	105.5%	92.1%	86.5%	84.7%	91.1%					
Six years later	118.8%	104.4%	92.1%	87.0%	85.2%						
Seven years later	117.9%	104.9%	92.8%	87.5%							
Eight years later	118.7%	105.8%	93.7%								
Nine years later	119.9%	107.2%									
Ten years later	121.6%										
Cumulative deficiency (redundancy) (a)	21.6%	7.2%	(6.3%)	(12.5%)	(14.8%)	(8.9%)	(6.0%)	(3.0%)	(0.7%)	(0.4%)	N/A
Cumulative paid as of:											
One year later	27.3%	25.4%	23.5%	22.3%	21.0%	24.0%	21.3%	23.3%	27.7%	27.4%	
Two years later	46.4%	40.8%	37.5%	34.8%	32.9%	37.2%	35.9%	38.6%	45.7%		
Three years later	58.8%	52.4%	46.9%	43.6%	41.6%	47.0%	47.1%	52.7%			
Four years later	68.5%	60.1%	53.6%	49.9%	47.5%	54.5%	57.7%				
Five years later	75.2%	65.6%	58.7%	54.2%	52.6%	62.4%					
Six years later	80.1%	70.5%	62.1%	58.0%	58.5%						
Seven years later	84.4%	73.8%	65.3%	63.2%							
Eight years later	87.4%	77.1%	70.3%								
Nine years later	90.8%	82.5%									
Ten years later	96.4%										
(a) Cumulative deficiency (redundancy):											
Special A&E charges, settlements and reallocations	12.8%	11.7%	5.3%	5.0%	3.8%	3.2%	3.5%	3.2%	2.0%	1.3%	
Other	8.8%	(4.5%)	(11.6%)	(17.5%)	(18.6%)	(12.1%)	(9.5%)	(6.2%)	(2.7%)	(1.7%)	
Total	21.6%	7.2%	(6.3%)	(12.5%)	(14.8%)	(8.9%)	(6.0%)	(3.0%)	(0.7%)	(0.4%)	N/A

The following is a reconciliation of the net liability to the gross liability for unpaid losses and LAE.

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
As originally estimated:											
Net liability shown above	$ 2,901	$ 3,155	$ 3,619	$ 3,791	$ 3,868	$ 4,154	$ 3,899	$ 4,164	$ 4,282	$ 4,129	$ 4,288
Add reinsurance recoverables	2,059	2,234	2,243	2,309	2,300	2,610	2,513	2,249	2,238	2,716	2,122
Gross liability	$ 4,960	$ 5,389	$ 5,862	$ 6,100	$ 6,168	$ 6,764	$ 6,412	$ 6,413	$ 6,520	$ 6,845	$ 6,410
As re-estimated at December 31, 2013:											
Net liability shown above	$ 3,527	$ 3,383	$ 3,391	$ 3,317	$ 3,295	$ 3,784	$ 3,664	$ 4,041	$ 4,252	$ 4,114	
Add reinsurance recoverables	2,791	2,586	2,348	2,138	1,930	2,292	1,981	1,987	2,082	3,010	
Gross liability	$ 6,318	$ 5,969	$ 5,739	$ 5,455	$ 5,225	$ 6,076	$ 5,645	$ 6,028	$ 6,334	$ 7,124	N/A
Gross cumulative deficiency (redundancy) (a)	27.4%	10.8%	(2.1%)	(10.6%)	(15.3%)	(10.2%)	(12.0%)	(6.0%)	(2.9%)	4.1%	N/A

(a) Gross cumulative deficiency (redundancy):	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Special A&E charges, settlements and reallocations	9.2%	8.6%	4.4%	4.2%	3.2%	2.6%	2.8%	2.8%	1.9%	6.9%	
Other	18.2%	2.2%	(6.5%)	(14.8%)	(18.5%)	(12.8%)	(14.8%)	(8.8%)	(4.8%)	(2.8%)	
Total	27.4%	10.8%	(2.1%)	(10.6%)	(15.3%)	(10.2%)	(12.0%)	(6.0%)	(2.9%)	4.1%	N/A

In evaluating the re-estimated liability and cumulative deficiency (redundancy), it should be noted that each percentage includes the effects of changes in amounts for prior periods. For example, AFG's $54 million special A&E charge related to losses recorded in 2013, but incurred before 2003, is included in the re-estimated liability and cumulative deficiency (redundancy) percentage for each of the previous years shown. Conditions and trends that have affected development of the liability in the past may not necessarily exist in the future. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on this table.

A significant portion of the adverse development in the tables is due to A&E exposures for which AFG has been held liable under general liability policies written prior to 1987, even though such coverage was not intended. Other factors affecting adverse development included changes in the legal environment, including more liberal coverage decisions and higher jury awards, higher legal fees, the general state of the economy and medical cost inflation.

The differences between the liability for losses and LAE reported in the annual statements filed with the state insurance departments in accordance with statutory accounting principles ("SAP") and that reported in the accompanying consolidated financial statements in accordance with GAAP at December 31, 2013 are as follows (in millions):

Liability reported on a SAP basis, net of $135 million of retroactive reinsurance	$ 3,709
Reinsurance recoverables, net of allowance	2,122
Other, including reserves of foreign insurers	579
Liability reported on a GAAP basis	$ 6,410

Asbestos and Environmental ("A&E") Reserves AFG's property and casualty group, like many others in the industry, has A&E claims arising in most cases from general liability policies written more than twenty-five years ago. The establishment of reserves for such A&E claims presents unique and difficult challenges and is subject to uncertainties significantly greater than those presented by other types of claims. For a discussion of these uncertainties, see *Item 7 — Management's Discussion and Analysis — "Uncertainties — Asbestos and Environmental-related ("A&E") Insurance Reserves" and Note M — "Contingencies"* to the financial statements.

Management has periodically conducted comprehensive studies of its asbestos and environmental reserves with the aid of outside actuarial and engineering firms and specialty outside counsel, generally every two years, with an in-depth internal review during the intervening years. Charges resulting from these studies and reviews are included in "Incurred losses and LAE" in the table below. As a result of the 2013 external study, AFG recorded a $54 million pretax special charge in the third quarter of 2013 to increase the property and casualty group's asbestos reserves by $16 million (net of reinsurance) and its environmental reserves by $38 million (net of reinsurance). The increase in asbestos reserves was driven primarily by slightly higher than expected loss experience, higher defense costs and some increased claim severity. As the overall industry exposure to asbestos has matured, the focus of litigation has shifted to smaller companies and companies with ancillary exposures. AFG's insureds with these exposures have been the driver of the property and casualty segment's asbestos reserve increases.

The increase in environmental reserves was attributed primarily to a small number of claims where the estimated costs of remediation have increased. There were no newly identified or emerging broad industry trends that were identified in this study. In addition to the third quarter special charge, AFG increased A&E reserves for one claim by $5 million in early 2013 due to fact specific developments. As a result of the in-depth internal review in 2012, AFG recorded a $31 million pretax special charge (net of reinsurance) to increase the property and casualty group's A&E reserves. The charge relates primarily to an increase in environmental investigative costs and related loss adjustment expenses. In addition to the third quarter special charge, AFG increased A&E reserves for two individual claims by an aggregate of $12 million in 2012 due to fact specific developments and refined estimates of exposure. The 2011 comprehensive study resulted in a $50 million pretax special charge (net of reinsurance) in the second quarter of 2011 to increase the property and casualty group's A&E reserves.

The following table (in millions) is a progression of the property and casualty group's A&E reserves.

	2013	2012	2011
Reserves at beginning of year	$ 373	$ 362	$ 342
Incurred losses and LAE	59	43	50
Paid losses and LAE (*)	(131)	(32)	(30)
Reserves at end of year, net of reinsurance recoverable	301	373	362
Reinsurance recoverable, net of allowance	83	98	92
Gross reserves at end of year	$ 384	$ 471	$ 454

(*) Paid losses and LAE in 2013 include payments totaling $106 million (net of reinsurance recoveries) associated with the settlement of A.P. Green Industries and another large claim.

Marketing

The property and casualty insurance group directs its sales efforts primarily through independent insurance agents and brokers, although small portions are written through employee agents. Independent agents and brokers generally receive a commission on the sale of each policy. Some agents and brokers are eligible for a bonus commission based on the overall profitability of policies placed with AFG by the broker or agent in a particular year. The property and casualty insurance group writes insurance through several thousand agents and brokers.

Competition

AFG's property and casualty insurance businesses compete with other individual insurers, state funds and insurance groups of varying sizes, some of which are mutual insurance companies possessing competitive advantages in that all their profits inure to their policyholders. See *Item 1A — Risk Factors.* They also compete with self-insurance plans, captive programs and risk retention groups. Due to the specialty nature of these coverages, competition is based primarily on service to policyholders and agents, specific characteristics of products offered and reputation for claims handling. Financial strength ratings, price, commissions and profit sharing terms are also important factors. Management believes that sophisticated data analysis for refinement of risk profiles, extensive specialized knowledge and loss prevention service have helped AFG compete successfully.

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Annuity Segment

General

AFG sells traditional fixed and fixed-indexed annuities in the retail, financial institutions and education markets through independent producers and through direct relationships with certain financial institutions. The annuity operations employed approximately 500 people at December 31, 2013. These operations are conducted primarily through the subsidiaries listed in the following table, which includes 2013 statutory annuity premiums (in millions), annuity policies in force and independent ratings.

Company	Annuity Premiums	Annuity Policies In Force	Ratings AM Best	Ratings S&P
Great American Life Insurance Company	$ 3,795	329,500	A	A+
Annuity Investors Life Insurance Company	233	129,000	A	A+

AFG believes that the ratings assigned by independent insurance rating agencies are an important competitive factor because agents, potential policyholders, banks, and school districts often use a company's rating as an initial screening device in considering annuity products. AFG believes that a rating in the "A" category by A.M. Best is necessary to successfully market tax-deferred annuities to public education employees and other non-profit groups and a rating in the "A" category by at least one rating agency is necessary to successfully compete in its other annuity markets. AFG believes that these entities can successfully compete in these markets with their respective ratings.

Statutory premiums of AFG's annuity operations the last three years were as follows (in millions):

	Premiums 2013	Premiums 2012	Premiums 2011
Retail single premium annuities — indexed	$ 1,879	$ 1,662	$ 1,549
Retail single premium annuities — fixed	165	153	239
Financial institutions single premium annuities — indexed	1,102	291	216
Financial institutions single premium annuities — fixed	628	587	755
Education market — 403(b) fixed and indexed annuities	207	237	257
Total fixed annuity premiums	3,981	2,930	3,016
Variable annuities	52	61	70
Total annuity premiums	$ 4,033	$ 2,991	$ 3,086

Annuities are long-term retirement saving instruments that benefit from income accruing on a tax-deferred basis. The issuer of the annuity collects premiums, credits interest or earnings on the policy and pays out a benefit upon death, surrender or annuitization. Single premium annuities are generally issued in exchange for a one-time lump-sum premium payment. Certain annuities, primarily in the education market, have premium payments that are flexible in both amount and timing as determined by the policyholder and are generally made through payroll deductions.

Annuity contracts are generally classified as either fixed rate (including fixed-indexed) or variable. With a traditional fixed rate annuity, AFG seeks to maintain a desired spread between the yield on its investment portfolio and the rate it credits. AFG accomplishes this by: (i) offering crediting rates that it has the option to change after any initial guarantee period (subject to minimum interest rate and other contractual guarantees); (ii) designing annuity products that encourage persistency; and (iii) maintaining an appropriate matching of assets and liabilities.

A fixed-indexed annuity provides policyholders with the opportunity to receive a crediting rate tied, in part, to the performance of an existing market index (generally the S&P 500) while protecting against the related downside risk through a guarantee of principal (excluding surrender charges, market value adjustments, and certain benefit charges). AFG purchases call options designed to substantially offset the effect of the index participation in the liabilities associated with fixed-indexed annuities.

As an ancillary product in its education market, AFG offers a limited amount of variable annuities. With a variable annuity, the earnings credited to the policy vary based on the investment results of the underlying investment options chosen by the policyholder, generally without any guarantee of principal except in the case of death of the insured. Premiums directed to the underlying investment options maintained in separate accounts are invested in funds managed by various independent investment managers. AFG earns a fee on amounts deposited into separate accounts. Subject to contractual provisions,

policyholders may also choose to direct all or a portion of their premiums to various fixed rate options, in which case AFG earns a spread on amounts deposited.

Marketing

AFG sells its single premium annuities, excluding bank production (discussed below), primarily through a retail network of approximately 65 national marketing organizations ("NMOs") and managing general agents ("MGAs") who, in turn, direct over 1,500 actively producing agents.

AFG also sells single premium annuities in financial institutions through direct relationships with certain banks and through independent agents and brokers. Premiums generated through AFG's direct relationship with PNC Bank and through BB&T and Regions Bank by independent brokers were the largest individual sources of annuity premiums in 2013 and accounted for approximately 11%, 7% and 6%, respectively, of AFG's overall annuity premiums in 2013.

In the education market, schools may allow employees to save for retirement through contributions made on a before-tax basis. Federal income taxes are not payable on pretax contributions or earnings until amounts are withdrawn. AFG sells its education market annuities directly through writing agents rather than through NMOs and MGAs.

AFG is licensed to sell its fixed annuity products in all states except New York; it is licensed to sell its variable products in all states except New York and Vermont. In 2013, the only states that accounted for 5% or more of AFG's annuity premiums were Florida (9%), California (7%), Ohio (7%), Pennsylvania (7%) and North Carolina (5%). At December 31, 2013, AFG had approximately 480,000 annuity policies in force.

Competition

AFG's annuity businesses operate in highly competitive markets. They compete with other insurers and financial institutions based on many factors, including: (i) ratings; (ii) financial strength; (iii) reputation; (iv) service to policyholders and agents; (v) product design (including interest rates credited, bonus features and index participation); (vi) commissions; and (vii) number of school districts in which a company has approval to sell. Since most policies are marketed and distributed through independent agents, the insurance companies must also compete for agents.

No single insurer dominates the markets in which AFG's annuity businesses compete. See *Item 1A — Risk Factors.* Competitors include (i) individual insurers and insurance groups, (ii) mutual funds and (iii) other financial institutions. In a broader sense, AFG's annuity businesses compete for retirement savings with a variety of financial institutions offering a full range of financial services. In the bank annuity market, AFG's annuities compete directly against competitors' bank annuities, certificates of deposit and other investment alternatives at the point of sale. In addition, over the last few years, several offshore and/or hedge fund companies have made significant acquisitions of annuity businesses, resulting in annuity groups that are larger in size than AFG's annuity business and that are likely to become more aggressive in marketing their products.

Sales of annuities, including renewal premiums, are affected by many factors, including: (i) competitive annuity products and rates; (ii) the general level and volatility of interest rates, including the slope of the yield curve; (iii) the favorable tax treatment of annuities; (iv) commissions paid to agents; (v) services offered; (vi) ratings from independent insurance rating agencies; (vii) other alternative investments; (viii) performance and volatility of the equity markets; (ix) media coverage of annuities; (x) regulatory developments regarding suitability and the sales process; and (xi) general economic conditions.

Run-off Long-term Care and Life Segment

AFG ceased new sales of long-term care insurance in January 2010. Renewal premiums on approximately 56,000 policies covering approximately 60,000 lives will be accepted unless those policies lapse. Renewal premiums, net of reinsurance, were $76 million in 2013, $79 million in 2012 and $81 million in 2011. At December 31, 2013, AFG's long-term care insurance reserves were $726 million, net of reinsurance recoverables.

Although AFG no longer actively markets new life insurance products, it continues to service and receive renewal premiums on its in-force block of approximately 180,000 policies and $17.98 billion gross ($4.55 billion net of reinsurance) of life insurance in force at December 31, 2013. Renewal premiums, net of reinsurance, were $33 million in 2013, $34 million in 2012 and $35 million in 2011. At December 31, 2013, AFG's life insurance reserves were $406 million, net of reinsurance recoverables.

The vast majority of AFG's investment in its run-off long-term care and life operations (including 100% of its long-term care business) is in the following subsidiaries:

Company	Products
United Teacher Associates Insurance Company	Long-term care, life, annuities
Continental General Insurance Company	Long-term care, life, annuities
Manhattan National Life Insurance Company	Life

The combined GAAP equity (excluding net unrealized gains on marketable securities) of these three companies was $227 million at December 31, 2013. Approximately 80% of this equity was associated with the run-off long-term care business and about 10% was associated with run-off life business. The remainder of this equity was associated with AFG's ongoing annuity operations.

Medicare Supplement and Critical Illness Segment

In 2012, AFG sold its Medicare supplement and critical illness businesses, which included Loyal American Life Insurance Company and four other insurance companies, to Cigna Corporation for $326 million in cash. This business generated premiums of $199 million in 2012 (through the August sale date) and $304 million in 2011.

Other Operations

Through subsidiaries, AFG is engaged in a variety of other operations, including commercial real estate operations in Cincinnati (office buildings and The Cincinnatian Hotel), New Orleans (Le Pavillon Hotel), Whitefield, New Hampshire (Mountain View Grand Resort), Chesapeake Bay (Skipjack Cove Yachting Resort and Bay Bridge Marina), Charleston (Charleston Harbor Resort and Marina), Palm Beach (Sailfish Marina and Resort), Florida City, Florida (retail commercial development) and apartments in Louisville and Pittsburgh. These operations employed approximately 500 full-time employees at December 31, 2013.

Investment Portfolio

General

A summary of AFG's fixed maturities and equity securities is shown in *Note E* to the financial statements. For additional information on AFG's investments, see *Item 7 — Management's Discussion and Analysis — "Investments."* Portfolio yields are shown below.

	2013	2012	2011
Yield on Fixed Maturities (a):			
Excluding realized gains and losses	5.2%	5.6%	5.7%
Including realized gains and losses	5.3%	5.8%	5.8%
Yield on Equity Securities (a):			
Excluding realized gains and losses	5.5%	4.5%	4.8%
Including realized gains and losses	26.4%	25.2%	18.5%

(a) Based on amortized cost; excludes effects of changes in unrealized gains and losses. Realized losses include impairment charges.

The table below compares total returns, which include changes in fair value, on AFG's fixed maturities and equity securities to comparable public indices. While there are no directly comparable indices to AFG's portfolio, the two shown below are widely used benchmarks in the financial services industry.

	2013	2012	2011
Total return on AFG's fixed maturities	1.3%	9.1%	7.7%
Barclays Capital U.S. Universal Bond Index	(1.3%)	5.5%	7.4%
Total return on AFG's equity securities	27.1%	18.7%	6.9%
Standard & Poor's 500 Index	32.4%	16.0%	2.1%

Fixed Maturity Investments

AFG's bond portfolio is invested primarily in taxable bonds. The following table shows AFG's available for sale fixed maturities by Standard & Poor's Corporation or comparable rating as of December 31, 2013 (dollars in millions).

	Amortized	Fair Value	
	Cost	Amount	%
S&P or comparable rating			
AAA, AA, A	$ 17,048	$ 17,542	66%
BBB	4,907	5,160	20%
Total investment grade	21,955	22,702	86%
BB	686	717	3%
B	504	524	2%
CCC, CC, C	1,010	1,154	4%
D, not rated	1,211	1,359	5%
Total non-investment grade	3,411	3,754	14%
Total	$ 25,366	$ 26,456	100%

The National Association of Insurance Commissioners ("NAIC") has retained third-party investment management firms to assist in the determination of appropriate NAIC designations for mortgage-backed securities ("MBS") based not only on the probability of loss (which is the primary basis of ratings by the major ratings firms), but also on the severity of loss and statutory carrying value. Approximately 26% of AFG's fixed maturity investments are MBS. At December 31, 2013, 97% (based on statutory carrying value of $25.38 billion) of AFG's fixed maturity investments held by its insurance companies had an NAIC designation of 1 or 2 (the highest of the six designations).

Equity Investments

At December 31, 2013, AFG held common and perpetual preferred stocks with a fair value of $1.18 billion.

Regulation

AFG's insurance company subsidiaries are subject to regulation in the jurisdictions where they do business. In general, the insurance laws of the various states establish regulatory agencies with broad administrative powers governing, among other things, premium rates, solvency standards, licensing of insurers, agents and brokers, trade practices, forms of policies, maintenance of specified reserves and capital for the protection of policyholders, deposits of securities for the benefit of policyholders, investment activities and relationships between insurance subsidiaries and their parents and affiliates. Material transactions between insurance subsidiaries and their parents and affiliates generally must receive prior approval of the applicable insurance regulatory authorities and be disclosed. In addition, while differing from state to state, these regulations typically restrict the maximum amount of dividends that may be paid by an insurer to its shareholders in any twelve-month period without advance regulatory approval. Such limitations are generally based on net earnings or statutory surplus. Under applicable restrictions, the maximum amount of dividends available to AFG in 2014 from its insurance subsidiaries without seeking regulatory clearance is approximately $610 million.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act"), among other things, established a Federal Insurance Office ("FIO") within the U.S. Treasury. Under this law, regulations will need to be created for the FIO to carry out its mandate to focus on systemic risk oversight. The FIO has gathered information regarding the insurance industry and submitted a report to Congress in December 2013. The report concluded that a hybrid approach to regulation,

involving a combination of state and federal government action, could improve the U.S. insurance system by attaining uniformity, efficiency and consistency, particularly with respect to solvency and market conduct regulation. It is too early to predict the extent to which the report's recommendations might result in changes to the current state-based system of insurance industry regulation or ultimately impact AFG's operations.

Marketform, AFG's UK-based Lloyd's insurer, is subject to regulation by the European Union's executive body, the European Commission. In 2016, Marketform will likely be required to adopt new capital adequacy and risk management regulations known as Solvency II. Because Lloyd's insurers are already operating under the proposed Solvency II guidelines, implementation is not expected to be material to AFG.

Most states have created insurance guaranty associations that assess solvent insurers to pay claims of insurance companies that become insolvent. In the second quarter of 2013, AFG's annuity segment recorded a pretax charge of $5 million to cover expected assessments from state guaranty funds related to the insolvency and liquidation of Executive Life Insurance Company of New York, an unaffiliated life insurance company. Annual guaranty assessments for AFG's insurance companies have not been material.

ITEM 1A

Risk Factors

In addition to the other information set forth in this report, the following factors could materially affect AFG's business, financial condition, cash flows or future results. Any one of these factors could cause AFG's actual results to vary materially from recent results or from anticipated future results. The risks described below are not the only risks facing AFG. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect AFG's business, financial condition and/or operating results.

Adverse developments in the financial markets and deterioration in global economic conditions could have a material adverse effect on AFG's results of operations and financial condition.

The highly volatile debt and equity markets, lack of liquidity, widening credit spreads and the collapse of several financial institutions during 2008 and early 2009 resulted in significant realized and unrealized losses in AFG's investment portfolio. Although global economic conditions and financial markets have improved, there is continued uncertainty regarding the duration and strength of the economic recovery, particularly in Europe. Economic growth in the U.S. and internationally may not continue or may be slow for an extended period of time. In addition, other economic conditions (such as unemployment) may continue to be weak. See *Item 7A — Quantitative and Qualitative Disclosures about Market Risk — "European Debt Exposure."* At December 31, 2013, AFG's net unrealized gain on fixed maturity investments was $1.09 billion consisting of gross gains of $1.40 billion and gross losses of $305 million. Although AFG intends to hold its investments with unrealized losses until they recover in value, its intent may change for a variety of reasons as discussed in *Item 7 — Management's Discussion and Analysis — "Investments."* A change in AFG's ability or intent with regard to a security in an unrealized loss position would result in the recognition of a realized loss.

AFG's investment performance could also be adversely impacted by the types of investments, industry groups and/or individual securities in which it invests. As of December 31, 2013, 85% of AFG's investment portfolio was invested in fixed maturity securities. Certain risks are inherent in connection with fixed maturity securities including loss upon default and price volatility in reaction to changes in interest rates and general market factors. AFG's equity securities, which represent 4% of its investment portfolio, are subject to market price volatility.

MBS represented about 26% of AFG's fixed maturity securities at December 31, 2013. AFG's MBS portfolio will continue to be impacted by general economic conditions, including unemployment levels, real estate values and other factors that could negatively affect the creditworthiness of borrowers. MBS in which the underlying collateral is subprime mortgages represented 3% of AFG's total fixed maturity portfolio at December 31, 2013; MBS in which the underlying collateral is Alt-A mortgages (risk profile between prime and subprime) represented approximately 4%. See *Item 7A — Quantitative and Qualitative Disclosures about Market Risk — "Fixed Maturity Portfolio."*

AFG cannot predict whether, and the extent to which, industry sectors in which it maintains investments may suffer losses as a result of potential declines in commercial and economic activity, or how any such decline might impact the ability of companies within the affected industry sectors to pay interest or principal on their securities, or how the value of any underlying collateral might be affected.

Investment returns are an important part of AFG's overall profitability. Accordingly, adverse fluctuations in the fixed income or equity markets could adversely impact AFG's profitability, financial condition or cash flows.

In addition, should economic conditions deteriorate, it could have a material adverse effect on AFG's insureds and reinsurers. However, the impact that this would have on AFG's business cannot be predicted.

Intense competition could adversely affect AFG's profitability.

The property and casualty insurance segment operates in a highly competitive industry that is affected by many factors that can cause significant fluctuations in its results of operations. The trend of AFG's underwriting results typically follows that of the industry and a prolonged downcycle could adversely affect AFG's results of operations. The businesses in this segment compete with other individual insurers, state funds and insurance groups of varying sizes, some of which are mutual insurance companies possessing competitive advantages in that all their profits inure to their policyholders. In addition, certain foreign insurers can write business in the U.S. on a tax-advantaged basis and therefore hold a competitive advantage over AFG. AFG also competes with self-insurance plans, captive programs and risk retention groups. Peer companies and major competitors in some or all of AFG's specialty lines include the following companies and/or their subsidiaries: ACE Ltd., American International Group Inc., Arch Capital Group Ltd., Chubb Corp., Cincinnati Financial Corp., CNA Financial Corp., Liberty Mutual, Markel Corp., Munich Re Group (American Modern Insurance), Hartford Financial Services Group, HCC Insurance Holdings, Inc., Ironshore Insurance Ltd., RLI Corp., The Travelers Companies Inc., Tokio Marine Holdings, Inc. (Philadelphia Consolidated), W.R. Berkley Corp., Wells Fargo Corp. (Rural Community Insurance), XL Group Plc, Fairfax Financial Holdings Limited (Zenith National) and Zurich Financial Services Group.

AFG's annuity segment competes with individual insurers and insurance groups, mutual funds and other financial institutions. Competitors include the following companies and/or their subsidiaries: ING Life Insurance and Annuity Company, Metropolitan Life Insurance Company, American International Group Inc., Western National Life Insurance Company, Life Insurance Company of the Southwest, Midland National Life Insurance Company, Allianz Life Insurance Company of North America, Guggenheim Life and Annuity Company, Apollo Global Management (Aviva Life and Annuity Company and Athene), Forethought Life Insurance Company, Jackson National Life Insurance Company, Pacific Life Insurance Company and Mutual of Omaha Insurance Company. Financial institutions annuity premiums represented 43% of AFG's annuity premiums in 2013 and have been a key driver in the growth of AFG's annuity business since 2009. Approximately 57% of AFG's financial institutions annuity premiums in 2013 were generated through three large banks. Although AFG has been able to add several new banks in the last few years, the failure to replace these banks if they significantly reduce sales of AFG annuities could reduce AFG's future growth and profitability. In the financial institutions annuity market, AFG competes directly against competitors' bank annuities, certificates of deposit and other investment alternatives at the point of sale.

Competition is based on many factors, including service to policyholders and agents, product design, reputation for claims handling, ratings and financial strength. Price, commissions, fees, profit sharing terms, interest crediting rates, technology and distribution channels are also important factors. Some of AFG's competitors have more capital and greater resources than AFG, and may offer a broader range of products and lower prices than AFG offers. If competition limits AFG's ability to write new or renewal business at adequate rates, its results of operations will be adversely affected.

AFG's revenues could be negatively affected if it is not able to attract and retain independent agents.

AFG's reliance on the independent agency market makes it vulnerable to a reduction in the amount of business written by agents. Many of AFG's competitors also rely significantly on the independent agency market. Accordingly, AFG must compete with other insurance carriers for independent agents' business. Some of its competitors offer a wider variety of products, lower price for insurance coverage or higher commissions. Loss of a substantial portion of the business that AFG writes through independent agents could adversely affect AFG's revenues and profitability.

The inability to obtain reinsurance or to collect on ceded reinsurance could adversely impact AFG's results.

AFG relies on the use of reinsurance to limit the amount of risk it retains. The following amounts of gross property and casualty premiums have been ceded to other insurers: 2013 — $1.46 billion (31%), 2012 — $1.37 billion (32%) and 2011 — $1.34 billion (33%). The availability and cost of reinsurance are subject to prevailing market conditions, which are beyond AFG's control and which may affect AFG's level of business and profitability. Outside of its property and casualty operations, AFG also has reinsurance recoverables totaling $953 million, including $586 million from Hannover Life Reassurance Company of America (rated A+ by A.M. Best) and $200 million from Loyal American Life Insurance Company, a subsidiary of Cigna (rated A- by A.M. Best), related primarily to the reinsurance of certain benefits in its run-off long-term care and life operations and the August 2012 sale of its Medicare supplement and critical illness businesses. AFG is also subject to credit

risk with respect to its reinsurers, as AFG will remain liable to its insureds if any reinsurer is unable to meet its obligations under agreements covering the reinsurance ceded.

AFG is subject to comprehensive regulation, and its ability to earn profits may be restricted by these regulations.

As previously discussed under *Item 1 — Business — "Regulation,"* AFG is subject to comprehensive regulation by government agencies in the states and countries where its insurance company subsidiaries are domiciled and where these subsidiaries issue policies and handle claims. AFG must obtain prior approval for certain corporate actions. The regulations may limit AFG's ability to obtain rate increases or take other actions designed to increase AFG's profitability. Such regulation is primarily intended for the protection of policyholders rather than securityholders.

In July 2010, the Dodd-Frank Act was signed into law. Among other things, this law established the Federal Insurance Office within the U.S. Treasury and authorizes it to gather information regarding the insurance industry and submit to Congress a plan to modernize and improve insurance regulation in the U.S.

Existing insurance-related laws and regulations may become more restrictive in the future or new restrictive laws may be enacted; it is not possible to predict the potential effects of these laws and regulations. The costs of compliance or the failure to comply with existing or future regulations could harm AFG's financial results and its reputation with customers.

The failure of AFG's insurance subsidiaries to maintain a commercially acceptable financial strength rating would have a significant negative effect on their ability to compete successfully.

As discussed under *Item 1 — Business — "Property and Casualty Insurance Segment"* and *"Annuity Segment — General,"* financial strength ratings are an important factor in establishing the competitive position of insurance companies and may be expected to have an effect on an insurance company's sales. A downgrade out of the "A" category in AFG's insurers' claims-paying and financial strength ratings could significantly reduce AFG's business volumes in certain lines of business, adversely impact AFG's ability to access the capital markets and increase AFG's borrowing costs.

The continued threat of terrorism and ongoing military and other actions, as well as civil unrest, may adversely affect AFG's financial results.

The continued threat of terrorism, both within the United States and abroad, and the ongoing military and other actions and heightened security measures in response to these types of threats, as well as civil unrest, may cause significant volatility and declines in the equity markets in the United States, Europe and elsewhere, loss of life, property damage, additional disruptions to commerce and reduced economic activity. Actual terrorist attacks could cause losses from insurance claims related to AFG's property and casualty and life insurance operations with adverse financial consequences. In addition, some of the assets in AFG's investment portfolios may be adversely affected by declines in the capital markets and economic activity caused by the continued threat of terrorism, ongoing military and other action, heightened security measures and civil unrest.

The Terrorism Risk Insurance Program Reauthorization Act authorizes the Federal Terrorism Risk Insurance Program, which provides for a system of shared public and private responsibility for certain insured losses resulting from defined acts of terrorism. AFG did not incur any losses due to "acts of terrorism" in 2013, 2012 or 2011. In 2014, AFG would have to sustain terrorism losses in excess of $400 million to be eligible for reinsurance under the program, which also has a total industry cap of $100 billion. The program is due to expire at the end of 2014; however, legislation to extend the program has been introduced in Congress. If Congress eliminates or modifies the program, such action could adversely affect AFG's property and casualty business through increased exposure to a catastrophic level of terrorism losses.

AFG may experience difficulties with technology or data security, which could have an adverse effect on its business or reputation.

AFG uses computer systems to store, retrieve, evaluate and utilize company and customer data and information. Systems failures or outages could compromise AFG's ability to perform business functions in a timely manner, which could harm its ability to conduct business and hurt its relationships with business partners and customers. In the event of a disaster such as a natural catastrophe, an industrial accident, a blackout, a computer virus, a terrorist attack or war, AFG's systems may be inaccessible to employees, customers or business partners for an extended period of time. Even if AFG's employees are able to report to work, they may be unable to perform their duties for an extended period of time if the Company's data or systems are disabled or destroyed.

Despite the implementation of security measures, these systems may also be vulnerable to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. Any compromise of security could have a material adverse effect on AFG's business or reputation and could subject AFG to liability if confidential customer information is misappropriated from its computer systems.

AFG's property and casualty reserves may be inadequate, which could significantly affect AFG's financial results.

AFG's property and casualty insurance subsidiaries record reserve liabilities for the estimated payment of losses and loss adjustment expenses for both reported and unreported claims. Due to the inherent uncertainty of estimating reserves, it has been necessary in the past, and will continue to be necessary in the future, to revise estimated liabilities as reflected in AFG's reserves for claims and related expenses. The historic development of reserves for losses and loss adjustment expense may not necessarily reflect future trends in the development of these amounts. Accordingly, it is not appropriate to extrapolate future redundancies or deficiencies based on historical information. To the extent that reserves are inadequate and are strengthened, the amount of such increase is treated as a charge to earnings in the period in which the deficiency is recognized.

AFG's results could be negatively impacted by severe weather conditions or other catastrophes.

AFG recorded current accident year catastrophe losses of $31 million in 2013 (primarily from spring storms in the southeastern United States), $46 million in 2012 (primarily from Superstorm Sandy) and $43 million in 2011 (primarily from tornadoes). Catastrophes (some of which are seasonal) can be caused by natural events such as hurricanes, windstorms, severe storms, tornadoes, floods, hailstorms, severe winter weather, earthquakes, explosions and fire, and by man-made events, such as terrorist attacks and riots. While not considered a catastrophe by industry standards, droughts can have a significant adverse impact on AFG's crop insurance results and did negatively impact 2012 results. The extent of losses from a catastrophe is a function of the amount of insured exposure in the area affected by the event and the severity of the event. In addition, certain catastrophes could result in both property and non-property claims from the same event. A severe catastrophe or a series of catastrophes could result in losses exceeding AFG's reinsurance protection and may have a material adverse impact on its results of operations or financial condition.

Climate change and related regulation could adversely affect AFG's property and casualty insurance operations.

While AFG does not believe that its operations are likely to be significantly impacted by existing laws and regulations regarding climate change, it is possible that future regulation in this area could result in additional compliance costs and demands on management time.

To the extent that global climate change meaningfully alters weather and tidal patterns, or sea levels, it is possible that AFG's property and casualty insurance operations could experience an increase in claims, primarily in coastal areas and in the crop and agricultural businesses.

Volatility in crop prices could negatively impact AFG's financial results.

Weather conditions and the level of crop prices in the commodities market heavily impact AFG's crop insurance business. These factors are inherently unpredictable and could result in significant volatility in the results of the crop insurance business from one year to the next. AFG's crop results could also be negatively impacted by pests and disease.

Exposure to asbestos or environmental claims could materially adversely affect AFG's results of operations and financial condition.

AFG has asbestos and environmental ("A&E") exposures arising from its insurance operations and former railroad and manufacturing operations. A&E liabilities are especially difficult to estimate for many reasons, including the long delays between exposure and manifestation of any bodily injury or property damage, difficulty in identifying the source of the asbestos or environmental contamination, long reporting delays and difficulty in properly allocating liability for the asbestos or environmental damage. Claimants continue to assert new theories of recovery, and from time to time, there is proposed state and federal legislation regarding A&E liability, which would also affect AFG's exposure. If AFG has not established adequate reserves to cover future claims, AFG's results of operations and financial condition could be materially adversely affected.

Changes in interest rates could adversely impact the spread AFG earns on its annuity products.

The profitability of AFG's annuity business is largely dependent on spread (the difference between what it earns on its investments and the crediting rate it pays on its annuity contracts). Most of AFG's annuity products have guaranteed minimum

crediting rates (ranging from 4% down to currently 1% on new business). During periods of falling interest rates, AFG may not be able to fully offset the decline in investment earnings with lower crediting rates. During periods of rising rates, there may be competitive pressure to increase crediting rates to avoid a decline in sales or increased surrenders, thus resulting in lower spreads. In addition, an increase in surrenders could require the sale of investments at a time when the prices of those assets are lower due to the increase in market rates, which may result in realized investment losses.

Variations from the actuarial assumptions used to establish certain assets and liabilities in AFG's annuity business could negatively impact AFG's reported financial results.

The earnings on AFG's annuity products depend significantly upon the extent to which actual experience is consistent with the assumptions used in setting reserves and establishing and amortizing deferred policy acquisition costs ("DPAC"). These assumptions relate to investment yields (and spreads over fixed annuity crediting rates), benefit utilization rates, equity market performance, mortality, surrenders, annuitizations and other withdrawals. Developing such assumptions is complex and involves information obtained from company-specific and industry-wide data, as well as general economic information. These assumptions, and therefore AFG's results of operations, could be negatively impacted by changes in any of the factors listed above. For example, AFG recorded a $2 million pretax charge in 2013 in its annuity business from the net impact of changes in assumptions related to future investment yields, future expected call option costs in the fixed-indexed annuity business, crediting rates and lapses.

The ability to get price increases and appropriate investment yields and variations from the actuarial assumptions used in loss recognition testing in AFG's closed block of long-term care policies may adversely affect AFG's profitability.

AFG ceased writing new long-term care insurance policies in January 2010. Previous policies written are guaranteed renewable, but can be re-priced, subject to regulatory approval, to reflect adverse experience. Inability to get needed regulatory approval may adversely impact AFG's results of operations. In addition, given the duration of the long-term care product, AFG may be unable to purchase appropriate assets with cash flows and durations necessary to match those of future claims in that business.

For long-duration contracts (such as long-term care policies), loss recognition occurs when, based on current expectations as of the measurement date, the existing contract liabilities plus the present value of future premiums (including reasonably expected rate increases), are not expected to cover the present value of future claims payments, related settlement and maintenance costs, and unamortized acquisition costs. Based on loss recognition testing at December 31, 2012, AFG recorded a $153 million pretax charge in 2012 to write off deferred policy acquisition costs and strengthen reserves on its closed block of long-term care insurance, due primarily to the impact of changes in assumptions related to future investment yields resulting from the continued low interest rate environment, as well as changes in claims, expense and persistency assumptions. Although no additional loss recognition charges were recorded in 2013, adverse changes in any of the reserve assumptions in future periods could result in additional loss recognition for this business.

As a holding company, AFG is dependent on the operations of its insurance company subsidiaries to meet its obligations and pay future dividends.

AFG is a holding company and a legal entity separate and distinct from its insurance company subsidiaries. As a holding company without significant operations of its own, AFG's principal sources of funds are dividends and other distributions from its insurance company subsidiaries. As discussed under *Item 1 — Business — "Regulation,"* state insurance laws limit the ability of insurance companies to pay dividends or other distributions and require insurance companies to maintain specified levels of statutory capital and surplus. AFG's rights to participate in any distribution of assets of its insurance company subsidiaries are subject to prior claims of policyholders and creditors (except to the extent that its rights, if any, as a creditor are recognized). Consequently, AFG's ability to pay debts, expenses and cash dividends to its shareholders may be limited.

Adverse developments in the financial markets may limit AFG's access to capital.

Financial markets in the U.S. and elsewhere can experience extreme volatility, which exerts downward pressure on stock prices and limits access to the equity and debt markets for certain issuers, including AFG.

AFG can borrow up to $500 million under its revolving credit facility which expires in December 2016. There is no assurance that this facility will be renewed. In addition, AFG's access to funds through this facility is dependent on the ability of its banks to meet their funding commitments. There were no borrowings outstanding under AFG's bank credit line or any other parent company short-term borrowing arrangements during 2013.

If AFG cannot obtain adequate capital or sources of credit on favorable terms, or at all, its business, operating results and financial condition would be adversely affected.

AFG may be adversely impacted by a downgrade in the ratings of its debt securities.

AFG's debt securities are rated by Standard & Poor's and Moody's independent corporate credit rating agencies. AFG's senior indebtedness is currently rated BBB+ by Standard & Poor's and Baa2 by Moody's. Securities ratings are subject to revision or withdrawal at any time by the assigning rating organization. A security rating is not a recommendation to buy, sell or hold securities. An unfavorable change in either of these ratings could make it more expensive to access the capital markets and may increase the interest rate charged under AFG's current bank credit line.

AFG is a party to litigation which, if decided adversely, could impact its financial results.

AFG and its subsidiaries are named as defendants in a number of lawsuits. See *Item 1 — Business — "Property and Casualty Insurance Segment — Asbestos and Environmental ("A&E") Reserves," Item 3 — Legal Proceedings,* and *Item* 7 — *Management's Discussion and Analysis — "Uncertainties."* Litigation, by its very nature, is unpredictable and the outcome of these cases is uncertain and could result in liabilities that may vary from amounts AFG has currently recorded and a material variance could have a material effect on AFG's business, operations, profitability or financial condition.

Certain shareholders exercise substantial control over AFG's affairs, which may impede a change of control transaction.

Carl H. Lindner III and S. Craig Lindner are each Co-Chief Executive Officers and Directors of AFG. Together, Carl H. Lindner III and S. Craig Lindner beneficially own 10.1% of AFG's outstanding Common Stock as of February 1, 2014. As a result, certain members of the Lindner family have the ability to exercise significant influence over AFG's management, including over matters requiring shareholder approval.

The price of AFG Common Stock may fluctuate significantly, which may make it difficult for holders to resell common stock when they want or at a price they find attractive.

The price of AFG's Common Stock, listed on the NYSE and Nasdaq Global Select Market, constantly changes. During 2013, AFG's Common Stock traded at prices ranging between $39.76 and $58.44. AFG's Common Stock price can fluctuate as a result of a variety of factors, many of which are beyond its control. These factors include but are not limited to:

- actual or anticipated variations in quarterly operating results;
- actual or anticipated changes in the dividends paid on AFG Common Stock;
- rating agency actions;
- recommendations by securities analysts;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving AFG or its competitors;
- operating and stock price performance of other companies that investors deem comparable to AFG;
- news reports relating to trends, concerns and other issues in AFG's lines of business;
- general economic conditions, including volatility in the financial markets; and
- geopolitical conditions such as acts or threats of terrorism or military conflicts.

ITEM 2

Properties

Subsidiaries of AFG own several buildings in downtown Cincinnati. AFG and its affiliates occupy approximately 40% of the aggregate 675,000 square feet of commercial and office space in these buildings.

AFG and its insurance subsidiaries lease the majority of their office and storage facilities in numerous cities throughout the United States, including the Company’s home offices in Cincinnati. National Interstate occupies approximately 85% of the 177,000 square feet of office space on 17.5 acres of land that it owns in Richfield, Ohio. See *Item 1 — Business — “Other Operations”* for a discussion of AFG’s other commercial real estate operations.

ITEM 3

Legal Proceedings

AFG and its subsidiaries are involved in litigation from time to time, generally arising in the ordinary course of business. This litigation may include, but is not limited to, general commercial disputes, lawsuits brought by policyholders, employment matters, reinsurance collection matters and actions challenging certain business practices of insurance subsidiaries. Except for the following, management believes that none of the litigation meets the threshold for disclosure under this Item.

AFG’s insurance company subsidiaries and its 100%-owned subsidiary, American Premier Underwriters (including its subsidiaries, “American Premier”), are parties to litigation and receive claims alleging injuries and damages from asbestos, environmental and other substances and workplace hazards and have established loss accruals for such potential liabilities. None of such litigation or claims is individually material to AFG; however, the ultimate loss for these claims may vary materially from amounts currently recorded as the conditions surrounding resolution of these claims continue to change.

American Premier is a party or named as a potentially responsible party in a number of proceedings and claims by regulatory agencies and private parties under various environmental protection laws, including the Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”), seeking to impose responsibility on American Premier for hazardous waste or discharge remediation costs at certain railroad sites formerly owned by its predecessor, Penn Central Transportation Company (“PCTC”), and at certain other sites where hazardous waste or discharge allegedly generated by PCTC’s railroad operations and American Premier’s former manufacturing operations is present. It is difficult to estimate American Premier’s liability for remediation costs at these sites for a number of reasons, including the number and financial resources of other potentially responsible parties involved at a given site, the varying availability of evidence by which to allocate responsibility among such parties, the wide range of costs for possible remediation alternatives, changing technology and the period of time over which these matters develop. Nevertheless, American Premier believes that its accruals for potential environmental liabilities are adequate to cover the probable amount of such liabilities, based on American Premier’s estimates of remediation costs and related expenses and its estimates of the portions of such costs that will be borne by other parties. Such estimates are based on information currently available to American Premier and are subject to future change as additional information becomes available.

PART II

ITEM 5

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

AFG Common Stock is listed and traded on the New York Stock Exchange and the Nasdaq Global Select Market under the symbol AFG. The information presented in the table below represents the high and low sales prices per share reported on the NYSE Composite Tape.

	2013		2012	
	High	Low	High	Low
First Quarter	$ 47.50	$ 39.76	$ 38.97	$ 36.24
Second Quarter	49.88	46.45	40.54	37.37
Third Quarter	54.48	49.01	39.64	36.28
Fourth Quarter	58.44	52.44	40.40	36.92

There were approximately 6,200 shareholders of record of AFG Common Stock at February 1, 2014. AFG declared and paid regular quarterly dividends of $0.195 per share in January, April and July 2013. In August 2013, AFG increased its quarterly dividend to $0.22 and declared and paid its first dividend at that rate in October 2013. In December 2013, AFG declared and paid a special cash dividend of $1.00 per share of AFG Common Stock. In 2012, AFG declared and paid quarterly dividends of $0.175 per share in January, April and July and $0.195 per share in October. In December 2012, AFG declared and paid a special cash dividend of $0.25 per share of AFG Common Stock. The ability of AFG to pay dividends will be dependent upon, among other things, the availability of dividends and payments under intercompany tax allocation agreements from its insurance company subsidiaries.

Issuer Purchases of Equity Securities AFG repurchased shares of its Common Stock during 2013 as follows:

	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 (a)
First Quarter	61,586	$ 43.71	61,586	7,501,271
Second Quarter	1,386,570	48.37	1,386,570	6,114,701
Third Quarter	—	—	—	6,114,701
Fourth Quarter	—	—	—	6,114,701
Total	1,448,156	$ 48.17	1,448,156	

(a) Represents the remaining shares that may be repurchased under the Plans authorized by AFG's Board of Directors in August 2012 and February 2013.

In addition, AFG acquired 45,179 shares of its Common Stock (at an average of $46.38 per share) in the first nine months of 2013, 4,412 shares (at an average of $56.18 per share) in November 2013 and 9,383 shares (at an average of $57.96 per share) in December 2013 in connection with its stock incentive plans.

ITEM 6

Selected Financial Data

The following table sets forth certain data for the periods indicated (dollars in millions, except per share data).

	2013	2012	2011	2010	2009
Earnings Statement Data:					
Total revenues	$ 5,092	$ 4,957	$ 4,643	$ 4,400	$ 4,208
Earnings before income taxes	689	537	558	694	818
Net earnings, including noncontrolling interests	453	402	319	426	534
Less: Net earnings (loss) attributable to noncontrolling interests	(18)	(86)	(23)	(56)	11
Net earnings attributable to shareholders	471	488	342	482	523
Earnings attributable to shareholders per Common Share:					
Basic	$ 5.27	$ 5.18	$ 3.37	$ 4.41	$ 4.52
Diluted	5.16	5.09	3.32	4.36	4.48
Cash dividends paid per share of Common Stock (a)	$ 1.805	$ 0.97	$ 0.6625	$ 0.575	$ 0.52
Ratio of earnings to fixed charges including annuity benefits (b)	2.15	1.98	1.95	2.42	2.59
Balance Sheet Data:					
Cash and investments	$ 31,313	$ 28,449	$ 25,577	$ 22,670	$ 19,791
Total assets	42,087	39,171	35,838	32,241	27,442
Property and casualty insurance reserves:					
Unpaid losses and loss adjustment expenses	6,410	6,845	6,520	6,413	6,412
Unearned premiums	1,757	1,651	1,484	1,534	1,568
Annuity benefits accumulated	20,944	17,609	15,420	12,905	11,335
Life, accident and health reserves	2,008	2,059	1,727	1,650	1,603
Long-term debt	913	953	934	952	828
Shareholders’ equity	4,599	4,578	4,411	4,331	3,623
Less:					
Net unrealized gain on fixed maturities (c)	441	719	459	341	49
Appropriated retained earnings	49	75	173	197	—
Adjusted shareholders’ equity (d)	4,109	3,784	3,779	3,793	3,574
Book value per share	$ 51.38	$ 51.45	$ 45.08	$ 41.18	$ 31.95
Adjusted book value per share (d)	45.90	42.52	38.63	36.06	31.52

(a) Includes special cash dividends of $1.00 and $0.25 per share paid in December 2013 and 2012, respectively.

(b) Fixed charges are computed on a “total enterprise” basis. For purposes of calculating the ratios, “earnings” have been computed by adding to pretax earnings the fixed charges and the noncontrolling interests in earnings of subsidiaries having fixed charges and the undistributed equity in losses of investees. Fixed charges include interest (including annuity benefits as indicated), amortization of debt premium/discount and expense, preferred dividend and distribution requirements of subsidiaries and a portion of rental expense deemed to be representative of the interest factor. The ratio of earnings to fixed charges excluding annuity benefits was 8.86, 7.16, 6.59, 9.14 and 11.03 for 2013, 2012, 2011, 2010 and 2009, respectively. Although the ratio of earnings to fixed charges excluding annuity benefits is not required or encouraged to be disclosed under Securities and Exchange Commission rules, some investors and lenders may not consider interest credited to annuity policyholders’ accounts a borrowing cost for an insurance company, and accordingly, believe this ratio is meaningful.

(c) The net unrealized gain on fixed maturities is a component of accumulated other comprehensive income and is shown net of related adjustments to deferred policy acquisition costs and certain liabilities in the annuity, long-term care and life businesses.

(d) Adjusted shareholders’ equity and adjusted book value per share exclude appropriated retained earnings and net unrealized gains related to fixed maturity securities. Management believes that investors find a measurement of shareholders’ equity excluding these items to be meaningful as (i) the unrealized gain on fixed maturities fluctuates with changes in interest rates in a way that is primarily only meaningful to AFG if it sells those investments and (ii) appropriated retained earnings represents amounts that will ultimately inure to the benefit of the debt holders of the collateralized loan obligations managed by AFG.

ITEM 7

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

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GENERAL

Following is a discussion and analysis of the financial statements and other statistical data that management believes will enhance the understanding of AFG's financial condition and results of operations. This discussion should be read in conjunction with the financial statements beginning on page F-1.

OVERVIEW

Financial Condition

AFG is organized as a holding company with almost all of its operations being conducted by subsidiaries. AFG, however, has continuing cash needs for administrative expenses, the payment of principal and interest on borrowings, shareholder dividends, and taxes. Therefore, certain analyses are most meaningfully presented on a parent only basis while others are best done on a total enterprise basis. In addition, because most of its businesses are financial in nature, AFG does not prepare its consolidated financial statements using a current-noncurrent format. Consequently, certain traditional ratios and financial analysis tests are not meaningful.

At December 31, 2013, AFG (parent) held approximately $576 million in cash and securities and had $500 million available under a bank line of credit expiring in December 2016. See *"Liquidity and Capital Resources — Parent and Subsidiary Liquidity"* for a discussion of the planned acquisition of Summit Holdings Southeast, Inc.

Results of Operations

Through the operations of its subsidiaries, AFG is engaged primarily in property and casualty insurance, focusing on specialized commercial products for businesses and in the sale of fixed and fixed-indexed annuities in the retail, financial institutions and education markets.

Net earnings attributable to AFG's shareholders were $158 million ($1.73 per share, diluted) for the fourth quarter of 2013 compared to $50 million ($0.54 per share) in the fourth quarter of 2012, reflecting significantly higher profits in the annuity segment and improved underwriting results in the Specialty property and casualty businesses. The fourth quarter 2012 results include a $99 million ($1.08 per share) after-tax charge to write off deferred policy acquisition costs and strengthen reserves in AFG's closed block of long-term care insurance. This non-core charge was partially offset by $39 million ($0.43 per share) of tax benefits related to the settlement of open tax years following the favorable resolution of certain tax litigation.

Net earnings attributable to AFG's shareholders were $471 million ($5.16 per share) in 2013 compared to $488 million ($5.09 per share) in 2012. Significantly higher profits in the annuity segment and improved underwriting results in the Specialty property and casualty businesses were partially offset by higher special A&E charges and the absence of earnings from the Medicare supplement and critical illness segment, which was sold in August 2012. The $17 million overall decrease in net earnings attributable to shareholders reflects the net impact of the following items recorded during 2012: (i) the gain on the sale of the Medicare supplement and critical illness segment, (ii) tax benefits related to the favorable resolution of certain tax litigation and settlement of open tax years, and (iii) a fourth quarter charge to write off deferred policy acquisition costs and strengthen reserves in AFG's closed block of long-term care insurance.

CRITICAL ACCOUNTING POLICIES

Significant accounting policies are summarized in *Note A — "Accounting Policies"* to the financial statements. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that can have a significant effect on amounts reported in the financial statements. As more information becomes known, these estimates and assumptions change and, thus, impact amounts reported in the future. The areas where management believes the degree of judgment required to determine amounts recorded in the financial statements make accounting policies critical are as follows:

- the establishment of insurance reserves, especially asbestos and environmental-related reserves and reserves for AFG's closed block of long-term care insurance,
- the recoverability of reinsurance,
- the recoverability of deferred acquisition costs,
- the establishment of asbestos and environmental reserves of former railroad and manufacturing operations, and
- the valuation of investments, including the determination of "other-than-temporary" impairments.

See *"Liquidity and Capital Resources — Uncertainties"* for a discussion of insurance reserves, recoverables from reinsurers, and contingencies related to American Premier's former operations and *"Liquidity and Capital Resources — Investments"* for a discussion of impairments on investments. DPAC and certain liabilities related to annuities and universal life insurance products are amortized in relation to the present value of expected gross profits on the policies. Assumptions considered in determining expected gross profits involve significant judgment and include management's estimates of interest rates and investment spreads, surrenders, annuitizations, renewal premiums and mortality. Should actual experience require management to change its assumptions (commonly referred to as "unlocking"), a charge or credit would be recorded to adjust DPAC or annuity liabilities to the levels they would have been if the new assumptions had been used from the inception date of each policy.

Reserves for future policy benefits related to AFG's closed block of long-term care insurance are established (and related acquisition costs are amortized) over the life of the policies based on policy benefit assumptions as of the date of issuance, including investment yields, mortality, morbidity, persistency, and expenses. Once these assumptions are established for a given policy or group of policies, they are not changed over the life of the policy unless a loss recognition event (premium deficiency) occurs. Loss recognition occurs when, based on current expectations as of the measurement date, existing contract liabilities plus the present value of future premiums, including reasonably expected rate increases, are not expected to cover the present value of future claims payments and related settlement and maintenance costs as well as unamortized acquisition costs. AFG recorded a loss recognition charge in its long-term care business in the fourth quarter of 2012. As a result of this charge, all remaining unamortized acquisition costs in the long-term care business were written off and policy benefit assumptions were reset to 2012 assumptions, resulting in an increase to the reserve for future policy benefits. These assumptions will not be changed again unless a future loss recognition event occurs. Although no additional loss recognition occurred in 2013, adverse changes in any of the current policy benefit assumptions could result in a future loss recognition event and additional charges to earnings.

LIQUIDITY AND CAPITAL RESOURCES

Ratios AFG's debt to total capital ratio on a consolidated basis is shown below (dollars in millions). Management intends to maintain the ratio of debt to capital at or below 25% and intends to maintain the capital of its significant insurance subsidiaries at or above levels currently indicated by rating agencies as appropriate for the current ratings.

	December 31,	
	2013	2012
Long-term debt	$ 913	$ 953
Total capital	5,192	4,907
Ratio of debt to total capital:		
Including debt secured by real estate	17.6%	19.4%
Excluding debt secured by real estate	16.6%	18.4%

The ratio of debt to total capital is a non-GAAP measure that management believes is useful for investors, analysts and independent ratings agencies to evaluate AFG's financial strength and liquidity and to provide insight into how AFG finances its operations. The ratio is calculated by dividing AFG's long-term debt by its total capital, which includes long-term debt, noncontrolling interests and shareholders' equity (excluding unrealized gains (losses) related to fixed maturity investments and appropriated retained earnings related to managed investment entities).

AFG's ratio of earnings to fixed charges, including annuity benefits as a fixed charge, was 2.15 for the year ended December 31, 2013. Excluding annuity benefits, this ratio was 8.86. Although the ratio excluding annuity benefits is not required or encouraged to be disclosed under Securities and Exchange Commission rules, it is presented because interest credited to annuity policyholder accounts is not always considered a borrowing cost for an insurance company.

The NAIC's model law for risk based capital ("RBC") applies to both life and property and casualty companies. RBC formulas determine the amount of capital that an insurance company needs so that it has an acceptable expectation of not becoming financially impaired. At December 31, 2013, the capital ratios of all AFG insurance companies substantially exceeded the RBC requirements.

Condensed Consolidated Cash Flows AFG's principal sources of cash include insurance premiums, income from its investment portfolio and proceeds from the maturities, redemptions and sales of investments. Insurance premiums in excess of acquisition expenses and operating costs are invested until they are needed to meet policyholder obligations or made available to the parent company through dividends to cover debt obligations and corporate expenses, and to provide returns to shareholders through share repurchases and dividends. AFG's cash flows from operating, investing and financing activities as detailed in its Consolidated Statement of Cash Flows are shown below (in millions):

	Year ended December 31,		
	2013	2012	2011
Net cash provided by operating activities	$ 760	$ 817	$ 667
Net cash used in investing activities	(2,915)	(1,425)	(2,439)
Net cash provided by financing activities	2,089	989	1,997
Net change in cash and cash equivalents	$ (66)	$ 381	$ 225

Net Cash Provided by Operating Activities AFG's property and casualty insurance operations typically produce positive net operating cash flows as premiums collected and investment income exceed policy acquisition costs, claims payments and operating expenses. AFG's net cash provided by operating activities is impacted by the level and timing of property and casualty premiums, claim and expense payments and recoveries from reinsurers. AFG's annuity operations typically produce positive net operating cash flows as investment income exceeds acquisition costs and operating expenses. Interest credited on annuity policyholder funds is a non-cash increase in AFG's annuity benefits accumulated liability and annuity premiums, benefits and withdrawals are considered financing activities due to the deposit-type nature of annuities. Net cash provided by operating activities was $760 million, $817 million and $667 million in 2013, 2012 and 2011, respectively. The $57 million decrease in net cash provided by operating activities in 2013 compared to 2012 and the $150 million increase in net cash provided by operating activities in 2012 compared to 2011 is due primarily to the timing of claims payments and reinsurance recoveries in the property and casualty insurance operations.

Net Cash Used in Investing Activities AFG's investing activities consist primarily of the investment of funds provided by its property and casualty and annuity products. Net cash used in investing activities was $2.92 billion in 2013 compared to $1.43 billion in 2012, an increase of $1.49 billion. The $1.15 billion increase in net cash flows from annuity policyholders in 2013 as compared to 2012 (discussed below under net cash provided by financing activities) increased the amount of cash available for investment in 2013 compared to 2012. In addition, the increase in net cash used in investing activities reflects the use of cash and cash equivalents held in the property and casualty operations to purchase fixed maturity and equity securities during 2013. Investing activities also include the purchase and disposal of managed investment entity (collateralized loan obligation) investments, which are presented separately in AFG's Balance Sheet. Net investment activity in the managed investment entities was a $478 million source of cash in 2013 compared to an $8 million source of cash in 2012. See *Note A — "Accounting Policies — Managed Investment Entities"* and *Note H — "Managed Investment Entities*" to the financial statements.

Net cash used in investing activities was $1.43 billion in 2012 compared to $2.44 billion in 2011, a decrease of $1.01 billion. The $519 million decrease in net cash flows from annuity policyholders in 2012 as compared to 2011 (discussed below under net cash provided by financing activities) reduced the amount of cash available for investment in 2012 compared to 2011. In addition, cash on hand in the annuity and run-off long-term care and life segments increased by $190 million during 2012 from year-end 2011 as net cash flows from annuity policyholders outpaced the investment of the funds received. Net investment activity in the managed investment entities was an $8 million source of cash in 2012 compared to a $172 million use of cash in 2011.

Net Cash Provided by Financing Activities AFG's financing activities consist primarily of transactions with annuity policyholders, issuances and retirements of long-term debt, repurchases of common stock and dividend payments. Net cash provided by financing activities was $2.09 billion in 2013 compared to $989 million in 2012, an increase of $1.10 billion. Annuity receipts exceeded annuity surrenders, benefits, withdrawals and transfers by $2.68 billion in 2013 compared to $1.53 billion in 2012, resulting in a $1.15 billion increase in net cash provided by financing activities. During 2013, AFG repurchased 1.4 million shares of its Common Stock for $70 million compared to 10.9 million shares repurchased in 2012 for $415 million, which accounted for $345 million of the increase in net cash provided by financing activities in 2013 compared to 2012. Financing activities also include the issuance and retirement of managed investment entity liabilities, which are nonrecourse to AFG and presented separately in AFG's Balance Sheet. The retirement of managed investment entity liabilities exceed issuances by $368 million in 2013 compared to $49 million in 2012, accounting for a $319 million reduction in net cash provided by financing activities in 2013 compared to 2012. See *Managed Investment Entities* in *Note A — "Accounting Policies"* and *Note H — "Managed Investment Entities*" to the financial statements.

Net cash provided by financing activities was $989 million in 2012 compared to $2.00 billion in 2011, a decrease of $1.01 billion. Annuity receipts exceeded annuity surrenders, benefits, withdrawals and transfers by $1.53 billion in 2012 compared to $2.04 billion in 2011, resulting in a $519 million decrease in net cash provided by financing activities. During 2012, AFG repurchased 10.9 million shares of its Common Stock for $415 million compared to 9.3 million shares repurchased in 2011 for $315 million, which accounted for $100 million of the decline in net cash provided by financing activities. The retirement of managed investment entity liabilities exceed issuances by $49 million in 2012 while issuances of managed investment entity liabilities exceed retirements by $328 million in 2011, accounting for $377 million of the decrease in net cash provided by financing activities in 2012 compared to 2011.

Parent and Subsidiary Liquidity

Parent Holding Company Liquidity Management believes AFG has sufficient resources to meet its liquidity requirements. If funds generated from operations, including dividends, tax payments and borrowings from subsidiaries, are insufficient to meet fixed charges in any period, AFG would be required to utilize parent company cash and marketable securities or to generate cash through borrowings, sales of other assets, or similar transactions.

In December 2012, AFG replaced its bank credit facility with a four-year, $500 million revolving credit line. Amounts borrowed under this agreement bear interest at rates ranging from 1.00% to 1.875% (currently 1.375%) over LIBOR based on AFG's credit rating. There were no borrowings under this agreement, or under any other parent company short-term borrowing arrangements, during 2013.

In January 2014, AFG announced that it had reached a definitive agreement to acquire Summit Holdings Southeast, Inc., from Liberty Mutual for $250 million. Including a planned capital contribution at closing, AFG's total capital investment in the Summit business will be approximately $400 million.

During 2013, AFG repurchased 1.4 million shares of its Common Stock for $70 million. In December 2013, AFG paid a special cash dividend of $1.00 per share of AFG Common Stock totaling approximately $89 million.

In 2012, AFG issued $125 million of 5-3/4% Senior Notes due 2042 and $230 million of 6-3/8% Senior Notes due 2042 and used the proceeds to redeem outstanding higher rate debt. During 2012, AFG repurchased 10.9 million shares of its Common Stock for $415 million. In December 2012, AFG paid a special cash dividend of $0.25 per share of AFG Common Stock totaling approximately $23 million. During 2011, AFG repurchased 9.3 million shares of its Common Stock for $315 million.

All debentures and notes issued by AFG are rated investment grade by two nationally recognized rating agencies. Under a currently effective shelf registration statement, AFG can offer additional equity or debt securities. The shelf registration provides AFG with flexibility to access the capital markets from time to time as market and other conditions permit.

Under tax allocation agreements with AFG, its 80%-owned U.S. subsidiaries generally pay taxes to (or recover taxes from) AFG based on each subsidiary's contribution to amounts due under AFG's consolidated tax return.

Subsidiary Liquidity In February 2014, Great American Insurance Company ("GAI"), AFG's wholly-owned property and casualty insurance subsidiary, initiated a tender offer to acquire the 9.5 million shares of National Interstate Corporation ("NATL") that it does not currently own for $286 million ($30.00 per share, as adjusted). NATL is a 52%-owned property and casualty insurance subsidiary of GAI.

Great American Life Insurance Company ("GALIC"), a wholly-owned annuity subsidiary, is a member of the Federal Home Loan Bank of Cincinnati ("FHLB"). The FHLB makes advances and provides other banking services to member institutions, which provides the annuity operations with a substantial additional source of liquidity. These advances further the FHLB's mission of improving access to housing by increasing liquidity in the residential mortgage-backed securities market. The FHLB advanced GALIC $240 million in the fourth quarter of 2011 and $200 million in the second quarter of 2013 (included in annuity benefits accumulated). The interest rates on the advances range from 0.02% to 0.23% over LIBOR (average rate of 0.32% at December 31, 2013). While these advances must be repaid between 2016 and 2018, GALIC has the option to prepay all or a portion of the advances. GALIC has invested the proceeds from the advances in fixed maturity securities for the purpose of earning a spread over the interest payments due to the FHLB.

In November 2012, NATL replaced its $50 million bank credit facility with a five-year, $100 million unsecured credit agreement. There was $12 million borrowed under this agreement at December 31, 2013, bearing interest at 1.11% (three-month LIBOR plus 0.875%). The maximum outstanding balance in 2013 was $12 million.

The liquidity requirements of AFG's insurance subsidiaries relate primarily to the liabilities associated with their products as well as operating costs and expenses, payments of dividends and taxes to AFG and contributions of capital to their subsidiaries. Historically, cash flows from premiums and investment income have generally provided more than sufficient funds to meet these requirements. Funds received in excess of cash requirements are generally invested in additional marketable securities. In addition, the insurance subsidiaries generally hold a significant amount of highly liquid, short-term investments.

The excess cash flow of AFG's property and casualty group allows it to extend the duration of its investment portfolio somewhat beyond that of its claim reserves.

In the annuity business, where profitability is largely dependent on earning a "spread" between invested assets and annuity liabilities, the duration of investments is generally maintained close to that of liabilities. In a rising interest rate environment, significant protection from withdrawals exists in the form of temporary and permanent surrender charges on AFG's annuity products. With declining rates, AFG receives some protection (from spread compression) due to the ability to lower crediting rates, subject to contractually guaranteed minimum interest rates ("GMIRs"). AFG began selling policies with GMIRs below 2% in 2003; almost all new business since late 2010 has been issued with a 1% GMIR. At December 31, 2013, AFG could reduce the average crediting rate of its $16 billion of traditional fixed and fixed-indexed deferred annuities without guaranteed withdrawal benefits by approximately 48 basis points (on a weighted average basis).

For statutory accounting purposes, equity securities of non-affiliates are generally carried at fair value. At December 31, 2013, AFG's insurance companies owned publicly traded equity securities with a fair value of $1.14 billion. In addition, GAI's investment in NATL common stock had a fair value of $235 million and a statutory carrying value of $186 million at December 31, 2013. Decreases in market prices could adversely affect the insurance group's capital, potentially impacting the amount of dividends available or necessitating a capital contribution. Conversely, increases in market prices could have a favorable impact on the group's dividend-paying capability.

AFG believes its insurance subsidiaries maintain sufficient liquidity to pay claims and benefits and operating expenses. In addition, these subsidiaries have sufficient capital to meet commitments in the event of unforeseen events such as reserve deficiencies, inadequate premium rates or reinsurer insolvencies. Nonetheless, changes in statutory accounting rules, significant declines in the fair value of the insurance subsidiaries' investment portfolios or significant ratings downgrades on these investments, could create a need for additional capital.

Condensed Parent Only Cash Flows AFG's parent holding company only condensed cash flows from operating, investing and financing activities are shown below (in millions):

	Year ended December 31,		
	2013	2012	2011
Net cash provided by operating activities	$ 428	$ 380	$ 462
Net cash used in investing activities	(4)	(284)	(72)
Net cash used in financing activities	(180)	(232)	(345)
Net change in cash and cash equivalents	$ 244	$ (136)	$ 45

Parent Net Cash Provided by Operating Activities Parent holding company cash flows from operating activities consist primarily of dividends and tax payments received from AFG's insurance subsidiaries, reduced by tax payments to the IRS and holding company interest and other expenses. Parent holding company net cash provided by operating activities was $428 million in 2013 compared to $380 million in 2012 and $462 million in 2011. Higher dividends from subsidiaries received in 2013 and 2011 as compared to 2012 were the primary driver of the $48 million increase in net cash provided by operating activities in 2013 compared to 2012 and the $82 million decrease in net cash provided by operating activities in 2012 compared to 2011.

Parent Net Cash Used in Investing Activities Parent holding company investing activities consist of capital contributions to and returns of capital from subsidiaries and, to a much lesser extent, parent company investment activity. Parent holding company net cash used in investing activities was $4 million in 2013 compared to $284 million in 2012 and $72 million in 2011. The $284 million in net cash used in investing activities in 2012 is significantly higher than the cash used in investing activities in 2013 and 2011 due primarily to capital contributions made to AAG Holding Company, Inc. to fund the July 2012 redemption of $199 million of AAG Holding senior debentures.

Parent Net Cash Used in Financing Activities Parent company financing activities consist primarily of repurchases of AFG Common Stock, dividends to shareholders, the issuance and retirement of long-term debt and, to a lesser extent, proceeds from employee stock option exercises. Significant long-term debt and common stock transactions are discussed above. Parent holding company net cash used in financing activities was $180 million in 2013 compared to $232 million in 2012 and $345 million in 2011. The $52 million decrease in net cash used in financing activities in 2013 as compared to 2012 reflects a $345 million decrease in common stock repurchases partially offset by the impact of $229 million in cash provided in 2012 from debt issuances in excess of debt retirements and a $70 million increase in cash dividends paid. The $113 million decrease in net cash used in financing activities in 2012 compared to 2011 was due primarily to cash provided by the net debt issuances in 2012, partially offset by a $100 million increase in common stock repurchases.

Contractual Obligations The following table shows an estimate (based on historical patterns and expected trends) of payments to be made for insurance reserve liabilities, as well as scheduled payments for major contractual obligations (in millions).

	Total	Within One Year	2-3 Years	4-5 Years	More than 5 Years
Annuities (a)	$ 20,944	$ 1,808	$ 4,319	$ 4,659	$ 10,158
Life, accident and health liabilities (a)	2,008	196	252	214	1,346
Property and casualty unpaid losses and loss adjustment expenses (b)	6,410	1,600	1,500	800	2,510
Long-term debt, including interest	2,075	71	196	143	1,665
Liability for uncertain tax positions (c)	19	19	—	—	—
Purchase of Summit Holdings Southeast, Inc.	250	250	—	—	—
Operating leases	389	57	94	65	173
Total	$ 32,095	$ 4,001	$ 6,361	$ 5,881	$ 15,852

(a) Reserve projections include anticipated cash benefit payments only. Projections do not include any impact for future earnings or additional premiums. Based on the same assumptions, AFG projects reinsurance recoveries related to life, accident and health reserves totaling $953 million as follows: Within 1 year — $114 million; 2-3 years — $142 million; 4-5 years — $124 million; and thereafter — $573 million. Actual payments and their timing could differ significantly from these estimates.

(b) Dollar amounts and time periods are estimates based on historical net payment patterns applied to the gross reserves and do not represent actual contractual obligations. Based on the same assumptions, AFG projects reinsurance recoveries related to these reserves totaling $2.1 billion as follows: Within 1 year — $500 million; 2-3 years — $500 million; 4-5 years — $300 million; and thereafter — $800 million. Actual payments and their timing could differ significantly from these estimates.

(c) As a result of discussions with the IRS Appeals Office during the third quarter of 2013, AFG believes that its liability for uncertain tax positions may be reduced by up to the full $19 million balance within the coming year due to a settlement with the IRS. The majority of the reduction in this liability would result in offsetting adjustments to AFG's deferred tax liability.

AFG has no material contractual purchase obligations or other long-term liabilities at December 31, 2013.

Off-Balance Sheet Arrangements See *Note P — "Additional Information — Financial Instruments — Unfunded Commitments"* to the financial statements.

Investments AFG attempts to optimize investment income while building the value of its portfolio, placing emphasis upon total long-term performance.

AFG's investment portfolio at December 31, 2013, contained $26.46 billion in "Fixed maturities" classified as available for sale and $1.18 billion in "Equity securities," all carried at fair value with unrealized gains and losses included in a separate component of shareholders' equity on an after-tax basis. In addition, $305 million in fixed maturities were classified as trading with changes in unrealized holding gains or losses included in investment income.

As detailed in *Note E — "Investments — Net Unrealized Gain on Marketable Securities"* to the financial statements, unrealized gains and losses on AFG's fixed maturity and equity securities are included in shareholders' equity after adjustments for related changes in DPAC and certain liabilities related to annuity, long-term care and life businesses, noncontrolling interests and deferred income taxes. DPAC and certain other balance sheet amounts applicable to annuity, long-term care and life businesses are adjusted for the impact of unrealized gains or losses on investments as if these gains or losses had been realized, with corresponding increases or decreases (net of tax) included in accumulated other comprehensive income in AFG's Balance Sheet.

Fixed income investment funds are generally invested in securities with intermediate-term maturities with an objective of optimizing total return while allowing flexibility to react to changes in market conditions. At December 31, 2013, the average life of AFG's fixed maturities was about 6-1/2 years.

Fair values for AFG's portfolio are determined by AFG's internal investment professionals using data from nationally recognized pricing services as well as non-binding broker quotes. Fair values of equity securities are generally based on closing prices obtained from the pricing services. For mortgage-backed securities ("MBS"), which comprise approximately 26% of AFG's fixed maturities, prices for each security are generally obtained from both pricing services and broker quotes. For the remainder of AFG's fixed maturity portfolio, approximately 86% are priced using pricing services and the balance is priced primarily by using non-binding broker quotes. When prices obtained for the same security vary, AFG's internal investment professionals select the price they believe is most indicative of an exit price.

The pricing services use a variety of observable inputs to estimate fair value of fixed maturities that do not trade on a daily basis. Based upon information provided by the pricing services, these inputs include, but are not limited to, recent reported trades, benchmark yields, issuer spreads, bids or offers, reference data, and measures of volatility. Included in the pricing of MBS are estimates of the rate of future prepayments and defaults of principal over the remaining life of the underlying collateral. Due to the lack of transparency in the process that brokers use to develop prices, valuations that are based on brokers' prices are classified as Level 3 in the GAAP hierarchy unless the price can be corroborated, for example, by comparison to similar securities priced using observable inputs.

Valuation techniques utilized by pricing services and prices obtained from external sources are reviewed by AFG's internal investment professionals who are familiar with the securities being priced and the markets in which they trade to ensure the fair value determination is representative of an exit price. To validate the appropriateness of the prices obtained, these investment managers consider widely published indices (as benchmarks), recent trades, changes in interest rates, general economic conditions and the credit quality of the specific issuers. In addition, AFG communicates directly with pricing services regarding the methods and assumptions used in pricing, including verifying, on a test basis, the inputs used by the services to value specific securities.

In general, the fair value of AFG's fixed maturity investments is inversely correlated to changes in interest rates. The following table demonstrates the sensitivity of such fair values to reasonably likely changes in interest rates by illustrating the estimated effect on AFG's fixed maturity portfolio that an immediate increase of 100 basis points in the interest rate yield curve would have at December 31, 2013 (dollars in millions). Effects of increases or decreases from the 100 basis points illustrated would be approximately proportional.

Fair value of fixed maturity portfolio	$	26,761
Pretax impact on fair value of 100 bps increase in interest rates	$	(1,204)
Pretax impact as % of total fixed maturity portfolio		(4.5%)

Approximately 86% of the fixed maturities held by AFG at December 31, 2013, were rated "investment grade" (credit rating of AAA to BBB) by nationally recognized rating agencies. Investment grade securities generally bear lower yields and lower degrees of risk than those that are unrated and non-investment grade. Management believes that the high quality investment portfolio should generate a stable and predictable investment return.

MBS are subject to significant prepayment risk due to the fact that, in periods of declining interest rates, mortgages may be repaid more rapidly than scheduled as borrowers refinance higher rate mortgages to take advantage of lower rates. Although interest rates have been low for the last few years, tighter lending standards have resulted in fewer buyers being able to refinance the mortgages underlying much of AFG's non-agency residential MBS portfolio.

Summarized information for AFG's MBS (including those classified as trading) at December 31, 2013, is shown (dollars in millions) in the table below. Agency-backed securities are those issued by a U.S. government-backed agency; Alt-A mortgages are those with risk profiles between prime and subprime. The majority of the Alt-A securities and substantially all of the subprime securities are backed by fixed-rate mortgages. The average life of the residential and commercial MBS is approximately 5 years and 4 years, respectively.

	Amortized Cost	Fair Value	Fair Value as % of Cost	Unrealized Gain (Loss)	% Rated Investment Grade
Collateral type					
Residential:					
Agency-backed	$ 297	$ 300	101%	$ 3	100%
Non-agency prime	1,866	2,070	111%	204	41%
Alt-A	938	1,028	110%	90	23%
Subprime	857	923	108%	66	18%
Commercial	2,543	2,732	107%	189	100%
	$ 6,501	$ 7,053	108%	$ 552	61%

The National Association of Insurance Commissioners ("NAIC") assigns creditworthiness designations on a scale of 1 to 6 with 1 being the highest quality and 6 being the lowest quality. The NAIC retains third-party investment management firms to assist in the determination of appropriate NAIC designations for mortgage-backed securities based not only on the probability of loss (which is the primary basis of ratings by the major ratings firms), but also on the severity of loss and statutory carrying value. At December 31, 2013, 98% (based on statutory carrying value of $6.42 billion) of AFG's MBS securities had a NAIC designation of 1 or 2.

Municipal bonds represented approximately 20% of AFG's fixed maturity portfolio at December 31, 2013. AFG's municipal bond portfolio is high quality, with 99% of the securities rated investment grade at that date. The portfolio is well diversified across the states of issuance and individual issuers. At December 31, 2013, approximately 73% of the municipal bond portfolio was held in revenue bonds, with the remaining 27% held in general obligation bonds. General obligation securities of California, Illinois, Michigan, New Jersey, New York and Puerto Rico collectively represented less than 2% of this portfolio.

Summarized information for the unrealized gains and losses recorded in AFG's Balance Sheet at December 31, 2013, is shown in the following table (dollars in millions). Approximately $187 million of available for sale fixed maturity securities and $75 million of equity securities had no unrealized gains or losses at December 31, 2013.

	Securities With Unrealized Gains	Securities With Unrealized Losses
Available for Sale Fixed Maturities		
Fair value of securities	$ 18,987	$ 7,282
Amortized cost of securities	$ 17,592	$ 7,587
Gross unrealized gain (loss)	$ 1,395	$ (305)
Fair value as % of amortized cost	108%	96%
Number of security positions	3,684	1,195
Number individually exceeding $2 million gain or loss	122	17
Concentration of gains (losses) by type or industry (exceeding 5% of unrealized):		
Mortgage-backed securities	$ 583	$ (31)
States and municipalities	156	(144)
Gas and electric services	111	(6)
Asset-backed securities	35	(19)
Banks, savings and credit institutions	106	(19)
Percentage rated investment grade	84%	90%
Equity Securities		
Fair value of securities	$ 835	$ 269
Cost of securities	$ 617	$ 295
Gross unrealized gain (loss)	$ 218	$ (26)
Fair value as % of cost	135%	91%
Number of security positions	181	56
Number individually exceeding $2 million gain or loss	43	3

The table below sets forth the scheduled maturities of AFG's available for sale fixed maturity securities at December 31, 2013, based on their fair values. Securities with sinking funds are reported at average maturity. Actual maturities may differ from contractual maturities because certain securities may be called or prepaid by the issuers.

	Securities With Unrealized Gains	Securities With Unrealized Losses
Maturity		
One year or less	4%	1%
After one year through five years	24%	5%
After five years through ten years	26%	35%
After ten years	8%	29%
	62%	70%
Asset-backed securities (average life of approximately 5 years)	6%	18%
Mortgage-backed securities (average life of approximately 4-1/2 years)	32%	12%
	100%	100%

The table below (dollars in millions) summarizes the unrealized gains and losses on fixed maturity securities by dollar amount:

	Aggregate Fair Value	Aggregate Unrealized Gain (Loss)	Fair Value as % of Cost Basis
Fixed Maturities at December 31, 2013			
Securities with unrealized gains:			
Exceeding $500,000 (818 securities)	$ 9,203	$ 986	112%
$500,000 or less (2,866 securities)	9,784	409	104%
	$ 18,987	$ 1,395	108%
Securities with unrealized losses:			
Exceeding $500,000 (179 securities)	$ 2,254	$ (186)	92%
$500,000 or less (1,016 securities)	5,028	(119)	98%
	$ 7,282	$ (305)	96%

The following table summarizes (dollars in millions) the unrealized loss for all securities with unrealized losses by issuer quality and the length of time those securities have been in an unrealized loss position:

	Aggregate Fair Value	Aggregate Unrealized Loss	Fair Value as % of Cost Basis
Securities with Unrealized Losses at December 31, 2013			
Investment grade fixed maturities with losses for:			
Less than one year (944 securities)	$ 6,371	$ (255)	96%
One year or longer (50 securities)	217	(18)	92%
	$ 6,588	$ (273)	96%
Non-investment grade fixed maturities with losses for:			
Less than one year (106 securities)	$ 511	$ (14)	97%
One year or longer (95 securities)	183	(18)	91%
	$ 694	$ (32)	96%
Common equity securities with losses for:			
Less than one year (26 securities)	$ 158	$ (16)	91%
One year or longer (3 securities)	—	—	—%
	$ 158	$ (16)	91%
Perpetual preferred equity securities with losses for:			
Less than one year (17 securities)	$ 91	$ (6)	94%
One year or longer (10 securities)	20	(4)	83%
	$ 111	$ (10)	92%

When a decline in the value of a specific investment is considered to be “other-than-temporary,” a provision for impairment is charged to earnings (accounted for as a realized loss) and the cost basis of that investment is reduced by the amount of the charge. The determination of whether unrealized losses are “other-than-temporary” requires judgment based on subjective as well as objective factors. Factors considered and resources used by management include:

a) whether the unrealized loss is credit-driven or a result of changes in market interest rates,
b) the extent to which fair value is less than cost basis,
c) cash flow projections received from independent sources,
d) historical operating, balance sheet and cash flow data contained in issuer SEC filings and news releases,
e) near-term prospects for improvement in the issuer and/or its industry,
f) third party research and communications with industry specialists,
g) financial models and forecasts,
h) the continuity of dividend payments, maintenance of investment grade ratings and hybrid nature of certain investments,
i) discussions with issuer management, and
j) ability and intent to hold the investment for a period of time sufficient to allow for anticipated recovery in fair value.

Based on its analysis of the factors listed above, management believes AFG will recover its cost basis in the securities with unrealized losses and that AFG has the ability to hold the securities until they recover in value and had no intent to sell them at December 31, 2013. Although AFG has the ability to continue holding its investments with unrealized losses, its intent to hold them may change due to deterioration in the issuers' creditworthiness, decisions to lessen exposure to a particular issuer or industry, asset/liability management decisions, market movements, changes in views about appropriate asset allocation or the desire to offset taxable realized gains. Should AFG's ability or intent change with regard to a particular security, a charge for impairment would likely be required. While it is not possible to accurately predict if or when a specific security will become impaired, charges for other-than-temporary impairment could be material to results of operations in future periods. Significant declines in the fair value of AFG's investment portfolio could have a significant adverse effect on AFG's liquidity. For information on AFG's realized gains (losses) on securities, including charges for "other-than-temporary" impairment, see *"Results of Operations — Consolidated Realized Gains (Losses) on Securities."*

Uncertainties As more fully explained in the following paragraphs, management believes that the areas posing the greatest risk of material loss are the adequacy of its insurance reserves and contingencies arising out of its former railroad and manufacturing operations.

Property and Casualty Insurance Reserves Estimating the liability for unpaid losses and loss adjustment expenses ("LAE") is inherently judgmental and is influenced by factors that are subject to significant variation. Determining the liability is a complex process incorporating input from many areas of the Company including actuarial, underwriting, pricing, claims and operations management.

The estimates of liabilities for unpaid claims and for expenses of investigation and adjustment of unpaid claims are based upon: (i) the accumulation of case estimates for losses reported prior to the close of the accounting periods on direct business written ("case reserves"); (ii) estimates received from ceding reinsurers and insurance pools and associations; (iii) estimates of claims incurred but not reported or "IBNR" (including possible development on known claims); (iv) estimates (based on experience) of expense for investigating and adjusting claims; and (v) the current state of law and coverage litigation.

The process used to determine the total reserve for liabilities involves estimating the ultimate incurred losses and LAE, adjusted for amounts already paid on the claims. The IBNR reserve is derived by first estimating the ultimate unpaid reserve liability and subtracting case reserves for loss and LAE.

In determining management's best estimate of the ultimate liability, management (including Company actuaries) considers items such as the effect of inflation on medical, hospitalization, material, repair and replacement costs, the nature and maturity of lines of insurance, general economic trends and the legal environment. In addition, historical trends adjusted for changes in underwriting standards, policy provisions, product mix and other factors are analyzed using actuarial reserve development techniques. Weighing all of the factors, the management team determines a single or "point" estimate that it records as its best estimate of the ultimate liability. Ranges of loss reserves are not developed by Company actuaries. This reserve analysis and review is completed each quarter and for almost every line of business.

Each quarterly review includes in-depth analysis of over 400 subdivisions of the business, employing multiple actuarial techniques. For each subdivision, actuaries use informed, professional judgment to adjust these techniques as necessary to respond to specific conditions in the data or within the business.

Some of the standard actuarial methods employed for the quarterly reserve analysis may include (but may not be limited to):

- Case Incurred Development Method
- Paid Development Method
- Projected Claim Count Times Projected Claim Severity
- Bornhuetter-Ferguson Method
- Incremental Paid LAE to Paid Loss Methods

Management believes that each method has particular strengths and weaknesses and that no single estimation method is most accurate in all situations. When applied to a particular group of claims, the relative strengths and weaknesses of each method can change over time based on the facts and circumstances. Ultimately, the estimation methods chosen are those which management believes produce the most reliable indication for the particular liabilities under review.

The period of time from the occurrence of a loss through the settlement of the liability is referred to as the "tail". Generally, the same actuarial methods are considered for both short-tail and long-tail lines of business because most of them work properly for both. The methods are designed to incorporate the effects of the differing length of time to settle particular claims. For short-tail

lines, management tends to give more weight to the Case Incurred and Paid Development methods, although the various methods tend to produce similar results. For long-tail lines, more judgment is involved, and more weight may be given to the Bornhuetter-Ferguson method. Liability claims for long-tail lines are more susceptible to litigation and can be significantly affected by changing contract interpretation and the legal environment. Therefore, the estimation of loss reserves for these classes is more complex and subject to a higher degree of variability.

The level of detail in which data is analyzed varies among the different lines of business. Data is generally analyzed by major product or by coverage within product, using countrywide data; however, in some situations, data may be reviewed by state for a few large volume states. Appropriate segmentation of the data is determined based on data volume, data credibility, mix of business, and other actuarial considerations.

Supplementary statistical information is also reviewed to determine which methods are most appropriate to use or if adjustments are needed to particular methods. Such information includes:

- Open and closed claim counts
- Average case reserves and average incurred on open claims
- Closure rates and statistics related to closed and open claim percentages
- Average closed claim severity
- Ultimate claim severity
- Reported loss ratios
- Projected ultimate loss ratios
- Loss payment patterns

Within each line, results of individual methods are reviewed, supplementary statistical information is analyzed, and all data from underwriting, operating and claim management are considered in deriving management’s best estimate of the ultimate liability. This estimate may be the result of one method, a weighted average of several methods, or a judgmental selection as the management team determines is appropriate.

The following table shows (in millions) the breakdown of AFG’s property and casualty reserves between case reserves, IBNR reserves and LAE reserves (estimated amounts required to adjust, record and settle claims, other than the claim payments themselves).

	Gross Loss Reserves at December 31, 2013			
	Case	IBNR	LAE	Total Reserve
Statutory Line of Business				
Other liability — occurrence	$ 407	$ 1,270	$ 274	$ 1,951
Workers’ compensation	711	415	143	1,269
Special property (fire, allied lines, inland marine, earthquake)	402	76	24	502
Other liability — claims made	186	245	64	495
Commercial auto/truck liability/medical	189	212	80	481
Commercial multi-peril	157	85	80	322
Other lines	182	379	163	724
Total Statutory Reserves	2,234	2,682	828	5,744
Adjustments for GAAP:				
Reserves of foreign operations	297	318	11	626
Deferred gains on retroactive reinsurance	—	56	—	56
Loss reserve discounting	(13)	—	—	(13)
Other	(3)	—	—	(3)
Total Adjustments for GAAP	281	374	11	666
Total GAAP Reserves	$ 2,515	$ 3,056	$ 839	$ 6,410

While current factors and reasonably likely changes in variable factors are considered in estimating the liability for unpaid losses, there is no method or system that can eliminate the risk of actual ultimate results differing from such estimates. As shown in footnote (a) to the reserve development table (loss triangle) on page 7, the original estimates of AFG’s liability for losses and loss adjustment expenses, net of reinsurance and excluding the effect of special charges for asbestos and environmental exposures, over the past 10 years have developed through December 31, 2013, to be deficient (for one year) by

8.8% and redundant (for nine years) by as much as 18.6%. This development illustrates the historical impact caused by variability in factors considered in estimating insurance reserves.

Following is a discussion of certain critical variables affecting the estimation of loss reserves of the more significant long-tail lines of business (asbestos and environmental liabilities are separately discussed below). Many other variables may also impact ultimate claim costs.

An important assumption underlying reserve estimates is that the cost trends implicitly built into development patterns will continue into the future. However, future results could vary due to an unexpected change in the underlying cost trends. This unexpected change could arise from a variety of sources including a general increase in economic inflation, inflation from social programs, new medical technologies, or other factors such as those listed below in connection with AFG's largest lines of business. It is not possible to isolate and measure the potential impact of just one of these variables, and future cost trends could be partially impacted by several such variables. However, it is reasonable to address the sensitivity of the reserves to potential impact from changes in these variables by measuring the effect of a possible overall 1% change in future cost trends that may be caused by one or more variables. Utilizing the effect of a 1% change in overall cost trends enables changes greater than 1% to be estimated by extrapolation. Each additional 1% change in the cost trend would increase the effect on net earnings by an amount slightly (about 5%) greater than the effect of the previous 1%. For example, if a 1% change in cost trends in a line of business would change net earnings by $20 million, a 2% change would change net earnings by approximately $41 million.

The estimated cumulative impact that a 1% change in cost trends would have on net earnings is shown below (in millions).

Line of business	Effect of 1% Change in Cost Trends
Other liability — occurrence	$ 21
Workers' compensation	26
Other liability — claims made	9
Commercial auto/truck liability/medical	6
Commercial multi-peril	3

The judgments and uncertainties surrounding management's reserve estimation process and the potential for reasonably possible variability in management's most recent reserve estimates may also be viewed by looking at how recent historical estimates of reserves have developed. The following table shows (dollars in millions) what the impact on AFG's net earnings would be on the more significant lines of business if the December 31, 2013, reserves (net of reinsurance) developed at the same rate as the average development of the most recent five years.

	5-yr. Average Development (*)	Net Reserves (**) December 31, 2013	Effect on Net Earnings (**)
Other liability — occurrence	(4.3%)	$ 747	$ 32
Workers' compensation	(0.2%)	926	2
Other liability — claims made	(7.2%)	373	27
Commercial auto/truck liability/ medical	(0.1%)	364	—
Commercial multi-peril	4.4%	175	(8)

(*) Adverse (favorable), net of tax effect.
(**) Excludes asbestos and environmental liabilities.

The following discussion describes key assumptions and important variables that affect the estimate of the reserve for loss and loss adjustment expenses of the more significant lines of business and explains what caused them to change from assumptions used in the preceding period.

Other Liability — Occurrence

This long-tail line of business consists of coverages protecting the insured against legal liability resulting from negligence, carelessness, or a failure to act causing property damage or personal injury to others. Some of the important variables affecting estimation of loss reserves for other liability — occurrence include:

- Litigious climate
- Unpredictability of judicial decisions regarding coverage issues
- Magnitude of jury awards
- Outside counsel costs
- Timing of claims reporting

AFG recorded favorable reserve development of $11 million in 2013, $43 million in 2012 and $50 million in 2011 related to its other liability — occurrence coverage where both the frequency and severity of claims were lower than previously projected.

During 2012, AFG recorded $28 million of favorable reserve development on claims related to the use of Chinese drywall in residential construction in prior years. Much of the uncertainty in estimating the potential exposure and possible liabilities for such claims was clarified during 2012 by favorable judicial decisions and the announcements of settlements of class action lawsuits making the potential liabilities better defined and more effectively anticipated.

While management applies the actuarial methods mentioned above, more judgment is involved in arriving at the final reserve to be held. For recent accident years, more weight is given to the Bornhuetter-Ferguson method.

Workers' Compensation

This long-tail line of business provides coverage to employees who may be injured in the course of employment. Some of the important variables affecting estimation of loss reserves for workers' compensation include:

- Legislative actions and regulatory and legal interpretations
- Future medical cost inflation
- Economic conditions
- Timing of claims reporting

Approximately 44% of AFG's workers compensation business is currently written in California. Over the last 11 years, there have been numerous reforms, revisions and interpretations of regulations. Reforms in 2003 and 2004 tended to reduce costs and benefits. During the economic downturn, these trends were reversed and costs began to increase, causing results to differ from expectations. In recent years, AFG has experienced an improved pricing environment leading to improved results for this business. At this time, there is uncertainty around the impact of California Senate Bill 863, which was passed in August 2012. The legislation has led to increased benefits for injured workers, while cost-saving efficiencies have yet to be implemented. Such frequent, significant changes in the operating environment make it difficult to appropriately price these insurance policies and estimate related liabilities.

AFG's subsidiary that writes workers' compensation business in California recorded favorable reserve development of $7 million in 2013 compared to less than $1 million in 2012 and $5 million in 2011.

Other Liability — Claims Made

This long-tail line of business consists mostly of directors' and officers' liability ("D&O"). Some of the important variables affecting estimation of loss reserves for other liability — claims made include:

- Litigious climate
- Economic conditions
- Variability of stock prices
- Magnitude of jury awards

The general state of the economy and the variability of the stock price of the insured can affect the frequency and severity of shareholder class action suits and other situations that trigger coverage under D&O policies. From 2008 to 2010, economic

conditions led to higher frequency and severity of claims, particularly in the D&O policies for small account and not-for-profit organizations. Recently, claim frequency has decreased from its peak in 2010.

AFG recorded favorable prior year loss development of $41 million in 2013, $16 million in 2012 and $66 million in 2011 on its D&O business as claim severity was less than expected across several prior accident years.

AFG's legal professional liability business has been in run-off since 2008 with only 41 claims remaining open at December 31, 2013. These claims are expected to settle within the existing reserves. AFG recorded favorable reserve development of $2 million in 2013 compared to less than $1 million in 2012 and $17 million in 2011 on the run-off legal and professional liability business.

While management applies the actuarial methods mentioned above, more judgment may be needed to determine appropriate reserves due to the complexity of claims, litigation and the length of time necessary to determine exposure.

Commercial Auto/Truck Liability/Medical

This line of business is a mix of coverage protecting the insured against legal liability for property damage or personal injury to others arising from the operation of commercial motor vehicles. The property damage liability exposure is usually short-tail with relatively quick reporting and settlement of claims. The bodily injury and medical payments exposures are longer-tailed; although the claim reporting is relatively quick, the final settlement can take longer to achieve. Some of the important variables affecting estimation of loss reserves for commercial auto/truck liability/medical are similar to other liability — occurrence and include:

- Magnitude of jury awards
- Unpredictability of judicial decisions regarding coverage issues
- Litigious climate and trends
- Change in frequency of severe accidents
- Health care costs and utilization of medical services by injured parties

AFG recorded adverse prior year reserve development of $37 million in 2013 and $1 million in 2012 for this line of business as claim severity was significantly higher than expected, particularly from accident years 2010 to 2012. AFG recorded favorable prior year loss development of $8 million in 2011 as claim severity was lower than in prior assumptions.

Commercial Multi-Peril

This long-tail line of business consists of two or more coverages protecting the insured from various property and liability risk exposures. The commercial multi-peril line of business includes coverage similar to other liability — occurrence, so in general, variables affecting estimation of loss reserves for commercial multi-peril include those mentioned above for other liability —occurrence. In addition, this line includes reserves for a run-off book of homebuilders' business covering contractors' liability for construction defects. Variables important to estimating the liabilities for this coverage include:

- Changing legal/regulatory interpretations of coverage
- Statutes of limitations and statutes of repose in filing claims
- Changes in policy forms and endorsements

AFG recorded adverse prior year reserve development of less than $1 million in 2013, $35 million in 2012 and $13 million in 2011 on this line of business. The adverse development resulted from higher claim frequency and severity in a block of program business related to motel/hotel, apartments, restaurants, taverns and recreation. This adverse development more than offset favorable development in coverage for non-profit organizations of $4 million in 2013, $6 million in 2012 and $6 million in 2011 as claim severity was less than anticipated.

Reserves of Foreign Operations

Reserves of foreign operations relate primarily to the operations of Marketform Group, Limited, AFG's wholly-owned United Kingdom-based Lloyd's insurer. Historically, the largest line of business written by Marketform has been non-U.S. medical malpractice, which provides coverage for injuries and damages caused by medical care providers, including but not limited to, hospitals and their physicians. Although Marketform offers this product in approximately 30 countries, the majority of the business has been written in the United Kingdom, Australia and Italy. Significant variables in estimating the loss reserves for the medical malpractice business include:

- Litigious environment
- Magnitude of court awards
- A slow moving judicial system including varying approaches to medical malpractice claims among courts in different regions of Italy
- Third party claims administration in Italy
- Trends in claim costs, including medical cost inflation and, in Italy, escalating tables used to establish damages for personal injury

Marketform recorded adverse prior year reserve development of $1 million in 2013, $10 million in 2012 and $44 million in 2011. Development in 2012 and 2011 related primarily to Italian public hospital medical malpractice business, which Marketform ceased writing in 2008. The development resulted from significant issues related to third party administration of claims and a challenging legal environment in Italy. Management believes that current reserves, which represent its best estimate of future liabilities, are adequate. Nonetheless, it concluded that sufficient uncertainty exists with respect to Italian public hospital medical malpractice reserves to leave open the 2007 year of account, in accordance with Lloyd's provisions until a larger percentage of claims have been paid and the ultimate liabilities can be estimated with greater certainty.

Traditional actuarial techniques are not applicable to the Italian public hospital medical malpractice business due to the significant changes in this account over time. Accordingly, more detailed methods are used, including claim count development times average severity, and uplifting case reserves to historical severity levels.

Recoverables from Reinsurers and Availability of Reinsurance AFG is subject to credit risk with respect to its reinsurers, as reinsurance contracts do not relieve AFG of its liability to policyholders. To mitigate this risk, substantially all reinsurance is ceded to companies with investment grade S&P ratings or is secured by "funds withheld" or other collateral.

The availability and cost of reinsurance are subject to prevailing market conditions, which are beyond AFG's control and which may affect AFG's level of business and profitability. Although the cost of certain reinsurance programs may increase, management believes that AFG will be able to maintain adequate reinsurance coverage at acceptable rates without a material adverse effect on AFG's results of operations. AFG's gross and net combined ratios are shown in the table below.

See *Item 1 — Business — "Property and Casualty Insurance Segment — Reinsurance"* for more information on AFG's reinsurance programs. For additional information on the effect of reinsurance on AFG's historical results of operations see *Note O — "Insurance — Reinsurance"* to the financial statements and the gross loss development table under *Item 1 — Business — "Property and Casualty Insurance Segment — Loss and Loss Adjustment Expense Reserves."*

The following table illustrates the effect that purchasing property and casualty reinsurance has had on AFG's combined ratio over the last three years.

	2013	2012	2011
Before reinsurance (gross)	93.3%	108.7 %	89.0%
Effect of reinsurance	2.2%	(11.8%)	4.4%
Actual (net of reinsurance)	95.5%	96.9 %	93.4%

Outside of its property and casualty operations, AFG has reinsurance recoverables totaling $953 million, including $586 million from Hannover Life Reassurance Company of America (rated A+ by A.M. Best) and $200 million from Loyal American Life Insurance Company, a subsidiary of Cigna (rated A- by A.M. Best). This reinsurance is related primarily to the reinsurance of certain benefits in AFG's run-off long-term care and life operations and the August 2012 sale of its Medicare supplement and critical illness businesses.

Asbestos and Environmental-related ("A&E") Insurance Reserves Asbestos and environmental reserves of the property and casualty group consisted of the following (in millions):

	December 31,	
	2013	2012
Asbestos	$ 210	$ 305
Environmental	91	68
A&E reserves, net of reinsurance recoverable	301	373
Reinsurance recoverable, net of allowance	83	98
Gross A&E reserves	$ 384	$ 471

Asbestos reserves include claims asserting alleged injuries and damages from exposure to asbestos. Environmental reserves include claims relating to polluted waste sites.

Asbestos claims against manufacturers, distributors or installers of asbestos products were presented under the products liability section of their policies which typically had aggregate limits that capped an insurer's liability. In recent years, a number of asbestos claims are being presented as "non-products" claims, such as those by installers of asbestos products and by property owners or operators who allegedly had asbestos on their property, under the premises or operations section of their policies. Unlike products exposures, these non-products exposures typically had no aggregate limits, creating potentially greater exposure for insurers. Further, in an effort to seek additional insurance coverage, some insureds with installation activities who have substantially eroded their products coverage are presenting new asbestos claims as non-products operations claims or attempting to reclassify previously settled products claims as non-products claims to restore a portion of previously exhausted products aggregate limits. AFG, along with other insurers, is and will be subject to such non-products claims. It is difficult to predict whether insureds will be successful in asserting claims under non-products coverage or whether AFG and other insurers will be successful in asserting additional defenses. Therefore, the future impact of such efforts is uncertain.

Approximately 39% of AFG's net asbestos reserves relate to policies written directly by AFG subsidiaries. Claims from these policies generally are product oriented claims with only a limited amount of non-products exposures, and are dominated by small to mid-sized commercial entities that are mostly regional policyholders with few national target defendants. The remainder is assumed reinsurance business that includes exposures for the periods 1954 to 1983. The asbestos and environmental assumed claims are ceded by various insurance companies under reinsurance treaties. A majority of the individual assumed claims have exposures of less than $100,000 to AFG. Asbestos losses assumed include some of the industry known manufacturers, distributors and installers. Pollution losses include industry known insured names and sites.

Establishing reserves for A&E claims relating to policies and participations in reinsurance treaties and former operations is subject to uncertainties that are significantly greater than those presented by other types of claims. For this group of claims, traditional actuarial techniques that rely on historical loss development trends cannot be used and a range of reasonably possible losses cannot be estimated. Case reserves and expense reserves are established by the claims department as specific policies are identified. In addition to the case reserves established for known claims, management establishes additional reserves for claims not yet known or reported and for possible development on known claims. These additional reserves are management's best estimate based on periodic comprehensive studies and internal reviews adjusted for payments and identifiable changes, supplemented by management's review of industry information about such claims, with due consideration to individual claim situations.

Management believes that estimating the ultimate liability for asbestos claims presents a unique and difficult challenge to the insurance industry due to, among other things, inconsistent court decisions, an increase in bankruptcy filings as a result of asbestos-related liabilities, novel theories of coverage, and judicial interpretations that often expand theories of recovery and broaden the scope of coverage. The casualty insurance industry is engaged in extensive litigation over these coverage and liability issues as the volume and severity of claims against asbestos defendants continue to increase. Environmental claims likewise present challenges in prediction, due to uncertainty regarding the interpretation of insurance policies, complexities regarding multi-party involvements at sites, evolving cleanup standards and protracted time periods required to assess the level of cleanup required at contaminated sites.

The following factors could impact AFG's reserves and payments:

- There is a growing interest at the state level to attempt to legislatively address asbestos liabilities and the manner in which asbestos claims are resolved. These developments are fluid and could result in piecemeal state-by-state solutions.
- The manner by which bankruptcy courts are addressing asbestos liabilities is in flux.
- AFG's insureds may make claims alleging significant non-products exposures.

While management believes that AFG's reserves for A&E claims are a reasonable estimate of ultimate liability for such claims, actual results may vary materially from the amounts currently recorded due to the difficulty in predicting the number of future claims, the impact of recent bankruptcy filings, and unresolved issues such as whether coverage exists, whether policies are subject to aggregate limits on coverage, how claims are to be allocated among triggered policies and implicated years, and whether claimants who exhibit no signs of illness will be successful in pursuing their claims. A 1% variation in loss cost trends, caused by any of the factors previously described, would change net income by approximately $15 million.

AFG tracks its A&E claims by policyholder. The following table shows, by type of claim, the number of policyholders that did not receive any payments in the calendar year separate from policyholders that did receive a payment. Policyholder counts represent policies written by AFG subsidiaries and do not include assumed reinsurance.

	2013	2012	2011
Number of policyholders with no indemnity payments:			
Asbestos	142	129	113
Environmental	116	97	98
	258	226	211
Number of policyholders with indemnity payments:			
Asbestos	48	54	58
Environmental	24	21	26
	72	75	84
Total	330	301	295

Amounts paid (net of reinsurance recoveries) for asbestos and environmental claims, including loss adjustment expenses, were as follows (in millions):

	2013	2012	2011
Asbestos	$ 116	$ 15	$ 13
Environmental	15	17	17
Total	$ 131	$ 32	$ 30

Asbestos claims paid in 2013 include payments totaling $106 million associated with the settlement of A.P. Green Industries and another large claim. Substantially all of the settlement amounts had been accrued for in prior years. The survival ratio is a measure often used by industry analysts to compare A&E reserves strength among companies. This ratio is typically calculated by dividing reserves for A&E exposures by the three year average of paid losses, and therefore measures the number of years that it would take to pay off current reserves based on recent average payments. Because this ratio can be significantly impacted by a number of factors such as loss payout variability, caution should be exercised in attempting to determine reserve adequacy based simply on the survival ratio. At December 31, 2013, the property and casualty insurance segment's three year survival ratios, excluding amounts associated with the settlements of A.P. Green Industries and another large claim, were 16.6 times paid losses for the asbestos reserves, 5.7 times paid losses for environmental reserves and 10.5 times paid losses for total A&E reserves. Overall, these ratios compare favorably with data published by A.M. Best in October 2013, which indicate that industry survival ratios were 10.0 for asbestos, 5.8 for environmental, and 8.8 for total A&E reserves at December 31, 2012.

AFG has periodically conducted comprehensive external studies of its asbestos and environmental exposures relating to the run-off operations of its property and casualty insurance segment and exposures related to its former railroad and manufacturing operations with the aid of specialty actuarial, engineering and consulting firms and outside counsel, generally every two years, with an in-depth internal review during the intervening years.

As a result of the comprehensive external study completed in the third quarter of 2013, AFG's property and casualty insurance segment recorded a $54 million pretax special charge to increase its asbestos reserves by $16 million (net of reinsurance) and its environmental reserves by $38 million (net of reinsurance). The increase in the property and casualty segment's asbestos reserves was driven primarily by slightly higher than expected loss experience, higher defense costs and some increased claim

severity. As the overall industry exposure to asbestos has matured, the focus of litigation has shifted to smaller companies and companies with ancillary exposures. AFG’s insureds with these exposures have been the driver of the property and casualty segment’s asbestos reserve increases. The increase in property and casualty environmental reserves was attributed primarily to a small number of claims where the estimated costs of remediation have increased. There were no newly identified or emerging broad industry trends that were identified in this study.

An in-depth internal review of AFG’s A&E reserves was completed in the third quarter of 2012 by AFG’s internal A&E claims specialists and actuaries in consultation with specialty outside counsel and an outside consultant. As a result of the review, AFG recorded a $31 million pretax special charge to increase the property and casualty segment’s asbestos reserves by $19 million (net of reinsurance) and its environmental reserves by $12 million (net of reinsurance). The charge relates primarily to an increase in environmental investigative costs and related loss adjustment expenses.

As a result of the comprehensive external study completed in 2011, AFG recorded a $50 million pretax special charge to increase its property and casualty group’s asbestos reserves by $28 million (net of reinsurance) and its environmental reserves by $22 million (net of reinsurance). The property and casualty group’s asbestos reserves increase related primarily to exposures on business assumed from other insurers resulting from an increase in anticipated aggregate exposures in several large settlements involving several insurers in which AFG has a small proportional share. Asbestos reserves related to the property and casualty group’s direct asbestos exposures were increased to reflect higher frequency and severity of mesothelioma and other cancer claims as well as increased defense costs on many of these claims. The increase in the property and casualty group’s environmental reserves was attributed primarily to a small number of increases on specific environmental claims at several sites.

Run-off Long-term Care Insurance AFG, as well as other companies that sell long-term care products, have accumulated relatively limited claims, lapse and mortality experience, making it difficult to predict future claims. Long-term care claims tend to be much higher in dollar amount and longer in duration than other health care products. In addition, long-term care claims are incurred much later in the life of a policy than most other health products. These factors made it difficult to appropriately price this product and were instrumental in AFG’s decision to stop writing new policies in January 2010. AFG’s outstanding long-term care policies have level premiums and are guaranteed renewable. Premium rates can potentially be increased in reaction to adverse experience; however, any rate increases would require regulatory approval.

Reserves for future policy benefits under long-term care policies are established (and related acquisition costs are amortized) over the life of the policies based on policy benefit assumptions as of the date of issuance, including investment yields, mortality, morbidity, persistency and expenses. Once these assumptions are established for a given policy or group of policies, they are not changed over the life of the policy unless a loss recognition event (premium deficiency) occurs. Loss recognition occurs when, based on current expectations as of the measurement date, the existing contract liabilities plus the present value of future premiums (including reasonably expected rate increases), are not expected to cover the present value of future claims payments, related settlement and maintenance costs, and unamortized acquisition costs. In performing loss recognition testing on the closed block of long-term care business, AFG estimates future claims, persistency, expenses, investment performance, and reinvestment rates, among other assumptions.

At December 31, 2012, loss recognition testing assumptions for claim costs, expenses and persistency were updated based on the results of AFG's periodic internal analysis of claim experience, including the impact of supplemental data from an external actuarial study that used a large, uniform database of industry experience. Ultimate voluntary lapse rates for most in-force business range from 0.5% to 2.5%, varying by policy form, marital status, and the presence of inflation protection. Projected reinvestment rates are based on assumptions about future treasury rates, investment spreads and the types and duration of future investments. In aggregate, net reinvestment rates (net of expense and default assumptions) in the 2012 loss recognition testing were estimated at 4.54% for 2013, and projected to increase gradually to 6.00% in 2023. After 2023, reinvestment rates were projected to be relatively flat. As a result of the updated assumptions discussed above, AFG recorded a $153 million pretax loss recognition charge in the fourth quarter of 2012 to write off all of the remaining deferred policy acquisition costs and strengthen reserves in this business. As part of the loss recognition charge, policy benefit assumptions were reset to the 2012 assumptions and will not be changed again unless a future loss recognition event occurs.

At December 31, 2013, the most significant loss recognition testing assumption update was to projected reinvestment rates. Due to higher than anticipated increases in interest rates, net reinvestment rates (net of expense and default assumptions) were estimated at 5.01% for 2014 and projected to increase gradually to 6.25% in 2022. After 2022, reinvestment rates were projected to be relatively flat. As a result of the updated assumptions, the existing contract liabilities plus the present value of future premiums (including reasonably expected rate increases) exceeded the present value of future claims payments and related settlement and maintenance costs by approximately $64 million (a loss recognition margin). As a result, no additional

loss recognition charges were recorded and the assumptions used to establish reserves for future policy benefits from the 2012 loss recognition charge continue to be used.

Although management believes that its loss recognition assumptions at December 31, 2013, are reasonable, actual results will depend on how well future experience conforms to these assumptions, including the level and type of claim activity, persistency, expected rate increase approvals, and reinvestment rates. The relationship among these assumptions is complex, with deviations in one assumption often influencing the outcome of others. External factors, including, but not limited to changes in the regulatory and judicial environment, along with medical advancements and innovation in long-term care delivery systems, could have a material impact on the ultimate performance of this closed block of business. The loss recognition charge recorded in 2012 did not include any margin for adverse deviation in the reserve assumptions (in accordance with accounting guidance).

The following table (in millions) illustrates the impact on the loss recognition margin of adverse changes in key loss recognition assumptions. Once the loss recognition margin (approximately $64 million at December 31, 2013) is reduced to zero, the impact of adverse changes in assumptions, unless offset by other favorable assumption changes, would be recorded as an increase in long-term care reserves through a charge to earnings. The result of each assumption change represents a reduction in the loss recognition margin that would result from using the more adverse assumption. Each item reflects a change to a single assumption without changes to other assumptions. For example, assuming increased claim payments did not change the assumption on future rate increases and persistency, nor did it change projected investment yields resulting from cash flow differences. These amounts are valid for a point in time, and will change in future periods as the in-force block ages, and as actual performance deviates from the assumptions used at December 31, 2013.

Assumption Change	Reduction in Loss Recognition Margin (pretax)
5% higher morbidity in all future years	$50 — $60
5% lower lapse and mortality rates in all future years	$30 — $35
25 bps lower reinvestment rates in all future years	$20 — $25
Every expected rate increase approval is 1% lower	$15 — $20

Conversely, favorable changes in the assumptions above would increase the loss recognition margin. For example, the increase in the loss recognition margin that occurred in 2013 resulted primarily from an increase in projected reinvestment rates.

Contingencies related to Subsidiaries' Former Operations The A&E studies and reviews discussed above encompassed reserves for various environmental and occupational injury and disease claims and other contingencies arising out of the railroad operations disposed of by American Premier's predecessor and certain manufacturing operations disposed of by American Premier and its subsidiaries and by Great American Financial Resources, Inc. Charges resulting from the A&E studies and review were $22 million in 2013, and less than $10 million in 2012 and 2011. For a discussion of the $22 million charge recorded for those operations in 2013, see *"Holding Company, Other and Unallocated — Results of Operations."* In the third quarter of 2012, AFG recorded a pretax charge of $15 million for an adverse judgment received in a long-standing labor dispute involving American Premier's former railroad employees, the likelihood of which was previously considered to be remote. Liabilities for claims and contingencies arising from these former railroad and manufacturing operations totaled $96 million at December 31, 2013. For a discussion of the uncertainties in determining the ultimate liability, see *Note M — "Contingencies"* to the financial statements.

MANAGED INVESTMENT ENTITIES

Accounting standards require AFG to consolidate its investments in collateralized loan obligation ("CLO") entities that it manages and owns an interest in (in the form of debt). See *Note A — "Accounting Policies — Managed Investment Entities"* and *Note H — "Managed Investment Entities"* to the financial statements. The effect of consolidating these entities is shown in the tables below (in millions). The "Before CLO Consolidation" columns include AFG's investment and earnings in the CLOs on an unconsolidated basis.

CONDENSED CONSOLIDATING BALANCE SHEET

	Before CLO Consolidation	Managed Investment Entities	Consol. Entries		Consolidated As Reported
December 31, 2013					
Assets:					
Cash and investments	$ 31,584	$ —	$ (271)	(a)	$ 31,313
Assets of managed investment entities	—	2,888	—		2,888
Other assets	7,887	—	(1)	(a)	7,886
Total assets	$ 39,471	$ 2,888	$ (272)		$ 42,087
Liabilities:					
Unpaid losses and loss adjustment expenses and unearned premiums	$ 8,167	$ —	$ —		$ 8,167
Annuity, life, accident and health benefits and reserves	22,952	—	—		22,952
Liabilities of managed investment entities	—	2,839	(272)	(a)	2,567
Long-term debt and other liabilities	3,632	—	—		3,632
Total liabilities	34,751	2,839	(272)		37,318
Shareholders’ equity:					
Common Stock and Capital surplus	1,213	—	—		1,213
Retained earnings:					
Appropriated — managed investment entities	—	49	—		49
Unappropriated	2,777	—	—		2,777
Accumulated other comprehensive income, net of tax	560	—	—		560
Total shareholders’ equity	4,550	49	—		4,599
Noncontrolling interests	170	—	—		170
Total equity	4,720	49	—		4,769
Total liabilities and equity	$ 39,471	$ 2,888	$ (272)		$ 42,087
December 31, 2012					
Assets:					
Cash and investments	$ 28,706	$ —	$ (257)	(a)	$ 28,449
Assets of managed investment entities	—	3,225	—		3,225
Other assets	7,498	—	(1)	(a)	7,497
Total assets	$ 36,204	$ 3,225	$ (258)		$ 39,171
Liabilities:					
Unpaid losses and loss adjustment expenses and unearned premiums	$ 8,496	$ —	$ —		$ 8,496
Annuity, life, accident and health benefits and reserves	19,668	—	—		19,668
Liabilities of managed investment entities	—	3,130	(238)	(a)	2,892
Long-term debt and other liabilities	3,367	—	—		3,367
Total liabilities	31,531	3,130	(238)		34,423
Shareholders’ equity:					
Common Stock and Capital surplus	1,152	20	(20)		1,152
Retained earnings:					
Appropriated — managed investment entities	—	75	—		75
Unappropriated	2,520	—	—		2,520
Accumulated other comprehensive income, net of tax	831	—	—		831
Total shareholders’ equity	4,503	95	(20)		4,578
Noncontrolling interests	170	—	—		170
Total equity	4,673	95	(20)		4,748
Total liabilities and equity	$ 36,204	$ 3,225	$ (258)		$ 39,171

(a) Elimination of the fair value of AFG’s investment in CLOs and related accrued interest.

CONDENSED CONSOLIDATING STATEMENT OF EARNINGS

	Before CLO Consolidation (a)	Managed Investment Entities	Consol. Entries		Consolidated As Reported
Three months ended December 31, 2013					
Revenues:					
Insurance net earned premiums	$ 886	$ —	$ —		$ 886
Net investment income	358	—	(8)	(b)	350
Realized gains on securities	67	—	—		67
Realized losses on subsidiaries	(4)	—	—		(4)
Income (loss) of managed investment entities:					
Investment income	—	30	—		30
Gain (loss) on change in fair value of assets/liabilities	—	6	1	(b)	7
Other income	30	—	(4)	(c)	26
Total revenues	1,337	36	(11)		1,362
Costs and Expenses:					
Insurance benefits and expenses	1,000	—	—		1,000
Expenses of managed investment entities	—	31	(10)	(b)(c)	21
Interest charges on borrowed money and other expenses	95	—	—		95
Total costs and expenses	1,095	31	(10)		1,116
Earnings before income taxes	242	5	(1)		246
Provision for income taxes	81	—	—		81
Net earnings, including noncontrolling interests	161	5	(1)		165
Less: Net earnings (loss) attributable to noncontrolling interests	3	—	4	(d)	7
Net earnings attributable to shareholders	$ 158	$ 5	$ (5)		$ 158
Three months ended December 31, 2012					
Revenues:					
Insurance net earned premiums	$ 784	$ —	$ —		$ 784
Net investment income	339	—	(10)	(b)	329
Realized gains on securities	65	—	—		65
Realized gains on subsidiaries	6	—	—		6
Income (loss) of managed investment entities:					
Investment income	—	33	—		33
Gain (loss) on change in fair value of assets/liabilities	—	(35)	4	(b)	(31)
Other income	26	—	(4)	(c)	22
Total revenues	1,220	(2)	(10)		1,208
Costs and Expenses:					
Insurance benefits and expenses	1,132	—	—		1,132
Expenses of managed investment entities	—	32	(10)	(b)(c)	22
Interest charges on borrowed money and other expenses	84	—	—		84
Total costs and expenses	1,216	32	(10)		1,238
Earnings (loss) before income taxes	4	(34)	—		(30)
Provision (benefit) for income taxes	(49)	—	—		(49)
Net earnings, including noncontrolling interests	53	(34)	—		19
Less: Net earnings (loss) attributable to noncontrolling interests	3	—	(34)	(d)	(31)
Net earnings attributable to shareholders	$ 50	$ (34)	$ 34		$ 50

(a) Includes $8 million and $10 million in 2013 and 2012, respectively, in net investment income representing the change in fair value of AFG’s CLO investments plus $4 million in each period in CLO management fees earned.

(b) Elimination of the change in fair value of AFG’s investments in the CLOs, including $6 million in each period in distributions recorded as interest expense by the CLOs.

(c) Elimination of management fees earned by AFG.

(d) Allocate losses of CLOs attributable to other debt holders to noncontrolling interests.

CONDENSED CONSOLIDATING STATEMENT OF EARNINGS - CONTINUED

	Before CLO Consolidation (a)	Managed Investment Entities	Consol. Entries		Consolidated As Reported
Year ended December 31, 2013					
Revenues:					
Insurance net earned premiums	$ 3,318	$ —	$ —		$ 3,318
Net investment income	1,381	—	(35)	(b)	1,346
Realized gains on securities	221	—	—		221
Realized losses on subsidiaries	(4)	—	—		(4)
Income (loss) of managed investment entities:					
Investment income	—	128	—		128
Gain (loss) on change in fair value of assets/liabilities	—	(19)	5	(b)	(14)
Other income	113	—	(16)	(c)	97
Total revenues	5,029	109	(46)		5,092
Costs and Expenses:					
Insurance benefits and expenses	3,917	—	—		3,917
Expenses of managed investment entities	—	130	(41)	(b)(c)	89
Interest charges on borrowed money and other expenses	397	—	—		397
Total costs and expenses	4,314	130	(41)		4,403
Earnings before income taxes	715	(21)	(5)		689
Provision for income taxes	236	—	—		236
Net earnings, including noncontrolling interests	479	(21)	(5)		453
Less: Net earnings (loss) attributable to noncontrolling interests	8	—	(26)	(d)	(18)
Net earnings attributable to shareholders	$ 471	$ (21)	$ 21		$ 471
Year ended December 31, 2012					
Revenues:					
Insurance net earned premiums	$ 3,165	$ —	$ —		$ 3,165
Net investment income	1,332	—	(31)	(b)	1,301
Realized gains on securities	210	—	—		210
Realized gains on subsidiaries	161	—	—		161
Income (loss) of managed investment entities:					
Investment income	—	125	—		125
Gain (loss) on change in fair value of assets/liabilities	—	(107)	13	(b)	(94)
Other income	107	—	(18)	(c)	89
Total revenues	4,975	18	(36)		4,957
Costs and Expenses:					
Insurance benefits and expenses	3,939	—	—		3,939
Expenses of managed investment entities	—	116	(36)	(b)(c)	80
Interest charges on borrowed money and other expenses	401	—	—		401
Total costs and expenses	4,340	116	(36)		4,420
Earnings before income taxes	635	(98)	—		537
Provision for income taxes	135	—	—		135
Net earnings, including noncontrolling interests	500	(98)	—		402
Less: Net earnings (loss) attributable to noncontrolling interests	12	—	(98)	(d)	(86)
Net earnings attributable to shareholders	$ 488	$ (98)	$ 98		$ 488

(a) Includes $35 million and $31 million in 2013 and 2012, respectively, in net investment income representing the change in fair value of AFG’s CLO investments plus $16 million and $18 million in 2013 and 2012, respectively, in CLO management fees earned.

(b) Elimination of the change in fair value of AFG’s investments in the CLOs, including $25 million and $18 million in 2013 and 2012, respectively, in distributions recorded as interest expense by the CLOs.

(c) Elimination of management fees earned by AFG.

(d) Allocate losses of CLOs attributable to other debt holders to noncontrolling interests.

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CONDENSED CONSOLIDATING STATEMENT OF EARNINGS - CONTINUED

	Before CLO Consolidation (a)	Managed Investment Entities	Consol. Entries		Consolidated As Reported
Year ended December 31, 2011					
Revenues:					
Insurance net earned premiums	$ 3,189	$ —	$ —		$ 3,189
Net investment income	1,231	—	(6)	(b)	1,225
Realized gains on securities	76	—	—		76
Realized losses on subsidiaries	(3)	—	—		(3)
Income (loss) of managed investment entities:					
Investment income	—	105	—		105
Gain (loss) on change in fair value of assets/liabilities	—	(29)	(4)	(b)	(33)
Other income	103	—	(19)	(c)	84
Total revenues	4,596	76	(29)		4,643
Costs and Expenses:					
Insurance benefits and expenses	3,644	—	—		3,644
Expenses of managed investment entities	—	100	(29)	(b)(c)	71
Interest charges on borrowed money and other expenses	370	—	—		370
Total costs and expenses	4,014	100	(29)		4,085
Earnings before income taxes	582	(24)	—		558
Provision for income taxes	239	—	—		239
Net earnings, including noncontrolling interests	343	(24)	—		319
Less: Net earnings (loss) attributable to noncontrolling interests	1	—	(24)	(d)	(23)
Net earnings attributable to shareholders	$ 342	$ (24)	$ 24		$ 342

(a) Includes $6 million in net investment income representing the change in fair value of AFG's CLO investments plus $19 million in CLO management fees earned.

(b) Elimination of the change in fair value of AFG's investments in the CLOs, including $10 million in distributions recorded as interest expense by the CLOs.

(c) Elimination of management fees earned by AFG.

(d) Allocate losses of CLOs attributable to other debt holders to noncontrolling interests.

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RESULTS OF OPERATIONS

General AFG's net earnings attributable to shareholders, determined in accordance with GAAP, include certain items that may not be indicative of its ongoing core operations. The following table identifies such items and reconciles net earnings attributable to shareholders to core net operating earnings, a non-GAAP financial measure that AFG believes is a useful tool for investors and analysts in analyzing ongoing operating trends (in millions, except per share amounts):

	Three months ended December 31,		Year ended December 31,		
	2013	2012	2013	2012	2011
Core net operating earnings	$ 117	$ 61	$ 385	$ 314	$ 363
Gain on sale of Medicare supplement and critical illness businesses (a)	—	13	—	114	—
Other realized gains (a)	41	36	138	128	45
Long-term care reserve charge (a)	—	(99)	—	(99)	—
Special A&E charges (a)	—	—	(49)	(21)	(38)
Executive Life Insurance Company of New York ("ELNY") guaranty fund assessments (a)	—	—	(3)	—	—
AFG tax case and settlement of open tax years	—	39	—	67	—
Valuation allowance on deferred tax assets (b)	—	—	—	—	(28)
Other (a)	—	—	—	(15)	—
Net earnings attributable to shareholders	$ 158	$ 50	$ 471	$ 488	$ 342
Diluted per share amounts:					
Core net operating earnings	$ 1.28	$ 0.67	$ 4.22	$ 3.27	$ 3.52
Gain on sale of Medicare supplement and critical illness businesses	—	0.15	—	1.19	—
Other realized gains	0.45	0.37	1.52	1.34	0.45
Long-term care reserve charge	—	(1.08)	—	(1.03)	—
Special A&E charges	—	—	(0.54)	(0.22)	(0.37)
ELNY guaranty fund assessments	—	—	(0.04)	—	—
AFG tax case and settlement of open tax years	—	0.43	—	0.70	—
Valuation allowance on deferred tax assets	—	—	—	—	(0.28)
Other	—	—	—	(0.16)	—
Net earnings attributable to shareholders	$ 1.73	$ 0.54	$ 5.16	$ 5.09	$ 3.32

(a) The tax effects of reconciling items are shown below (in millions):

Gain on sale of Medicare supplement and critical illness businesses	$ —	$ (2)	$ —	$ (56)	$ —
Other realized gains	(23)	(19)	(78)	(71)	(27)
Long-term care reserve charge	—	54	—	54	—
Special A&E charges	—	—	27	12	21
ELNY guaranty fund assessments	—	—	2	—	—
Other	—	—	—	8	—

In addition, other realized gains are shown net of noncontrolling interests as follows (in millions):

Noncontrolling interests	$ 1	$ (1)	$ (1)	$ (2)	$ (1)

(b) The valuation allowance is net of $6 million in noncontrolling interest.

Net earnings attributable to shareholders increased $108 million in the fourth quarter of 2013 compared to the same period as 2012 reflecting significantly improved core net operating earnings and the impact of the fourth quarter 2012 long-term care reserve charge offset by the impact of the tax benefit recorded in the fourth quarter of 2012 related to the settlement of open tax years. Core net operating earnings increased $56 million in the fourth quarter of 2013 compared to the fourth quarter of 2012

due to significantly higher profits in the annuity segment and higher underwriting profits in the property and casualty insurance segment.

For the full-year of 2013 compared to 2012, net earnings attributable to shareholders decreased compared to 2012 as higher core net operating earnings were more than offset by the net impact of the following items recorded in 2012: (i) a $114 million after tax gain on the sale of AFG's Medicare supplement and critical illness businesses, (ii) tax benefits of $67 million related to the favorable resolution of certain tax litigation and settlement of open tax years, and (iii) an after tax charge of $99 million to write off deferred acquisition costs and strengthen reserves in the closed block of long-term care insurance. Net earnings attributable to shareholders were also impacted by special A&E charges, which were higher in 2013 compared to 2012. Core net operating earnings increased $71 million in 2013 compared to 2012 reflecting significantly higher profits in both the annuity segment and Specialty property and casualty insurance operations, partially offset by the absence of earnings from the Medicare supplement and critical illness businesses, which were sold in August 2012.

Net earnings attributable to shareholders increased in 2012 compared to 2011 due primarily to the gain on the sale of AFG's Medicare supplement and critical illness businesses, favorable tax benefits and partially offsetting long-term care charge discussed above, as well as higher realized gains on securities. Core net operating earnings decreased in 2012 compared to 2011 as higher earnings in the annuity segment were more than offset by lower underwriting profits and lower investment income in the property and casualty insurance segment.

RESULTS OF OPERATIONS — QUARTERS ENDED DECEMBER 31, 2013 AND 2012

Segmented Statement of Earnings AFG manages its business as five segments: (i) Property and casualty insurance (“P&C”), (ii) Annuity, (iii) Run-off long-term care and life, (iv) Medicare supplement and critical illness (sold in August 2012) and (v) Other, which includes holding company costs and operations attributable to the noncontrolling interests of the managed investment entities (“MIEs”).

AFG's net earnings attributable to shareholders, determined in accordance with GAAP, include certain items that may not be indicative of its ongoing core operations. The following tables for the quarters ended December 31, 2013 and 2012 identify such items by segment and reconcile net earnings attributable to shareholders to core net operating earnings, a non-GAAP financial measure that AFG believes is a useful tool for investors and analysts in analyzing ongoing operating trends (in millions):

				Other				
	P&C	Annuity	Run-off long-term care and life	Consol. MIEs	Holding Co., other and unallocated	Total	Non-core reclass	GAAP Total
Quarter ended December 31, 2013								
Revenues:								
Property and casualty insurance net earned premiums	$ 859	$ —	$ —	$ —	$ —	$ 859	$ —	$ 859
Life, accident and health net earned premiums	—	—	27	—	—	27	—	27
Net investment income	67	270	19	(8)	2	350	—	350
Realized gains on securities	—	—	—	—	—	—	67	67
Realized losses on subsidiaries	—	—	—	—	—	—	(4)	(4)
Income (loss) of MIEs:								
Investment income	—	—	—	30	—	30	—	30
Gain (loss) on change in fair value of assets/liabilities	—	—	—	7	—	7	—	7
Other income	5	21	1	(4)	3	26	—	26
Total revenues	931	291	47	25	5	1,299	63	1,362
Costs and Expenses:								
Property and casualty insurance:								
Losses and loss adjustment expenses	537	—	—	—	—	537	—	537
Commissions and other underwriting expenses	247	—	—	—	—	247	—	247
Annuity benefits	—	137	—	—	—	137	—	137
Life, accident and health benefits	—	—	40	—	—	40	—	40
Annuity and supplemental insurance acquisition expenses	—	35	4	—	—	39	—	39
Interest charges on borrowed money	—	—	—	—	17	17	—	17
Expenses of MIEs	—	—	—	21	—	21	—	21
Other expenses	11	27	6	—	34	78	—	78
Total costs and expenses	795	199	50	21	51	1,116	—	1,116
Earnings before income taxes	136	92	(3)	4	(46)	183	63	246
Provision for income taxes	41	32	(1)	—	(14)	58	23	81
Net earnings, including noncontrolling interests	95	60	(2)	4	(32)	125	40	165
Less: Net earnings (loss) attributable to noncontrolling interests	5	—	—	4	(1)	8	(1)	7
Core Net Operating Earnings	90	60	(2)	—	(31)	117		
Non-core earnings attributable to shareholders (a):								
Realized gains, net of tax	—	—	—	—	41	41	(41)	—
Net Earnings Attributable to Shareholders	$ 90	$ 60	$ (2)	$ —	$ 10	$ 158	$ —	$ 158

	P&C	Annuity	Run-off long-term care and life	Medicare supplement and critical illness	Other: Consol. MIEs	Other: Holding Co., other and unallocated	Total	Non-core reclass	GAAP Total
Quarter ended December 31, 2012									
Revenues:									
Property and casualty insurance net earned premiums	$ 756	$ —	$ —	$ —	$ —	$ —	$ 756	$ —	$ 756
Life, accident and health net earned premiums	—	—	28	—	—	—	28	—	28
Net investment income	69	254	15	—	(10)	1	329	—	329
Realized gains on securities	—	—	—	—	—	—	—	65	65
Realized gains on subsidiaries	—	—	—	—	—	—	—	6	6
Income (loss) of MIEs:									
Investment income	—	—	—	—	33	—	33	—	33
Gain (loss) on change in fair value of assets/liabilities	—	—	—	—	(31)	—	(31)	—	(31)
Other income	7	13	2	—	(4)	4	22	—	22
Total revenues	832	267	45	—	(12)	5	1,137	71	1,208
Costs and Expenses:									
Property and casualty insurance:									
Losses and loss adjustment expenses	556	—	—	—	—	—	556	—	556
Commissions and other underwriting expenses	190	—	—	—	—	—	190	—	190
Annuity benefits	—	124	—	—	—	—	124	—	124
Life, accident and health benefits	—	—	44	—	—	—	44	74	118
Annuity and supplemental insurance acquisition expenses	—	58	7	—	—	—	65	79	144
Interest charges on borrowed money	1	—	—	—	—	17	18	—	18
Expenses of MIEs	—	—	—	—	22	—	22	—	22
Other expenses	13	17	6	—	—	30	66	—	66
Total costs and expenses	760	199	57	—	22	47	1,085	153	1,238
Earnings (loss) before income taxes	72	68	(12)	—	(34)	(42)	52	(82)	(30)
Provision (benefit) for income taxes	14	25	(4)	—	—	(12)	23	(72)	(49)
Net earnings, including noncontrolling interests	58	43	(8)	—	(34)	(30)	29	(10)	19
Less: Net earnings (loss) attributable to noncontrolling interests	3	—	—	—	(34)	(1)	(32)	1	(31)
Core Net Operating Earnings	55	43	(8)	—	—	(29)	61		
Non-core earnings attributable to shareholders (a):									
Gain on sale of Medicare supplement and critical illness businesses, net of tax	—	—	—	13	—	—	13	(13)	—
Other realized gains, net of tax	—	—	—	—	—	36	36	(36)	—
Long-term care reserve charge, net of tax	—	—	(99)	—	—	—	(99)	99	—
AFG tax case and settlement of open tax years	—	—	—	—	—	39	39	(39)	—
Net Earnings Attributable to Shareholders	$ 55	$ 43	$ (107)	$ 13	$ —	$ 46	$ 50	$ —	$ 50

(a) See the reconciliation of core earnings to GAAP net earnings under *"Results of Operations — General"* for details on the tax and noncontrolling interest impacts of these reconciling items.

Property and Casualty Insurance Segment — Results of Operations Performance measures such as underwriting profit or loss and related combined ratios are often used by property and casualty insurers to help users of their financial statements better understand the company's performance. Underwriting profitability is measured by the combined ratio, which is a sum of the ratios of losses and loss adjustment expenses, and commissions and other underwriting expenses to premiums. A combined ratio under 100% indicates an underwriting profit. The combined ratio does not reflect net investment income, other income, other expenses or federal income taxes. AFG's property and casualty insurance operations contributed $136 million in GAAP pretax earnings in the fourth quarter of 2013 compared to $72 million in the fourth quarter of 2012, an increase of $64 million

(89%). The increase in pretax earnings reflects significantly higher underwriting profit across each of AFG’s property and casualty insurance sub-segments.

The following table details AFG's earnings before income taxes from its property and casualty operations for the three months ended December 31, 2013 and 2012 (dollars in millions):

	Three months ended December 31,		
	2013	2012	% Change
Gross written premiums	$ 1,071	$ 965	11%
Reinsurance premiums ceded	(250)	(263)	(5%)
Net written premiums	821	702	17%
Change in unearned premiums	38	54	(30%)
Net earned premiums	859	756	14%
Loss and loss adjustment expenses	537	556	(3%)
Commissions and other underwriting expenses	247	190	30%
Underwriting gain	75	10	650%
Net investment income	67	69	(3%)
Other income and expenses, net	(6)	(7)	(14%)
Earnings before income taxes	$ 136	$ 72	89%
Combined Ratios:			
Specialty lines			Change
Loss and LAE ratio	62.4%	72.9%	(10.5%)
Underwriting expense ratio	28.9%	25.1%	3.8%
Combined ratio	91.3%	98.0%	(6.7%)
Aggregate — including discontinued lines			
Loss and LAE ratio	62.5%	73.6%	(11.1%)
Underwriting expense ratio	28.9%	25.1%	3.8%
Combined ratio	91.4%	98.7%	(7.3%)

AFG’s combined ratio has been better than the industry average for 26 of the last 28 years. Management believes that AFG’s insurance operations have performed better than the industry as a result of its specialty niche focus, product line diversification, stringent underwriting discipline and alignment of compensation incentives.

While AFG desires and seeks to earn an underwriting profit on all of its business, it is not always possible to do so. As a result, AFG attempts to expand in the most profitable businesses and control growth or even reduce its involvement in the least profitable businesses.

AFG reports the underwriting performance of its Specialty insurance business in the following sub-components: (i) Property and transportation, (ii) Specialty casualty and (iii) Specialty financial.

To understand the overall profitability of particular lines, the timing of claims payments and the related impact of investment income must be considered. Certain “short-tail” lines of business (primarily property coverages) generally have quick loss payouts, which reduce the time funds are held, thereby limiting investment income earned thereon. In contrast, “long-tail” lines of business (primarily liability coverages and workers' compensation) generally have payouts that are either structured over many years or take many years to settle, thereby significantly increasing investment income earned on related premiums received.

Gross Written Premiums

Gross written premiums ("GWP") for AFG's property and casualty insurance segment were $1.07 billion for the fourth quarter of 2013 compared to $965 million for the fourth quarter of 2012, an increase of $106 million (11%). Detail of AFG's property and casualty gross written premiums is shown below (dollars in millions):

	Three months ended December 31,				
	2013		2012		
	GWP	%	GWP	%	% Change
Property and transportation	$ 447	42%	$ 431	44%	4%
Specialty casualty	459	43%	384	40%	20%
Specialty financial	164	15%	151	16%	9%
Other specialty	1	—%	(1)	—%	
	$ 1,071	100%	$ 965	100%	11%

Reinsurance Premiums Ceded

Reinsurance premiums ceded ("Ceded") for AFG's property and casualty insurance segment were 23% of gross written premiums for the fourth quarter of 2013 compared to 27% for the fourth quarter of 2012, a decrease of 4 percentage points. Detail of AFG's property and casualty reinsurance premiums ceded is shown below (dollars in millions):

	Three months ended December 31,				
	2013		2012		Change in
	Ceded	% of GWP	Ceded	% of GWP	% of GWP
Property and transportation	$ (98)	22%	$ (116)	27%	(5%)
Specialty casualty	(138)	30%	(126)	33%	(3%)
Specialty financial	(32)	20%	(43)	28%	(8%)
Other specialty	18		22		
	$ (250)	23%	$ (263)	27%	(4%)

Net Written Premiums

Net written premiums ("NWP") for AFG's property and casualty insurance segment were $821 million for the fourth quarter of 2013 compared to $702 million for the fourth quarter of 2012, an increase of $119 million (17%). Detail of AFG's property and casualty net written premiums is shown below (dollars in millions):

	Three months ended December 31,				
	2013		2012		
	NWP	%	NWP	%	% Change
Property and transportation	$ 349	43%	$ 315	45%	11%
Specialty casualty	321	39%	258	37%	24%
Specialty financial	132	16%	108	15%	22%
Other specialty	19	2%	21	3%	(10%)
	$ 821	100%	$ 702	100%	17%

Net Earned Premiums

Net earned premiums ("NEP") for AFG's property and casualty insurance segment were $859 million for the fourth quarter of 2013 compared to $756 million for the fourth quarter of 2012, an increase of $103 million (14%). Detail of AFG's property and casualty net earned premiums is shown below (dollars in millions):

	Three months ended December 31,				
	2013		2012		
	NEP	%	NEP	%	% Change
Property and transportation	$ 410	48%	$ 383	50%	7%
Specialty casualty	310	36%	249	33%	24%
Specialty financial	119	14%	104	14%	14%
Other specialty	20	2%	20	3%	—%
	$ 859	100%	$ 756	100%	14%

The $106 million increase in gross written premiums for the fourth quarter of 2013 compared to the fourth quarter of 2012 is due primarily to higher premiums in the Specialty casualty sub-segment. Overall average renewal rates increased approximately 3% in the fourth quarter of 2013.

Property and transportation Gross written premiums increased $16 million (4%) in the fourth quarter of 2013 compared to the same period in 2012 reflecting growth in nearly every business unit, partially offset by lower premiums in the crop operations. Delayed planting of winter wheat resulted in late acreage reporting, the effect of which is expected to shift a portion of AFG’s crop premiums from the fourth quarter of 2013 to the first quarter of 2014. Excluding crop premiums, fourth quarter 2013 gross and net written premiums grew by 10% and 13%, respectively, when compared to the 2012 fourth quarter. Average renewal rates for this group were up approximately 5% in the fourth quarter of 2013. Reinsurance premiums ceded as a percentage of gross written premiums declined 5 percentage points in the fourth quarter of 2013 compared to the fourth quarter of 2012 due to lower cessions of winter wheat premiums related to the delayed acreage reporting and lower reinstatement premiums due to the impact of large reinsured losses in 2012 (related to Superstorm Sandy).

Specialty casualty Gross written premiums increased $75 million (20%) for the fourth quarter of 2013 compared to the fourth quarter of 2012 as a result of increased premiums in nearly all businesses in this group, especially in the workers’ compensation, excess and surplus lines and agency captive insurance businesses. New business opportunities, increased exposures from higher payroll on existing accounts, and sustained pricing increases have contributed to increased premiums in the workers’ compensation businesses. Strong premium growth in the excess and surplus operations is the result of broadening opportunities to write business coupled with the benefit from rate increases over multiple quarters. Average renewal rates were up approximately 3% for this group in the fourth quarter of 2013. Reinsurance premiums ceded as a percentage of gross written premiums declined 3 percentage points for the fourth quarter of 2013 compared to the fourth quarter of 2012 reflecting higher retention of gross premiums in certain operations and changes in the mix of business.

Specialty financial Gross written premiums increased $13 million (9%) for the fourth quarter of 2013 compared to the fourth quarter of 2012. This increase was due primarily to premium growth related to real estate owned and collateral products for financial institutions and growth in the surety operations. Gross written premiums for the fourth quarter of 2013 include $5 million in risk fees from AFG’s warranty operations. Prior to 2013, fees in the warranty operations were included in other income. Average renewal rates for this group were flat in the fourth quarter of 2013. Reinsurance premiums ceded as a percentage of gross written premiums declined 8 percentage points due to the sale of the service contract business, which was 100% reinsured, and lower reinsurance reinstatement premiums reflecting the impact of large reinsured losses in the fourth quarter of 2012 in the surety business.

Other specialty The amounts shown as reinsurance premiums ceded represent business assumed by AFG's internal reinsurance program from the operations that make up AFG's other Specialty sub-components.

Combined Ratio

Performance measures such as the combined ratio are often used by property and casualty insurers to help users of their financial statements better understand the company's performance. The combined ratio is the sum of the loss and loss adjustment expenses (“LAE”) and underwriting expense ratios. These ratios are calculated by dividing each of the respective expenses by net earned premiums. The table below (dollars in millions) details the components of the combined ratio for AFG's property and casualty segment:

	Three months ended December 31,			Three months ended December 31,	
	2013	2012	Change	2013	2012
Property and transportation					
Loss and LAE ratio	74.9%	88.9%	(14.0%)		
Underwriting expense ratio	20.9%	14.8%	6.1%		
Combined ratio	95.8%	103.7%	(7.9%)		
Underwriting profit (loss)				$ 17	$ (14)
Specialty casualty					
Loss and LAE ratio	59.0%	65.9%	(6.9%)		
Underwriting expense ratio	30.7%	30.9%	(0.2%)		
Combined ratio	89.7%	96.8%	(7.1%)		
Underwriting profit				$ 32	$ 8
Specialty financial					
Loss and LAE ratio	34.2%	38.2%	(4.0%)		
Underwriting expense ratio	51.0%	46.7%	4.3%		
Combined ratio	85.2%	84.9%	0.3%		
Underwriting profit				$ 17	$ 16
Total Specialty					
Loss and LAE ratio	62.4%	72.9%	(10.5%)		
Underwriting expense ratio	28.9%	25.1%	3.8%		
Combined ratio	91.3%	98.0%	(6.7%)		
Underwriting profit				$ 75	$ 15
Aggregate — including discontinued lines					
Loss and LAE ratio	62.5%	73.6%	(11.1%)		
Underwriting expense ratio	28.9%	25.1%	3.8%		
Combined ratio	91.4%	98.7%	(7.3%)		
Underwriting profit				$ 75	$ 10

The Specialty property and casualty insurance operations generated an underwriting profit of $75 million in the fourth quarter of 2013 compared to $15 million in the fourth quarter of 2012, an increase of $60 million (400%). The higher profit in the 2013 quarter reflects higher underwriting profits across each of the property and casualty insurance sub-segments. Catastrophe losses were less than $1 million (0.1 points on the combined ratio), compared to $33 million, including $9 million of reinstatement premiums (3.2 points) in the fourth quarter of 2012.

Property and transportation This group reported an underwriting profit of $17 million for the fourth quarter of 2013, compared to an underwriting loss of $14 million for the fourth quarter of 2012, reflecting higher profitability in the crop insurance and property and inland marine operations. Although the 22% decline in corn pricing at harvest time as compared to 2013 spring discovery prices adversely impacted 2013 results, profitability in the crop insurance operations improved over the 2012 quarter, which was adversely impacted by the effects of the Midwest drought. The improved underwriting profitability in the property and inland marine operations reflects primarily the 2012 fourth quarter losses from Superstorm Sandy. Catastrophe losses were minimal for this group during the fourth quarter of 2013, compared to $28 million, including $8 million of reinstatement premiums (5.1 points) in the fourth quarter of 2012.

Specialty casualty Underwriting profit was $32 million for the fourth quarter of 2013 compared to $8 million in the fourth quarter of 2012, an increase of $24 million (300%). This increase was due primarily to higher profitability in the workers' compensation businesses and a $5 million improvement in prior year reserve development.

Specialty financial Underwriting profit was $17 million for the fourth quarter of 2013 compared to $16 million in the fourth quarter of 2012, an increase of $1 million (6%). Higher underwriting profits in the financial institutions business were partially offset by lower underwriting profitability in the surety and fidelity businesses. In addition, results for the fourth quarter of 2012 include a loss of $6 million in the vehicle services business, primarily from foreclosed and real estate owned property and collateral insurance.

Aggregate Aggregate results for AFG's property and casualty segment also include $5 million of adverse development in the fourth quarter of 2012 related to asbestos and environmental reserves.

Losses and Loss Adjustment Expenses
AFG's overall loss and LAE ratio was 62.5% for the fourth quarter of 2013 compared to 73.6% for fourth quarter of 2012, an improvement of 11.1 percentage points. The components of AFG's property and casualty losses and LAE amounts and ratio are detailed below (dollars in millions):

	Three months ended December 31,				Change in
	Amount		Ratio		
	2013	2012	2013	2012	Ratio
Property and transportation					
Current year, excluding catastrophe losses	$ 304	$ 322	74.1%	84.3%	(10.2%)
Prior accident years development	3	(2)	0.8%	(0.5%)	1.3%
Current year catastrophe losses	—	20	—%	5.1%	(5.1%)
Property and transportation losses and LAE and ratio	$ 307	$ 340	74.9%	88.9%	(14.0%)
Specialty casualty					
Current year, excluding catastrophe losses	$ 181	$ 157	58.5%	62.5%	(4.0%)
Prior accident years development	2	7	0.5%	3.0%	(2.5%)
Current year catastrophe losses	—	1	—%	0.4%	(0.4%)
Specialty casualty losses and LAE and ratio	$ 183	$ 165	59.0%	65.9%	(6.9%)
Specialty financial					
Current year, excluding catastrophe losses	$ 45	$ 51	36.7%	48.2%	(11.5%)
Prior accident years development	(4)	(13)	(3.2%)	(12.1%)	8.9%
Current year catastrophe losses	1	2	0.7%	2.1%	(1.4%)
Specialty financial losses and LAE and ratio	$ 42	$ 40	34.2%	38.2%	(4.0%)
Total Specialty					
Current year, excluding catastrophe losses	$ 541	$ 539	62.8%	71.2%	(8.4%)
Prior accident years development	(5)	(12)	(0.5%)	(1.5%)	1.0%
Current year catastrophe losses	1	24	0.1%	3.2%	(3.1%)
Total Specialty losses and LAE and ratio	$ 537	$ 551	62.4%	72.9%	(10.5%)
Aggregate — including discontinued lines					
Current year, excluding catastrophe losses	$ 541	$ 539	62.8%	71.2%	(8.4%)
Prior accident years development	(5)	(7)	(0.4%)	(0.8%)	0.4%
Current year catastrophe losses	1	24	0.1%	3.2%	(3.1%)
Aggregate losses and LAE and ratio	$ 537	$ 556	62.5%	73.6%	(11.1%)

Net prior year reserve development
AFG's Specialty property and casualty operations recorded net favorable reserve development related to prior accident years of $5 million in the fourth quarter of 2013 compared to $12 million in the fourth quarter of 2012, a decrease of $7 million (58%).

Property and transportation Net adverse reserve development of $3 million in the fourth quarter of 2013 reflects higher than expected claim severity in commercial auto liability business written in the transportation businesses, partially offset by lower than expected claim severity in the ocean marine business. Net favorable reserve development of $2 million in the fourth quarter of 2012 reflects lower severity in the inland marine and ocean marine businesses partially offset by an increase in severity of commercial auto liability insurance claims in the transportation businesses.

Specialty casualty Net adverse reserve development of $2 million in the fourth quarter of 2013 reflects higher than expected claim severity in products liability claims and contractor claims as well as adverse reserve development at Marketform, substantially offset by lower frequency of severe claims in the directors and officers and workers' compensation businesses. Net adverse reserve development of $7 million in the fourth quarter of 2012 reflects higher claim frequency and severity in a run-off book of U.S.-based program (motel/hotel, restaurants, taverns and recreational) business and adverse development in the excess and surplus lines, partially offset by lower than expected claim severity in the California workers' compensation and directors and officers liability insurance businesses.

Specialty financial Net favorable reserve development of $4 million in the fourth quarter of 2013 reflects lower than expected frequency of significant claims in the foreign credit business where economic conditions did not affect this line as adversely as previously anticipated. Net favorable reserve development of $13 million in the fourth quarter of 2012 reflects lower than expected claim frequency and severity in the foreign credit and financial institution businesses as economic conditions did not affect these lines as adversely as had been anticipated.

Other specialty In addition to the development discussed above, total specialty net favorable reserve development reflects amortization of the deferred gain on the retroactive insurance transaction entered into in connection with the sale of a business in 1998 and favorable reserve development associated with AFG's internal reinsurance program.

Aggregate Aggregate net prior accident years reserve development for AFG's property and casualty segment includes $5 million of adverse development in the fourth quarter of 2012 related to asbestos and environmental reserves.

Catastrophe losses

AFG generally seeks to reduce its exposure to catastrophes through individual risk selection, including minimizing coastal and known fault-line exposures, and the purchase of reinsurance. Based on data available at December 31, 2013, AFG's exposure to a catastrophic earthquake or windstorm that industry models indicate could occur once in every 500 years (a "500-year event") is expected to be less than 2.5% of AFG's shareholders' equity.

Commissions and Other Underwriting Expenses

AFG's property and casualty commissions and other underwriting expenses ("U/W Exp") were $247 million in the fourth quarter of 2013 compared to $190 million for the fourth quarter of 2012, an increase of $57 million (30%). AFG's underwriting expense ratio, calculated as commissions and other underwriting expenses divided by net premiums earned, was 28.9% for the fourth quarter of 2013 compared to 25.1% for the fourth quarter of 2012, an increase of 3.8 percentage points. Detail of AFG's property and casualty commissions and other underwriting expenses and underwriting expense ratios is shown below (dollars in millions):

	Three months ended December 31,				Change in
	2013		2012		
	U/W Exp	% of NEP	U/W Exp	% of NEP	% of NEP
Property and transportation	$ 86	20.9%	$ 57	14.8%	6.1%
Specialty casualty	95	30.7%	76	30.9%	(0.2%)
Specialty financial	60	51.0%	48	46.7%	4.3%
Other specialty	6	32.1%	9	37.3%	(5.2%)
	$ 247	28.9%	$ 190	25.1%	3.8%

The overall increase of 3.8% in AFG's expense ratio for the fourth quarter of 2013 as compared to the fourth quarter of 2012, as well as the fluctuations in AFG's sub-components, reflects the timing of the determination of reimbursements for administrative and operating expenses under the Federal crop insurance program, higher profitability-based commissions paid to agents/brokers and lower profitability-based commissions received from reinsurers, partially offset by the impact of higher premiums on the ratio.

Property and transportation Commissions and other underwriting expenses as a percentage of net earned premiums increased 6.1 percentage points for the fourth quarter of 2013 compared to the fourth quarter of 2012 reflecting the timing of the

determination of reimbursements for administrative and operating expenses under the Federal crop insurance program, partially offset by the impact of higher premiums on the ratio.

Specialty casualty Commissions and other underwriting expenses as a percentage of net earned premiums decreased 0.2 percentage points for the fourth quarter of 2013 compared to the fourth quarter of 2012, reflecting the impact of higher premiums on the ratio, partially offset by higher profitability-based commissions paid to agents/brokers and lower ceding commissions from reinsurers.

Specialty financial Commissions and other underwriting expenses as a percentage of net earned premiums increased 4.3 percentage points for the fourth quarter of 2013 compared to the fourth quarter of 2012 reflecting higher profitability-based commissions paid to agents/brokers.

Property and Casualty Net Investment Income

Net investment income in AFG's property and casualty operations was $67 million for the fourth quarter of 2013 compared to $69 million in the fourth quarter of 2012, a decrease of $2 million (3%). In recent years, yields available in the financial markets on fixed maturity securities have generally declined, placing downward pressure on AFG's investment portfolio yield. The average invested assets and overall earned yield on investments held by AFG's property and casualty operations are provided below (dollars in millions):

	Three months ended December 31,			
	2013	2012	Change	% Change
Net investment income	$ 67	$ 69	$ (2)	(3%)
Average invested assets (at amortized cost)	$ 6,805	$ 6,768	$ 37	1%
Yield (net investment income as a % of average invested assets)	3.94%	4.08%	(0.14%)	

The property and casualty segment's overall yield on investments (net investment income as a percentage of average invested assets) was 3.94% for the fourth quarter of 2013 compared to 4.08% for the fourth quarter of 2012, a decline of 0.14 percentage points, reflecting the impact of lower yields available in the financial markets.

Property and Casualty Other Income and Expenses, Net

Other income and expenses, net for AFG's property and casualty operations was a net expense of $6 million for the fourth quarter of 2013 compared to $7 million for the fourth quarter of 2012, a decrease of $1 million (14%). The table below details the items included in other income and expenses, net for AFG's property and casualty operations (in millions):

	Three months ended December 31,	
	2013	2012
Other income		
Warranty operations	$ —	$ 5
Income from the sale of real estate	2	—
Other	3	2
Total other income	5	7
Other expenses		
Warranty operations	—	5
Amortization of intangibles	4	4
Other	7	4
Total other expense	11	13
Interest expense	—	1
Other income and expenses, net	$ (6)	$ (7)

Beginning in 2013, AFG's warranty operations are included in the Specialty financial underwriting results.

Interest expense for AFG's property and casualty operations includes interest charges on long-term debt within the property and casualty operations, primarily notes secured by real estate and other secured borrowings.

Annuity Segment — Results of Operations

AFG's annuity operations contributed $92 million in pretax earnings in the fourth quarter of 2013 compared to $68 million in the fourth quarter of 2012, an increase of $24 million (35%). Higher pretax earnings were primarily a result of a growing asset base, partially offset by the runoff of higher yielding investments. AFG's average fixed annuity investments (at amortized cost) were 17% higher for the fourth quarter of 2013 as compared to the fourth quarter of 2012. In addition, results for the fourth quarter of 2013 reflect the positive impact of higher interest rates and strong stock market performance on the fixed-indexed annuity ("FIA") business. AFG's periodic detailed review ("unlocking") of the major actuarial assumptions underlying its annuity operations resulted in a charge of $2 million in the fourth quarter of 2013 compared to a $14 million charge in the fourth quarter of 2012.

The following table details AFG's earnings before income taxes from its annuity operations for the three months ended December 31, 2013 and 2012 (dollars in millions).

	Three months ended December 31,		
	2013	2012	% Change
Revenues:			
Net investment income	$ 270	$ 254	6%
Other income:			
Guaranteed withdrawal benefit fees	7	5	40%
Policy charges and other miscellaneous income	14	8	75%
Total revenues	291	267	9%
Costs and Expenses:			
Annuity benefits (*)	137	124	10%
Acquisition expenses	35	58	(40%)
Other expenses	27	17	59%
Total costs and expenses	199	199	—%
Earnings before income taxes	$ 92	$ 68	35%

(*) Annuity benefits consisted of the following (in millions):

	Three months ended December 31,		
	2013	2012	% Change
Interest credited — fixed	$ 118	$ 109	8%
Interest credited — fixed component of variable annuities	1	2	(50%)
Change in expected death and annuitization reserve	5	5	—%
Amortization of sales inducements	7	9	(22%)
Change in guaranteed withdrawal benefit reserve	10	5	100%
Change in other benefit reserves	1	3	(67%)
Derivatives related to fixed-indexed annuities:			
Embedded derivative mark-to-market	74	(4)	(1,950%)
Equity option mark-to-market	(85)	1	(8,600%)
Unlocking	6	(6)	(200%)
Total annuity benefits	$ 137	$ 124	10%

See *"Annuity Unlocking"* below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity benefit expense.

The profitability of a fixed annuity business is largely dependent on the ability of a company to earn income on the assets supporting the business in excess of the amounts credited to policyholder accounts plus expenses incurred (earning a "spread"). Performance measures such as net interest spread and net spread earned are often presented by annuity businesses to help users of their financial statements better understand the company's performance.

Net Spread on Fixed Annuities (excludes variable annuity earnings)
The table below (dollars in millions) details the components of these spreads for AFG's fixed annuity operations (including fixed-indexed annuities):

	Three months ended December 31,		
	2013	2012	% Change
Average fixed annuity investments (at amortized cost)	$ 20,524	$ 17,485	17%
Average fixed annuity benefits accumulated	20,092	17,137	17%
As % of fixed annuity benefits accumulated (except as noted):			
Net investment income (as % of fixed annuity investments)	5.21%	5.74%	
Interest credited — fixed	(2.35%)	(2.56%)	
Net interest spread	2.86%	3.18%	
Policy charges and other miscellaneous income	0.22%	0.14%	
Other annuity benefit expenses, net of guaranteed withdrawal benefit fees	(0.31%)	(0.39%)	
Acquisition expenses	(0.75%)	(0.85%)	
Other expenses	(0.53%)	(0.39%)	
Change in fair value of derivatives related to fixed-indexed annuities	0.22%	0.09%	
Unlocking	(0.04%)	(0.29%)	
Net spread earned on fixed annuities	1.67%	1.49%	

Annuity Net Investment Income
Net investment income for the fourth quarter of 2013 was $270 million compared to $254 million for the fourth quarter of 2012, an increase of $16 million (6%). This increase reflects primarily the growth in AFG’s annuity business. The overall yield earned on investments in AFG's annuity operations, calculated as net investment income divided by average investment balances (at amortized cost), declined by 0.53 percentage points in the fourth quarter of 2013 compared to the fourth quarter of 2012. This decline in net investment yield reflects (i) the investment of new premium dollars in the recent low interest rate environment, (ii) the impact of the maturity and redemption of higher yielding investments and (iii) the impact of higher non-recurring investment income in the fourth quarter of 2012 as compared to the same period in 2013.

Annuity Interest Credited — Fixed
Interest credited — fixed for the fourth quarter of 2013 was $118 million compared to $109 million for the fourth quarter of 2012, an increase of $9 million (8%). The impact of growth in the annuity business was partially offset by lower interest crediting rates on new premiums as compared to the crediting rates on policyholder funds surrendered or withdrawn. The average interest rate credited to policyholders, calculated as interest credited divided by average fixed annuity benefits accumulated, declined 0.21 percentage points in the fourth quarter of 2013 compared to the fourth quarter of 2012. During the fourth quarter of 2013, interest rates credited on new premiums generally ranged from 1.00% to 2.00%.

Excluding those annuities that have guaranteed withdrawal benefits, at December 31, 2013, AFG could reduce the average crediting rate on approximately $16 billion of traditional fixed and fixed-indexed deferred annuities by an additional 0.48% (on a weighted average basis). Annuity policies are subject to Guaranteed Minimum Interest Rates (“GMIRs”) at policy issuance. The table below shows the breakdown of annuity reserves by GMIR. The current interest crediting rates on substantially all of AFG's annuities with a GMIR of 3% or higher are at their minimum.

GMIR	% of Reserves
1 — 1.99%	52%
2 — 2.99%	11%
3 — 3.99%	21%
4.00% and above	16%

Annuity Net Interest Spread
AFG's net interest spread decreased 0.32 percentage points in the fourth quarter of 2013 compared to the same period in 2012 due primarily to the run-off of higher yielding investments. In addition, the 2012 quarter included higher non-recurring investment income as compared to the 2013 quarter. Due to the continued run-off of higher yielding investments, AFG expects its net interest spread to narrow in the future.

Annuity Policy Charges and Other Miscellaneous Income
Annuity policy charges and other miscellaneous income, which consist primarily of surrender charges, was $14 million in the fourth quarter of 2013 compared to $8 million in the fourth quarter of 2012, an increase of $6 million (75%). The increase reflects $4 million in income from the sale of real estate recorded in the 2013 quarter.

Other Annuity Benefits
Other annuity benefits, net of guaranteed withdrawal benefit fees (excluding the impact of unlocking) for the fourth quarter of 2013 was $16 million compared to $17 million for the fourth quarter of 2012, a decrease of $1 million (6%). In addition to interest credited to policyholders' accounts, annuity benefits expense also includes the following expenses (in millions, net of guaranteed withdrawal benefit fees):

	Three months ended December 31,	
	2013	2012
Change in expected death and annuitization reserve	$ 5	$ 5
Amortization of sales inducements	7	9
Change in guaranteed withdrawal benefit reserve	10	5
Change in other benefit reserves	1	3
Other annuity benefits	23	22
Offset guaranteed withdrawal benefit fees	(7)	(5)
Other annuity benefits, net	$ 16	$ 17

Annuity Acquisition Expenses
Excluding the impact of unlocking charges, AFG's amortization of DPAC and commission expenses as a percentage of average fixed annuity benefits accumulated was 0.75% for the fourth quarter of 2013 and 0.85% for the fourth quarter of 2012 and has generally ranged between 0.70% and 0.80%. Variances from the general range relate primarily to the impact of (i) material changes in interest rates or the stock market on AFG's fixed-indexed annuity business, and (ii) differences in actual experience from actuarially projected estimates and assumptions.

Annuity Other Expenses
Annuity other expenses for the fourth quarter of 2013 were $27 million compared to $17 million for the fourth quarter of 2012, an increase of $10 million (59%). Annuity other expenses represent primarily general and administrative expenses, as well as selling and issuance expenses that are not deferred. As a percentage of average fixed annuity benefits accumulated, these expenses increased 0.14 percentage points for the fourth quarter of 2013 as compared to the fourth quarter of 2012. The fourth quarter of 2013 includes a $7 million charge to write off certain previously capitalized project costs.

Change in Fair Value of Derivatives Related to Fixed-Indexed Annuities
AFG's fixed-indexed annuities, which represented approximately 47% of annuity benefits accumulated at December 31, 2013, provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase of call options on the appropriate index. AFG's strategy is designed so that an increase in the liabilities, due to an increase in the market index, will generally be offset by unrealized and realized gains on the call options purchased by AFG. Both the index-based component of the annuities and the related call options are considered derivatives that must be marked-to-market through earnings each period. The fair values of these derivatives are impacted by actual and expected stock market performance and interest rates as well as other factors. For a list of other factors impacting the fair value of the index-based component of AFG's annuity benefits accumulated, see *Note D — "Fair Value Measurements"* to the financial statements. Excluding the impact of unlocking charges, the net change in fair value of derivatives related to fixed-indexed annuities decreased annuity benefits by $11 million and $3 million in the fourth quarter of 2013 and 2012, respectively. The decrease in 2013 reflects the positive impact of higher interest rates and strong stock market performance on the fixed-indexed annuity business.

See *"Annuity Unlocking"* below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity and supplemental insurance acquisition expenses. Unanticipated spread compression, decreases in the stock market, adverse mortality experience, and higher than expected lapse rates could lead to future write-offs of DPAC or the present value of future profits on business in force of companies acquired ("PVFP").

Annuity Net Spread Earned on Fixed Annuities
AFG's net spread earned on fixed annuities increased 0.18 percentage points in the fourth quarter of 2013 compared to the same period in 2012 as the 0.32 percentage points decrease in AFG's net interest spread and higher other expenses in the 2013 fourth quarter were more than offset by (i) the impact of lower amortization of deferred acquisition costs during the fourth quarter of 2013 compared to the fourth quarter of 2012, (ii) a larger favorable impact from the change in fair value of FIA-related derivatives, and (iii) a higher unlocking charge in the fourth quarter of 2012 compared to the fourth quarter of 2013. AFG expects its net spread earned on fixed annuities to be closer to 1.35% to 1.40% in 2014 as compared to the 1.67% earned in the fourth quarter of 2013.

Annuity Benefits Accumulated
Annuity premiums received and benefit payments are recorded as increases or decreases in annuity benefits accumulated rather than as revenue and expense. Increases in this liability for interest credited and other benefits are charged to expense and decreases for surrender and other policy charges are credited to other income.

For certain products, annuity benefits accumulated also includes reserves for accrued persistency and premium bonuses, excess benefits expected to be paid on future deaths and annuitizations ("EDAR") and guaranteed withdrawal benefits. Annuity benefits accumulated also includes amounts advanced from the Federal Home Loan Bank of Cincinnati. The following table is a progression of AFG's annuity benefits accumulated liability for the three months ended December 31, 2013 and 2012 (in millions):

	Three months ended December 31,	
	2013	2012
Beginning fixed annuity reserves	$ 19,505	$ 16,999
Fixed annuity premiums (receipts)	1,368	545
Surrenders, benefits and other withdrawals	(408)	(355)
Interest and other annuity benefit expenses:		
Interest credited	118	109
Embedded derivative mark-to-market	74	(4)
Change in other benefit reserves	18	(10)
Unlocking	4	(10)
Ending fixed annuity reserves	$ 20,679	$ 17,274
Reconciliation to annuity benefits accumulated per balance sheet:		
Ending fixed annuity reserves (from above)	$ 20,679	$ 17,274
Impact of unrealized investment gains	71	136
Fixed component of variable annuities	194	199
Annuity benefits accumulated per balance sheet	$ 20,944	$ 17,609

Statutory Annuity Premiums
AFG's annuity operations generated statutory premiums of $1.38 billion in the fourth quarter of 2013 compared to $560 million in the fourth quarter of 2012, an increase of $821 million (147%). The following table summarizes AFG's annuity sales (dollars in millions):

	Three months ended December 31,		
	2013	2012	% Change
Retail single premium annuities — indexed	$ 565	$ 305	85%
Retail single premium annuities — fixed	53	35	51%
Financial institutions single premium annuities — indexed	498	59	744%
Financial institutions single premium annuities — fixed	201	86	134%
Education market — 403(b) fixed and indexed annuities	51	60	(15%)
Total fixed annuity premiums	1,368	545	151%
Variable annuities	13	15	(13%)
Total annuity premiums	$ 1,381	$ 560	147%

The 147% increase in annuity premiums as compared to the fourth quarter of 2012 reflects continued successful distribution channel expansion, primarily in the financial institutions market, as well as new product offerings. Management also believes

that AFG has benefited from its strong ratings, and that the entire annuity industry has benefited from the rise in interest rates in 2013, particularly in the financial institutions market.

Annuity Unlocking
In the fourth quarters of 2013 and 2012, AFG conducted a detailed review ("unlocking") of the major actuarial assumptions underlying its annuity operations. As a result of these reviews, AFG recorded charges (expense reductions) in annuity benefits expense and annuity and supplemental insurance acquisition expenses related to its annuity business. AFG's net annuity unlocking charge of $2 million in 2013 and $14 million in 2012 impacted AFG's financial statements as follows (in millions):

	Three months ended December 31,	
	2013	2012
Annuity benefits:		
Fixed indexed annuity embedded derivative	$ (2)	$ (36)
Sales inducements	2	4
Other reserves	6	26
Total annuity benefits	6	(6)
Annuity and supplemental insurance acquisition expenses:		
Deferred policy acquisition costs	(4)	33
Unearned revenue	—	(13)
Net charge	$ 2	$ 14

Although the table above includes the impact of assumption changes in both the fixed and variable annuity businesses, the vast majority of the net charge in each period relates to the fixed (including fixed-indexed) annuity business. The 2013 net charge was due primarily to the impact of changes in assumptions to reflect increased future investment yields being more than offset by an increase in future expected call option costs related to the fixed-indexed annuity business, and higher crediting rates and lapse assumptions. Reinvestment rates used to project future investment yields are based primarily on 7-year and 10-year corporate bond yields. For the 2013 unlocking, AFG assumed a net reinvestment rate (net of default and expense assumptions) of 4.05% in 2014, grading up to an ultimate net reinvestment rate of 5.52% in 2020 and beyond.

The 2012 net charge was due primarily to the impact of changes in assumptions related to future investment yields partially offset by changes in assumptions related to crediting rates, surrenders and annuitization and death benefits. For the 2012 unlocking, AFG assumed a net reinvestment rate (net of default and expense assumptions) of 3.50% in 2013, grading up ratably to an ultimate net reinvestment rate of 5.27% in 2022 and beyond.

Annuity Earnings before Income Taxes Reconciliation
The following table reconciles the net spread earned on AFG's fixed annuities to overall annuity pretax earnings for the three months ended December 31, 2013 and 2012 (in millions):

	Three months ended December 31,	
	2013	2012
Earnings on fixed annuity benefits accumulated	$ 84	$ 64
Earnings on investments in excess of fixed annuity benefits accumulated (*)	6	5
Variable annuity earnings	2	(1)
Earnings before income taxes	$ 92	$ 68

(*) Net investment income (as a % of investments) of 5.21% and 5.74% for the three months ended December 31, 2013 and 2012, respectively, multiplied by the difference between average fixed annuity investments (at amortized cost) and average fixed annuity benefits accumulated in each period.

Run-off Long-Term Care and Life Segment — Results of Operations As previously discussed under *"Uncertainties — Run-off Long-term Care Insurance,"* AFG recorded a $153 million loss recognition charge in the fourth quarter of 2012 to write off deferred policy acquisition costs and strengthen reserves in its closed block of long-term care insurance. The charge was due primarily to lower projected future investment rates resulting from the continued low interest rate environment, as well as changes in claims, expense and persistency assumptions. Excluding this charge, pretax core operating losses for the run-off long-term care and life segment were $3 million in the fourth quarter of 2013 compared to $12 million in the fourth quarter of 2012, an improvement of $9 million (75%). This improvement reflects the impact of higher long-term care benefits expense in the 2012 quarter due to charges to increase reserves related primarily to existing open claims and certain policyholder benefit features. The following table details AFG's GAAP and core losses before income taxes from its run-off long-term care and life operations for the three months ended December 31, 2013 and 2012 (dollars in millions):

	Three months ended December 31,		
	2013	2012	% Change
Revenues:			
Net earned premiums:			
Long-term care	$ 18	$ 19	(5%)
Life operations	9	9	—%
Net investment income	19	15	27%
Other income	1	2	(50%)
Total revenues	47	45	4%
Costs and Expenses:			
Life, accident and health benefits:			
Long-term care (*)	28	33	(15%)
Life operations	12	11	9%
Acquisition expenses (*)	4	7	(43%)
Other expenses	6	6	—%
Total costs and expenses	50	57	(12%)
Core loss before income taxes	(3)	(12)	(75%)
Pretax non-core loss recognition charge	—	(153)	(100%)
GAAP loss before income taxes	$ (3)	$ (165)	(98%)

(*) Excludes the pretax non-core loss recognition charge recorded in the fourth quarter of 2012, which increased life, accident and health benefits by $74 million and acquisition expenses by $79 million.

AFG expects revenues and expenses related to the long-term care business to generally increase over time as this closed block of business ages. Due to the age and relatively small size of its long-term care business, AFG expects claims volatility from period to period. Management continues to monitor its claims experience and update its loss recognition assumptions as needed.

Medicare Supplement and Critical Illness Segment — Results of Operations AFG's Medicare supplement and critical illness segment for the fourth quarter of 2012 reflects a $15 million GAAP pretax (non-core) post-closing adjustment to the gain on the August 2012 sale of these businesses. See *Note B — "Acquisitions and Sales of Subsidiaries"* to the financial statements.

Holding Company, Other and Unallocated — Results of Operations AFG's pretax loss outside of its insurance operations totaled $46 million for the fourth quarter of 2013 compared to $42 million for the fourth quarter of 2012, an increase of $4 million (10%).

The following table details AFG's loss before income taxes from operations outside of its insurance operations for three months ended December 31, 2013 and 2012 (dollars in millions):

	Three months ended December 31,		
	2013	2012	% Change
Revenues:			
Net investment income	$ 2	$ 1	100%
Other income	3	4	(25%)
Total revenues	5	5	—%
Costs and Expenses:			
Interest charges on borrowed money	17	17	—%
Other expenses	34	30	13%
Total costs and expenses	51	47	9%
Loss before income taxes, excluding realized gains	$ (46)	$ (42)	10%

Holding Company and Other — Net Investment Income
Net investment income for the fourth quarter of 2013 was $2 million compared to $1 million in the fourth quarter of 2012. The parent company holds a small portfolio of securities that are classified as "trading" and marked-to-market through investment income. These trading securities increased in value by approximately $2 million in the fourth quarter of 2013 compared to less than $1 million in the 2012 period.

Holding Company and Other — Other Income
Other income in the table above includes $4 million in both the fourth quarter of 2013 and 2012 in management fees paid to AFG by the AFG-managed CLOs (AFG's consolidated managed investment entities). These fees are eliminated in consolidation — see the other income line in the Consolidate MIEs column under *"Results of Operations — Segmented Statement of Earnings."* Results for the fourth quarter of 2013 and 2012 include losses related to the sale of fixed assets of $2 million and $3 million, respectively.

Holding Company and Other — Interest Charges on Borrowed Money
AFG's holding companies and other operations outside of its insurance operations recorded interest expense of $17 million in both the fourth quarter of 2013 and 2012. The following table details AFG's long-term debt balances as of December 31, 2013 compared to October 1, 2012 (dollars in millions):

	December 31, 2013	October 1, 2012
Direct obligations of AFG:		
9-7/8% Senior Notes due June 2019	$ 350	$ 350
6-3/8% Senior Notes due June 2042	230	230
5-3/4% Senior Notes due August 2042	125	125
7% Senior Notes due September 2050	132	132
Other	3	3
	840	840
Other holding company obligations:		
Secured borrowings (guaranteed by AFG)	—	16
AAG Holding Variable Rate Subordinated Debentures	—	20
	—	36
Total Holding Company and Other Debt	$ 840	$ 876
Weighted Average Interest Rate	7.8%	7.7%

Holding Company and Other — Other Expenses
AFG’s holding companies and other operations outside of its insurance operations, recorded other expenses of $34 million in the fourth quarter of 2013 compared to $30 million in the fourth quarter of 2012, an increase of $4 million (13%). The $4 million increase reflects higher expense associated with employee benefit plans that are tied to stock market performance and slightly higher stock-based compensation expense.

Consolidated Realized Gains (Losses) on Securities AFG's consolidated realized gains on securities, which are not allocated to segments, were $67 million in the fourth quarter of 2013 compared to $65 million in the fourth quarter of 2012, an increase of $2 million (3%). Realized gains (losses) on securities consisted of the following (in millions):

	Three months ended December 31,	
	2013	2012
Realized gains (losses) before impairments:		
Disposals	$ 75	$ 74
Change in the fair value of derivatives	(1)	—
Adjustments to annuity deferred policy acquisition costs and related items	(1)	(2)
	73	72
Impairment charges:		
Securities	(9)	(9)
Adjustments to annuity deferred policy acquisition costs and related items	3	2
	(6)	(7)
Realized gains on securities	$ 67	$ 65

Consolidated Income Taxes AFG's consolidated provision for income taxes was $81 million for the fourth quarter of 2013 compared to a tax benefit of $49 million in the fourth quarter of 2012, an increase of $130 million (265%). The income tax benefit recorded in the fourth quarter of 2012 includes a $39 million non-core tax benefit related to the settlement of open tax years following the resolution of the tax litigation with the IRS. See *Note L — “Income Taxes”* to the financial statements. The following is a reconciliation of income taxes at the statutory rate of 35% to the provision (benefit) for income taxes as shown in the Segmented Statement of Earnings (dollars in millions):

	Three months ended December 31,			
	2013		2012	
	Amount	% of EBT	Amount	% of EBT
Earnings (loss) before income taxes (“EBT”)	$ 246		$ (30)	
Income taxes at statutory rate	$ 86	35%	$ (10)	35%
Effect of:				
Tax exempt interest	(5)	(2%)	(5)	16%
Losses of managed investment entities	(2)	(1%)	12	(40%)
Subsidiaries not in AFG’s tax return	1	—%	(5)	17%
Settlement of open tax years	—	—%	(39)	130%
Other	1	1%	(2)	6%
Provision (benefit) for income taxes	$ 81	33%	$ (49)	164%

Consolidated Noncontrolling Interests AFG's consolidated net earnings attributable to noncontrolling interests were $7 million for the fourth quarter of 2013 compared to a net loss of $31 million for the fourth quarter of 2012. The following table details net earnings (loss) in consolidated subsidiaries attributable to holders other than AFG (dollars in millions):

	Three months ended December 31,		
	2013	2012	% Change
National Interstate	$ 4	$ 4	—%
Managed Investment Entities	4	(34)	(112%)
Other	(1)	(1)	—%
Earnings (loss) attributable to noncontrolling interests	$ 7	$ (31)	(123%)

As discussed in *Note A — “Accounting Policies,”* and *Note H — “Managed Investment Entities”* to the financial statements, the losses of Managed Investment Entities represent CLO losses that ultimately inure to holders of the CLO debt.

RESULTS OF OPERATIONS — YEARS ENDED DECEMBER 31, 2013, 2012 AND 2011

Segmented Statement of Earnings AFG reports its business as five segments: (i) Property and casualty insurance ("P&C"), (ii) Annuity, (iii) Run-off long-term care and life, (iv) Medicare supplement and critical illness (sold in August 2012) and (v) Other, which includes holding company costs and operations attributable to the noncontrolling interests of the managed investment entities ("MIEs").

AFG's net earnings attributable to shareholders, determined in accordance with GAAP, include certain items that may not be indicative of its ongoing core operations. The following tables for the years ended December 31, 2013, 2012 and 2011 identify such items by segment and reconcile net earnings attributable to shareholders to core net operating earnings, a non-GAAP financial measure that AFG believes is a useful tool for investors and analysts in analyzing ongoing operating trends (in millions):

				Other				
	P&C	Annuity	Run-off long-term care and life	Consol. MIEs	Holding Co., other and unallocated	Total	Non-core reclass	GAAP Total
Year ended December 31, 2013								
Revenues:								
Property and casualty insurance net earned premiums	$ 3,204	$ —	$ —	$ —	$ —	$ 3,204	$ —	$ 3,204
Life, accident and health net earned premiums	—	—	114	—	—	114	—	114
Net investment income	263	1,034	76	(35)	8	1,346	—	1,346
Realized gains on securities	—	—	—	—	—	—	221	221
Realized losses on subsidiaries	—	—	—	—	—	—	(4)	(4)
Income (loss) of MIEs:								
Investment income	—	—	—	128	—	128	—	128
Gain (loss) on change in fair value of assets/liabilities	—	—	—	(14)	—	(14)	—	(14)
Other income	15	67	4	(16)	27	97	—	97
Total revenues	3,482	1,101	194	63	35	4,875	217	5,092
Costs and Expenses:								
Property and casualty insurance:								
Losses and loss adjustment expenses	1,986	—	—	—	—	1,986	54	2,040
Commissions and other underwriting expenses	1,019	—	—	—	—	1,019	—	1,019
Annuity benefits	—	531	—	—	—	531	—	531
Life, accident and health benefits	—	—	160	—	—	160	—	160
Annuity and supplemental insurance acquisition expenses	—	149	18	—	—	167	—	167
Interest charges on borrowed money	3	—	—	—	68	71	—	71
Expenses of MIEs	—	—	—	89	—	89	—	89
Other expenses	45	93	26	—	135	299	27	326
Total costs and expenses	3,053	773	204	89	203	4,322	81	4,403
Earnings before income taxes	429	328	(10)	(26)	(168)	553	136	689
Provision for income taxes	132	113	(4)	—	(54)	187	49	236
Net earnings, including noncontrolling interests	297	215	(6)	(26)	(114)	366	87	453
Less: Net earnings (loss) attributable to noncontrolling interests	7	—	—	(26)	—	(19)	1	(18)
Core Net Operating Earnings	290	215	(6)	—	(114)	385		
Non-core earnings attributable to shareholders (a):								
Realized gains, net of tax	—	—	—	—	138	138	(138)	—
Special A&E charges, net of tax	(35)	—	—	—	(14)	(49)	49	—
ELNY guaranty fund assessments, net of tax	—	(3)	—	—	—	(3)	3	—
Net Earnings Attributable to Shareholders	$ 255	$ 212	$ (6)	$ —	$ 10	$ 471	$ —	$ 471

	P&C	Annuity	Run-off long-term care and life	Medicare supplement and critical illness	Other: Consol. MIEs	Other: Holding Co., other and unallocated	Total	Non-core reclass	GAAP Total
Year ended December 31, 2012									
Revenues:									
Property and casualty insurance net earned premiums	$ 2,847	$ —	$ —	$ —	$ —	$ —	$ 2,847	$ —	$ 2,847
Life, accident and health net earned premiums	—	—	119	199	—	—	318	—	318
Net investment income	275	976	69	7	(31)	5	1,301	—	1,301
Realized gains on securities	—	—	—	—	—	—	—	210	210
Realized gains on subsidiaries	—	—	—	—	—	—	—	161	161
Income (loss) of MIEs:									
Investment income	—	—	—	—	125	—	125	—	125
Gain (loss) on change in fair value of assets/liabilities	—	—	—	—	(94)	—	(94)	—	(94)
Other income	24	52	3	6	(18)	22	89	—	89
Total revenues	3,146	1,028	191	212	(18)	27	4,586	371	4,957
Costs and Expenses:									
Property and casualty insurance:									
Losses and loss adjustment expenses	1,842	—	—	—	—	—	1,842	31	1,873
Commissions and other underwriting expenses	887	—	—	—	—	—	887	—	887
Annuity benefits	—	541	—	—	—	—	541	—	541
Life, accident and health benefits	—	—	151	131	—	—	282	74	356
Annuity and supplemental insurance acquisition expenses	—	150	22	31	—	—	203	79	282
Interest charges on borrowed money	4	—	—	—	—	71	75	—	75
Expenses of MIEs	—	—	—	—	80	—	80	—	80
Other expenses	60	81	22	22	—	116	301	25	326
Total costs and expenses	2,793	772	195	184	80	187	4,211	209	4,420
Earnings before income taxes	353	256	(4)	28	(98)	(160)	375	162	537
Provision for income taxes	102	89	(1)	10	—	(51)	149	(14)	135
Net earnings, including noncontrolling interests	251	167	(3)	18	(98)	(109)	226	176	402
Less: Net earnings (loss) attributable to noncontrolling interests	10	—	—	—	(98)	—	(88)	2	(86)
Core Net Operating Earnings	241	167	(3)	18	—	(109)	314		
Non-core earnings attributable to shareholders (a):									
Gain on sale of Medicare supplement and critical illness businesses, net of tax	—	—	—	114	—	—	114	(114)	—
Other realized gains, net of tax	—	—	—	—	—	128	128	(128)	—
Long-term care reserve charge, net of tax	—	—	(99)	—	—	—	(99)	99	—
Special A&E charges, net of tax	(20)	—	—	—	—	(1)	(21)	21	—
AFG tax case and settlement of open tax years	—	—	—	—	—	67	67	(67)	—
Other, net of tax	—	—	—	—	—	(15)	(15)	15	—
Net Earnings Attributable to Shareholders	$ 221	$ 167	$ (102)	$ 132	$ —	$ 70	$ 488	$ —	$ 488

	P&C	Annuity	Run-off long-term care and life	Medicare supplement and critical illness	Other: Consol. MIEs	Other: Holding Co., other and unallocated	Total	Non-core reclass	GAAP Total
Year ended December 31, 2011									
Revenues:									
Property and casualty insurance net earned premiums	$ 2,759	$ —	$ —	$ —	$ —	$ —	$ 2,759	$ —	$ 2,759
Life, accident and health net earned premiums	—	—	126	304	—	—	430	—	430
Net investment income	291	859	66	10	(6)	5	1,225	—	1,225
Realized gains on securities	—	—	—	—	—	—	—	76	76
Realized losses on subsidiaries	—	—	—	—	—	—	—	(3)	(3)
Income (loss) of MIEs:									
Investment income	—	—	—	—	105	—	105	—	105
Gain (loss) on change in fair value of assets/liabilities	—	—	—	—	(33)	—	(33)	—	(33)
Other income	26	43	(2)	11	(19)	25	84	—	84
Total revenues	3,076	902	190	325	47	30	4,570	73	4,643
Costs and Expenses:									
Property and casualty insurance:									
Losses and loss adjustment expenses	1,694	—	—	—	—	—	1,694	50	1,744
Commissions and other underwriting expenses	835	—	—	—	—	—	835	—	835
Annuity benefits	—	510	—	—	—	—	510	—	510
Life, accident and health benefits	—	—	151	209	—	—	360	—	360
Annuity and supplemental insurance acquisition expenses	—	124	22	49	—	—	195	—	195
Interest charges on borrowed money	5	—	—	—	—	69	74	—	74
Expenses of MIEs	—	—	—	—	71	—	71	—	71
Other expenses	50	80	17	33	—	107	287	9	296
Total costs and expenses	2,584	714	190	291	71	176	4,026	59	4,085
Earnings before income taxes	492	188	—	34	(24)	(146)	544	14	558
Provision for income taxes	165	63	—	12	—	(41)	199	40	239
Net earnings, including noncontrolling interests	327	125	—	22	(24)	(105)	345	(26)	319
Less: Net earnings (loss) attributable to noncontrolling interests	5	—	—	—	(24)	1	(18)	(5)	(23)
Core Net Operating Earnings	322	125	—	22	—	(106)	363		
Non-core earnings attributable to shareholders (a):									
Other realized gains, net of tax	—	—	—	—	—	45	45	(45)	—
Special A&E charges, net of tax	(32)	—	—	—	—	(6)	(38)	38	—
Valuation allowance on deferred taxes	(28)	—	—	—	—	—	(28)	28	—
Net Earnings Attributable to Shareholders	$ 262	$ 125	$ —	$ 22	$ —	$ (67)	$ 342	$ —	$ 342

(a) See the reconciliation of core earnings to GAAP net earnings under *"Results of Operations — General"* for details on the tax and noncontrolling interest impacts of these reconciling items.

Property and Casualty Insurance Segment — Results of Operations AFG's property and casualty insurance operations contributed $375 million in GAAP pretax earnings in 2013 compared to $322 million in 2012, an increase of $53 million (16%). Property and casualty core pretax earnings were $429 million for the 2013 compared to $353 million for the 2012, an increase of $76 million (22%). Higher underwriting profits in the Specialty casualty group and Specialty financial group were partially offset by a decline in the underwriting profits in the Property and transportation group during the first half of the year.

AFG's property and casualty insurance operations contributed $322 million in GAAP pretax earnings in 2012 compared to $442 million in 2011, a decrease of $120 million (27%). Property and casualty core pretax earnings were $353 million in 2012 compared to $492 million in 2011, a decrease of $139 million (28%). The decrease is due mainly to lower underwriting profits

in the Property and transportation group due primarily to the effects of the Midwest drought on the crop operations and losses from Superstorm Sandy in 2012.

The following table details AFG's GAAP and core earnings before income taxes from its property and casualty operations for the years ended December 31, 2013, 2012 and 2011 (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Gross written premiums	$ 4,805	$ 4,321	$ 4,106	11%	5%
Reinsurance premiums ceded	(1,464)	(1,372)	(1,336)	7%	3%
Net written premiums	3,341	2,949	2,770	13%	6%
Change in unearned premiums	(137)	(102)	(11)	34%	827%
Net earned premiums	3,204	2,847	2,759	13%	3%
Loss and loss adjustment expenses (*)	1,986	1,842	1,694	8%	9%
Commissions and other underwriting expenses	1,019	887	835	15%	6%
Core underwriting gain	199	118	230	69%	(49%)
Net investment income	263	275	291	(4%)	(5%)
Other income and expenses, net	(33)	(40)	(29)	(18%)	38%
Core earnings before income taxes	429	353	492	22%	(28%)
Pretax non-core special A&E charges	(54)	(31)	(50)	74%	(38%)
GAAP earnings before income taxes	$ 375	$ 322	$ 442	16%	(27%)

(*) Excluding non-core special A&E charges

Combined Ratios:				Change	
Specialty lines				2013 - 2012	2012 - 2011
Loss and LAE ratio	61.7%	64.3%	61.4%	(2.6%)	2.9%
Underwriting expense ratio	31.8%	31.1%	30.2%	0.7%	0.9%
Combined ratio	93.5%	95.4%	91.6%	(1.9%)	3.8%
Aggregate — including discontinued lines					
Loss and LAE ratio	63.7%	65.8%	63.2%	(2.1%)	2.6%
Underwriting expense ratio	31.8%	31.1%	30.2%	0.7%	0.9%
Combined ratio	95.5%	96.9%	93.4%	(1.4%)	3.5%

AFG reports the underwriting performance of its Specialty insurance business in the following sub-components: (i) Property and transportation, (ii) Specialty casualty and (iii) Specialty financial.

Gross Written Premiums

Gross written premiums ("GWP") for AFG's property and casualty insurance segment were $4.81 billion in 2013 compared to $4.32 billion in 2012, an increase of $484 million (11%). GWP increased $215 million (5%) in 2012 compared to 2011. Detail of AFG's property and casualty gross written premiums is shown below (dollars in millions):

	Year ended December 31,						% Change	
	2013		2012		2011		2013 - 2012	2012 - 2011
	GWP	%	GWP	%	GWP	%		
Property and transportation	$ 2,392	50%	$ 2,271	53%	$ 2,273	55%	5%	—%
Specialty casualty	1,790	37%	1,484	34%	1,302	32%	21%	14%
Specialty financial	622	13%	566	13%	529	13%	10%	7%
Other specialty	1	—%	—	—%	2	—%	—%	—%
	$ 4,805	100%	$ 4,321	100%	$ 4,106	100%	11%	5%

Reinsurance Premiums Ceded

Reinsurance premiums ceded ("Ceded") for AFG's property and casualty insurance segment were 30%, 32% and 33% of gross written premiums for the years ended December 31, 2013, 2012 and 2011, respectively. Detail of AFG's property and casualty reinsurance premiums ceded is shown below (dollars in millions):

	Year ended December 31,						Change in % of GWP	
	2013		2012		2011		2013 - 2012	2012 - 2011
	Ceded	% of GWP	Ceded	% of GWP	Ceded	% of GWP		
Property and transportation	$ (845)	35%	$ (798)	35%	$ (837)	37%	—%	(2%)
Specialty casualty	(566)	32%	(492)	33%	(435)	33%	(1%)	—%
Specialty financial	(136)	22%	(155)	27%	(131)	25%	(5%)	2%
Other specialty	83		73		67			
	$ (1,464)	30%	$ (1,372)	32%	$ (1,336)	33%	(2%)	(1%)

Net Written Premiums

Net written premiums ("NWP") for AFG's property and casualty insurance segment were $3.34 billion in 2013 compared to $2.95 billion in 2012, an increase of $392 million (13%). NWP increased $179 million (6%) in 2012 compared to 2011. Detail of AFG's property and casualty net written premiums is shown below (dollars in millions):

	Year ended December 31,						% Change	
	2013		2012		2011		2013 - 2012	2012 - 2011
	NWP	%	NWP	%	NWP	%		
Property and transportation	$ 1,547	45%	$ 1,473	50%	$ 1,436	53%	5%	3%
Specialty casualty	1,224	37%	992	34%	867	31%	23%	14%
Specialty financial	486	15%	411	14%	398	14%	18%	3%
Other specialty	84	3%	73	2%	69	2%	15%	6%
	$ 3,341	100%	$ 2,949	100%	$ 2,770	100%	13%	6%

Net Earned Premiums

Net earned premiums ("NEP") for AFG's property and casualty insurance segment were $3.20 billion in 2013 compared to $2.85 billion in 2012, an increase of $357 million (13%). NEP increased $88 million (3%) in 2012 compared to 2011. Detail of AFG's property and casualty net earned premiums is shown below (dollars in millions):

	Year ended December 31,						% Change	
	2013		2012		2011		2013 - 2012	2012 - 2011
	NEP	%	NEP	%	NEP	%		
Property and transportation	$ 1,521	48%	$ 1,423	50%	$ 1,412	51%	7%	1%
Specialty casualty	1,135	35%	948	33%	872	32%	20%	9%
Specialty financial	469	15%	405	14%	408	15%	16%	(1%)
Other specialty	79	2%	71	3%	67	2%	11%	6%
	$ 3,204	100%	$ 2,847	100%	$ 2,759	100%	13%	3%

The $484 million increase in gross written premiums in 2013 compared to 2012 reflects growth across each of the property and casualty sub-segments. Overall average renewal rates increased approximately 4% in 2013.

The $215 million increase in gross written premiums in 2012 compared to 2011 is due primarily to higher premiums in the Specialty casualty group, particularly in the worker’s compensation and excess and surplus businesses. Overall average renewal rates increased approximately 3% in 2012.

Property and transportation Gross written premiums increased $121 million in 2013 compared to 2012 due primarily to higher crop premiums and growth in the transportation businesses. Average renewal rates were up approximately 5% in 2013. Reinsurance premiums ceded as a percentage of gross written premiums were 35% in both 2013 and 2012. Higher cessions of multi-peril crop business and higher cost of reinsurance on the property business were offset by higher retention of gross premiums in certain operations and lower reinsurance reinstatement premiums due to the impact of large reinsured losses in 2012 (related to Superstorm Sandy).

Gross written premiums decreased $2 million in 2012 compared to 2011 as the impact of lower spring agricultural commodity prices for corn and soybeans, which had the effect of reducing crop insurance premiums, was partially offset by growth in the transportation businesses. Average renewal rates were up approximately 3% in 2012. Reinsurance premiums ceded as a percentage of gross written premiums declined 2 percentage points in 2012 compared to 2011 reflecting lower cessions of multi-peril crop business.

Specialty casualty Gross written premiums increased $306 million (21%) in 2013 compared to 2012 as a result of increased premiums in nearly all businesses in this group, particularly in the workers' compensation and excess and surplus lines. New business opportunities, increased exposures from higher payroll on existing accounts, strong retentions and higher renewal pricing have contributed to increased premiums in the workers' compensation businesses. In addition, new business opportunities and general market hardening have generated increased premiums in several of the excess and surplus lines businesses. Average renewal rates were up approximately 5% for this group in 2013. Reinsurance premiums ceded as a percentage of gross written premiums declined 1 percentage point for 2013 compared to 2012 reflecting changes in the mix of business and higher retention of gross premiums in certain operations.

Gross written premiums increased $182 million (14%) in 2012 compared to 2011 as a result of business opportunities in the excess and surplus operations, growth in the workers' compensation and agency captive insurance businesses and market hardening in many of the other Specialty casualty operations. Average renewal rates were up approximately 4% for this group in 2012. Reinsurance premiums ceded as a percentage of gross written premiums was 33% for both 2012 and 2011.

Specialty financial Gross written premiums increased $56 million (10%) in 2013 compared to 2012. This increase was due primarily to premium growth related to real estate owned and collateral products for financial institutions and growth in the surety operations. Gross written premiums in 2013 include $22 million in risk fees from AFG's warranty operations. Prior to 2013, fees in the warranty operations were included in other income. Average renewal rates for this group remained relatively unchanged in 2013. Reinsurance premiums ceded as a percentage of gross written premiums declined 5 percentage points in 2013 compared to 2012 reflecting the sale of the service contract business, which was 100% reinsured and lower reinsurance reinstatement premiums reflecting the impact of large reinsured losses in 2012 in the surety and foreign credit businesses.

Gross written premiums increased 37 million (7%) in 2012 compared to 2011 due to higher premiums in the financial institutions business, as well as growth in a service contract business. All of the premiums in the service contract business were ceded under reinsurance agreements. Average renewal rates for this group remained relatively unchanged in 2012. Reinsurance premiums ceded as a percentage of gross written premiums increased 2% percentage points in 2012 compared to 2011 due to the increase in service contract business, which was 100% reinsured.

Other specialty The amounts shown as reinsurance premiums ceded represent business assumed by AFG's internal reinsurance program from the operations that make up AFG's other Specialty sub-components.

Combined Ratio

The table below details the components of the combined ratio for AFG's property and casualty segment for 2013, 2012 and 2011 (dollars in millions):

	Year ended December 31,			Change		Year ended December 31,		
	2013	2012	2011	2013 - 2012	2012 - 2011	2013	2012	2011
Property and transportation								
Loss and LAE ratio	75.1%	74.7%	69.8%	0.4%	4.9%			
Underwriting expense ratio	24.1%	24.0%	22.2%	0.1%	1.8%			
Combined ratio	99.2%	98.7%	92.0%	0.5%	6.7%			
Underwriting profit (loss)						$ 12	$ 19	$ 113
Specialty casualty								
Loss and LAE ratio	57.5%	61.3%	60.9%	(3.8%)	0.4%			
Underwriting expense ratio	33.4%	33.2%	35.0%	0.2%	(1.8%)			
Combined ratio	90.9%	94.5%	95.9%	(3.6%)	(1.4%)			
Underwriting profit						$ 102	$ 53	$ 35
Specialty financial								
Loss and LAE ratio	33.5%	38.8%	37.1%	(5.3%)	1.7%			
Underwriting expense ratio	52.1%	50.4%	47.0%	1.7%	3.4%			
Combined ratio	85.6%	89.2%	84.1%	(3.6%)	5.1%			
Underwriting profit						$ 67	$ 44	$ 65
Total Specialty								
Loss and LAE ratio	61.7%	64.3%	61.4%	(2.6%)	2.9%			
Underwriting expense ratio	31.8%	31.1%	30.2%	0.7%	0.9%			
Combined ratio	93.5%	95.4%	91.6%	(1.9%)	3.8%			
Underwriting profit						$ 206	$ 131	$ 231
Aggregate — including discontinued lines								
Loss and LAE ratio	63.7%	65.8%	63.2%	(2.1%)	2.6%			
Underwriting expense ratio	31.8%	31.1%	30.2%	0.7%	0.9%			
Combined ratio	95.5%	96.9%	93.4%	(1.4%)	3.5%			
Underwriting profit						$ 145	$ 87	$ 180

The Specialty insurance operations generated an underwriting profit of $206 million in 2013 compared to $131 million in 2012, an increase of $75 million (57%). The higher profit in 2013 is primarily the result of higher underwriting profits in the Specialty casualty and Specialty financial groups partially offset by lower underwriting profits in the Property and transportation businesses. Overall catastrophe losses were $31 million (1.0 points on the combined ratio) in 2013 compared to $46 million, including $9 million of reinstatement premiums (1.3 points) in 2012.

The Specialty insurance operations generated an underwriting profit of $131 million in 2012 compared to $231 million in 2011, a decrease of $100 million (43%). The decline in 2012 was due primarily to lower profitability in the crop insurance business as a result of the Midwest drought and lower favorable reserve development in several of the Specialty casualty businesses. Overall catastrophe losses were $46 million, including $9 million of reinstatement premiums (1.3 points) in 2012 compared to $43 million (1.6 points) in 2011.

Property and transportation This group reported an underwriting profit of $12 million in 2013 compared to $19 million in 2012, a decrease of $7 million (37%). This decline is due primarily to lower profitability in the transportation businesses, partially offset by improved profitability in the crop operations. Catastrophe losses were $27 million (1.8 points) for this group in 2013 compared to $35 million, including $8 million of reinstatement premiums (1.9 points) in 2012.

This group reported an underwriting profit of $19 million in 2012 compared to $113 million in 2011, a decrease of $94 million (83%). This decline is due primarily to the effects of the Midwest drought on the crop operations and losses from Superstorm Sandy. Catastrophe losses were $35 million, including $8 million of reinstatement premiums (1.9 points) in 2012 compared to $29 million (2.1 points) in 2011.

Specialty casualty Underwriting profit was $102 million in 2013 compared to $53 million in 2012, an increase of $49 million (92%), reflecting improved results in the workers' compensation business as well as increased favorable reserve development in other operations.

Underwriting profit was $53 million in 2012 compared to $35 million in 2011, an increase of $18 million (51%). Improved 2012 accident year results in several operations and increased favorable reserve development in the general liability lines were partially offset by lower favorable reserve development in the executive liability and excess and surplus businesses.

Specialty financial Underwriting profit was $67 million in 2013 compared to $44 million in 2012, an increase of $23 million (52%). The improved results were due primarily to higher underwriting profits in the financial institutions business, primarily from foreclosed and real estate owned property and collateral insurance and the absence of losses from a run-off book of automotive-related business that were included in the results for 2012.

Underwriting profit was $44 million in 2012 compared to $65 million in 2011, a decrease of $21 million (32%). Lower profitability in the financial institutions, surety and foreign credit businesses contributed to these results.

Losses and Loss Adjustment Expenses
AFG's overall loss and LAE ratio was 63.7%, 65.8% and 63.2% in 2013, 2012 and 2011, respectively. The components of AFG's property and casualty losses and LAE amounts and ratio are detailed below (dollars in millions):

	Year ended December 31,							
	Amount			Ratio			Change in Ratio	
	2013	2012	2011	2013	2012	2011	2013 - 2012	2012 - 2011
Property and transportation								
Current year, excluding catastrophe losses	$ 1,116	$ 1,051	$ 983	73.4%	73.8%	69.6%	(0.4%)	4.2%
Prior accident years development	(1)	(16)	(26)	(0.1%)	(1.0%)	(1.9%)	0.9%	0.9%
Current year catastrophe losses	27	27	29	1.8%	1.9%	2.1%	(0.1%)	(0.2%)
Property and transportation losses and LAE and ratio	$ 1,142	$ 1,062	$ 986	75.1%	74.7%	69.8%	0.4%	4.9%
Specialty casualty								
Current year, excluding catastrophe losses	$ 692	$ 596	$ 598	61.0%	62.8%	68.6%	(1.8%)	(5.8%)
Prior accident years development	(40)	(18)	(71)	(3.6%)	(1.8%)	(8.2%)	(1.8%)	6.4%
Current year catastrophe losses	1	3	4	0.1%	0.3%	0.5%	(0.2%)	(0.2%)
Specialty casualty losses and LAE and ratio	$ 653	$ 581	$ 531	57.5%	61.3%	60.9%	(3.8%)	0.4%
Specialty financial								
Current year, excluding catastrophe losses	$ 169	$ 181	$ 152	35.9%	44.6%	37.6%	(8.7%)	7.0%
Prior accident years development	(14)	(29)	(10)	(3.0%)	(7.1%)	(2.6%)	4.1%	(4.5%)
Current year catastrophe losses	3	5	9	0.6%	1.3%	2.1%	(0.7%)	(0.8%)
Specialty financial losses and LAE and ratio	$ 158	$ 157	$ 151	33.5%	38.8%	37.1%	(5.3%)	1.7%
Total Specialty								
Current year, excluding catastrophe losses	$ 2,023	$ 1,866	$ 1,770	63.1%	65.5%	64.1%	(2.4%)	1.4%
Prior accident years development	(75)	(74)	(120)	(2.4%)	(2.5%)	(4.3%)	0.1%	1.8%
Current year catastrophe losses	31	37	43	1.0%	1.3%	1.6%	(0.3%)	(0.3%)
Total Specialty losses and LAE and ratio	$ 1,979	$ 1,829	$ 1,693	61.7%	64.3%	61.4%	(2.6%)	2.9%
Aggregate — including discontinued lines								
Current year, excluding catastrophe losses	$ 2,024	$ 1,866	$ 1,770	63.1%	65.5%	64.1%	(2.4%)	1.4%
Prior accident years development	(15)	(30)	(69)	(0.4%)	(1.0%)	(2.5%)	0.6%	1.5%
Current year catastrophe losses	31	37	43	1.0%	1.3%	1.6%	(0.3%)	(0.3%)
Aggregate losses and LAE and ratio	$ 2,040	$ 1,873	$ 1,744	63.7%	65.8%	63.2%	(2.1%)	2.6%

Net prior year reserve development
AFG's Specialty property and casualty operations recorded net favorable reserve development related to prior accident years of $75 million in 2013 compared to $74 million in 2012, an increase of $1 million (1%).

AFG's Specialty property and casualty operations recorded net favorable reserve development related to prior accident years of $74 million in 2012 compared to $120 million in 2011, a decrease of $46 million (38%).

Property and transportation Net favorable reserve development of $1 million in 2013 reflects lower than expected claims handling expense in the crop business and lower claim severity in the property inland marine and ocean marine businesses, substantially offset by adverse development from higher than expected claim severity in commercial auto liability business written in the transportation businesses. Net favorable reserve development of $16 million in 2012 reflects lower than expected loss frequency in crop products, partially offset by higher than expected claim severity in the property and inland marine and commercial auto liability in the transportation businesses. Net favorable reserve development of $26 million in 2011 reflects lower than expected loss frequency in crop products.

Specialty casualty Net favorable reserve development of $40 million in 2013 reflects lower than expected claim severity in directors and officers liability insurance and lower than expected claim severity and frequency in excess liability business, partially offset by adverse development from higher than expected claim frequency and severity in products liability claims and higher than expected claim severity in contractor claims. Net favorable reserve development of $18 million in 2012 is due primarily to the release of loss reserves on claims related to the use of Chinese drywall in residential construction as a result of judicial decisions and class action settlements in 2012 that clarified the liability of insured homebuilders. Favorable reserve development in 2012 also reflects lower claim severity in executive liability products partially offset by higher claim severity on losses in a run-off book of U.S.-based program (motel/hotel, restaurants, taverns and recreational) business and adverse reserve development on run-off Italian public hospital medical malpractice liability products written by Marketform. Favorable reserve development of $71 million in 2011 is due primarily to lower than expected claim severity in directors and officers liability, excess and surplus lines and the run-off legal professional liability business, partially offset by adverse development due to higher frequency and severity on run-off Italian public hospital medical malpractice liability products and a block of program business.

Specialty financial Net favorable reserve development of $14 million in 2013 is due to lower than expected frequency and severity in the foreign credit and financial institution services businesses as economic conditions did not affect these lines as adversely as had been anticipated. Net favorable reserve development of $29 million in 2012 and $10 million in 2011 reflects lower than expected frequency and severity in the surety, fidelity, crime, foreign credit and financial institution services businesses as economic conditions did not affect these lines as adversely as had been anticipated.

Other specialty In addition to the development discussed above, total specialty net favorable reserve development reflects amortization of the deferred gain on the retroactive insurance transaction entered into in connection with the sale of a business in 1998 and reserve development associated with AFG’s internal reinsurance program.

Asbestos and Environmental Reserve Charges As previously discussed under “*Uncertainties*” — “*Asbestos and Environmental-related (“A&E”) Insurance Reserves*,” AFG has established property and casualty reserves for claims related to environmental exposures and asbestos claims. AFG has also recorded liabilities for various environmental and occupational injury and disease claims arising out of former railroad and manufacturing operations. Total charges recorded to increase reserves (net of reinsurance recoverable) for A&E exposures of AFG’s property and casualty group (included in loss and loss adjustment expenses) and its former railroad and manufacturing operations (included in other operating and general expenses) were as follows (in millions):

	2013	2012	2011
Property and casualty group	$ 59	$ 43	$ 50
Former operations	29	12	18

Aggregate Aggregate net prior accident years reserve development for AFG’s property and casualty segment includes the A&E charges mentioned above.

Catastrophe losses
AFG generally seeks to reduce its exposure to catastrophes through individual risk selection, including minimizing coastal and known fault-line exposures, and the purchase of reinsurance. The $27 million in catastrophe losses in the Property and transportation group in 2013 resulted primarily from spring storms in the southeastern United States. The $27 million in

catastrophe losses in the Property and transportation group in 2012 resulted primarily from Superstorm Sandy. The $29 million in catastrophe losses in the Property and transportation group in 2011 resulted primarily from tornadoes.

Commissions and Other Underwriting Expenses
AFG's property and casualty commissions and other underwriting expenses ("U/W Exp") were $1.02 billion in 2013 compared to $887 million in 2012, an increase of $132 million (15%). AFG's underwriting expense ratio was 31.8% in 2013 compared to 31.1% in 2012, an increase of 0.7 percentage points.

AFG's property and casualty U/W Exp were $887 million in 2012 compared to $835 million in 2011, an increase of $52 million (6%). AFG's underwriting expense ratio was 31.1% in 2012 compared to 30.2% in 2011, an increase of 0.9 percentage points.

Detail of AFG's property and casualty commissions and other underwriting expenses and underwriting expense ratios is shown below (dollars in millions):

	Year ended December 31,						Change in % of NEP	
	2013		2012		2011		2013 - 2012	2012 - 2011
	U/W Exp	% of NEP	U/W Exp	% of NEP	U/W Exp	% of NEP		
Property and transportation	$ 367	24.1%	$ 342	24.0%	$ 313	22.2%	0.1%	1.8%
Specialty casualty	380	33.4%	314	33.2%	306	35.0%	0.2%	(1.8%)
Specialty financial	244	52.1%	204	50.4%	192	47.0%	1.7%	3.4%
Other specialty	28	35.9%	27	37.2%	24	36.8%	(1.3%)	0.4%
	$ 1,019	31.8%	$ 887	31.1%	$ 835	30.2%	0.7%	0.9%

The overall increase of 0.7% in AFG's expense ratio in 2013 as compared to 2012, as well as the fluctuations in AFG's sub-components, reflects higher profitability-based commissions paid to agents/brokers and lower profitability-based commissions received from reinsurers, partially offset by the impact of higher premiums on the ratio.

The overall increase of 0.9% in AFG's expense ratio in 2012 as compared to 2011, as well as the fluctuations in AFG's sub-components, reflects the impact of higher premiums on the ratio was more than offset by changes in the mix of AFG's business and the impact of certain reinsurance ceding commissions received that are partially based on the profitability of the business ceded.

Property and transportation Commissions and other underwriting expenses as a percentage of net earned premiums increased 0.1 percentage points in 2013 compared to 2012 reflecting higher profitability-based commissions paid to agents/brokers and lower profitability-based commissions received from reinsurers, partially offset by higher reimbursements for administrative and operating expenses under the Federal crop insurance program and the impact of higher premiums on the ratio.

Commissions and other underwriting expenses as a percentage of net earned premiums increased 1.8 percentage points in 2012 compared to 2011 due to lower profitability-based commissions received from reinsurers partially offset by lower profitability-based commissions paid to agents/brokers, particularly in the crop operations.

Specialty casualty Commissions and other underwriting expenses as a percentage of net earned premiums increased 0.2 percentage points in 2013 compared to 2012 reflecting higher profitability-based commissions related to international business and increases in staffing costs related to business growth, partially offset by the impact of higher premiums on the ratio.

Commissions and other underwriting expenses as a percentage of net earned premiums decreased 1.8 percentage points in 2012 compared to 2011 primarily due to the impact of higher premiums on the ratio.

Specialty financial Commissions and other underwriting expenses as a percentage of net earned premiums increased 1.7 percentage points in 2013 compared to 2012 reflecting higher profitability-based commissions and lower ceding commissions from reinsurers, partially offset by the impact of higher premiums on the ratio.

Commissions and other underwriting expenses as a percentage of net earned premiums increased 3.4 percentage points in 2012 compared to 2011 primarily due to a change in mix of business.

Property and Casualty Net Investment Income

Net investment income in AFG's property and casualty operations was $263 million in 2013 compared to $275 million in 2012, a decrease of $12 million (4%). Net investment income in AFG's property and casualty operations was $275 million in 2012 compared to $291 million in 2011, a decrease of $16 million (5%). In recent years, yields available in the financial markets on fixed maturity securities have generally declined, placing downward pressure on AFG's investment portfolio yield. The average invested assets and overall earned yield on investments held by AFG's property and casualty operations are provided below (dollars in millions):

	Year ended December 31,			2013 - 2012		2012 - 2011	
	2013	2012	2011	Change	% Change	Change	% Change
Net investment income	$ 263	$ 275	$ 291	$ (12)	(4%)	$ (16)	(5%)
Average invested assets (at amortized cost)	$ 6,863	$ 6,675	$ 6,752	$ 188	3%	$ (77)	(1%)
Yield (net investment income as a % of average invested assets)	3.83%	4.12%	4.31%	(0.29%)		(0.19%)	

The property and casualty segment's overall yield on investments (net investment income as a percentage of average invested assets) was 3.83% in 2013 compared to 4.12% in 2012, a decline of 0.29% percentage points. In addition to the impact of lower yields available in the financial markets, the $188 million increase in average invested assets reflects primarily higher average balances of cash and cash equivalents.

The property and casualty segment's overall yield on investments (net investment income as a percentage of average invested assets) was 4.12% in 2012 compared to 4.31% in 2011, a decline of 0.19% percentage points. The decline is due primarily to the impact of lower yields available in the financial markets.

Property and Casualty Other Income and Expenses, Net

Other income and expenses, net for AFG's property and casualty operations was a net expense of $33 million in 2013, $40 million in 2012 and $29 million in 2011, representing a decrease of $7 million (18%) in 2013 compared to 2012 and an increase of $11 million (38%) in 2012 compared to 2011. The table below details the items included in other income and expenses, net for AFG's property and casualty operations (in millions):

	Year ended December 31,		
	2013	2012	2011
Other income			
Warranty operations	$ —	$ 17	$ 14
Income from the sale of real estate	6	—	—
Other	9	7	12
Total other income	15	24	26
Other expenses			
Warranty operations	—	19	17
Amortization of intangibles	14	14	12
Other	31	27	21
Total other expense	45	60	50
Interest expense	3	4	5
Other income and expenses, net	$ (33)	$ (40)	$ (29)

Beginning in 2013, AFG's warranty operations are included in the Specialty financial underwriting results.

Interest expense for AFG's property and casualty operations includes interest charges on long-term debt within the property and casualty operations, primarily notes secured by real estate and other secured borrowings.

Annuity Segment — Results of Operations

AFG's annuity operations contributed $323 million in GAAP pretax earnings in 2013 compared to $256 million in 2012, an increase of $67 million (26%). AFG's annuity operations contributed $328 million in core pretax earnings in 2013 compared to $256 million in 2012, an increase of $72 million (28%). The increase in both GAAP and core pretax earnings was a result of growth in the annuity business and the positive impact of higher interest rates and strong stock market performance in 2013 on AFG's FIA business. Results for 2012 reflect the negative impact of sharply lower interest rates on the FIA business. AFG's periodic detailed review ("unlocking") of the major actuarial assumptions underlying its annuity operations resulted in a charge of $2 million in 2013 compared to a $14 million charge in 2012.

AFG's annuity operations contributed $256 million in GAAP pretax earnings in 2012 compared to $188 million in 2011, an increase of $68 million (36%). The increase is due primarily to AFG's ability to maintain spreads on a larger base of invested assets as well as exceptionally strong investment results. Lower interest rates negatively impacted earnings in AFG's FIA business in both 2012 and 2011. Operating earnings also include a net unlocking charge of $14 million in 2012 compared to $1 million in 2011.

In the second quarter of 2013, AFG recorded a pretax charge of $5 million in its annuity operations to cover expected assessments from state guaranty funds related to the insolvency and liquidation of Executive Life Insurance Company of New York ("ELNY"), an unaffiliated life insurance company. ELNY was placed into rehabilitation by the New York Insurance Department in 1991. In April 2012, ELNY was declared insolvent and ordered into liquidation. AFG's life insurance subsidiaries are required under the solvency or guaranty laws of most states in which they do business to pay assessments up to certain prescribed limits to fund policyholder losses or liabilities of insolvent insurance companies such as ELNY and started receiving guaranty fund assessments related to ELNY from various states in the second quarter of 2013. AFG does not expect to record significant additional charges for ELNY guaranty fund assessments in future quarters.

The following table details AFG's GAAP and core earnings before income taxes from its annuity operations for 2013, 2012 and 2011 (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Revenues:					
Net investment income	$ 1,034	$ 976	$ 859	6%	14%
Other income:					
Guaranteed withdrawal benefit fees	25	14	4	79%	250%
Policy charges and other miscellaneous income	42	38	39	11%	(3%)
Total revenues	1,101	1,028	902	7%	14%
Costs and Expenses:					
Annuity benefits (a)	531	541	510	(2%)	6%
Acquisition expenses	149	150	124	(1%)	21%
Other expenses (b)	93	81	80	15%	1%
Total costs and expenses	773	772	714	—%	8%
Core earnings before income taxes	328	256	188	28%	36%
Pretax non-core ELNY guaranty fund assessments	(5)	—	—	—%	—%
GAAP earnings before income taxes	$ 323	$ 256	$ 188	26%	36%

(a) Annuity benefits consisted of the following (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Interest credited — fixed	$ 451	$ 438	$ 417	3%	5%
Interest credited — fixed component of variable annuities	6	7	8	(14%)	(13%)
Change in expected death and annuitization reserve	19	19	14	—%	36%
Amortization of sales inducements	30	32	30	(6%)	7%
Change in guaranteed withdrawal benefit reserve	38	14	4	171%	250%
Change in other benefit reserves	7	10	5	(30%)	100%
Derivatives related to fixed-indexed annuities:					
Embedded derivative mark-to-market	184	93	29	98%	221%
Equity option mark-to-market	(210)	(66)	13	218%	(608%)
Unlocking	6	(6)	(10)	(200%)	(40%)
Total annuity benefits	$ 531	$ 541	$ 510	(2%)	6%

(b) Other expenses exclude the $5 million pretax non-core charge for ELNY guaranty fund assessments in 2013.

See "*Annuity Unlocking*" below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity benefit expense.

Net Spread on Fixed Annuities (excludes variable annuity earnings)
The table below (dollars in millions) details the components of these spreads for AFG's fixed annuity operations (including fixed-indexed annuities):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Average fixed annuity investments (at amortized cost)	$ 19,151	$ 16,650	$ 14,146	15%	18%
Average fixed annuity benefits accumulated	18,696	16,394	13,929	14%	18%
As % of fixed annuity benefits accumulated (except as noted):					
Net investment income (as % of fixed annuity investments)	5.35%	5.80%	5.99%		
Interest credited — fixed	(2.41%)	(2.68%)	(2.99%)		
Net interest spread	2.94%	3.12%	3.00%		
Policy charges and other miscellaneous income	0.16%	0.16%	0.20%		
Other annuity benefit expenses, net of guaranteed withdrawal benefit fees	(0.37%)	(0.36%)	(0.35%)		
Acquisition expenses	(0.79%)	(0.75%)	(0.73%)		
Other expenses (*)	(0.46%)	(0.46%)	(0.53%)		
Change in fair value of derivatives related to fixed-indexed annuities	0.13%	(0.16%)	(0.31%)		
Unlocking	(0.01%)	(0.07%)	(0.01%)		
Net spread earned on fixed annuities	1.60%	1.48%	1.27%		

(*) Excludes the $5 million pretax non-core charge for ELNY guaranty fund assessments. Including this charge, the net spread earned on fixed annuities was 1.57% in 2013.

Annuity Net Investment Income
Net investment income in 2013 was $1.03 billion compared to $976 million in 2012, an increase of $58 million (6%). This increase reflects primarily the growth in AFG's annuity business. The overall yield earned on investments in AFG's annuity operations, calculated as net investment income divided by average investment balances (at amortized cost), declined by 0.45 percentage points in 2013 compared to 2012. This decline in net investment yield reflects (i) the investment of new premium dollars in the recent low interest rate environment and (ii) the impact of the maturity and redemption of higher yielding investments.

Net investment income in 2012 was $976 million compared to $859 million in 2011, an increase of $117 million (14%). This increase reflects primarily the growth in AFG's annuity business and exceptionally strong investment results in 2012. The overall yield earned on investments in AFG's annuity operations, calculated as net investment income divided by average investment balances (at amortized cost), declined by 0.19 percentage points in 2012 compared to 2011. This decline in net investment yield reflects (i) the investment of new premium dollars in the recent low interest rate environment and (ii) the impact of the maturity and redemption of higher yielding investments, partially offset by (iii) exceptionally strong investment results.

Annuity Interest Credited — Fixed
Interest credited — fixed in 2013 was $451 million compared to $438 million in 2012, an increase of $13 million (3%). The impact of growth in the annuity business was partially offset by lower interest crediting rates on new premiums as compared to the crediting rates on policyholder funds surrendered or withdrawn as well as the full-year impact of crediting rate reductions on existing policyholder funds that were implemented in the second half of 2012. The average interest rate credited to policyholders, calculated as interest credited divided by average fixed annuity benefits accumulated, decreased 0.27 percentage points in 2013 compared to 2012. During 2013, interest rates credited on new premiums generally ranged from 1.00% to 2.00%.

Interest credited — fixed in 2012 was $438 million compared to $417 million in 2011, an increase of $21 million (5%). The impact of growth in the annuity business was partially offset by lower interest crediting rates on new premiums as compared to the crediting rates on policyholder funds surrendered or withdrawn as well as the impact of crediting rate reductions on existing policyholder funds that were implemented in the second half of 2012. The average interest rate credited to policyholders, calculated as interest credited divided by average fixed annuity benefits accumulated, decreased 0.31 percentage points in 2012 compared to 2011. During 2012, interest rates credited on new premiums generally ranged from 1.00% to 2.00%.

Annuity Net Interest Spread
AFG's net interest spread decreased 0.18 percentage points in 2013 compared to 2012 due primarily to the run-off of higher yielding investments, partially offset by lower crediting rates.

AFG's net interest spread increased 0.12 percentage points in 2012 compared to 2011 due primarily to exceptionally strong investment results in 2012 and lower crediting rates, partially offset by the run-off of higher yielding investments.

Annuity Policy Charges and Other Miscellaneous Income
Annuity policy charges and other miscellaneous income, which consist primarily of surrender charges, in 2013 was $42 million compared to $38 million in 2012, an increase of $4 million (11%). The increase reflects $4 million in income from the sale of real estate recorded in 2013.

Annuity policy charges and other miscellaneous income in 2012 were $38 million compared to $39 million in 2011, a decrease of $1 million (3%), primarily reflecting lower surrender charge rates.

Other Annuity Benefits
Other annuity benefits, net of guaranteed withdrawal benefit fees (excluding the impact of unlocking) were $69 million in 2013, $61 million in 2012 and $49 million in 2011, representing an increase of $8 million (13%) in 2013 compared to 2012 and $12 million (24%) in 2012 compared to 2011. In addition to interest credited to policyholders' accounts, annuity benefits expense also includes the following expenses (in millions, net of guaranteed withdrawal benefit fees):

	Year ended December 31,		
	2013	2012	2011
Change in expected death and annuitization reserve	$ 19	$ 19	$ 14
Amortization of sales inducements	30	32	30
Change in guaranteed withdrawal benefit reserve	38	14	4
Change in other benefit reserves	7	10	5
Other annuity benefits	94	75	53
Offset guaranteed withdrawal benefit fees	(25)	(14)	(4)
Other annuity benefits, net	$ 69	$ 61	$ 49

The $8 million increase in other annuity benefits, net of guaranteed withdrawal benefit fees in 2013 compared to 2012 primarily reflects increased sales of products with guaranteed withdrawal benefit features.

The $12 million increase in other annuity benefits, net of guaranteed withdrawal benefit fees in 2012 compared to 2011 primarily reflects increased benefit reserves due to low lapse rates.

See *"Annuity Unlocking"* below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity benefit expense.

Annuity Acquisition Expenses
AFG's amortization of DPAC and commission expenses as a percentage of average fixed annuity benefits accumulated was 0.79% in 2013 compared to 0.75% in 2012 and 0.73% in 2011 and has generally ranged between 0.70% and 0.80%. Variances in these percentages generally relate to the impact of (i) material changes in interest rates or the stock market on AFG's fixed-indexed annuity business, and (ii) differences in actual experience from actuarially projected estimates and assumptions. For example, the favorable impact of the increase in market interest rates during 2013 on the fair value of derivatives related to fixed-indexed annuities (discussed below) resulted in a partially offsetting acceleration in the amortization of DPAC.

See *"Annuity Unlocking"* below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity and supplemental insurance acquisition expenses. Unanticipated spread compression, decreases in the stock market, adverse mortality experience, and higher than expected lapse rates could lead to write-offs of DPAC or PVFP in the future.

Annuity Other Expenses
Excluding the non-core ELNY guaranty fund assessments charge, annuity other expenses were $93 million in 2013, $81 million in 2012 and $80 million in 2011, representing an increase of $12 million (15%) in 2013 compared to 2012 and $1 million (1%) in 2012 compared to 2011. Annuity other expenses represent primarily general and administrative expenses, as well as selling and issuance expenses that are not deferred. As a percentage of average fixed annuity benefits accumulated, these expenses were flat in 2013 compared to 2012 and declined 0.07 percentage points in 2012 compared to 2011. In general this percentage is expected to decrease as AFG's annuity business grows. However, annuity other expenses for 2013 includes a $7 million charge to write off certain previously capitalized project costs.

Change in Fair Value of Derivatives Related to Fixed-Indexed Annuities
AFG's fixed-indexed annuities, which represented approximately 47% of annuity benefits accumulated at December 31, 2013, provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase of call options on the appropriate index. AFG's strategy is designed so that an increase in the liabilities, due to an increase in the market index, will generally be offset by unrealized and realized gains on the call options purchased by AFG. Both the index-based component of the annuities and the related call options are considered derivatives that must be marked-to-market through earnings each period. The fair values of these derivatives are impacted by actual and expected stock market performance and interest rates as well as other factors. For a list of other factors impacting the fair value of the index-based component of AFG's annuity benefits accumulated, see *Note D — "Fair Value Measurements"* to the financial statements. Excluding the impact of unlocking charges, the net change in fair value of derivatives related to fixed-indexed annuities reduced annuity benefits by $26 million in 2013 due to the positive impact of higher market interest rates and the net impact of strong stock market performance on the derivatives. Conversely, the net change in fair value of the derivatives related to fixed-indexed annuities, excluding the impact of unlocking charges, increased annuity benefits expense by $27 million in 2012 and $42 million in 2011 reflecting the negative impact of sharply lower market interest rates on the embedded derivative.

Annuity Net Spread Earned on Fixed Annuities
AFG's net spread earned on fixed annuities increased 0.12 percentage points in 2013 compared to 2012 as the 0.18 percentage points decrease in AFG's net interest spread was more than offset by the impact of changes in the fair value of derivatives discussed above.

AFG's net spread earned on fixed annuities increased 0.21 percentage points in 2012 compared to 2011 due primarily to the 0.12 percentage points increase in AFG's net interest spread and the impact of changes in the fair value of derivatives discussed above.

Annuity Benefits Accumulated
Annuity premiums received and benefit payments are recorded as increases or decreases in annuity benefits accumulated rather than as revenue and expense. Increases in this liability for interest credited and other benefits are charged to expense and decreases for surrender and other policy charges are credited to other income.

For certain products, annuity benefits accumulated also includes reserves for accrued persistency and premium bonuses, excess benefits expected to be paid on future deaths and annuitizations (“EDAR”) and guaranteed withdrawal benefits. Annuity benefits accumulated also includes amounts advanced from the Federal Home Loan Bank of Cincinnati. The following table is a progression of AFG's annuity benefits accumulated liability for 2013, 2012 and 2011 (in millions):

	Year ended December 31,		
	2013	2012	2011
Beginning fixed annuity reserves	$ 17,274	$ 15,188	$ 12,670
Fixed annuity premiums (receipts)	3,981	2,930	3,016
Federal Home Loan Bank advances	200	—	240
Surrenders, benefits and other withdrawals	(1,493)	(1,397)	(1,193)
Interest and other annuity benefit expenses:			
Interest credited	451	438	417
Embedded derivative mark-to-market	184	93	29
Change in other benefit reserves	78	32	13
Unlocking	4	(10)	(4)
Ending fixed annuity reserves	$ 20,679	$ 17,274	$ 15,188
Reconciliation to annuity benefits accumulated per balance sheet:			
Ending fixed annuity reserves (from above)	$ 20,679	$ 17,274	$ 15,188
Impact of unrealized investment gains	71	136	30
Fixed component of variable annuities	194	199	202
Annuity benefits accumulated per balance sheet	$ 20,944	$ 17,609	$ 15,420

Statutory Annuity Premiums
AFG's annuity operations generated statutory premiums of $4.03 billion in 2013, $2.99 billion in 2012 and $3.09 billion in 2011, an increase of $1.04 billion (35%) in 2013 compared to 2012 and a decrease of $95 million (3%) in 2012 compared to 2011. The following table summarizes AFG's annuity sales (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Retail single premium annuities — indexed	$ 1,879	$ 1,662	$ 1,549	13%	7%
Retail single premium annuities — fixed	165	153	239	8%	(36%)
Financial institutions single premium annuities — indexed	1,102	291	216	279%	35%
Financial institutions single premium annuities — fixed	628	587	755	7%	(22%)
Education market — 403(b) fixed and indexed annuities	207	237	257	(13%)	(8%)
Total fixed annuity premiums	3,981	2,930	3,016	36%	(3%)
Variable annuities	52	61	70	(15%)	(13%)
Total annuity premiums	$ 4,033	$ 2,991	$ 3,086	35%	(3%)

The 35% increase in annuity premiums in 2013 compared to 2012 reflects continued successful distribution channel expansion, primarily in the financial institutions market, as well as new product offerings. Management also believes that AFG has benefitted from its strong ratings, and that the entire annuity industry has benefitted from the rise in interest rates in 2013, particularly in the financial institutions market.

The 3% decrease in annuity premiums in 2012 compared to 2011 reflects actions taken by AFG in response to the significant drop in interest rates that began in the second quarter of 2012. These actions included reductions in interest rates credited to policyholders and in commissions paid to agents. Management believes that fixed-indexed annuities continued to sell well in both the retail and financial institutions markets due to their market participation and other features. Conversely, management believes that traditional fixed annuity sales decreased due to low absolute crediting rates in the market, and that this decrease is

consistent with industry experience. In addition, AFG was impacted by aggressive participants and new entrants in certain of its markets.

Annuity Unlocking

In 2013, 2012 and 2011, AFG conducted its detailed review ("unlocking") of the major actuarial assumptions underlying its annuity operations. As a result of these reviews, AFG recorded charges (expense reductions) in annuity benefits expense and annuity and supplemental insurance acquisition expenses related to its annuity business. AFG's net annuity unlocking charges of $2 million in 2013, $14 million in 2012 and $1 million in 2011 impacted AFG's financial statements as follows (in millions):

	Year ended December 31,		
	2013	2012	2011
Annuity benefits:			
Fixed-indexed annuities embedded derivative	$ (2)	$ (36)	$ —
Sales inducements	2	4	(6)
Other reserves	6	26	(4)
Total annuity benefits	6	(6)	(10)
Annuity and supplemental insurance acquisition expenses:			
Deferred policy acquisition costs	(4)	33	1
Unearned revenue	—	(13)	10
Net charge	$ 2	$ 14	$ 1

See "*Results of Operations — Quarters ended December 31, 2013 and 2012 — Annuity Segment — Results of Operations — Annuity Unlocking*" for a discussion of the overall net charge from the periodic review of actuarial assumptions in 2013 and 2012.

Annuity Earnings before Income Taxes Reconciliation

The following table reconciles the GAAP and core net spread earned on AFG's fixed annuities to overall annuity pretax earnings for 2013, 2012 and 2011 (in millions):

	Year ended December 31,		
	2013	2012	2011
Earnings on fixed annuity benefits accumulated (a)	$ 300	$ 243	$ 177
Earnings on investments in excess of fixed annuity benefits accumulated (b)	24	14	13
Variable annuity earnings (loss)	4	(1)	(2)
Core earnings before income taxes	328	256	188
Pretax non-core ELNY guaranty fund assessments	(5)	—	—
GAAP earnings before income taxes	$ 323	$ 256	$ 188

(a) Excludes the $5 million pretax non-core charge for ELNY guarantee fund assessments in 2013.

(b) Net investment income (as a % of investments) of 5.35% and 5.80% and 5.99% in 2013, 2012 and 2011, respectively, multiplied by the difference between average fixed annuity investments (at amortized cost) and average fixed annuity benefits accumulated in each period.

Run-off Long-Term Care and Life Segment — Results of Operations As previously discussed under *"Uncertainties — Run-off Long-term Care Insurance,"* AFG recorded a $153 million loss recognition charge in the fourth quarter of 2012 to write off deferred policy acquisition costs and strengthen reserves in its closed block of long-term care insurance. The charge was due primarily to lower projected future investment rates resulting from the continued low interest rate environment, as well as changes in claims, expenses and persistency assumptions. Excluding this charge, pretax core operating losses for the run-off long-term care and life segment were $10 million in 2013 and $4 million in 2012 compared to pretax operating earnings of less than $1 million in 2011. The following table details AFG's GAAP and core earnings (losses) before income taxes from its run-off long-term care and life operations in 2013, 2012 and 2011 (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Revenues:					
Net earned premiums:					
Long-term care	$ 76	$ 78	$ 81	(3%)	(4%)
Life operations	38	41	45	(7%)	(9%)
Net investment income	76	69	66	10%	5%
Other income	4	3	(2)	33%	(250%)
Total revenues	194	191	190	2%	1%
Costs and Expenses:					
Life, accident and health benefits:					
Long-term care (*)	113	99	91	14%	9%
Life operations	47	52	60	(10%)	(13%)
Acquisition expenses (*)	18	22	22	(18%)	—%
Other expenses	26	22	17	18%	29%
Total costs and expenses	204	195	190	5%	3%
Core earnings (loss) before income taxes	(10)	(4)	—	150%	—%
Pretax non-core loss recognition charge	—	(153)	—	(100%)	—%
GAAP earnings (loss) before income taxes	$ (10)	$ (157)	$ —	(94%)	—%

(*) Excludes the pretax non-core loss recognition charge recorded in the fourth quarter of 2012 to increase life, accident and health benefits by $74 million and acquisition expenses by $79 million.

The increase in long-term care benefits expense in 2013 as compared to 2012 is due primarily to an increase in new claims. The decrease in life benefits expense in 2013 as compared to 2012 is due primarily to improved claims experience in the first half of 2013.

The increase in long-term care benefits expense in 2012 as compared to 2011 is due primarily to charges recorded in 2012 to increase reserves related to existing open claims and certain policyholder benefit features. The decrease in life benefits expense in 2012 as compared to 2011 is due primarily to improved claims experience.

AFG expects revenues and expenses related to the long-term care business to generally increase over time as this closed block of business ages. Due to the age and relatively small size of its long-term care business, AFG expects claims volatility from period to period. Management continues to monitor its claims experience and update its loss recognition assumptions as needed.

Medicare Supplement and Critical Illness Segment — Results of Operations AFG's Medicare supplement and critical illness segment contributed $198 million in GAAP pretax earnings in 2012, which includes a $170 million pretax non-core realized gain on the August 2012 sale of these businesses, and GAAP pretax earnings of $34 million in 2011. See *Note B — "Acquisitions and Sales of Subsidiaries"* to the financial statements. The following table details AFG's GAAP and core earnings before income taxes from its Medicare supplement and critical illness business (in millions):

	Year ended December 31,		
	2013	2012	2011
Revenues:			
Net earned premiums	$ —	$ 199	$ 304
Net investment income	—	7	10
Other income	—	6	11
Total revenues	—	212	325
Costs and Expenses:			
Life, accident and health benefits	—	131	209
Acquisition expenses	—	31	49
Other expenses	—	22	33
Total costs and expenses	—	184	291
Core earnings before income taxes	—	28	34
Pretax non-core realized gain on sale of Medicare supplement and critical illness businesses	—	170	—
GAAP earnings before income taxes	$ —	$ 198	$ 34

Holding Company, Other and Unallocated — Results of Operations AFG's net GAAP pretax loss outside of its insurance operations (excluding realized gains) totaled $190 million in 2013 compared to $185 million in 2012, an increase of $5 million (3%). AFG's net core pretax loss outside of its insurance operations (excluding realized gains) totaled $168 million in 2013 compared to $160 million in 2012, an increase of $8 million (5%).

AFG's net GAAP pretax loss outside of its insurance operations (excluding realized gains) totaled $185 million in 2012 compared to $155 million in 2011, an increase of $30 million (19%). AFG's net core pretax loss outside of its insurance operations (excluding realized gains) totaled $160 million in 2012 compared to $146 million in 2011, an increase of $14 million (10%).

The following table details AFG's GAAP and core loss before income taxes from operations outside of its insurance operations in 2013, 2012 and 2011 (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
Revenues:					
Net investment income	$ 8	$ 5	$ 5	60%	—%
Other income	27	22	25	23%	(12%)
Total revenues	35	27	30	30%	(10%)
Costs and Expenses:					
Interest charges on borrowed money	68	71	69	(4%)	3%
Other expenses (*)	135	116	107	16%	8%
Total costs and expenses	203	187	176	9%	6%
Core loss before income taxes, excluding realized gains	(168)	(160)	(146)	5%	10%
Pretax non-core items, excluding realized gains:					
Special A&E charges	(22)	(2)	(9)	1,000%	(78%)
Other	—	(23)	—	(100%)	—%
GAAP loss before income taxes, excluding realized gains	$ (190)	$ (185)	$ (155)	3%	19%

(*) Excludes pretax non-core special A&E charges of $22 million, $2 million and $9 million in 2013, 2012 and 2011, respectively. Other expenses in 2012 also exclude $23 million in other non-core charges (discussed below).

Holding Company and Other — Net Investment Income
AFG recorded investment income on investments held outside of its insurance operations of $8 million, $5 million and $5 million in 2013, 2012 and 2011, respectively.

Holding Company and Other — Other Income
Other income in the table above includes management fees paid to AFG by the AFG-managed CLOs (AFG's consolidated managed investment entities) of $16 million, $18 million and $19 million in 2013, 2012 and 2011, respectively. These fees are eliminated in consolidation — see the other income line in the Consolidated MIEs column under *“Results of Operations — Segmented Statement of Earnings.”* Excluding amounts eliminated in consolidation, AFG recorded other income outside of its insurance operations of $11 million in 2013 compared to $4 million in 2012 and $6 million in 2011. Results for 2012 include a loss related to the sale of fixed assets of $7 million.

Holding Company and Other — Interest Charges on Borrowed Money
AFG's holding companies and other operations outside of its insurance operations recorded interest expense of $68 million in 2013 compared to $71 million in 2012, a decrease of $3 million (4%). In 2012, AFG issued new Senior Notes and used the proceeds to redeem higher rate debt.

AFG's holding companies and other operations outside of its insurance operations recorded interest expense of $71 million in 2012 compared to $69 million in 2011, an increase of $2 million (3%).

Holding Company and Other — Other Expenses
As a result of the comprehensive study of A&E exposures discussed under *“Uncertainties — Asbestos and Environmental-related (“A&E”) Insurance Reserves,”* AFG’s holding companies and other operations outside of its insurance operations recorded non-core special charges of $22 million, $2 million and $9 million in 2013, 2012 and 2011, respectively, to increase liabilities related to the A&E exposures of AFG’s former railroad and manufacturing operations. The 2013 charge resulted primarily from slightly higher estimated operation and maintenance costs at sites where remediation is underway, coupled with higher estimated cleanup costs at a limited number of sites. In 2012, these operations also recorded a $15 million non-core charge resulting from an adverse judgment in a long-standing labor contract dispute related to AFG’s former railroad operations and an $8 million non-core loss on the retirement of debt.

Excluding the non-core charges, AFG's holding companies and other operations outside of its insurance operations recorded other expenses of $135 million in 2013, $116 million in 2012 and $107 million in 2011. The $19 million (16%) increase in 2013 compared to 2012 and the $9 million (8%) increase in 2012 compared to 2011 reflect the impact of higher holding company expenses, primarily related to employee benefit plans that are tied to stock market performance and certain share-based incentive plans.

Consolidated Realized Gains (Losses) on Securities AFG's consolidated realized gains on securities, which are not allocated to segments, were $221 million in 2013 compared to $210 million in 2012, an increase of $11 million (5%). AFG's consolidated realized gains on securities were $210 million in 2012 compared to $76 million in 2011, an increase of $134 million (176%). Realized gains (losses) on securities consisted of the following (in millions):

	Year ended December 31,		
	2013	2012	2011
Realized gains (losses) before impairments:			
Disposals	$ 233	$ 243	$ 156
Change in the fair value of derivatives	1	1	(24)
Adjustments to annuity deferred policy acquisition costs and related items	(1)	(8)	(4)
	233	236	128
Impairment charges:			
Securities	(15)	(33)	(68)
Adjustments to annuity deferred policy acquisition costs and related items	3	7	16
	(12)	(26)	(52)
Realized gains on securities	$ 221	$ 210	$ 76

Realized gains on disposals include gains on sales of shares of Verisk Analytics, Inc. of $49 million, $93 million and $76 million in 2013, 2012 and 2011, respectively.

Consolidated Income Taxes AFG's consolidated provision for income taxes was $236 million in 2013 compared to $135 million in 2012, an increase of $101 million (75%). The provision for income taxes recorded in 2012 includes a $67 million non-core tax benefit related to the favorable resolution of certain tax litigation and settlement of open tax years. AFG's consolidated provision for income taxes was $135 million in 2012 compared to $239 million in 2011, a decrease of $104 million (44%). See *Note L — "Income Taxes"* to the financial statements for an analysis of items affecting AFG's effective tax rate.

Consolidated Noncontrolling Interests AFG's consolidated net loss attributable to noncontrolling interests was $18 million in 2013 compared to $86 million in 2012, a decrease of $68 million (79%). AFG's consolidated net loss attributable to noncontrolling interests was $86 million in 2012 compared to $23 million in 2011, an increase of $63 million (274%). The following table details net earnings (loss) in consolidated subsidiaries attributable to holders other than AFG (dollars in millions):

	Year ended December 31,			% Change	
	2013	2012	2011	2013 - 2012	2012 - 2011
National Interstate	$ 8	$ 16	$ 15	(50%)	7%
Marketform	—	(4)	(15)	(100%)	(73%)
Managed Investment Entities	(26)	(98)	(24)	(73%)	308%
Other	—	—	1	—%	(100%)
Loss attributable to noncontrolling interests	$ (18)	$ (86)	$ (23)	(79%)	274%

During the third quarter of 2012, AFG acquired the remaining 28% of Marketform that it did not already own. Marketform's losses reflect adverse reserve development in its run-off Italian public hospital medical malpractice business. As discussed in *Note A* — "*Accounting Policies*" and *Note H* — "*Managed Investment Entities*" to the financial statements, the losses of Managed Investment Entities in 2013, 2012 and 2011 represent CLO losses that ultimately inure to holders of CLO debt other than AFG.

NEW ACCOUNTING STANDARDS

See *Note A — "Accounting Policies — Accounting Standard Adopted in 2013"* to the financial statements for a discussion of a recent accounting standard adopted by AFG.

ITEM 7A

Quantitative and Qualitative Disclosures about Market Risk

Market risk represents the potential economic loss arising from adverse changes in the fair value of financial instruments. AFG’s exposures to market risk relate primarily to its investment portfolio and annuity contracts, which are exposed to interest rate risk and, to a lesser extent, equity price risk. To a much lesser extent, AFG’s long-term debt is also exposed to interest rate risk.

Fixed Maturity Portfolio The fair value of AFG’s fixed maturity portfolio is directly impacted by changes in market interest rates. AFG’s fixed maturity portfolio is comprised of primarily fixed rate investments with intermediate-term maturities. This practice is designed to allow flexibility in reacting to fluctuations of interest rates. The portfolios of AFG’s insurance operations are managed with an attempt to achieve an adequate risk-adjusted return while maintaining sufficient liquidity to meet policyholder obligations. AFG’s annuity and run-off long-term care and life operations attempt to align the duration of their invested assets to the projected cash flows of policyholder liabilities.

Consistent with the discussion in *Item 7 — Management’s Discussion and Analysis — “Investments,”* the following table demonstrates the sensitivity of the fair value of AFG’s fixed maturity portfolio to reasonably likely changes in interest rates by illustrating the estimated effect on AFG’s fixed maturity portfolio that an immediate increase of 100 basis points in the interest rate yield curve would have at December 31 (based on the duration of the portfolio, dollars in millions). Increases or decreases from the 100 basis points illustrated would be approximately proportional.

	2013	2012
Fair value of fixed maturity portfolio	$ 26,761	$ 24,439
Pretax impact on fair value of 100 bps increase in interest rates	$ (1,204)	$ (1,124)
Pretax impact as % of total fixed maturity portfolio	(4.5%)	(4.6%)

European Debt Exposure Certain European countries, including the so-called “peripheral countries” (Greece, Portugal, Ireland, Italy and Spain) have been experiencing varying degrees of financial stress over the past few years and there remains uncertainty as to future developments and the impact on global financial markets. At December 31, 2013, less than 5% of AFG’s cash and investments consisted of European debt and AFG owned no sovereign debt issued by the peripheral countries.

Annuity Contracts Substantially all of AFG’s fixed rate annuity contracts permit AFG to change crediting rates (subject to minimum interest rate guarantees as determined by applicable law) enabling management to react to changes in market interest rates. In late 2003, AFG began issuing products with guaranteed minimum interest rates (”GMIRs”) of less than 2% in states where required approvals have been received. The GMIR on virtually all new product sales since 2010 is 1%. At December 31, 2013, AFG is able to reduce the average crediting rate of its $16 billion of traditional and fixed-indexed annuities without guaranteed withdrawal benefits by approximately 48 basis points (on a weighted average basis).

As presented in *Item* 7 — *Management’s Discussion and Analysis — “Results of Operations — Years ended December 31, 2013, 2012 and 2011” — “Net Spread on Fixed Annuities”,* the weighted average interest credited rate on AFG’s in-force block of fixed annuities was 2.41% for the year ended December 31, 2013. Management estimates that the interest credited rate on this in-force business will increase to approximately 2.50% over the next five years. This rate reflects actuarial assumptions as to (i) expected investment spreads, (ii) deaths, (iii) annuitizations, (iv) surrenders and other withdrawals and (v) renewal premiums. Actual experience and changes in actuarial assumptions may result in different effective crediting rates than those above. The current stated crediting rates (excluding bonus interest) on new sales of AFG’s fixed annuity products generally range from 1.0% to 2.0%.

Actuarial assumptions used to estimate DPAC and certain annuity liabilities, as well as AFG’s ability to maintain spread, could be impacted if a low interest rate environment continues for an extended period, or if increases in interest rates cause policyholder behavior to differ significantly from current expectations.

Projected payments (in millions) in each of the subsequent five years and for all years thereafter on AFG's fixed annuity liabilities at December 31 were as follows.

	First	Second	Third	Fourth	Fifth	Thereafter	Total	Fair Value (*)
2013	$ 1,808	$ 2,071	$ 2,248	$ 2,303	$ 2,356	$ 10,158	$ 20,944	$ 19,959
2012	1,669	1,656	1,803	1,899	1,905	8,677	17,609	17,588

(*) Fair value excludes life contingent annuities in the payout phase (carrying value of $203 million and $204 million at December 31, 2013 and 2012, respectively).

AFG's fixed-indexed annuities represented approximately 47% of annuity benefits accumulated at December 31, 2013. These annuities provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase of call options on the appropriate index. AFG's strategy is designed so that an increase in the liabilities, due to an increase in the market index, will generally be offset by unrealized and realized gains on the call options purchased by AFG. Both the index-based component of the annuities and the related call options are considered derivatives that must be marked to market through earnings each period. See *Note D — "Fair Value Measurements"* and *Note F — "Derivatives"* to the financial statements for a discussion of these derivatives.

Long-Term Debt The following table shows scheduled principal payments on fixed-rate long-term debt of AFG and its subsidiaries and related weighted average interest rates for each of the subsequent five years and for all years thereafter (dollars in millions):

	December 31, 2013			December 31, 2012	
	Scheduled Principal Payments	Rate		Scheduled Principal Payments	Rate
2014	$ 2	5.9%	2013	$ 1	5.9%
2015	14	5.7%	2014	2	5.9%
2016	45	6.1%	2015	14	5.7%
2017	—	—%	2016	45	6.1%
2018	—	—%	2017	—	—%
Thereafter	840	7.9%	Thereafter	840	7.9%
Total	$ 901	7.7%	Total	$ 902	7.7%
Fair Value	$ 973		Fair Value	$ 1,034	

National Interstate had $12 million in borrowings outstanding under a bank credit facility at December 31, 2013 and 2012. No amounts were outstanding under AFG's bank credit facility at December 31, 2013 or 2012.

ITEM 8

Financial Statements and Supplementary Data

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Selected Quarterly Financial Data has been included in *Note N* to the Consolidated Financial Statements.

ITEM 9A

Controls and Procedures

AFG's management, with participation of its Co-Chief Executive Officers and its principal financial officer, has evaluated AFG's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15) as of the end of the period covered by this report. Based on that evaluation, AFG's Co-CEOs and principal financial officer concluded that the controls and procedures are effective. There have been no changes in AFG's internal control over financial reporting during the fourth fiscal quarter of 2013 that materially affected, or are reasonably likely to materially affect, AFG's internal control over financial reporting.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

AFG's management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Securities Exchange Act Rules 13a-15(f). Under the supervision and with the participation of management, including AFG's principal executive officers and principal financial officer, AFG conducted an evaluation of the effectiveness of internal control over financial reporting as of December 31, 2013, based on the criteria set forth in "Internal Control — Integrated Framework" issued in 1992 by the Committee of Sponsoring Organizations of the Treadway Commission.

There are inherent limitations to the effectiveness of any system of internal controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective internal controls and procedures can only provide reasonable assurance of achieving their control objectives.

Based on AFG's evaluation, management concluded that internal control over financial reporting was effective as of December 31, 2013. The attestation report of AFG's independent registered public accounting firm on AFG's internal control over financial reporting as of December 31, 2013, is set forth below.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Board of Directors and Shareholders
American Financial Group, Inc.

We have audited American Financial Group, Inc. and subsidiaries' (the Company's) internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) (the COSO criteria). The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, American Financial Group, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of American Financial Group, Inc. and subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of earnings, comprehensive income, changes in equity and cash flows for each of the three years in the period ended December 31, 2013, and our report dated February 28, 2014, expressed an unqualified opinion thereon.

/s/ ERNST & YOUNG LLP

Cincinnati, Ohio
February 28, 2014

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
American Financial Group, Inc.

We have audited the accompanying consolidated balance sheets of American Financial Group, Inc. and subsidiaries (the Company) as of December 31, 2013 and 2012, and the related consolidated statements of earnings, comprehensive income, changes in equity and cash flows for each of the three years in the period ended December 31, 2013. Our audits also included the financial statement schedules listed in the Index at Item 15(a). These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of American Financial Group, Inc. and subsidiaries at December 31, 2013 and 2012 and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), American Financial Group, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) and our report dated February 28, 2014 expressed an unqualified opinion thereon.

/s/ ERNST & YOUNG LLP

Cincinnati, Ohio
February 28, 2014

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIAIRIES
CONSOLIDATED BALANCE SHEET
(Dollars in Millions)

	December 31,	
	2013	2012
Assets:		
Cash and cash equivalents	$ 1,639	$ 1,705
Investments:		
Fixed maturities, available for sale at fair value (amortized cost — $25,366 and $22,083)	26,456	24,118
Fixed maturities, trading at fair value	305	321
Equity securities, at fair value (cost — $987 and $778)	1,179	939
Mortgage loans	781	607
Policy loans	238	228
Real estate and other investments	715	531
Total cash and investments	31,313	28,449
Recoverables from reinsurers	3,157	3,750
Prepaid reinsurance premiums	408	471
Agents’ balances and premiums receivable	739	636
Deferred policy acquisition costs	975	550
Assets of managed investment entities	2,888	3,225
Other receivables	854	539
Variable annuity assets (separate accounts)	665	580
Other assets	903	786
Goodwill	185	185
Total assets	$ 42,087	$ 39,171
Liabilities and Equity:		
Unpaid losses and loss adjustment expenses	$ 6,410	$ 6,845
Unearned premiums	1,757	1,651
Annuity benefits accumulated	20,944	17,609
Life, accident and health reserves	2,008	2,059
Payable to reinsurers	508	475
Liabilities of managed investment entities	2,567	2,892
Long-term debt	913	953
Variable annuity liabilities (separate accounts)	665	580
Other liabilities	1,546	1,359
Total liabilities	37,318	34,423
Shareholders’ equity:		
Common Stock, no par value — 200,000,000 shares authorized — 89,513,386 and 88,979,303 shares outstanding	90	89
Capital surplus	1,123	1,063
Retained earnings:		
Appropriated — managed investment entities	49	75
Unappropriated	2,777	2,520
Accumulated other comprehensive income, net of tax	560	831
Total shareholders’ equity	4,599	4,578
Noncontrolling interests	170	170
Total equity	4,769	4,748
Total liabilities and equity	$ 42,087	$ 39,171

See notes to consolidated financial statements.

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIAIRIES
CONSOLIDATED STATEMENT OF EARNINGS
(In Millions, Except Per Share Data)

	Year ended December 31,		
	2013	2012	2011
Revenues:			
Property and casualty insurance net earned premiums	$ 3,204	$ 2,847	$ 2,759
Life, accident and health net earned premiums	114	318	430
Net investment income	1,346	1,301	1,225
Realized gains (losses) on:			
Securities (*)	221	210	76
Subsidiaries	(4)	161	(3)
Income (loss) of managed investment entities:			
Investment income	128	125	105
Loss on change in fair value of assets/liabilities	(14)	(94)	(33)
Other income	97	89	84
Total revenues	5,092	4,957	4,643
Costs and Expenses:			
Property and casualty insurance:			
Losses and loss adjustment expenses	2,040	1,873	1,744
Commissions and other underwriting expenses	1,019	887	835
Annuity benefits	531	541	510
Life, accident and health benefits	160	356	360
Annuity and supplemental insurance acquisition expenses	167	282	195
Interest charges on borrowed money	71	75	74
Expenses of managed investment entities	89	80	71
Other expenses	326	326	296
Total costs and expenses	4,403	4,420	4,085
Earnings before income taxes	689	537	558
Provision for income taxes	236	135	239
Net earnings, including noncontrolling interests	453	402	319
Less: Net earnings (loss) attributable to noncontrolling interests	(18)	(86)	(23)
Net Earnings Attributable to Shareholders	$ 471	$ 488	$ 342
Earnings Attributable to Shareholders per Common Share:			
Basic	$ 5.27	$ 5.18	$ 3.37
Diluted	$ 5.16	$ 5.09	$ 3.32
Average number of Common Shares:			
Basic	89.3	94.2	101.3
Diluted	91.2	95.9	102.9
Cash dividends per Common Share	$ 1.805	$ 0.97	$ 0.6625

(*) Consists of the following:			
Realized gains before impairments	$ 233	$ 236	$ 128
Losses on securities with impairment	(14)	(27)	(31)
Non-credit portion recognized in other comprehensive income (loss)	2	1	(21)
Impairment charges recognized in earnings	(12)	(26)	(52)
Total realized gains on securities	$ 221	$ 210	$ 76

See notes to consolidated financial statements.

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIAIRIES
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(In Millions)

	Year ended December 31,		
	2013	2012	2011
Net earnings, including noncontrolling interests	$ 453	$ 402	$ 319
Other comprehensive income (loss), net of tax:			
Net unrealized gains (losses) on securities:			
Unrealized holding gains (losses) on securities arising during the period	(122)	408	161
Reclassification adjustment for realized gains included in net earnings	(144)	(138)	(68)
Reclassification adjustment for unrealized gains of subsidiaries sold	—	(18)	(1)
Total net unrealized gains (losses) on securities	(266)	252	92
Foreign currency translation adjustments	(13)	6	(1)
Pension and other postretirement plans adjustments	2	2	—
Other comprehensive income (loss), net of tax	(277)	260	91
Total comprehensive income, net of tax	176	662	410
Less: Comprehensive income (loss) attributable to noncontrolling interests	(24)	(78)	(17)
Comprehensive income attributable to shareholders	$ 200	$ 740	$ 427

See notes to consolidated financial statements.

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIAIRIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(Dollars in Millions)

		Shareholders' Equity						
	Common	Common Stock and Capital	Retained Earnings		Accumulated Other Comp		Noncon-trolling	Total
	Shares	Surplus	Approp.	Unapprop.	Inc. (Loss)	Total	Interests	Equity
Balance at December 31, 2010	105,168,366	$ 1,271	$ 197	$ 2,368	$ 495	$ 4,331	$ 150	$ 4,481
Net earnings	—	—	—	342	—	342	(23)	319
Other comprehensive income	—	—	—	—	85	85	6	91
Allocation of losses of managed investment entities	—	—	(24)	—	—	(24)	24	—
Dividends on Common Stock	—	—	—	(69)	—	(69)	—	(69)
Shares issued:								
Exercise of stock options	1,576,664	38	—	—	—	38	—	38
Other benefit plans	387,746	9	—	—	—	9	—	9
Dividend reinvestment plan	15,763	1	—	—	—	1	—	1
Stock-based compensation expense	—	14	—	—	—	14	—	14
Shares acquired and retired	(9,281,386)	(113)	—	(202)	—	(315)	—	(315)
Shares exchanged — benefit plans	(20,751)	(1)	—	—	—	(1)	—	(1)
Other	—	—	—	—	—	—	(11)	(11)
Balance at December 31, 2011	97,846,402	$ 1,219	$ 173	$ 2,439	$ 580	$ 4,411	$ 146	$ 4,557
Net earnings	—	—	—	488	—	488	(86)	402
Other comprehensive income	—	—	—	—	252	252	8	260
Allocation of losses of managed investment entities	—	—	(98)	—	—	(98)	98	—
Dividends on Common Stock	—	—	—	(91)	—	(91)	—	(91)
Shares issued:								
Exercise of stock options	1,702,782	45	—	—	—	45	—	45
Other benefit plans	308,352	7	—	—	—	7	—	7
Dividend reinvestment plan	21,484	1	—	—	—	1	—	1
Stock-based compensation expense	—	18	—	—	—	18	—	18
Shares acquired and retired	(10,864,184)	(137)	—	(278)	—	(415)	—	(415)
Shares exchanged — benefit plans	(35,533)	(1)	—	—	—	(1)	—	(1)
Other	—	—	—	(38)	(1)	(39)	4	(35)
Balance at December 31, 2012	88,979,303	$ 1,152	$ 75	$ 2,520	$ 831	$ 4,578	$ 170	$ 4,748
Net earnings	—	—	—	471	—	471	(18)	453
Other comprehensive income (loss)	—	—	—	—	(271)	(271)	(6)	(277)
Allocation of losses of managed investment entities	—	—	(26)	—	—	(26)	26	—
Dividends on Common Stock	—	—	—	(161)	—	(161)	—	(161)
Shares issued:								
Exercise of stock options	1,625,023	53	—	—	—	53	—	53
Other benefit plans	388,043	7	—	—	—	7	—	7
Dividend reinvestment plan	28,147	2	—	—	—	2	—	2
Stock-based compensation expense	—	19	—	—	—	19	—	19
Shares acquired and retired	(1,448,156)	(19)	—	(51)	—	(70)	—	(70)
Shares exchanged — benefit plans	(58,974)	(1)	—	(2)	—	(3)	—	(3)
Other	—	—	—	—	—	—	(2)	(2)
Balance at December 31, 2013	89,513,386	$ 1,213	$ 49	$ 2,777	$ 560	$ 4,599	$ 170	$ 4,769

See notes to consolidated financial statements.

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIAIRIES
CONSOLIDATED STATEMENT OF CASH FLOWS
(In Millions)

	Year ended December 31,		
	2013	2012	2011
Operating Activities:			
Net earnings, including noncontrolling interests	$ 453	$ 402	$ 319
Adjustments:			
Depreciation and amortization	142	257	180
Annuity benefits	531	541	510
Realized gains on investing activities	(230)	(367)	(74)
Net (purchases) sales of trading securities	2	17	(45)
Deferred annuity and life policy acquisition costs	(222)	(212)	(239)
Change in:			
Reinsurance and other receivables	176	(495)	(228)
Other assets	(149)	(51)	(101)
Insurance claims and reserves	(200)	918	134
Payable to reinsurers	51	—	155
Other liabilities	280	(180)	245
Managed investment entities’ assets/liabilities	(98)	(21)	(212)
Other operating activities, net	24	8	23
Net cash provided by operating activities	760	817	667
Investing Activities:			
Purchases of:			
Fixed maturities	(6,690)	(4,458)	(5,321)
Equity securities	(461)	(281)	(397)
Mortgage loans	(274)	(269)	(190)
Real estate, property and equipment	(52)	(71)	(86)
Proceeds from:			
Maturities and redemptions of fixed maturities	3,236	2,262	1,974
Repayments of mortgage loans	102	46	269
Sales of fixed maturities	275	632	1,293
Sales of equity securities	434	437	198
Sales of real estate, property and equipment	34	4	3
Sales of subsidiaries	—	322	9
Cash and cash equivalents of businesses sold	(5)	(34)	(5)
Managed investment entities:			
Purchases of investments	(1,426)	(1,849)	(1,563)
Proceeds from sales and redemptions of investments	1,904	1,857	1,391
Other investing activities, net	8	(23)	(14)
Net cash used in investing activities	(2,915)	(1,425)	(2,439)
Financing Activities:			
Annuity receipts	4,233	2,993	3,326
Annuity surrenders, benefits and withdrawals	(1,588)	(1,504)	(1,321)
Net transfers from variable annuity assets	32	36	39
Additional long-term borrowings	—	372	2
Reductions of long-term debt	(40)	(365)	(20)
Issuances of managed investment entities’ liabilities	1,192	781	394
Retirement of managed investment entities’ liabilities	(1,560)	(830)	(66)
Issuances of Common Stock	54	46	39
Repurchases of Common Stock	(70)	(415)	(315)
Cash dividends paid on Common Stock	(160)	(90)	(67)
Other financing activities, net	(4)	(35)	(14)
Net cash provided by financing activities	2,089	989	1,997
Net Change in Cash and Cash Equivalents	(66)	381	225
Cash and cash equivalents at beginning of year	1,705	1,324	1,099
Cash and cash equivalents at end of year	$ 1,639	$ 1,705	$ 1,324

See notes to consolidated financial statements.

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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A. Accounting Policies

Basis of Presentation The consolidated financial statements include the accounts of American Financial Group, Inc. ("AFG") and its subsidiaries. Certain reclassifications have been made to prior years to conform to the current year's presentation, primarily the reclassification of investment expenses and real estate income and expenses to net investment income. All significant intercompany balances and transactions have been eliminated. The results of operations of companies since their formation or acquisition are included in the consolidated financial statements. Events or transactions occurring subsequent to December 31, 2013, and prior to the filing of this Form 10-K, have been evaluated for potential recognition or disclosure herein.

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Changes in circumstances could cause actual results to differ materially from those estimates.

Accounting Standard Adopted in 2013 Effective January 1, 2013, AFG prospectively adopted Accounting Standards Update ("ASU") 2013-02, which requires companies to disclose, in a single location within the financial statements or footnotes, reclassifications out of accumulated other comprehensive income ("AOCI") separately for each component of other comprehensive income. For significant reclassifications, the disclosure is required to include the respective line items in net earnings affected by the reclassification. Disclosures required by the guidance are included in *Note K — "Shareholders' Equity."* This new disclosure requirement had no impact on AFG's results of operations or financial position.

Fair Value Measurements Accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants on the measurement date. The standards establish a hierarchy of valuation techniques based on whether the assumptions that market participants would use in pricing the asset or liability ("inputs") are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect AFG's assumptions about the assumptions market participants would use in pricing the asset or liability. AFG did not have any significant nonrecurring fair value measurements of nonfinancial assets and liabilities in 2013 or 2012.

Investments Fixed maturity and equity securities classified as "available for sale" are reported at fair value with unrealized gains and losses included in AOCI in AFG's Balance Sheet. Fixed maturity and equity securities classified as "trading" are reported at fair value with changes in unrealized holding gains or losses during the period included in net investment income. Mortgage and policy loans are carried primarily at the aggregate unpaid balance.

Premiums and discounts on fixed maturity securities are amortized using the interest method; mortgage-backed securities ("MBS") are amortized over a period based on estimated future principal payments, including prepayments. Prepayment assumptions are reviewed periodically and adjusted to reflect actual prepayments and changes in expectations.

Gains or losses on securities are determined on the specific identification basis. When a decline in the value of a specific investment is considered to be other-than-temporary at the balance sheet date, a provision for impairment is charged to earnings (included in realized gains (losses) on securities) and the cost basis of that investment is reduced. If management can assert that it does not intend to sell an impaired fixed maturity security and it is not more likely than not that it will have to sell the security

before recovery of its amortized cost basis, then the other-than-temporary impairment is separated into two components: (i) the amount related to credit losses (recorded in earnings) and (ii) the amount related to all other factors (recorded in other comprehensive income). The credit-related portion of an other-than-temporary impairment is measured by comparing a security's amortized cost to the present value of its current expected cash flows discounted at its effective yield prior to the impairment charge. Both components are shown in the Statement of Earnings. If management intends to sell an impaired security, or it is more likely than not that it will be required to sell the security before recovery, an impairment charge to earnings is recorded to reduce the amortized cost of that security to fair value.

Derivatives Derivatives included in AFG's Balance Sheet are recorded at fair value and consist primarily of (i) components of certain fixed maturity securities (primarily interest-only MBS) and (ii) the equity-based component of certain annuity products (included in annuity benefits accumulated) and related call options (included in other investments) designed to be consistent with the characteristics of the liabilities and used to mitigate the risk embedded in those annuity products. Changes in the fair value of derivatives are included in earnings.

Goodwill Goodwill represents the excess of cost of subsidiaries over AFG's equity in their underlying net assets. Goodwill is not amortized, but is subject to an impairment test at least annually. An entity is not required to complete the quantitative annual goodwill impairment test on a reporting unit if the entity elects to perform a qualitative analysis and determines that it is more likely than not that the reporting unit's fair value exceeds its carrying amount.

Reinsurance Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policies. AFG's property and casualty insurance subsidiaries report as assets (i) the estimated reinsurance recoverable on paid and unpaid losses, including an estimate for losses incurred but not reported, and (ii) amounts paid or due to reinsurers applicable to the unexpired terms of policies in force. Payable to reinsurers includes ceded premiums due to reinsurers as well as ceded premiums retained by AFG's property and casualty insurance subsidiaries under contracts to fund ceded losses as they become due. AFG's insurance subsidiaries also assume reinsurance from other companies. Earnings on reinsurance assumed is recognized based on information received from ceding companies.

A subsidiary cedes life insurance policies to a third party on a funds withheld basis whereby the subsidiary retains the assets (securities) associated with the reinsurance contract. Interest is credited to the reinsurer based on the actual investment performance of the retained assets. This reinsurance contract is considered to contain an embedded derivative (that must be adjusted to fair value) because the yield on the payable is based on a specific block of the ceding company's assets, rather than the overall creditworthiness of the ceding company. AFG determined that changes in the fair value of the underlying portfolio of fixed maturity securities is an appropriate measure of the value of the embedded derivative. The securities related to this contract are classified as "trading." The adjustment to fair value on the embedded derivative offsets the investment income recorded on the adjustment to fair value of the related trading portfolio.

Deferred Policy Acquisition Costs ("DPAC") Policy acquisition costs (principally commissions, premium taxes and certain underwriting and policy issuance costs) directly related to the successful acquisition or renewal of an insurance contract are deferred. DPAC also includes capitalized costs associated with sales inducements offered to fixed annuity policyholders such as enhanced interest rates and premium and persistency bonuses.

For the property and casualty companies, DPAC is limited based upon recoverability without any consideration for anticipated investment income and is charged against income ratably over the terms of the related policies. A premium deficiency is recognized if the sum of expected claims costs, claims adjustment expenses and unamortized acquisition costs exceed the related unearned premiums. A premium deficiency is first recognized by charging any unamortized acquisition costs to expense to the extent required to eliminate the deficiency. If the premium deficiency is greater than unamortized acquisition costs, a liability is accrued for the excess deficiency and reported with unpaid losses and loss adjustment expenses.

DPAC related to annuities is deferred to the extent deemed recoverable and amortized, with interest, in relation to the present value of actual and expected gross profits on the policies. Expected gross profits consist principally of estimated future investment margin (estimated future net investment income less interest credited on policyholder funds) and surrender, mortality, and other life and annuity policy charges, less death, annuitization and guaranteed withdrawal benefits in excess of account balances and estimated future policy administration expenses. To the extent that realized gains and losses result in adjustments to the amortization of DPAC related to annuities, such adjustments are reflected as components of realized gains (losses) on securities.

DPAC related to traditional life and health insurance is amortized over the expected premium paying period of the related policies, in proportion to the ratio of annual premium revenues to total anticipated premium revenues. See *"Life, Accident and Health Reserves"* below for details on the impact of loss recognition on the accounting for traditional life and health insurance contracts.

DPAC includes the present value of future profits on business in force of annuity and life, accident and health insurance companies acquired ("PVFP"). PVFP represents the portion of the costs to acquire companies that is allocated to the value of the right to receive future cash flows from insurance contracts existing at the date of acquisition. PVFP is amortized with interest in relation to expected gross profits of the acquired policies for annuities and universal life products and in relation to the premium paying period for traditional life and health insurance products.

DPAC and certain other balance sheet amounts related to annuity, long-term care and life businesses are also adjusted, net of tax, for the change in expense that would have been recorded if the unrealized gains (losses) from securities had actually been realized. These adjustments are included in unrealized gains (losses) on marketable securities, a component of AOCI in AFG's Balance Sheet.

Managed Investment Entities A company is considered the primary beneficiary of, and therefore must consolidate, a variable interest entity ("VIE") based primarily on its ability to direct the activities of the VIE that most significantly impact that entity's economic performance and the obligation to absorb losses of, or receive benefits from, the entity that could potentially be significant to the VIE.

AFG manages, and has investments in, collateralized loan obligations ("CLOs") that are VIEs (see *Note H — "Managed Investment Entities"*). Both the management fees (payment of which is subordinate to other obligations of the CLOs) and the investments in the CLOs are considered variable interests. AFG has determined that it is the primary beneficiary of the CLOs because (i) its role as asset manager gives it the power to direct the activities that most significantly impact the economic performance of the CLOs and (ii) it has exposure to CLO losses (through its investments in the CLO debt tranches) and the right to receive benefits (through its subordinated management fees and returns on its investments), both of which could potentially be significant to the CLOs.

Because AFG has no right to use the CLO assets and no obligation to pay the CLO liabilities, the assets and liabilities of the CLOs are shown separately in AFG's Balance Sheet (at fair value). AFG has elected the fair value option for reporting on the CLO assets and liabilities to improve the transparency of financial reporting related to the CLOs. The excess of fair value of the CLOs' assets over the fair value of the liabilities is recorded in AFG's Balance Sheet as appropriated retained earnings — managed investment entities, representing amounts that ultimately will inure to the benefit of the CLO debt holders.

The net gain or loss from accounting for the CLO assets and liabilities at fair value is separately presented in AFG's Statement of Earnings. CLO earnings attributable to AFG's shareholders represent the change in fair value of AFG's investments in the CLOs (including distributions) and management fees earned. All other CLO earnings (losses) are not attributable to AFG's shareholders and will ultimately inure to the benefit of the CLO debt holders. As a result, such CLO earnings (losses) are included in net earnings (loss) attributable to noncontrolling interests in AFG's Statement of Earnings and in appropriated retained earnings — managed investment entities in the Balance Sheet. As the CLOs approach maturity (2016 to 2026), it is expected that losses attributable to noncontrolling interests will reduce appropriated retained earnings towards zero as the fair values of the assets and liabilities converge and the CLO assets are used to pay the CLO debt.

At December 31, 2012, assets and liabilities of managed investment entities include $107 million in assets and $87 million in liabilities of a temporary warehousing entity that was established in connection with the formation of a new CLO that closed in April 2013. Upon closing, all warehoused assets were transferred to the new CLO and the liabilities were repaid.

Unpaid Losses and Loss Adjustment Expenses The net liabilities stated for unpaid claims and for expenses of investigation and adjustment of unpaid claims represent management's best estimate and are based upon (i) the accumulation of case estimates for losses reported prior to the close of the accounting period on direct business written; (ii) estimates received from ceding reinsurers and insurance pools and associations; (iii) estimates of unreported losses (including possible development on known claims) based on past experience; (iv) estimates based on experience of expenses for investigating and adjusting claims; and (v) the current state of the law and coverage litigation. Establishing reserves for asbestos, environmental and other mass tort claims involves considerably more judgment than other types of claims due to, among other things, inconsistent court decisions, an increase in bankruptcy filings as a result of asbestos-related liabilities, novel theories of coverage, and judicial interpretations that often expand theories of recovery and broaden the scope of coverage.

Loss reserve liabilities are subject to the impact of changes in claim amounts and frequency and other factors. Changes in estimates of the liabilities for losses and loss adjustment expenses are reflected in the Statement of Earnings in the period in which determined. Despite the variability inherent in such estimates, management believes that the liabilities for unpaid losses and loss adjustment expenses are adequate.

Annuity Benefits Accumulated Annuity receipts and benefit payments are recorded as increases or decreases in annuity benefits accumulated rather than as revenue and expense. Increases in this liability for interest credited are charged to expense and decreases for policy charges are credited to other income.

For certain products, annuity benefits accumulated also includes reserves for accrued persistency and premium bonuses, guaranteed withdrawals and excess benefits expected to be paid on future deaths and annuitizations ("EDAR"). The liabilities for EDAR and guaranteed withdrawals are accrued for and modified using assumptions consistent with those used in determining DPAC and DPAC amortization, except that amounts are determined in relation to the present value of total expected assessments. Total expected assessments consist principally of estimated future investment margin, surrender, mortality, and other life and annuity policy charges, and unearned revenues once they are recognized as income.

Annuity benefits accumulated also includes amounts advanced from the Federal Home Loan Bank of Cincinnati.

Unearned Revenue Certain upfront policy charges on annuities are deferred as unearned revenue (included in other liabilities) and recognized in net earnings using the same assumptions and estimated gross profits used to amortize DPAC.

Life, Accident and Health Reserves Liabilities for future policy benefits under traditional life, accident and health policies are computed using the net level premium method. Computations are based on the original projections of investment yields, mortality, morbidity and surrenders and include provisions for unfavorable deviations unless a loss recognition event (premium deficiency) occurs. Claim reserves and liabilities established for accident and health claims are modified as necessary to reflect actual experience and developing trends.

For long-duration contracts (such as traditional life and long-term care policies), loss recognition occurs when, based on current expectations as of the measurement date, existing contract liabilities plus the present value of future premiums (including reasonably expected rate increases) are not expected to cover the present value of future claims payments and related settlement and maintenance costs (excluding overhead) as well as unamortized acquisition costs. If a block of business is determined to be in loss recognition, a charge is recorded in earnings in an amount equal to the excess of the present value of expected future claims costs and unamortized acquisition costs over existing reserves plus the present value of expected future premiums (with no provision for adverse deviation). The charge is recorded first to reduce unamortized acquisition costs and then as an additional reserve (if unamortized acquisition costs have been reduced to zero).

In addition, reserves for traditional life and long-term care policies are subject to adjustment for loss recognition charges that would have been recorded if the unrealized gains from securities had actually been realized. This adjustment is included in unrealized gains (losses) on marketable securities, a component of AOCI in AFG's Balance Sheet.

Variable Annuity Assets and Liabilities Separate accounts related to variable annuities represent the fair value of deposits invested in underlying investment funds on which AFG earns a fee. Investment funds are selected and may be changed only by the policyholder, who retains all investment risk.

AFG's variable annuity contracts contain a guaranteed minimum death benefit ("GMDB") to be paid if the policyholder dies before the annuity payout period commences. In periods of declining equity markets, the GMDB may exceed the value of the policyholder's account. A GMDB liability is established for future excess death benefits using assumptions together with a range of reasonably possible scenarios for investment fund performance that are consistent with DPAC capitalization and amortization assumptions.

Premium Recognition Property and casualty premiums are earned generally over the terms of the policies on a pro rata basis. Unearned premiums represent that portion of premiums written which is applicable to the unexpired terms of policies in force. On reinsurance assumed from other insurance companies or written through various underwriting organizations, unearned premiums are based on information received from such companies and organizations. For traditional life, accident and health products, premiums are recognized as revenue when legally collectible from policyholders. For interest-sensitive life and

universal life products, premiums are recorded in a policyholder account, which is reflected as a liability. Revenue is recognized as amounts are assessed against the policyholder account for mortality coverage and contract expenses.

Noncontrolling Interests For Balance Sheet purposes, noncontrolling interests represents the interests of shareholders other than AFG in consolidated entities. In the Statement of Earnings, net earnings and losses attributable to noncontrolling interests represents such shareholders' interest in the earnings and losses of those entities.

Income Taxes Deferred income taxes are calculated using the liability method. Under this method, deferred income tax assets and liabilities are determined based on differences between financial reporting and tax bases and are measured using enacted tax rates. A valuation allowance is established to reduce total deferred tax assets to an amount that will more likely than not be realized.

AFG recognizes the tax benefits of uncertain tax positions only when the position is more likely than not to be sustained under examination by the appropriate taxing authority. Interest and penalties on AFG's reserve for uncertain tax positions are recognized as a component of tax expense.

Stock-Based Compensation All share-based grants are recognized as compensation expense on a straight-line basis over their vesting periods based on their calculated fair value at the date of grant. AFG uses the Black-Scholes pricing model to measure the fair value of employee stock options. See *Note K — "Shareholders' Equity"* for further information.

Benefit Plans AFG provides retirement benefits to qualified employees of participating companies through the AFG 401(k) Retirement and Savings Plan, a defined contribution plan. AFG makes all contributions to the retirement fund portion of the plan and matches a percentage of employee contributions to the savings fund. Company contributions are expensed in the year for which they are declared. AFG and many of its subsidiaries provide health care and life insurance benefits to eligible retirees. AFG also provides postemployment benefits to former or inactive employees (primarily those on disability) who were not deemed retired under other company plans. The projected future cost of providing these benefits is expensed over the period employees earn such benefits.

Earnings Per Share Although basic earnings per share only considers shares of common stock outstanding during the period, the calculation of diluted earnings per share includes the following adjustments to weighted average common shares related to stock-based compensation plans: 2013 – 1.9 million, 2012 – 1.7 million and 2011 – 1.6 million.

AFG's weighted average diluted shares outstanding excludes the following anti-dilutive potential common shares related to stock compensation plans: 2013 – 1.1 million, 2012 – 1.8 million and 2011 – 2.3 million. Adjustments to net earnings attributable to shareholders in the calculation of diluted earnings per share were nominal in the 2013, 2012 and 2011 periods.

Statement of Cash Flows For cash flow purposes, "investing activities" are defined as making and collecting loans and acquiring and disposing of debt or equity instruments and property and equipment. "Financing activities" include obtaining resources from owners and providing them with a return on their investments, borrowing money and repaying amounts borrowed. Annuity receipts, surrenders, benefits and withdrawals are also reflected as financing activities. All other activities are considered "operating." Short-term investments having original maturities of three months or less when purchased are considered to be cash equivalents for purposes of the financial statements.

B. Acquisitions and Sales of Subsidiaries

Medicare Supplement and Critical Illness Segment In August 2012, AFG completed the sale of its Medicare supplement and critical illness businesses, which included Loyal American Life Insurance Company and four other insurance companies, to Cigna Corporation for $326 million in cash resulting in a pretax gain of $170 million (including post-closing adjustments). Since the transaction includes the ongoing cessions of certain business to Cigna, the operations being sold are not reported as discontinued operations.

The impact of the August 2012 sale of the Medicare supplement and critical illness segment on AFG's financial statements is shown below (in millions):

Sale proceeds	$	326
Expenses		(11)
Net proceeds	$	315
Assets of businesses sold:		
Cash and investments	$	217
Deferred policy acquisition costs		108
Other assets		31
Total assets		356
Liabilities of businesses sold:		
Life, accident and health reserves		209
Other liabilities		2
Total liabilities		211
Net assets of businesses sold	$	145
Gain on sale of subsidiaries	$	170

Summarized Statement of Earnings information for the Medicare supplement and critical illness segment through the sale date is shown below (in millions):

	Year ended December 31,			
	2012 (*)		2011	
Total revenues	$	212	$	325
Total costs and expenses		184		291
Earnings before income taxes	$	28	$	34

(*) Reflects revenues and expenses through the end of August 2012.

Other Businesses During 2012, AFG acquired the outstanding 28% of Marketform, its London-based Lloyd's property and casualty insurance operation, that it did not already own for $17 million and sold an additional small annuity company for $7 million.

C. Segments of Operations

AFG manages its business as five segments: (i) Property and casualty insurance, (ii) Annuity, (iii) Run-off long-term care and life, (iv) Medicare supplement and critical illness (sold in August 2012) and (v) Other, which includes holding company assets and costs, and the assets and operations attributable to the noncontrolling interests of the managed investment entities.

AFG reports its property and casualty insurance business in the following Specialty sub-segments: (i) Property and transportation, which includes physical damage and liability coverage for buses, trucks and recreational vehicles, inland and ocean marine, agricultural-related products and other property coverages, (ii) Specialty casualty, which includes primarily excess and surplus, general liability, executive liability, umbrella and excess liability, customized programs for small to mid-sized businesses and workers' compensation, and (iii) Specialty financial, which includes risk management insurance programs for leasing and financing institutions (including collateral and lender-placed mortgage property insurance), surety and fidelity products and trade credit insurance. AFG's annuity business markets traditional fixed and fixed-indexed annuities in the retail, financial institutions and education markets. AFG's reportable segments and their components were determined based primarily upon similar economic characteristics, products and services.

Sales of property and casualty insurance outside of the United States represented 5% of AFG's revenues in 2013, 2012 and 2011.

The following tables (in millions) show AFG's assets, revenues and earnings before income taxes by segment and sub-segment.

	2013	2012	2011
Assets			
Property and casualty insurance (a)	$ 11,717	$ 12,163	$ 11,740
Annuity	24,294	20,909	18,245
Run-off long-term care and life	2,408	2,304	1,785
Medicare supplement and critical illness (b)	—	—	359
Other	3,668	3,795	3,709
Total assets	$ 42,087	$ 39,171	$ 35,838
Revenues			
Property and casualty insurance:			
Premiums earned:			
Specialty			
Property and transportation	$ 1,521	$ 1,423	$ 1,412
Specialty casualty	1,135	948	872
Specialty financial	469	405	408
Other specialty	79	71	67
Total premiums earned	3,204	2,847	2,759
Net investment income	263	275	291
Other income	15	24	26
Total property and casualty insurance	3,482	3,146	3,076
Annuity:			
Net investment income	1,034	976	859
Other income	67	52	43
Total annuity	1,101	1,028	902
Run-off long-term care and life	194	191	190
Medicare supplement and critical illness (b)	—	212	325
Other	98	9	77
Total revenues before realized gains (losses)	4,875	4,586	4,570
Realized gains on securities	221	210	76
Realized gains (losses) on subsidiaries	(4)	161	(3)
Total revenues	$ 5,092	$ 4,957	$ 4,643

(a) Not allocable to sub-segments.
(b) Sold in August 2012.

	2013	2012	2011
Earnings Before Income Taxes			
Property and casualty insurance:			
Underwriting:			
Specialty			
Property and transportation	$ 12	$ 19	$ 113
Specialty casualty	102	53	35
Specialty financial	67	44	65
Other specialty	25	15	18
Other lines (a)	(61)	(44)	(51)
Total underwriting	145	87	180
Investment and other income, net	230	235	262
Total property and casualty insurance	375	322	442
Annuity (b)	323	256	188
Run-off long-term care and life (c)	(10)	(157)	—
Medicare supplement and critical illness (d)	—	28	34
Other (e)	(216)	(283)	(179)
Total earnings before realized gains (losses) and income taxes	472	166	485
Realized gains on securities	221	210	76
Realized gains (losses) on subsidiaries	(4)	161	(3)
Total earnings before income taxes	$ 689	$ 537	$ 558

(a) Includes special charges to increase asbestos and environmental (“A&E”) reserves of $54 million, $31 million and $50 million in 2013, 2012 and 2011, respectively.

(b) Includes a $5 million charge in the second quarter of 2013 to cover expected assessments from state guaranty funds related to insolvency and liquidation of an unaffiliated life insurance company.

(c) Includes a loss recognition charge of $153 million in the fourth quarter of 2012.

(d) Sold in August 2012.

(e) Includes holding company expenses, special charges to increase A&E reserves ($22 million in 2013, $2 million in 2012 and $9 million in 2011) and losses of managed investment entities attributable to noncontrolling interests ($26 million in 2013, $98 million in 2012 and $24 million in 2011). Holding company expenses in 2012 also include an $8 million loss on retirement of debt and a $15 million charge for a labor matter related to AFG’s former railroad operations.

D. Fair Value Measurements

Accounting standards for measuring fair value are based on inputs used in estimating fair value. The three levels of the hierarchy are as follows:

Level 1 — Quoted prices for identical assets or liabilities in active markets (markets in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis). AFG's Level 1 financial instruments consist primarily of publicly traded equity securities and highly liquid government bonds for which quoted market prices in active markets are available and short-term investments of managed investment entities.

Level 2 — Quoted prices for similar instruments in active markets; quoted prices for identical or similar assets or liabilities in inactive markets (markets in which there are few transactions, the prices are not current, price quotations vary substantially over time or among market makers, or in which little information is released publicly); and valuations based on other significant inputs that are observable in active markets. AFG's Level 2 financial instruments include separate account assets, corporate and municipal fixed maturity securities, mortgage-backed securities ("MBS") and investments of managed investment entities priced using observable inputs. Level 2 inputs include benchmark yields, reported trades, corroborated broker/dealer quotes, issuer spreads and benchmark securities. When non-binding broker quotes can be corroborated by comparison to similar securities priced using observable inputs, they are classified as Level 2.

Level 3 — Valuations derived from market valuation techniques generally consistent with those used to estimate the fair values of Level 2 financial instruments in which one or more significant inputs are unobservable or when the market for a security exhibits significantly less liquidity relative to markets supporting Level 2 fair value measurements. The unobservable inputs may include management's own assumptions about the assumptions market participants would use based on the best information available in the circumstances. AFG's Level 3 is comprised of financial instruments, including liabilities of managed investment entities, whose fair value is estimated based on non-binding broker quotes or internally developed using significant inputs not based on, or corroborated by, observable market information.

AFG's management is responsible for the valuation process and uses data from outside sources (including nationally recognized pricing services and broker/dealers) in establishing fair value. AFG's internal investment professionals are a group of approximately 20 analysts whose primary responsibility is to manage AFG's investment portfolio. These professionals monitor individual investments as well as overall industries and are active in the financial markets on a daily basis. The group is led by AFG's chief investment officer, who reports directly to one of AFG's Co-CEOs. Valuation techniques utilized by pricing services and prices obtained from external sources are reviewed by AFG's internal investment professionals who are familiar with the securities being priced and the markets in which they trade to ensure the fair value determination is representative of an exit price. To validate the appropriateness of the prices obtained, these investment managers consider widely published indices (as benchmarks), recent trades, changes in interest rates, general economic conditions and the credit quality of the specific issuers. In addition, the Company communicates directly with the pricing service regarding the methods and assumptions used in pricing, including verifying, on a test basis, the inputs used by the service to value specific securities.

Assets and liabilities measured and carried at fair value in the financial statements are summarized below (in millions):

	Level 1	Level 2	Level 3	Total
December 31, 2013				
Assets:				
Available for sale ("AFS") fixed maturities:				
U.S. Government and government agencies	$ 147	$ 152	$ 15	$ 314
States, municipalities and political subdivisions	—	5,311	61	5,372
Foreign government	—	208	—	208
Residential MBS	—	3,994	316	4,310
Commercial MBS	—	2,696	28	2,724
Asset-backed securities ("ABS")	—	2,418	75	2,493
Corporate and other	28	10,672	335	11,035
Total AFS fixed maturities	175	25,451	830	26,456
Trading fixed maturities	—	305	—	305
Equity securities	1,023	125	31	1,179
Assets of managed investment entities ("MIE")	266	2,592	30	2,888
Variable annuity assets (separate accounts) (a)	—	665	—	665
Other investments — derivatives	—	274	—	274
Total assets accounted for at fair value	$ 1,464	$ 29,412	$ 891	$ 31,767
Liabilities:				
Liabilities of managed investment entities	$ 156	$ —	$ 2,411	$ 2,567
Derivatives in annuity benefits accumulated	—	—	804	804
Other liabilities — derivatives	—	10	—	10
Total liabilities accounted for at fair value	$ 156	$ 10	$ 3,215	$ 3,381
December 31, 2012				
Assets:				
Available for sale fixed maturities:				
U.S. Government and government agencies	$ 227	$ 141	$ 20	$ 388
States, municipalities and political subdivisions	—	4,410	58	4,468
Foreign government	—	260	—	260
Residential MBS	—	3,833	371	4,204
Commercial MBS	—	2,896	22	2,918
Asset-backed securities	—	1,387	253	1,640
Corporate and other	5	9,999	236	10,240
Total AFS fixed maturities	232	22,926	960	24,118
Trading fixed maturities	—	321	—	321
Equity securities	781	121	37	939
Assets of managed investment entities	256	2,929	40	3,225
Variable annuity assets (separate accounts) (a)	—	580	—	580
Other investments — derivatives	—	133	—	133
Total assets accounted for at fair value	$ 1,269	$ 27,010	$ 1,037	$ 29,316
Liabilities:				
Liabilities of managed investment entities	$ 147	$ —	$ 2,745	$ 2,892
Derivatives in annuity benefits accumulated	—	—	465	465
Other liabilities — derivatives	—	17	—	17
Total liabilities accounted for at fair value	$ 147	$ 17	$ 3,210	$ 3,374

(a) Variable annuity liabilities equal the fair value of variable annuity assets.

The transfers between Level 1 and Level 2 are reflected in the table below at fair value as of the end of the reporting period (dollars in millions):

	Year ended December 31,							
	Level 2 To Level 1 Transfers				Level 1 To Level 2 Transfers			
	2013		2012		2013		2012	
	# of Transfers	Fair Value	# of Transfers	Fair Value	# of Transfers	Fair Value	# of Transfers	Fair Value
Perpetual preferred stocks	15	$ 70	2	$ 16	2	$ 10	7	$ 41
Common stocks	2	35	—	—	—	—	—	—
Redeemable preferred stocks	3	21	1	2	—	—	—	—

The transfers from Level 2 to Level 1 are due to increases in trade frequency, resulting in trade data sufficient to warrant classification in Level 1. The transfers from Level 1 to Level 2 are due to decreases in trade frequency, resulting in lack of available trade data sufficient to warrant classification in Level 1. Approximately 3% of the total assets carried at fair value on December 31, 2013, were Level 3 assets. Approximately 78% ($699 million) of the Level 3 assets were priced using non-binding broker quotes, for which there is a lack of transparency as to the inputs used to determine fair value. Details as to the quantitative inputs are neither provided by the brokers nor otherwise reasonably obtainable by AFG. Since internally developed Level 3 asset fair values represent less than one-half of 1% of the total assets measured at fair value and less than 2% of AFG's shareholders' equity, changes in unobservable inputs used to determine internally developed fair values would not have a material impact on AFG's financial position.

The fair values of the liabilities of managed investment entities were determined using primarily non-binding broker quotes, which were reviewed by AFG's investment professionals. AFG's investment professionals are familiar with the cash flow models used by the brokers to determine the fair value of these liabilities and review the broker quotes based on their knowledge of the CLO market and the market for the underlying assets. Their review includes consideration of expected reinvestment, default and recovery rates on the assets supporting the CLO liabilities, as well as surveying general CLO liability fair values and analysis provided by third parties.

The only significant Level 3 assets or liabilities carried at fair value in the financial statements that were not measured using broker quotes are the derivatives embedded in AFG's fixed-indexed annuity liabilities, which are measured using a discounted cash flow approach and had a fair value of $804 million at December 31, 2013. The following table presents information about the unobservable inputs used by management in determining fair value of these embedded derivatives. See *Note F — "Derivatives."*

Unobservable Input	Range
Adjustment for insurance subsidiary's credit risk	0.50% – 1.75% over the risk free rate
Risk margin for uncertainty in cash flows	0.3% reduction in the discount rate
Surrenders	4% – 16% of indexed account value
Partial surrenders	2% – 6% of indexed account value
Annuitizations	1% – 2% of indexed account value
Deaths	1.5% – 2.5% of indexed account value
Budgeted option costs	2.5% – 4.0% of indexed account value

The range of adjustments for insurance subsidiary's credit risk reflects credit spread variations across the yield curve. The range of projected surrender rates reflects the specific surrender charges and other features of AFG's individual fixed-indexed annuity products with an expected range of 6% to 12% in the majority of future calendar years (4% to 16% over all periods). Increasing the budgeted option cost or risk margin for uncertainty in cash flows assumptions in the table above would increase the fair value of the fixed-indexed annuity embedded derivatives, while increasing any of the other unobservable inputs in the table above would decrease the fair value of the embedded derivatives.

Changes in balances of Level 3 financial assets and liabilities carried at fair value during 2013, 2012 and 2011 are presented below (in millions). The transfers into and out of Level 3 were due to changes in the availability of market observable inputs. All transfers are reflected in the table at fair value as of the end of the reporting period.

		Total realized/unrealized gains (losses) included in						
	Balance at December 31, 2012	Net income	Other comprehensive income (loss)	Purchases and issuances	Sales and settlements	Transfer into Level 3	Transfer out of Level 3	Balance at December 31, 2013
AFS fixed maturities:								
U.S. government agency	$ 20	$ (2)	$ (3)	$ —	$ —	$ —	$ —	$ 15
State and municipal	58	(1)	(2)	10	—	—	(4)	61
Residential MBS	371	5	24	6	(53)	86	(123)	316
Commercial MBS	22	(1)	(1)	—	—	8	—	28
Asset-backed securities	253	4	(3)	12	(57)	11	(145)	75
Corporate and other	236	1	(14)	113	(17)	24	(8)	335
Equity securities	37	(1)	6	53	(12)	—	(52)	31
Assets of MIE	40	(5)	—	8	(7)	—	(6)	30
Liabilities of MIE (a)	(2,745)	(26)	—	(727)	1,068	—	19	(2,411)
Embedded derivatives (b)	(465)	(182)	—	(192)	35	—	—	(804)

(a) Total realized/unrealized loss included in net income includes gains of $7 million related to liabilities outstanding as of December 31, 2013. See *Note H — “Managed Investment Entities.”*

(b) Total realized/unrealized loss included in net income for the embedded derivatives reflects gains related to the unlocking of actuarial assumptions of $2 million in 2013.

		Total realized/unrealized gains (losses) included in						
	Balance at December 31, 2011	Net income	Other comprehensive income (loss)	Purchases and issuances	Sales and settlements	Transfer into Level 3	Transfer out of Level 3	Balance at December 31, 2012
AFS fixed maturities:								
U.S. government agency	$ —	$ —	$ —	$ 20	$ —	$ —	$ —	$ 20
State and municipal	83	—	4	19	(7)	8	(49)	58
Residential MBS	361	5	17	96	(45)	228	(291)	371
Commercial MBS	19	1	2	—	—	—	—	22
Asset-backed securities	228	7	8	55	(36)	14	(23)	253
Corporate and other	291	3	9	86	(35)	15	(133)	236
Trading fixed maturities	1	—	—	—	—	—	(1)	—
Equity securities	11	—	2	30	—	13	(19)	37
Assets of MIE	44	—	—	20	(14)	13	(23)	40
Liabilities of MIE (a)	(2,593)	(189)	—	(793)	830	—	—	(2,745)
Embedded derivatives (b)	(361)	(57)	—	(73)	26	—	—	(465)

(a) Total realized/unrealized loss included in net income includes losses of $125 million related to liabilities outstanding as of December 31, 2012. See *Note H — “Managed Investment Entities.”*

(b) Total realized/unrealized loss included in net income for the embedded derivatives reflects gains related to the unlocking of actuarial assumptions of $36 million in 2012.

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — CONTINUED

	Balance at December 31, 2010	Total realized/unrealized gains (losses) included in Net income	Other comprehensive income (loss)	Purchases and issuances	Sales and settlements	Transfer into Level 3	Transfer out of Level 3	Balance at December 31, 2011
AFS fixed maturities:								
State and municipal	$ 20	$ —	$ 4	$ 58	$ (4)	$ 17	$ (12)	$ 83
Residential MBS	312	3	(9)	42	(38)	127	(76)	361
Commercial MBS	6	1	—	9	—	13	(10)	19
Asset-backed securities	124	1	—	179	(29)	4	(51)	228
Corporate and other	312	1	15	57	(43)	86	(137)	291
Trading fixed maturities	3	—	—	—	—	—	(2)	1
Equity securities	21	—	1	2	(2)	2	(13)	11
Assets of MIE	48	(8)	—	32	(18)	9	(19)	44
Liabilities of MIE (a)	(2,258)	—	—	(401)	66	—	—	(2,593)
Embedded derivatives	(181)	(29)	—	(171)	20	—	—	(361)

(a) Total realized/unrealized loss included in net income includes losses of $3 million related to liabilities outstanding as of December 31, 2011. See *Note H — "Managed Investment Entities."*

Fair Value of Financial Instruments The carrying value and fair value of financial instruments that are not carried at fair value in the financial statements at December 31 are summarized below (in millions):

	Carrying Value	Fair Value	Level 1	Level 2	Level 3
2013					
Financial assets:					
Cash and cash equivalents	$ 1,639	$ 1,639	$ 1,639	$ —	$ —
Mortgage loans	781	779	—	—	779
Policy loans	238	238	—	—	238
Total financial assets not accounted for at fair value	$ 2,658	$ 2,656	$ 1,639	$ —	$ 1,017
Financial liabilities:					
Annuity benefits accumulated (*)	$ 20,741	$ 19,959	$ —	$ —	$ 19,959
Long-term debt	913	985	—	909	76
Total financial liabilities not accounted for at fair value	$ 21,654	$ 20,944	$ —	$ 909	$ 20,035
2012					
Financial assets:					
Cash and cash equivalents	$ 1,705	$ 1,705	$ 1,705	$ —	$ —
Mortgage loans	607	613	—	—	613
Policy loans	228	228	—	—	228
Total financial assets not accounted for at fair value	$ 2,540	$ 2,546	$ 1,705	$ —	$ 841
Financial liabilities:					
Annuity benefits accumulated (*)	$ 17,405	$ 17,558	$ —	$ —	$ 17,558
Long-term debt	953	1,086	—	990	96
Total financial liabilities not accounted for at fair value	$ 18,358	$ 18,644	$ —	$ 990	$ 17,654

(*) Excludes life contingent annuities in the payout phase.

The carrying amount of cash and cash equivalents approximates fair value. Fair values for mortgage loans are estimated by discounting the future contractual cash flows using the current rates at which similar loans would be made to borrowers with

similar credit ratings. The fair value of policy loans is estimated to approximate carrying value; policy loans have no defined maturity dates and are inseparable from insurance contracts. The fair value of annuity benefits was estimated based on expected cash flows discounted using forward interest rates adjusted for the Company's credit risk and includes the impact of maintenance expenses and capital costs. Fair values of long-term debt are based primarily on quoted market prices.

E. Investments

Available for sale fixed maturities and equity securities at December 31 consisted of the following (in millions):

	2013				2012			
			Gross Unrealized				Gross Unrealized	
	Amortized Cost	Fair Value	Gains	Losses	Amortized Cost	Fair Value	Gains	Losses
Fixed maturities:								
U.S. Government and government agencies	$ 310	$ 314	$ 7	$ (3)	$ 373	$ 388	$ 15	$ —
States, municipalities and political subdivisions	5,360	5,372	156	(144)	4,144	4,468	329	(5)
Foreign government	198	208	10	—	242	260	18	—
Residential MBS	3,947	4,310	391	(28)	3,921	4,204	337	(54)
Commercial MBS	2,535	2,724	192	(3)	2,583	2,918	335	—
Asset-backed securities	2,477	2,493	35	(19)	1,590	1,640	52	(2)
Corporate and other	10,539	11,035	604	(108)	9,230	10,240	1,015	(5)
Total fixed maturities	$ 25,366	$ 26,456	$ 1,395	$ (305)	$ 22,083	$ 24,118	$ 2,101	$ (66)
Common stocks	$ 721	$ 914	$ 209	$ (16)	$ 600	$ 749	$ 157	$ (8)
Perpetual preferred stocks	$ 266	$ 265	$ 9	$ (10)	$ 178	$ 190	$ 13	$ (1)

The non-credit related portion of other-than-temporary impairment charges is included in other comprehensive income. Cumulative non-credit charges taken for securities still owned at December 31, 2013 and December 31, 2012, respectively, were $229 million and $227 million; nearly all of these charges relate to residential MBS.

The following tables show gross unrealized losses (in millions) on fixed maturities and equity securities by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2013 and 2012.

	Less Than Twelve Months			Twelve Months or More		
	Unrealized Loss	Fair Value	Fair Value as % of Cost	Unrealized Loss	Fair Value	Fair Value as % of Cost
2013						
Fixed maturities:						
U.S. Government and government agencies	$ (3)	$ 60	95%	$ —	$ —	—%
States, municipalities and political subdivisions	(135)	2,219	94%	(9)	73	89%
Residential MBS	(9)	553	98%	(19)	212	92%
Commercial MBS	(3)	106	97%	—	2	100%
Asset-backed securities	(18)	1,310	99%	(1)	28	97%
Corporate and other	(101)	2,634	96%	(7)	85	92%
Total fixed maturities	$ (269)	$ 6,882	96%	$ (36)	$ 400	92%
Common stocks	$ (16)	$ 158	91%	$ —	$ —	—%
Perpetual preferred stocks	$ (6)	$ 91	94%	$ (4)	$ 20	83%
2012						
Fixed maturities:						
U.S. Government and government agencies	$ —	$ 22	100%	$ —	$ —	—%
States, municipalities and political subdivisions	(5)	285	98%	—	24	100%
Residential MBS	(3)	146	98%	(51)	411	89%
Commercial MBS	—	16	100%	—	—	—%
Asset-backed securities	—	146	100%	(2)	57	97%
Corporate and other	(3)	237	99%	(2)	51	96%
Total fixed maturities	$ (11)	$ 852	99%	$ (55)	$ 543	91%
Common stocks	$ (8)	$ 88	92%	$ —	$ —	—%
Perpetual preferred stocks	$ —	$ 7	100%	$ (1)	$ 25	96%

At December 31, 2013, the gross unrealized losses on fixed maturities of $305 million relate to approximately 1,200 securities. Investment grade securities (as determined by nationally recognized rating agencies) represented approximately 89% of the gross unrealized loss and 90% of the fair value.

The determination of whether unrealized losses are “other-than-temporary” requires judgment based on subjective as well as objective factors. Factors considered and resources used by management include:

a) whether the unrealized loss is credit-driven or a result of changes in market interest rates,
b) the extent to which fair value is less than cost basis,
c) cash flow projections received from independent sources,
d) historical operating, balance sheet and cash flow data contained in issuer SEC filings and news releases,
e) near-term prospects for improvement in the issuer and/or its industry,
f) third party research and communications with industry specialists,
g) financial models and forecasts,
h) the continuity of dividend payments, maintenance of investment grade ratings and hybrid nature of certain investments,
i) discussions with issuer management, and
j) ability and intent to hold the investment for a period of time sufficient to allow for anticipated recovery in fair value.

AFG analyzes its MBS securities for other-than-temporary impairment each quarter based upon expected future cash flows. Management estimates expected future cash flows based upon its knowledge of the MBS market, cash flow projections (which reflect loan to collateral values, subordination, vintage and geographic concentration) received from independent sources, implied cash flows inherent in security ratings and analysis of historical payment data. For 2013, AFG recorded less than $1 million in other-than-temporary impairment charges related to its residential MBS.

Management believes AFG will recover its cost basis in the securities with unrealized losses and that AFG has the ability to hold the securities until they recover in value and had no intent to sell them at December 31, 2013.

A progression of the credit portion of other-than-temporary impairments on fixed maturity securities for which the non-credit portion of an impairment has been recognized in other comprehensive income is shown below (in millions).

	2013	2012	2011
Balance at January 1	$ 192	$ 187	$ 143
Additional credit impairments on:			
Previously impaired securities	—	5	44
Securities without prior impairments	3	2	8
Reductions — disposals	(1)	(2)	(8)
Balance at December 31	$ 194	$ 192	$ 187

The table below sets forth the scheduled maturities of available for sale fixed maturities as of December 31, 2013 (in millions). Securities with sinking funds are reported at average maturity. Actual maturities may differ from contractual maturities because certain securities may be called or prepaid by the issuers.

	Amortized	Fair Value	
	Cost	Amount	%
Maturity			
One year or less	$ 886	$ 904	3%
After one year through five years	4,631	4,966	19%
After five years through ten years	7,287	7,497	28%
After ten years	3,603	3,562	14%
	16,407	16,929	64%
ABS (average life of approximately 5 years)	2,477	2,493	9%
MBS (average life of approximately 4 1/2 years)	6,482	7,034	27%
Total	$ 25,366	$ 26,456	100%

Certain risks are inherent in connection with fixed maturity securities, including loss upon default, price volatility in reaction to changes in interest rates, and general market factors and risks associated with reinvestment of proceeds due to prepayments or redemptions in a period of declining interest rates.

There were no investments in individual issuers that exceeded 10% of Shareholders’ Equity at December 31, 2013 or 2012.

Net Unrealized Gain on Marketable Securities In addition to adjusting equity securities and fixed maturity securities classified as "available for sale" to fair value, GAAP requires that deferred policy acquisition costs and certain other balance sheet amounts related to annuity, long-term care and life businesses be adjusted to the extent that unrealized gains and losses from securities would result in adjustments to those balances had the unrealized gains or losses actually been realized. The following table shows (in millions) the components of the net unrealized gain on securities that is included in AOCI in AFG's Balance Sheet.

	Pretax	Deferred Tax and Amounts Attributable to Noncontrolling Interests	Net
December 31, 2013			
Unrealized gain on:			
Fixed maturities - annuity segment (*)	$ 729	$ (255)	$ 474
Fixed maturities - all other	361	(133)	228
Equity securities	192	(70)	122
Deferred policy acquisition costs - annuity segment	(345)	121	(224)
Annuity benefits accumulated	(71)	25	(46)
Life, accident and health reserves	(8)	3	(5)
Unearned revenue	22	(8)	14
	$ 880	$ (317)	$ 563
December 31, 2012			
Unrealized gain on:			
Fixed maturities - annuity segment (*)	$ 1,401	$ (490)	$ 911
Fixed maturities - all other	634	(236)	398
Equity securities	161	(57)	104
Deferred policy acquisition costs - annuity segment	(710)	247	(463)
Annuity benefits accumulated	(136)	48	(88)
Life, accident and health reserves	(117)	41	(76)
Unearned revenue	57	(20)	37
	$ 1,290	$ (467)	$ 823

(*) Unrealized gains on fixed maturity investments supporting AFG's annuity benefits accumulated.

Net Investment Income The following table shows (in millions) investment income earned and investment expenses incurred.

	2013	2012	2011
Investment income:			
Fixed maturities	$ 1,241	$ 1,216	$ 1,142
Equity securities	50	36	29
Other	72	66	71
Gross investment income	1,363	1,318	1,242
Investment expenses	(17)	(17)	(17)
Net investment income	$ 1,346	$ 1,301	$ 1,225

Realized gains (losses) and changes in unrealized appreciation (depreciation) related to fixed maturity and equity security investments are summarized as follows (in millions):

	Fixed Maturities	Equity Securities	Mortgage Loans and Other Investments	Other (a)	Tax Effects	Noncon-trolling Interests	Total
Year ended December 31, 2013							
Realized before impairments	$ 36	$ 196	$ 2	$ (1)	$ (82)	$ (2)	$ 149
Realized — impairments	(5)	(5)	(5)	3	4	—	(8)
Change in unrealized	(945)	31	—	504	144	6	(260)
Year ended December 31, 2012							
Realized before impairments	$ 55	$ 192	$ (3)	$ (8)	$ (83)	$ (2)	$ 151
Realized — impairments	(9)	(24)	—	7	9	—	(17)
Change in unrealized	790	(23)	—	(379)	(136)	(7)	245
Year ended December 31, 2011							
Realized before impairments	$ 68	$ 88	$ (24)	$ (4)	$ (45)	$ (2)	$ 81
Realized — impairments	(57)	(6)	(5)	16	18	1	(33)
Change in unrealized	407	(48)	—	(218)	(49)	(5)	87

(a) Primarily adjustments to deferred policy acquisition costs and reserves related to annuities and long-term care business.

Realized gains (losses) on securities include net losses of $3 million in 2013 compared to net gains of $5 million in 2012 and net losses of less than $1 million in 2011 from the mark-to-market of certain MBS, primarily interest-only securities with interest rates that float inversely with short-term rates. Gross realized gains and losses (excluding impairment writedowns and mark-to-market of derivatives) on available for sale fixed maturity and equity security investment transactions included in the Statement of Cash Flows consisted of the following (in millions):

	2013	2012	2011
Fixed maturities:			
Gross gains	$ 44	$ 55	$ 77
Gross losses	(5)	(4)	(9)
Equity securities:			
Gross gains	193	196	90
Gross losses	—	(4)	(1)

F. Derivatives

As discussed in *Note A — "Accounting Policies — Derivatives,"* AFG uses derivatives in certain areas of its operations. AFG's derivatives do not qualify for hedge accounting under GAAP; changes in the fair value of derivatives are included in earnings.

The following derivatives are included in AFG's Balance Sheet at fair value (in millions):

		December 31, 2013		December 31, 2012	
Derivative	Balance Sheet Line	Asset	Liability	Asset	Liability
MBS with embedded derivatives	Fixed maturities	$ 140	$ —	$ 110	$ —
Public company warrants	Equity securities	19	—	—	—
Interest rate swaptions	Other investments	2	—	1	—
Fixed-indexed annuities (embedded derivative)	Annuity benefits accumulated	—	804	—	465
Equity index call options	Other investments	272	—	132	—
Reinsurance contracts (embedded derivative)	Other liabilities	—	10	—	17
		$ 433	$ 814	$ 243	$ 482

The MBS with embedded derivatives consist primarily of interest-only MBS with interest rates that float inversely with short-term rates. AFG records the entire change in the fair value of these securities in earnings. These investments are part of AFG's overall investment strategy and represent a small component of AFG's overall investment portfolio.

Warrants to purchase shares of publicly traded companies, which represent a small component of AFG's overall investment portfolio, are considered to be derivatives that must be marked to market through earnings.

AFG has $400 million notional amount of pay-fixed interest rate swaptions (options to enter into pay-fixed/receive floating interest rate swaps at future dates expiring between 2014 and 2015) outstanding at December 31, 2013, which are used to mitigate interest rate risk in its annuity operations. AFG paid $11 million to purchase these swaptions, which represents its maximum potential economic loss over the life of the contracts.

AFG's fixed-indexed annuities, which represented approximately half of annuity benefits accumulated at December 31, 2013, provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase of call options on the appropriate index. AFG receives collateral from its counterparties to support its purchased call option assets. This collateral ($248 million at December 31, 2013) is included in other assets in AFG's Balance Sheet with an offsetting liability to return the collateral, which is included in other liabilities. AFG's strategy is designed so that an increase in the liabilities, due to an increase in the market index, will be generally offset by unrealized and realized gains on the call options purchased by AFG. Both the index-based component of the annuities and the related call options are considered derivatives. Fluctuations in interest rates and the stock market, among other factors, can cause volatility in the periodic measurement of fair value of the embedded derivative that management believes can be inconsistent with the long-term economics of these products. For example, the impact of lower interest rates in 2011 resulted in both the embedded derivative and call options to decline in value. The decline in fair value of the options reflects the relatively flat stock market during 2011. However, the negative impact of lower interest rates more than offset the positive impact of the flat stock market on the fair value of the fixed-indexed annuities embedded derivative.

As discussed in *Note A — "Accounting Policies — Reinsurance,"* certain reinsurance contracts are considered to contain embedded derivatives.

The following table summarizes the gain (loss) included in the Statement of Earnings for changes in the fair value of these derivatives for 2013, 2012 and 2011 (in millions):

Derivative	Statement of Earnings Line	2013	2012	2011
MBS with embedded derivatives	Realized gains on securities	$ (3)	$ 5	$ —
Public company warrants	Realized gains on securities	3	—	—
Interest rate swaptions	Realized gains on securities	1	(4)	(24)
Fixed-indexed annuities (embedded derivative) (*)	Annuity benefits	(182)	(57)	(29)
Equity index call options	Annuity benefits	210	66	(13)
Reinsurance contracts (embedded derivative)	Net investment income	7	(6)	(9)
		$ 36	$ 4	$ (75)

(*) The change in fair value of the embedded derivative includes gains related to unlocking of actuarial assumptions of $2 million in 2013 and $36 million in 2012.

G. Deferred Policy Acquisition Costs

A progression of deferred policy acquisition costs is presented below (in millions):

	P&C	Annuity and Other (*)					
	Deferred Costs	Deferred Costs	Sales Inducements	Present Value of Future Profits	Unrealized	Total	Consolidated Total
Balance at December 31, 2010	$ 181	$ 812	$ 189	$ 164	$ (315)	$ 850	$ 1,031
Additions	433	239	18	—	—	257	690
Amortization:							
Periodic amortization	(425)	(146)	(24)	(21)	—	(191)	(616)
Annuity unlocking	—	(2)	6	1	—	5	5
Included in realized gains	—	13	—	—	—	13	13
Change in unrealized	—	—	—	—	(222)	(222)	(222)
Balance at December 31, 2011	189	916	189	144	(537)	712	901
Additions	438	212	15	—	—	227	665
Amortization:							
Periodic amortization	(423)	(148)	(30)	(17)	—	(195)	(618)
Annuity unlocking	—	(33)	(4)	—	—	(37)	(37)
Loss recognition charge	—	(67)	—	(12)	—	(79)	(79)
Included in realized gains	—	(1)	—	—	—	(1)	(1)
Sale of subsidiaries	—	(92)	—	(16)	—	(108)	(108)
Change in unrealized	—	—	—	—	(173)	(173)	(173)
Balance at December 31, 2012	204	787	170	99	(710)	346	550
Additions	468	222	11	—	—	233	701
Amortization:							
Periodic amortization	(460)	(140)	(30)	(14)	—	(184)	(644)
Annuity unlocking	—	4	(2)	—	—	2	2
Included in realized gains	—	2	—	—	—	2	2
Foreign currency translation	(1)	—	—	—	—	—	(1)
Change in unrealized	—	—	—	—	365	365	365
Balance at December 31, 2013	$ 211	$ 875	$ 149	$ 85	$ (345)	$ 764	$ 975

(*) Includes AFG's run-off long-term care and life segment and Medicare supplement and critical illness segment (sold in August 2012).

The present value of future profits ("PVFP") amounts in the table above are net of $198 million and $184 million of accumulated amortization at December 31, 2013 and 2012, respectively. The loss recognition charge recorded in the fourth quarter of 2012 for AFG's closed block of long-term care insurance resulted in the write off of all remaining deferred policy acquisition costs for this business. During each of the next five years, the PVFP is expected to decrease at a rate of approximately one-sixth of the balance at the beginning of each respective year.

H. Managed Investment Entities

AFG is the investment manager and its subsidiaries have investments ranging from 7.5% to 51.2% of the most subordinate debt tranche of eleven collateralized loan obligation entities or "CLOs," which are considered variable interest entities. AFG's subsidiaries also own portions of the senior debt tranches of certain of these CLOs. Upon formation between 2004 and 2013, these entities issued securities in various senior and subordinate classes and invested the proceeds primarily in secured bank loans, which serve as collateral for the debt securities issued by each particular CLO. None of the collateral was purchased from AFG. AFG's investments in the subordinate debt tranches of these entities receive residual income from the CLOs only after the CLOs pay expenses (including management fees to AFG), and interest on and returns of capital to senior levels of debt securities. There are no contractual requirements for AFG to provide additional funding for these entities. AFG has not provided and does not intend to provide any financial support to these entities.

AFG's maximum exposure to economic loss on its CLOs is limited to its investment in the CLOs, which had an aggregate fair value of $271 million (including $88 million invested in the most subordinate debt tranches) at December 31, 2013, and $257 million at December 31, 2012.

In 2013, AFG formed two new CLOs, which issued an aggregate of $829 million face amount of liabilities (including $85 million face amount purchased by subsidiaries of AFG). During 2013, AFG subsidiaries also purchased $94 million face amount of senior debt tranches of existing CLOs for $89 million and received $142 million in redemption proceeds from its CLO investments. In 2012, AFG formed two new CLOs, which issued an aggregate face amount of $860 million of liabilities (including $74 million face amount purchased by subsidiaries of AFG). In 2012, AFG subsidiaries also purchased $74 million face amount of senior debt tranches of existing CLOs for $69 million. In 2013, two AFG CLOs were substantially liquidated, as permitted by the CLO indentures.

The revenues and expenses of the CLOs are separately identified in AFG's Statement of Earnings, after the elimination of management fees and earnings attributable to shareholders of AFG as measured by the change in the fair value of AFG's investments in the CLOs. Selected financial information related to the CLOs is shown below (in millions):

	Year ended December 31,		
	2013	2012	2011
Gains (losses) on change in fair value of assets/liabilities (a):			
Assets	$ 11	$ 95	$ (33)
Liabilities	(25)	(189)	—
Management fees paid to AFG	16	18	19
CLO earnings (losses) attributable to (b):			
AFG shareholders	35	31	6
Noncontrolling interests	(26)	(98)	(24)

(a) Included in Revenues in AFG's Statement of Earnings.
(b) Included in Earnings before income taxes in AFG's Statement of Earnings.

The aggregate unpaid principal balance of the CLOs' fixed maturity investments exceeded the fair value of the investments by $15 million and $29 million at December 31, 2013 and 2012. The aggregate unpaid principal balance of the CLOs' debt exceeded its fair value by $109 million and $123 million at those dates. The CLO assets include $1 million and $5 million in loans (aggregate unpaid principal balance of $6 million and $12 million, respectively) at December 31, 2013 and 2012, for which the CLOs are not accruing interest because the loans are in default.

I. Goodwill and Other Intangibles

Changes in the carrying value of goodwill during 2011, 2012 and 2013, by reporting segment, are presented in the following table (in millions):

	Property and Casualty	Annuity	Total
Balance at January 1, 2011 and December 31, 2011	$ 152	$ 34	$ 186
Sale of subsidiary in 2012	—	(1)	(1)
Balance at December 31, 2012 and 2013	$ 152	$ 33	$ 185

In the third quarter of 2012, goodwill decreased $1 million due to the sale of a small annuity subsidiary.

Included in other assets in AFG's Balance Sheet is $14 million at December 31, 2013 and $28 million at December 31, 2012 in amortizable intangible assets related to property and casualty insurance acquisitions. These amounts are net of accumulated amortization of $75 million and $61 million, respectively. Amortization of these intangibles was $14 million in each of 2013 and 2012 and $12 million in 2011. Future amortization of intangibles is estimated to be $13 million in 2014 and $1 million in 2015. Other assets also include $8 million in non-amortizable intangible assets related to property and casualty insurance acquisitions.

J. Long-Term Debt

The carrying value of long-term debt consisted of the following at December 31 (in millions):

	2013	2012
Direct obligations of AFG:		
9-7/8% Senior Notes due June 2019	$ 350	$ 350
6-3/8% Senior Notes due June 2042	230	230
5-3/4% Senior Notes due August 2042	125	125
7% Senior Notes due September 2050	132	132
Other	3	3
	840	840
Subsidiaries:		
Notes payable secured by real estate due 2014 through 2016	61	62
Secured borrowings ($16 guaranteed by AFG)	—	19
National Interstate bank credit facility	12	12
	73	93
Payable to Subsidiary Trusts:		
AAG Holding Variable Rate Subordinated Debentures	—	20
	$ 913	$ 953

At December 31, 2013, scheduled principal payments on debt for the subsequent five years were as follows: 2014 — $2 million; 2015 — $14 million; 2016 — $45 million; 2017 — $12 million and 2018 — none.

As shown below at December 31 (in millions), the majority of AFG's long-term debt is unsecured obligations of the holding company and its subsidiaries:

	2013	2012
Unsecured obligations	$ 852	$ 872
Obligations secured by real estate	61	62
Other secured borrowings	—	19
	$ 913	$ 953

AFG can borrow up to $500 million under its revolving credit facility which expires in December 2016. Amounts borrowed under this agreement bear interest at rates ranging from 1.00% to 1.875% (currently 1.375%) over LIBOR based on AFG's credit rating. No amounts were borrowed under this facility at December 31, 2013 or December 31, 2012.

National Interstate can borrow up to $100 million under its unsecured credit agreement, which expires in November 2017. At December 31, 2013, there was $12 million outstanding under this agreement, bearing interest at 1.11% (three-month LIBOR plus 0.875%).

In August 2013, AAG Holding redeemed its Variable Rate Subordinated Debentures at par value. In September 2013, an AFG subsidiary paid off its remaining secured borrowing balance at maturity.

In June 2012, AFG issued $230 million in 6-3/8% Senior Notes due 2042 and used the proceeds to redeem the outstanding AAG Holding Company 7-1/2% and 7-1/4% Senior Debentures at par value in July 2012. In August 2012, AFG issued $125 million in 5-3/4% Senior Notes due 2042 and used the proceeds to redeem the outstanding AFG 7-1/8% Senior Debentures at par value in September 2012.

Cash interest payments on long-term debt were $71 million in 2013, $75 million in 2012 and $74 million in 2011.

K. Shareholders' Equity

AFG is authorized to issue 12.5 million shares of Voting Preferred Stock and 12.5 million shares of Nonvoting Preferred Stock, each without par value.

Stock Incentive Plans Under AFG's Stock Incentive Plans, employees of AFG and its subsidiaries are eligible to receive equity awards in the form of stock options, stock appreciation rights, restricted stock awards, restricted stock units and stock awards.

At December 31, 2013, there were 11.7 million shares of AFG Common Stock reserved for issuance under AFG's stock incentive plans. Options are granted with an exercise price equal to the market price of AFG Common Stock at the date of grant. Options generally become exercisable at the rate of 20% per year commencing one year after grant and expire ten years after the date of grant.

Data for stock options issued under AFG's stock incentive plans is presented below:

	Shares	Average Exercise Price	Average Remaining Contractual Term	Aggregate Intrinsic Value (in millions)
Outstanding at January 1, 2013	7,219,742	$ 29.40		
Granted	1,037,665	$ 44.01		
Exercised	(1,625,023)	$ 27.39		
Forfeited/Cancelled	(23,770)	$ 37.85		
Outstanding at December 31, 2013	6,608,614	$ 32.16	5.6 years	$ 169
Options exercisable at December 31, 2013	3,834,299	$ 28.81	4.0 years	$ 111

The total intrinsic value of options exercised during 2013, 2012 and 2011 was $35 million, $25 million and $23 million, respectively. During 2013, 2012 and 2011, AFG received $44 million, $40 million and $33 million, respectively, in cash from the exercise of stock options. The total tax benefit related to the exercises was $11 million, $8 million and $7 million, respectively.

AFG uses the Black-Scholes option pricing model to calculate the fair value of its option grants. The expected dividend yield is based on AFG's current dividend rate. To determine expected volatility, AFG considers its daily historical volatility as well as implied volatility on traded options. The expected term was estimated based on historical exercise patterns and post vesting cancellations. The risk-free rate for periods associated with the expected term is based upon the U.S. Treasury yield curve in effect on the grant date.

	2013	2012	2011
Exercise price	$ 44.01	$ 38.10	$ 34.34
Expected dividend yield	1.8%	1.8%	1.9%
Expected volatility	39%	39%	38%
Expected term (in years)	7.25	7.25	7.30
Risk-free rate	1.36%	1.40%	3.04%
Grant date fair value	$ 15.10	$ 13.02	$ 12.49

The restricted Common Stock that AFG has granted generally vests over a three or four year period. Data relating to grants of restricted stock is presented below:

	Shares	Average Grant Date Fair Value
Outstanding at January 1, 2013	445,249	$ 30.65
Granted	249,411	$ 44.01
Vested	(142,091)	$ 26.32
Outstanding at December 31, 2013	552,569	$ 37.79

AFG issued 88,602 shares of Common Stock (fair value of $47.12 per share) in the first quarter of 2013 and 111,270 shares (fair value of $38.38 per share) in the first quarter of 2012 under its Equity Bonus Plan.

Total compensation expense related to stock incentive plans of AFG and its subsidiaries for 2013, 2012 and 2011 was $36 million, $26 million and $22 million, respectively. Related tax benefits totaled $12 million in 2013, $8 million in 2012 and $7 million in 2011. At December 31, 2013, there was $27 million and $12 million of unrecognized compensation expense related to nonvested stock options and restricted stock awards, respectively. These amounts are expected to be recognized over a weighted average of 3.3 and 2.4 years, respectively.

Accumulated Other Comprehensive Income, Net of Tax (“AOCI”) Comprehensive income is defined as all changes in Shareholders’ Equity except those arising from transactions with shareholders. Comprehensive income includes net earnings and other comprehensive income, which consists primarily of changes in net unrealized gains or losses on available for sale securities. The progression of the components of accumulated other comprehensive income follows (in millions):

		Other Comprehensive Income						
	AOCI Beginning Balance	Pretax	Tax	Net of tax	Attributable to noncontrolling interests	Attributable to shareholders	Other (c)	AOCI Ending Balance
Year ended December 31, 2013								
Net unrealized gains on securities:								
Unrealized holding gains (losses) on securities arising during the period		$ (188)	$ 66	$ (122)	$ 4	$ (118)		
Reclassification adjustment for realized gains (losses) included in net earnings (a)		(222)	78	(144)	2	(142)		
Total net unrealized gains on securities (b)	$ 823	(410)	144	(266)	6	(260)	$ —	$ 563
Foreign currency translation adjustments	14	(13)	—	(13)	—	(13)	—	1
Pension and other postretirement plans adjustments	(6)	3	(1)	2	—	2	—	(4)
Total	$ 831	$ (420)	$ 143	$ (277)	$ 6	$ (271)	$ —	$ 560
Year ended December 31, 2012								
Net unrealized gains on securities (b)	$ 578	$ 388	$ (136)	$ 252	$ (7)	$ 245	$ —	$ 823
Foreign currency translation adjustments	10	6	—	6	(1)	5	(1)	14
Pension and other postretirement plans adjustments	(8)	2	—	2	—	2	—	(6)
Total	$ 580	$ 396	$ (136)	$ 260	$ (8)	$ 252	$ (1)	$ 831
Year ended December 31, 2011								
Net unrealized gains on securities (b)	$ 491	$ 141	$ (49)	$ 92	$ (5)	$ 87	$ —	$ 578
Foreign currency translation adjustments	12	(1)	—	(1)	(1)	(2)	—	10
Pension and other postretirement plans adjustments	(8)	—	—	—	—	—	—	(8)
Total	$ 495	$ 140	$ (49)	$ 91	$ (6)	$ 85	$ —	$ 580

(a) The reclassification adjustment out of net unrealized gains on securities affected the following lines in AFG’s Consolidated Statement of Earnings:

OCI component	Affected line in the Consolidated Statement of Earnings
Pretax	Realized gains on securities
Tax	Provision for income taxes
Attributable to noncontrolling interests	Net earnings (loss) attributable to noncontrolling interests

(b) Includes net unrealized gains of $54 million at December 31, 2013 compared to net unrealized gains of $33 million at December 31, 2012 and net unrealized losses of $16 million at December 31, 2011, related to securities for which only the credit portion of an other-than-temporary impairment has been recorded in earnings.

(c) Other relates to the 2012 acquisition of noncontrolling interest in a subsidiary.

L. Income Taxes

The following is a reconciliation of income taxes at the statutory rate of 35% to the provision for income taxes as shown in the Statement of Earnings (in millions):

	2013		2012		2011	
	Amount	% of EBT	Amount	% of EBT	Amount	% of EBT
Earnings before income taxes ("EBT")	$ 689		$ 537		$ 558	
Income taxes at statutory rate	$ 241	35%	$ 188	35%	$ 195	35%
Effect of:						
Tax exempt interest	(21)	(3%)	(23)	(4%)	(23)	(4%)
Losses of managed investment entities	9	1%	34	6%	9	2%
Subsidiaries not in AFG's tax return	2	—%	(1)	—%	5	1%
Tax case and settlement of open tax years	—	—%	(67)	(13%)	—	—%
Change in valuation allowance	1	—%	3	1%	44	8%
Other	4	1%	1	—%	9	1%
Provision for income taxes as shown in the Statement of Earnings	$ 236	34%	$ 135	25%	$ 239	43%

A decision in favor of AFG from litigation with the IRS regarding the calculation of tax reserves for certain annuity liabilities became final in August 2012. As a result, during the third quarter of 2012, AFG recorded net earnings of approximately $28 million, which included the expected refund of $17 million of tax and interest paid to the IRS in 2005 and 2006 as well as a decrease in the liability for uncertain tax positions. In December 2012, AFG reached an agreement with the IRS to close subsequent years held open by the tax case. As a result, AFG decreased its tax liabilities by approximately $39 million in the fourth quarter of 2012.

AFG's 2008 — 2013 tax years remain subject to examination by the IRS.

Total earnings before income taxes include income subject to tax in foreign jurisdictions of $12 million in 2013 compared to losses of $3 million in 2012 and $26 million in 2011.

The total income tax provision (credit) consists of (in millions):

	2013	2012	2011
Current taxes:			
Federal	$ 308	$ 146	$ 186
State	5	6	4
Deferred taxes:			
Federal	(77)	(17)	22
Foreign	—	—	27
Provision for income taxes	$ 236	$ 135	$ 239

For income tax purposes, AFG and its subsidiaries had the following carryforwards available at December 31, 2013 (in millions):

	Expiring	Amount
Operating Loss – U.S.	2014 - 2020	$ 74
	2021 - 2025	71
Operating Loss – United Kingdom	indefinite	137

Deferred income tax assets and liabilities reflect temporary differences between the carrying amounts of assets and liabilities recognized for financial reporting purposes and the amounts recognized for tax purposes. The significant components of deferred tax assets and liabilities included in the Balance Sheet at December 31 were as follows (in millions):

	2013	2012
Deferred tax assets:		
Federal net operating loss carryforwards	$ 51	$ 51
Foreign underwriting losses	50	46
Insurance claims and reserves	558	528
Employee benefits	98	91
Other, net	51	36
Total deferred tax assets before valuation allowance	808	752
Valuation allowance against deferred tax assets	(103)	(101)
Total deferred tax assets	705	651
Deferred tax liabilities:		
Subsidiaries not in AFG's tax return (*)	(60)	(58)
Investment securities	(443)	(753)
Deferred policy acquisition costs	(234)	(91)
Total deferred tax liabilities	(737)	(902)
Net deferred tax liability	$ (32)	$ (251)

(*) Related to National Interstate Corporation, a 52%-owned subsidiary.

AFG's net deferred tax liability at December 31, 2013 and 2012 is included in other liabilities in AFG's Balance Sheet.

The likelihood of realizing deferred tax assets is reviewed periodically; any adjustments required to the valuation allowance are made in the period during which developments requiring an adjustment become known.

"Foreign underwriting losses" in the table above include the net operating loss carryforward and other deferred tax assets related to the Marketform Lloyd's insurance business, which resulted primarily from underwriting losses in its run-off Italian public hospital medical malpractice business that has not been written since 2008. Due to uncertainty concerning the realization of the deferred tax benefits associated with these losses, AFG recorded a $44 million valuation allowance against the deferred tax assets related to the Lloyd's insurance business in 2011, approximately $34 million of which related to prior year losses. AFG will be able to reduce this valuation allowance in future periods when income is generated by the Lloyd's business.

In addition to the valuation allowance related to the Marketform Lloyd's insurance business discussed above, the gross deferred tax asset has also been reduced by a $50 million valuation allowance related to a portion of AFG's net operating loss carryforwards ("NOL") that is subject to the separate return limitation year ("SRLY") tax rules. A SRLY NOL can be used only by the entity that created it and only in years that the consolidated group has taxable income.

The changes in the deferred tax liabilities related to investment securities and deferred policy acquisition costs at year end 2013 compared to 2012 are due primarily to the decrease in unrealized gains on fixed maturity securities.

AFG increased its liability for uncertain tax positions by $1 million in 2013, $3 million in 2012 and $7 million in 2011, exclusive of interest, to reflect uncertainty as to the timing of tax return inclusion of income related to certain securities. Because the ultimate recognition of income with respect to these securities is highly certain, any adjustments to this liability will result in offsetting adjustments to AFG's deferred tax liability. Accordingly, the ultimate resolution of this item will not impact AFG's annual effective tax rate but could accelerate the payment of taxes. During 2012, AFG also increased its liability for uncertain tax positions by $2 million related to the deductibility of certain financing expenses.

The resolution of the tax case and closure of subsequent tax years during 2012 (discussed above) reduced AFG's liability for uncertain tax positions by $36 million and the related liability for interest by $14 million. Additionally, the IRS issued new guidance during the third quarter of 2012 that brought certainty to the timing of investment deductions, which caused AFG to reduce its liability for uncertain tax positions by $10 million. Because this was solely a timing issue, the reduction in AFG's

liability for uncertain tax positions for this item was offset by an increase in AFG's deferred tax liability with no overall impact on income tax expense.

A progression of the liability for uncertain tax positions, excluding interest and penalties, follows (in millions):

	2013	2012	2011
Balance at January 1	$ 18	$ 59	$ 52
Reductions for tax positions of prior years	—	(46)	—
Additions for tax positions of current year	1	5	7
Balance at December 31	$ 19	$ 18	$ 59

As a result of discussions with the IRS Appeals Office during the third quarter of 2013, AFG believes it is reasonably possible that its liability for uncertain tax positions may be reduced by up to the full $19 million balance due to a settlement with the IRS that is expected to become final in 2014. The majority of the reduction in this liability would result in offsetting adjustments to AFG's deferred tax liability. The total unrecognized tax benefits and related interest that, if recognized, would impact the effective tax rate is $4 million at December 31, 2013. AFG's provision for income taxes included an expense of $1 million in 2013, a benefit of $14 million in 2012 and an expense of $3 million in 2011 of interest (net of federal benefit or expense). AFG's liability for interest related to unrecognized tax benefits was $1 million at both December 31, 2013 and December 31, 2012 (net of federal benefit); no penalties were accrued at those dates.

Cash payments for income taxes, net of refunds, were $204 million, $277 million and $157 million for 2013, 2012 and 2011, respectively.

M. Contingencies

Establishing property and casualty insurance reserves for claims related to environmental exposures, asbestos and other mass tort claims is subject to uncertainties that are significantly greater than those presented by other types of claims. For this group of claims, traditional actuarial techniques that rely on historical loss development trends cannot be used and a range of reasonably possible losses cannot be estimated. In addition, accruals (included in other liabilities) have been recorded for various environmental and occupational injury and disease claims and other contingencies arising out of the railroad operations disposed of by American Premier's predecessor, Penn Central Transportation Company ("PCTC") and its subsidiaries, prior to its bankruptcy reorganization in 1978 and certain manufacturing operations disposed of by American Premier and Great American Financial Resources, Inc. ("GAFRI").

AFG paid $124 million in the second quarter of 2013 related to the settlement of the A.P. Green asbestos claim in its property and casualty operations that had been accrued in prior years. AFG completed a comprehensive study of its asbestos and environmental ("A&E") exposures in the third quarter of 2013 with the assistance of specialty actuarial, engineering and consulting firms and outside counsel. The study resulted in A&E charges of $54 million for the property and casualty group and $22 million for the former railroad and manufacturing operations. In the third quarter of 2012, AFG completed an in-depth internal review of its A&E exposures, which resulted in A&E charges of $31 million for the property and casualty group and $2 million for the former railroad and manufacturing operations. In the second quarter of 2011, AFG completed a comprehensive study of A&E exposures with the assistance of specialty actuarial, engineering and consulting firms and outside counsel, which resulted in A&E charges of $50 million for the property and casualty group and $9 million for the former railroad and manufacturing operations.

The insurance group's liability for asbestos and environmental reserves was $384 million at December 31, 2013; related recoverables from reinsurers (net of allowances for doubtful accounts) at that date were $83 million.

At December 31, 2013, American Premier and its subsidiaries had liabilities for environmental and personal injury claims and other contingencies aggregating $86 million. The environmental claims consist of a number of proceedings and claims seeking to impose responsibility for hazardous waste remediation costs related to certain sites formerly owned or operated by the railroad and manufacturing operations. Remediation costs are difficult to estimate for a number of reasons, including the number and financial resources of other potentially responsible parties, the range of costs for remediation alternatives, changing technology and the time period over which these matters develop. The personal injury claims and other contingencies include pending and expected claims, primarily by former employees of PCTC, for injury or disease allegedly caused by exposure to excessive noise, asbestos or other substances in the workplace and other labor disputes.

At December 31, 2013, GAFRI had a liability of approximately $10 million for environmental costs and certain other matters associated with the sales of its former manufacturing operations.

While management believes AFG has recorded adequate reserves for the items discussed above in this note, the outcome is uncertain and could result in liabilities that may vary from amounts AFG has currently recorded. Such amounts could have a material effect on AFG's future results of operations and financial condition.

In addition, AFG and its subsidiaries are involved in litigation from time to time, generally arising in the ordinary course of business. This litigation may include, but is not limited to, general commercial disputes, lawsuits brought by policyholders, employment matters, reinsurance collection matters and actions challenging certain business practices of insurance subsidiaries. None of these matters are expected to have a material adverse impact on AFG's results of operations or financial condition.

N. Quarterly Operating Results (Unaudited)

The operations of certain AFG business segments are seasonal in nature. While insurance premiums are recognized on a relatively level basis, claim losses related to adverse weather (snow, hail, hurricanes, severe storms, tornadoes, etc.) may be seasonal. The profitability of AFG's crop insurance business is primarily recognized during the second half of the year as crop prices and yields are determined. Quarterly results necessarily rely heavily on estimates. These estimates and certain other factors, such as the discretionary sales of assets, cause the quarterly results not to be necessarily indicative of results for longer periods of time.

The following are quarterly results of consolidated operations for the two years ended December 31, 2013 (in millions, except per share amounts). Quarterly earnings per share do not add to year-to-date amounts due to changes in shares outstanding.

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total Year
2013					
Revenues	$ 1,148	$ 1,139	$ 1,443	$ 1,362	$ 5,092
Net earnings, including noncontrolling interests	113	77	98	165	453
Net earnings attributable to shareholders	120	110	83	158	471
Earnings attributable to shareholders per Common Share:					
Basic	$ 1.34	$ 1.23	$ 0.94	$ 1.77	$ 5.27
Diluted	1.32	1.20	0.92	1.73	5.16
Average number of Common Shares:					
Basic	89.4	89.6	89.1	89.4	89.3
Diluted	91.0	91.5	91.0	91.4	91.2
2012					
Revenues	$ 1,087	$ 1,124	$ 1,538	$ 1,208	$ 4,957
Net earnings, including noncontrolling interests	88	84	211	19	402
Net earnings attributable to shareholders	113	99	226	50	488
Earnings attributable to shareholders per Common Share:					
Basic	$ 1.16	$ 1.02	$ 2.43	$ 0.55	$ 5.18
Diluted	1.14	1.01	2.39	0.54	5.09
Average number of Common Shares:					
Basic	97.7	96.4	92.9	89.8	94.2
Diluted	99.4	98.0	94.6	91.4	95.9

Pretax realized gains on subsidiaries and securities (including other-than-temporary impairments) and favorable (adverse) prior year development of AFG's liability for losses and loss adjustment expenses ("LAE") were as follows (in millions):

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total Year
Realized Gains					
2013	$ 57	$ 41	$ 56	$ 63	$ 217
2012	44	15	241	71	371
Prior Year Development Favorable (Adverse)					
2013	$ 28	$ 22	$ (40)	$ 5	$ 15
2012	19	27	(23)	7	30

Adverse prior year development (in the table above) for the third quarter of 2013 includes pretax special charges of $54 million to strengthen property and casualty insurance A&E reserves. Results for the third quarter of 2013 also include pretax special charges of $22 million to strengthen reserves for A&E exposures related to AFG's former railroad and manufacturing operations.

Realized gains (in the table above) for the third quarter of 2012 include a pretax gain of $155 million on the sale of AFG's Medicare supplement and critical illness segment. Adverse prior year development for the third quarter of 2012 includes pretax special charges of $31 million to strengthen property and casualty insurance A&E reserves. Results for the third quarter of 2012 also include a $28 million benefit from the resolution of AFG's tax case. Results for the fourth quarter of 2012 include a $15 million additional pretax realized gain resulting from post-closing adjustments related to the sale of the Medicare supplement and critical illness segment, a pretax charge of $153 million to write off deferred policy acquisition costs and strengthen reserves in the closed block of long-term care insurance, pretax catastrophe losses of $33 million, primarily from Superstorm Sandy, a $14 million pretax charge due to a review of major actuarial assumptions in the annuity business, and tax benefits of $39 million from the settlement of open tax years following the resolution of AFG's tax case.

O. Insurance

Securities owned by U.S.-based insurance subsidiaries having a carrying value of approximately $1.10 billion at December 31, 2013, were on deposit as required by regulatory authorities. At December 31, 2013, AFG and its subsidiaries had $189 million in undrawn letters of credit ($16 million of which was collateralized) supporting the underwriting capacity of its U.K.-based Lloyd's insurer.

Property and Casualty Insurance Reserves The liability for losses and LAE for long-term scheduled payments under certain workers' compensation insurance has been discounted at 4.5% at both December 31, 2013 and 2012, which represents an approximation of long-term investment yields. As a result, the total liability for losses and loss adjustment expenses at December 31, 2013 and 2012, has been reduced by $20 million and $22 million.

The following table provides an analysis of changes in the liability for losses and loss adjustment expenses, net of reinsurance (and grossed up), over the past three years (in millions):

	2013	2012	2011
Balance at beginning of period	$ 4,129	$ 4,282	$ 4,164
Provision for losses and LAE occurring in the current year	2,055	1,903	1,813
Net decrease in provision for claims of prior years	(15)	(30)	(69)
Total losses and LAE incurred	2,040	1,873	1,744
Payments for losses and LAE of:			
Current year	(739)	(841)	(652)
Prior years	(1,131)	(1,185)	(969)
Total payments	(1,870)	(2,026)	(1,621)
Foreign currency translation and other	(11)	—	(5)
Balance at end of period	4,288	4,129	4,282
Add back reinsurance recoverables, net of allowance	2,122	2,716	2,238
Gross unpaid losses and LAE included in the Balance Sheet	$ 6,410	$ 6,845	$ 6,520

Favorable development in 2013 was due primarily to lower than expected severity in directors and officers liability insurance and lower than expected claim severity and frequency in the excess liability business, both within the Specialty casualty sub-segment, lower than expected frequency and severity in the foreign credit and financial institution services businesses within the Specialty financial sub-segment, and favorable reserve development associated with AFG's internal reinsurance program, partially offset by the $54 million special charge to increase asbestos and environmental reserves. Favorable development in 2012 was due primarily to lower than expected frequency and severity in the homebuilders' general liability business within the Specialty casualty sub-segment and lower than expected frequency in the crop business within the Property and transportation sub-segment, partially offset by higher frequency and severity in a block of program business in the Specialty casualty sub-segment and the $31 million special charge to increase asbestos and environmental reserves. Favorable development in 2011 was due primarily to lower than expected severity in certain businesses within the Specialty casualty sub-segment and lower than expected frequency in crop business within the Property and transportation sub-segment, partially offset by the $50 million special charge to increase asbestos and environmental reserves.

Closed Block of Long-Term Care Insurance AFG, as well as other companies that sell long-term care products, have accumulated relatively limited claims, lapse and mortality experience, making it difficult to predict future claims. Long-term care claims tend to be much higher in dollar amount and longer in duration than other health care products. In addition, long-term care claims are incurred much later in the life of a policy than most other health products. These factors made it difficult to appropriately price this product and were instrumental in AFG's decision to stop writing new policies in January 2010. AFG's outstanding long-term care policies have level premiums and are guaranteed renewable. Premium rates can potentially be increased in reaction to adverse experience; however, any rate increases would require regulatory approval.

In 2012, AFG recorded a $153 million pretax loss recognition charge to write off deferred policy acquisition costs and strengthen reserves on its closed block of long-term care insurance, due primarily to the impact of changes in assumptions related to future investment yields resulting from the continued low interest rate environment, as well as changes in claims, expenses and persistency assumptions. No additional loss recognition charges were recorded in 2013. At December 31, 2013, AFG's long-term care insurance reserves were $726 million, net of reinsurance recoverables.

FHLB Funding Agreements Great American Life Insurance Company ("GALIC"), a wholly-owned annuity subsidiary, is a member of the Federal Home Loan Bank of Cincinnati ("FHLB"). The FHLB makes advances and provides other banking services to member institutions. Members are required to purchase stock in the FHLB in addition to maintaining collateral deposits that back any funds advanced. GALIC's $34 million investment in FHLB capital stock at December 31, 2013, is included in other investments at cost. Membership in the FHLB provides the annuity operations with a substantial additional source of liquidity. These advances further the FHLB's mission of improving access to housing by increasing liquidity in the residential mortgage-backed securities market. In the fourth quarter of 2011, the FHLB advanced GALIC $240 million (included in annuity benefits accumulated at December 31, 2012). In the second quarter of 2013, the FHLB advanced GALIC an additional $200 million, increasing the total amount advanced to $440 million at December 31, 2013. Interest rates under the various funding agreements on these advances range from 0.02% to 0.23% over LIBOR (average rate of 0.32% at December 31, 2013). While these advances must be repaid between 2016 and 2018, GALIC has the option to prepay all or a

portion of the advances. The advances on these agreements are collateralized by mortgage-backed securities with a fair value of $565 million (included in available for sale fixed maturity securities) at December 31, 2013. Interest credited on the funding agreements, which is included in annuity benefits, was $1 million in 2013 and less than $1 million in 2012 and 2011.

Statutory Information AFG's U.S.-based insurance subsidiaries are required to file financial statements with state insurance regulatory authorities prepared on an accounting basis prescribed or permitted by such authorities (statutory basis). Net earnings (loss) and capital and surplus on a statutory basis for the insurance subsidiaries were as follows (in millions):

	Net Earnings			Capital and Surplus	
	2013	2012	2011	2013	2012
Property and casualty companies	$ 332	$ 221	$ 375	$ 1,896	$ 2,015
Life insurance companies	294	171	190	1,619	1,343

The National Association of Insurance Commissioners' ("NAIC") model law for risk based capital ("RBC") applies to both life and property and casualty insurance companies. RBC formulas determine the amount of capital that an insurance company needs so that it has an acceptable expectation of not becoming financially impaired. Companies below specific trigger points or ratios are subject to regulatory action. At December 31, 2013 and 2012, the capital ratios of all AFG insurance companies substantially exceeded the RBC requirements. AFG's insurance companies did not use any prescribed or permitted statutory accounting practices that differed from the NAIC statutory accounting practices at December 31, 2013 or 2012.

Payments of dividends by AFG's insurance companies are subject to various state laws that limit the amount of dividends that can be paid. Under applicable restrictions, the maximum amount of dividends available to AFG in 2014 from its insurance subsidiaries without seeking regulatory clearance is $610 million. Additional amounts of dividends require regulatory approval.

AFG paid common stock dividends to shareholders totaling $161 million, $91 million and $69 million in 2013, 2012 and 2011, respectively. Currently, there are no regulatory restrictions on AFG's retained earnings or net income that materially impact its ability to pay dividends. Based on shareholders' equity at December 31, 2013, AFG could pay dividends in excess of $1 billion without violating its most restrictive debt covenant. However, the payment of future dividends will be at the discretion of AFG's Board of Directors and will be dependent on many factors including AFG's financial condition and results of operations, the capital requirements of its insurance subsidiaries, and rating agency commitments.

Reinsurance In the normal course of business, AFG's insurance subsidiaries cede reinsurance to other companies to diversify risk and limit maximum loss arising from large claims. To the extent that any reinsuring companies are unable to meet obligations under agreements covering reinsurance ceded, AFG's insurance subsidiaries would remain liable. The following table shows (in millions) (i) amounts deducted from property and casualty written and earned premiums in connection with reinsurance ceded, (ii) written and earned premiums included in income for reinsurance assumed and (iii) reinsurance recoveries, which represent ceded losses and loss adjustment expenses.

	2013	2012	2011
Direct premiums written	$ 4,744	$ 4,283	$ 4,061
Reinsurance assumed	61	38	45
Reinsurance ceded	(1,464)	(1,372)	(1,336)
Net written premiums	$ 3,341	$ 2,949	$ 2,770
Direct premiums earned	$ 4,684	$ 4,120	$ 4,062
Reinsurance assumed	45	36	41
Reinsurance ceded	(1,525)	(1,309)	(1,344)
Net earned premiums	$ 3,204	$ 2,847	$ 2,759
Reinsurance recoveries	$ 1,255	$ 1,743	$ 770

AFG has reinsured approximately $13.43 billion of its $17.98 billion in face amount of life insurance at December 31, 2013 compared to $14.54 billion of its $19.44 billion in face amount of life insurance at December 31, 2012. Life written premiums ceded were $44 million, $42 million and $44 million for 2013, 2012 and 2011, respectively.

Variable Annuities At December 31, 2013, the aggregate guaranteed minimum death benefit value (assuming every variable annuity policyholder died on that date) on AFG's variable annuity policies exceeded the fair value of the underlying variable annuities by $26 million, compared to $40 million at December 31, 2012. Death benefits paid in excess of the variable annuity account balances were less than $1 million in each of the last three years.

P. Additional Information

Losses and loss adjustment expenses included charges for possible losses on reinsurance recoverables of $1 million in 2013 and less than $1 million in 2012 and 2011. The aggregate allowance for losses on reinsurance recoverables amounted to approximately $27 million and $26 million at December 31, 2013 and 2012, respectively.

Operating Leases Total rental expense for various leases of office space and equipment was $57 million in 2013, $51 million in 2012 and $54 million in 2011. Future minimum rentals, related principally to office space, required under operating leases having initial or remaining noncancelable lease terms in excess of one year at December 31, 2013, were as follows: 2014 – $57 million; 2015 – $50 million; 2016 – $44 million; 2017 – $35 million; 2018 – $30 million; and $173 million thereafter.

Financial Instruments — Unfunded Commitments On occasion, AFG and its subsidiaries have entered into financial instrument transactions that may present off-balance-sheet risks of both a credit and market risk nature. These transactions include commitments to fund loans, loan guarantees and commitments to purchase and sell securities or loans. At December 31, 2013, AFG and its subsidiaries had commitments to fund credit facilities and contribute capital to limited partnerships and limited liability corporations of approximately $280 million.

Benefit Plans AFG expensed approximately $32 million in 2013, $27 million in 2012 and $26 million in 2011 for its retirement and employee savings plans.

Q. Subsequent Events (Unaudited)

On January 9, 2014, AFG reached a definitive agreement to acquire Summit Holdings Southeast, Inc. and its related companies ("Summit"), from Liberty Mutual using cash on hand at the parent company. Under the terms of the agreement, AFG will pay an estimated $250 million at closing, subject to adjustment through the closing date primarily for changes in Summit's GAAP tangible book value. Including an anticipated capital contribution at closing, AFG's total capital investment in the Summit business will be approximately $400 million. Summit is based in Lakeland, Florida and is a leading provider of workers' compensation solutions in the southeastern United States, with net written premiums expected to be in excess of $500 million in 2013. Following the transaction, Summit will continue to operate under the Summit brand as a member of AFG's Great American Insurance Group. The transaction is expected to close in the first or second quarter of 2014, following customary regulatory approvals.

On February 5, 2014, Great American Insurance Company ("GAI") commenced a tender offer to acquire all of the outstanding shares of National Interstate Corporation common stock not currently owned by GAI for $30.00 per share in cash (as adjusted on February 17). The tender offer and withdrawal rights are scheduled to expire on March 6, 2014, unless the offer is extended or earlier terminated in accordance with the terms of the offer and the applicable Securities and Exchange Commission rules and regulations. GAI intends to pay for any shares acquired in the tender offer with cash on hand. If the tender offer is completed, and following the tender offer, GAI owns at least 90% of the outstanding shares of National Interstate on a fully diluted basis, AFG and GAI intend to cause a second step, short-form, merger of National Interstate into GAI or an affiliate of GAI.

PART III

The information required by the following Items will be included in AFG's definitive Proxy Statement for the 2014 Annual Meeting of Shareholders which will be filed with the Securities and Exchange Commission within 120 days after the end of the Registrant's fiscal year and is incorporated herein by reference.

ITEM 10	**Directors, Executive Officers of the Registrant and Corporate Governance**
ITEM 11	**Executive Compensation**
ITEM 12	**Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**
ITEM 13	**Certain Relationships and Related Transactions, and Director Independence**
ITEM 14	**Principal Accountant Fees and Services**

PART IV

ITEM 15

Exhibits and Financial Statement Schedules

(a) Documents filed as part of this Report:

1. Financial Statements are included in Part II, Item 8.

2. Financial Statement Schedules:

   A. Selected Quarterly Financial Data is included in *Note N* to the Consolidated Financial Statements.

   B. Schedules filed herewith for 2013, 2012 and 2011:

	Page
II — Condensed Financial Information of Registrant	S-2
III — Supplementary Insurance Information	S-4

All other schedules for which provisions are made in the applicable regulation of the Securities and Exchange Commission have been omitted as they are not applicable, not required, or the information required thereby is set forth in the Financial Statements or the notes thereto.

3. Exhibits — See Exhibit Index on page E-1.

AMERICAN FINANCIAL GROUP, INC. — PARENT ONLY
SCHEDULE II — CONDENSED FINANCIAL INFORMATION OF REGISTRANT
(In Millions)

Condensed Balance Sheet

	December 31,	
	2013	2012
Assets:		
Cash and cash equivalents	$ 523	$ 279
Investment in securities	53	44
Investment in subsidiaries (a)	5,041	5,155
Other investments	2	2
Other assets	108	117
Total assets	$ 5,727	$ 5,597
Liabilities and Equity:		
Long-term debt	$ 840	$ 840
Other liabilities	288	179
Shareholders' equity	4,599	4,578
Total liabilities and equity	$ 5,727	$ 5,597

Condensed Statement of Earnings

	Year ended December 31,		
	2013	2012	2011
Revenues:			
Dividends from subsidiaries	$ 606	$ 433	$ 544
Equity in undistributed earnings of subsidiaries	260	325	164
Investment and other income	8	5	2
Total revenues	874	763	710
Costs and Expenses:			
Interest charges on intercompany borrowings	10	11	11
Interest charges on other borrowings	67	61	53
Other expenses	90	68	65
Total costs and expenses	167	140	129
Earnings before income taxes	707	623	581
Provision for income taxes	236	135	239
Net Earnings Attributable to Shareholders	$ 471	$ 488	$ 342

Condensed Statement of Comprehensive Income

Net earnings attributable to shareholders	$ 471	$ 488	$ 342
Other comprehensive income (loss), net of tax	(271)	252	85
Total comprehensive income, net of tax	$ 200	$ 740	$ 427

(a) Investment in subsidiaries includes intercompany receivables and payables.

AMERICAN FINANCIAL GROUP, INC. — PARENT ONLY
SCHEDULE II — CONDENSED FINANCIAL INFORMATION OF REGISTRANT — CONTINUED
(In Millions)

Condensed Statement of Cash Flows

	Year ended December 31,		
	2013	2012	2011
Operating Activities:			
Net earnings attributable to shareholders	$ 471	$ 488	$ 342
Adjustments:			
Equity in net earnings of subsidiaries	(579)	(515)	(439)
Dividends from subsidiaries	543	417	542
Other operating activities, net	(7)	(10)	17
Net cash provided by operating activities	428	380	462
Investing Activities:			
Capital contributions to subsidiaries	(38)	(274)	(29)
Returns of capital from subsidiaries	36	1	2
Purchases of investments, property and equipment	(2)	(11)	(54)
Proceeds from maturities and redemptions of investments	—	—	4
Proceeds from sales of investments, property and equipment	—	—	5
Net cash used in investing activities	(4)	(284)	(72)
Financing Activities:			
Additional long-term borrowings	—	344	—
Reductions of long-term debt	—	(115)	—
Issuances of Common Stock	50	44	37
Repurchases of Common Stock	(70)	(415)	(315)
Cash dividends paid on Common Stock	(160)	(90)	(67)
Net cash used in financing activities	(180)	(232)	(345)
Net Change in Cash and Cash Equivalents	244	(136)	45
Cash and cash equivalents at beginning of year	279	415	370
Cash and cash equivalents at end of year	$ 523	$ 279	$ 415

AMERICAN FINANCIAL GROUP, INC. AND SUBSIDIARIES
SCHEDULE III — SUPPLEMENTARY INSURANCE INFORMATION
THREE YEARS ENDED DECEMBER 31, 2013
(IN MILLIONS)

Segment	Deferred policy acquisition costs	Reserves for future policy benefits, claims and unpaid losses and LAE	Unearned premiums	Net earned premiums	Net investment income	Benefits, claims, losses and settlement expenses	Amortization of deferred policy acquisition costs	Other operating expenses	Net written premiums (excluding life)
2013									
Property and casualty insurance	$ 211	$ 6,410	$ 1,757	$ 3,204	$ 263	$ 2,040	$ 460	$ 607	$ 3,341
Annuity	723	20,944	—	—	1,034	531	144	103	—
Run-off long-term care and life	41	2,008	—	114	76	160	6	38	76
Other	—	—	—	—	(27)	—	—	314	—
Total	$ 975	$ 29,362	$ 1,757	$ 3,318	$ 1,346	$ 2,731	$ 610	$ 1,062	$ 3,417
2012									
Property and casualty insurance	$ 204	$ 6,845	$ 1,651	$ 2,847	$ 275	$ 1,873	$ 423	$ 528	$ 2,949
Annuity	299	17,609	—	—	976	541	163	68	—
Run-off long-term care and life	47	2,059	—	119	69	225	95	28	79
Medicare supplement and critical illness	—	—	—	199	7	131	19	34	199
Other	—	—	—	—	(26)	—	—	292	—
Total	$ 550	$ 26,513	$ 1,651	$ 3,165	$ 1,301	$ 2,770	$ 700	$ 950	$ 3,227
2011									
Property and casualty insurance	$ 189	$ 6,520	$ 1,484	$ 2,759	$ 291	$ 1,744	$ 425	$ 465	$ 2,770
Annuity	560	15,420	—	—	859	510	114	90	—
Run-off long-term care and life	43	1,478	—	126	66	151	19	20	81
Medicare supplement and critical illness	109	249	—	304	10	209	35	47	304
Other	—	—	—	—	(1)	—	—	256	—
Total	$ 901	$ 23,667	$ 1,484	$ 3,189	$ 1,225	$ 2,614	$ 593	$ 878	$ 3,155

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Signatures

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

American Financial Group, Inc.

February 28, 2014

By: /s/ Joseph E. (Jeff) Consolino
Joseph E. (Jeff) Consolino
Executive Vice President and Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

Signature	Capacity	Date
/s/ Carl H. Lindner III Carl H. Lindner III	Co-Chief Executive Officer and Director (Principal Executive Officer)	February 28, 2014
/s/ S. Craig Lindner S. Craig Lindner	Co-Chief Executive Officer and Director (Principal Executive Officer)	February 28, 2014
/s/ Joseph E. (Jeff) Consolino Joseph E. (Jeff) Consolino	Executive Vice President, Chief Financial Officer and Director (Principal Financial and Accounting Officer)	February 28, 2014
/s/ Kenneth C. Ambrecht Kenneth C. Ambrecht	Director	February 28, 2014
/s/ John B. Berding John B. Berding	Director	February 28, 2014
/s/ Virginia (Gina) C. Drosos Virginia (Gina) C. Drosos	Director*	February 28, 2014
/s/ James E. Evans James E. Evans	Director	February 28, 2014
/s/ Terry S. Jacobs Terry S. Jacobs	Director*	February 28, 2014
/s/ Gregory G. Joseph Gregory G. Joseph	Director*	February 28, 2014
/s/ William W. Verity William W. Verity	Director	February 28, 2014
/s/ John I. Von Lehman John I. Von Lehman	Director*	February 28, 2014

* Member of the Audit Committee

INDEX TO EXHIBITS

AMERICAN FINANCIAL GROUP, INC.

Number	Exhibit Description	
3(a)	Amended and Restated Articles of Incorporation, filed as Exhibit 3(a) to AFG's Form 10-K for 1997.	(*)
3(b)	Amended and Restated Code of Regulations, filed as Exhibit 3 to AFG's Form 8-K filed on August 16, 2012.	(*)
4	Instruments defining the rights of security holders.	Registrant has no outstanding debt issues exceeding 10% of the assets of Registrant and consolidated subsidiaries.
	Material Contracts:	
10(a)	Amended and Restated Non-Employee Directors Compensation Plan, filed as Exhibit 10 to the Form S-8 Registration Statement (File No. 333-181913) filed by AFG on November 13, 2012.	(*)
10(b)	Amended and Restated Deferred Compensation Plan, filed as Exhibit 10(b) to AFG's Form 10-K for 2008.	(*)
10(c)	2011 Equity Bonus Plan (formerly known as the 2011 Co-CEO Equity Bonus Plan), filed as Exhibit 10 to the Form S-8 Registration Statement (File No. 333-184915) filed by AFG on November 13, 2012.	(*)
10(d)	2011 Annual Senior Executive Bonus Plan, filed as Annex B to AFG's Proxy statement filed on March 30, 2011.	(*)
10(e)	Amended and restated Nonqualified Auxiliary RASP, filed as Exhibit 10(f) to AFG's Form 10-K for 2008.	(*)
10(f)	2005 Stock Incentive Plan Exhibit 10 to the Form S-8 Registration Statement (File No. 333-184914) filed by AFG on November 13, 2012.	(*)
10(g)	Credit Agreement dated December 5, 2012, among American Financial Group, Inc., Bank of America, N.A., as Administrative Agent, and several lenders, filed as Exhibit 10 to AFG's Form 8-K filed on December 7, 2012.	(*)
10(h)	Stock Purchase Agreement dated January 9, 2014 by and between Liberty Mutual Group Inc. and Great American Holding, Inc. (Summit Holdings Southeast, Inc.)	
12	Computation of ratios of earnings to fixed charges.	
21	Subsidiaries of the Registrant.	
23	Consent of independent registered public accounting firm.	
31(a)	Certification of Co-Chief Executive Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.	
31(b)	Certification of Co-Chief Executive Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.	
31(c)	Certification of Chief Financial Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.	
32	Certification of Co-Chief Executive Officers and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	
101	The following financial information from American Financial Group's Form 10-K for the year ended December 31, 2013, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheet (ii) Consolidated Statement of Earnings (iii) Consolidated Statement of Comprehensive Income (iv) Consolidated Statement of Changes in Equity (v) Consolidated Statement of Cash Flows (vi) Notes to Consolidated Financial Statements (vii) Financial Statement Schedules	

(*) Incorporated herein by reference.

EXECUTION COPY

STOCK PURCHASE AGREEMENT

by and between

LIBERTY MUTUAL GROUP INC.,

GREAT AMERICAN HOLDING, INC.,

and, solely for the purpose of Section 4.6,

AMERICAN FINANCIAL GROUP, INC.

Dated as of January 9, 2014

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Schedule 2.4 Form of Closing Statement

This STOCK PURCHASE AGREEMENT (this "Agreement"), dated as of January 9, 2014, is entered into by and between Liberty Mutual Group Inc., a Massachusetts corporation ("Seller"), Great American Holding, Inc., an Ohio corporation ("Purchaser"), and, solely for the purpose of Section 4.6, American Financial Group, Inc., an Ohio corporation ("AFG").

RECITALS:

WHEREAS, Seller is the direct parent of Liberty Mutual Insurance Company, a Massachusetts stock insurance company ("LMIC"), and Liberty Corporate Services LLC, a Massachusetts limited liability company ("LCS");

WHEREAS, LMIC owns all of the issued and outstanding shares of common stock (the "SHSI Shares") of Summit Holding Southeast, Inc. a Florida corporation ("SHSI");

WHEREAS, LCS owns 100% of the membership interests (the "SCL Membership Interests" and together with the SHSI Shares, the "Equity Interests") of Summit Consulting, LLC a Florida limited liability company ("SCL" and together with SHSI, the "Purchased Companies");

WHEREAS, Purchaser is a wholly-owned Subsidiary of AFG. Through its Subsidiaries, AFG is engaged, among other things, in property and casualty insurance, focusing on specialized commercial products for businesses; and

WHEREAS, subject to the terms, conditions and limitations set forth in this Agreement, Seller desires to sell, and Purchaser desires to purchase, the Equity Interests.

NOW, THEREFORE, in consideration of the mutual promises and covenants contained herein, and in reliance upon the representations, warranties, conditions and covenants contained herein, and intending to be legally bound hereby, the parties hereto do hereby agree as follows:

ARTICLE I
DEFINITIONS

Section 1.1 Definitions. The following terms shall have the respective meanings set forth below throughout this Agreement:

(a) "Action" means any claim, cause of action, demand, lawsuit, arbitration, notice of violation, proceeding, litigation, summons (excluding those with respect to claims arising under the workers compensation policies issued by

the Transferred Companies), subpoena or investigation of any nature, civil, criminal, administrative, regulatory or otherwise, whether at law or in equity.

(b) "Affiliate" means, with respect to any Person, at the time in question, any other Person that directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with, such Person. The term "control" (including the terms "controlled by" and "under common control with") means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a Person, whether through the ownership of voting securities, by contract or otherwise. For the avoidance of doubt, unless otherwise specified herein, the Transferred Companies shall be deemed "Affiliates" of Seller (and not Purchaser) prior to the Closing and shall be deemed "Affiliates" of Purchaser (and not Seller) from and after the Closing; it being understood, that for purposes of this definition, Seller shall not be deemed to be an Affiliate of Purchaser.

(c) "Ancillary Agreements" means collectively:

(i) The Transition Services Agreement; and

(ii) The Transitional Trademark License Agreement.

(d) "Applicable Law" means any U.S. federal, state or local statute, law, constitution, treaty, ordinance or code, or any written rules, regulations or administrative interpretations issued by any Governmental Authority pursuant to any of the foregoing and having the force of law, and any order, writ, injunction, directive, judgment or decree of any court of competent jurisdiction applicable to the parties hereto.

(e) "Books and Records" means all books and records in the possession of Seller or its respective Affiliates (other than the Transferred Companies) that relate principally to the Business or the Transferred Companies, including statutory filings as required under Applicable Law, administrative records, claim records, sales records, underwriting records, financial records, Tax records, compliance records and other records, in whatever form maintained. Notwithstanding the foregoing, the "Books and Records" exclude certificates of incorporation, bylaws, corporate seals, licenses to do business, minute books and other corporate records relating to corporate organization or capitalization of Seller or its respective Affiliates (other than the Transferred Companies), original Tax, legal and accounting records, and any books and records that are subject to the attorney-client, work product, or other similar privilege or doctrine except for books and records related to pending claims, compliance and regulatory matters,

reinsurance and any other matter that is the subject of a pending matter, settlement or Order and as to which the privilege shall, under Applicable Law, transfer to the Purchaser as owner of the Transferred Companies from and after the Closing, which books and records shall be included in the definition of Books and Records. To the extent any Books and Records contain material that does not relate to the Business, such material shall not constitute “Books and Records” for purposes of this Agreement and any such material may be redacted from the Books and Records.

(f) “Business” means the business conducted by the Transferred Companies, as of any relevant date of determination at or prior to the Closing Date, including but not limited to, underwriting monoline workers’ compensation insurance and providing underwriting, claims administration and managed care services to affiliated and unaffiliated workers’ compensation insurers and governmental entities, in each case in the States set forth in Section 1.1(f) of the Seller Disclosure Letter.

(g) “Business Day” means any day other than a Saturday, Sunday, a day on which banking institutions in the City of New York are permitted or obligated by Applicable Law to remain closed or a day on which the New York Stock Exchange is closed for trading.

(h) “Business Employee” means, on any date, those employees of Seller and its Affiliates whose employment relates primarily to the Business, including all such employees who are on an approved leave.

(i) “Business Material Adverse Effect” means any change, occurrence, development or effect, individually or together with other similar or related changes, occurrences, developments or effects, that is materially adverse to the business, assets, financial condition, operations or operating results of the Transferred Companies, or the ability of Seller to consummate the transactions contemplated hereby or to carry out its obligations under this Agreement or the Ancillary Agreements; provided that the following shall be excluded from the definition of “Business Material Adverse Effect” and from any determination as to whether a Business Material Adverse Effect has occurred or may occur: (i) any adverse effect that is caused by or that arises out of conditions affecting the economy or financial or capital markets in general; (ii) any adverse effect that is caused by or that arises out of conditions affecting the property and casualty insurance industry or the insurance industry generally; (iii) any adverse effect that is caused by or attributable to any changes in Applicable Law, GAAP, SAP or other accounting or actuarial principles or practices to the extent applicable to the Business; (iv) any adverse effect resulting from the announcement or the

pendency of the transactions contemplated by this Agreement (including, but not limited to, changes in relations with producers, vendors, reinsurers, customers, policyholders or employees and declines in sales volumes or net operating income) or the identity of the Purchaser; (v) acts of war, sabotage or terrorism, or any escalation or worsening of such acts, any earthquakes, hurricanes, tornados, and other storms, floods or other natural disasters, or any other force majeure event; (vi) any action taken or failed to be taken by Seller or any of its respective Affiliates, agents or representatives at the written instruction of or with the written consent of Purchaser, or not taken because Purchaser has unreasonably withheld or delayed its consent, or that is contemplated by this Agreement; (vii) any adverse effect resulting from or arising out of the actual or potential failure of any counterparty of the Transferred Companies or the Business (other than Seller and its Affiliates) to perform its obligations under any contract with respect to the Business; provided the Transferred Companies are in full compliance with such contracts; (viii) any matter, to the extent taken into account in determining the Purchase Price pursuant to Section 2.4; except that in the case of clauses (i), (ii), (iii), and (v) above, to the extent such effect or change is disproportionately adverse with respect to the Business as compared to other businesses engaged in the industry in which the Business operates.

(j) "Code" means the United States Internal Revenue Code of 1986, as amended, and the United States Treasury regulations promulgated thereunder.

(k) "Company Benefit Plans" means each material employee benefit plan, scheme, program, policy, arrangement and contract (including, but not limited to, any "employee benefit plan", as defined in Section 3(3) of ERISA, whether or not subject to ERISA, and any fringe benefit, bonus, incentive, deferred compensation, stock bonus, stock purchase, restricted stock, stock option or other equity-based arrangement, and any employment, termination, retention, bonus, change in control or severance plan, program, policy, arrangement or contract) for the benefit of any current or former Business Employee or director of the Transferred Companies or any spouse or dependent of such individual that is maintained or contributed to by any of the Transferred Companies or any of their Affiliates, or with respect to which any of them could incur aggregate liability in excess of $100,000 under Applicable Law, including the Code or ERISA or any similar non-U.S. law.

(l) "Competition Laws" means all Applicable Laws that are designed or intended to prohibit, restrict or regulate actions having the purpose or effect of monopolization or lessening of competition through merger or acquisition or restraint of trade.

(m) "Confidential Information Memorandum" means the materials titled "Project Sherpa" and "Materials Regarding: Project Sherpa Company Overview" provided to Purchaser in connection with the transactions contemplated by this Agreement.

(n) "Confidentiality Agreement" means the confidentiality agreement dated July 29, 2013, by and between Seller and AFG.

(o) "Consolidated Income Tax Liabilities" means any and all Income Taxes of any member of the Seller Group.

(p) "Consolidated or Combined Return" means any Tax Return that is filed or required to be filed and that includes one or more Transferred Companies, on the one hand, and one or more members of the Seller Group, on the other hand.

(q) "Contract Date" means the date of execution of this Agreement.

(r) "Contracts with Key Non-Affiliated Entities" means the Managing General Agency agreements, managed care agreements and any other agreements between any Transferred Company and any Key Non-Affiliated Entity.

(s) "Data Laws" means any Applicable Law regarding data privacy, data security, and/or the collection and use of personal information.

(t) "Environmental, Health, and Safety Requirements" means all applicable federal, state, local, and non-U.S. statutes, regulations, ordinances, and similar provisions having the force or effect of law as of the Closing Date, all judicial and administrative orders and determinations, and all common laws concerning worker health and safety as such relates to exposure to Hazardous Substances, pollution, or protection of natural resources or the environment, including all those relating to the presence, use, production, generation, handling, transportation, treatment, storage, disposal, distribution, labeling, testing, processing, discharge, release, threatened release, control, exposure to, or cleanup of any Hazardous Substances.

(u) "ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

(v) "GAAP" means United States generally accepted accounting principles, consistently applied.

(w) "GAAP Tangible Equity" means, as of any date of determination, an amount equal to the combined tangible equity of the Purchased Companies, determined in accordance with GAAP.

(x) "Governmental Authority" means any court, administrative or regulatory agency or commission, or other federal, state or local governmental authority or instrumentality having jurisdiction over any party hereto.

(y) "Governmental Order" means any Order entered by or with any Governmental Authority.

(z) "Hazardous Substance" means (a) any petroleum or petroleum products, asbestos, urea formaldehyde insulation or polychlorinated biphenyls and (b) any pollutant, contaminant, waste, material or substance defined in, regulated under or for which liability or standards of care are imposed by any applicable Environmental, Health, and Safety Requirement.

(aa) "HSR Act" means the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

(bb) "Income Tax" means any Tax on or measured by net income.

(cc) "Income Tax Return" means any tax return with respect to Income Taxes payable by the Transferred Companies.

(dd) "Insurance Contracts" means the insurance policies and contracts and the assumed reinsurance treaties, together with all amendments, binders, slips, certificates, endorsements and riders thereto issued or entered into by any Transferred Insurance Company prior to the Closing.

(ee) "Insurance Laws" means any U.S. federal, state or local insurance or reinsurance statute, law, constitution, treaty, ordinance or code, or any written rules, regulations or administrative interpretations related to insurance or reinsurance matters issued by any Governmental Authority pursuant to any of the foregoing and having the force of law, and any order, writ, injunction, directive, judgment or decree of any court of competent jurisdiction applicable to the parties hereto and relating to insurance or reinsurance matters.

(ff) "Insurance Regulator" means, with respect to any jurisdiction, the Governmental Authority principally responsible for administering the Insurance Laws of such jurisdiction and regulating insurance companies domiciled or doing business in such jurisdiction, including, workers' compensation regulators.

(gg) "Intellectual Property" means all Name and Source Identifiers (including any goodwill associated therewith), copyrights (including registrations and applications therefor), patentable and patented designs and inventions, patents, patent applications, policy forms and trade secrets.

(hh) "Intercompany Obligations" means any loans, notes, advances, pooling arrangement, receivables, payables or other obligations between Seller or any of its Affiliates (other than the Transferred Companies), on the one hand, and any Transferred Company, on the other hand.

(ii) "Investment Assets" means any investment assets (whether or not required by SAP to be reflected on a balance sheet) beneficially owned (within the meaning of Rule 13d-3 under the Securities Exchange Act) by any Transferred Insurance Company, including bonds, notes, debentures, mortgage loans, real estate and all other instruments of indebtedness, stocks, partnership or joint venture interests and all other equity interests, certificates issued by or interests in trusts, derivatives and all other assets acquired for investment purposes.

(jj) "Investment Company Act" means the Investment Company Act of 1940, as amended, together with the rules and regulations thereunder.

(kk) "IRS" means the Internal Revenue Service.

(ll) "Key Non-Affiliated Entities" means each of Retailers Casualty Insurance Company, a Louisiana corporation, BusinessFirst Insurance Company, a Florida corporation, and RetailFirst Insurance Company, a Florida corporation.

(mm) "Knowledge of Seller" means the actual knowledge of those persons identified in Section 1.1(mm) of the Seller Disclosure Letter, after due inquiry.

(nn) "Leased Real Property" means all material leasehold or subleasehold estate and other rights to use or occupy any land, buildings, structures, improvements, fixtures, or other interest in real property held by any of the Transferred Companies.

(oo) "Leases" means all material leases, subleases, licenses, concessions and other agreements (written or oral), including all amendments, extensions, renewals and guaranties related thereto, pursuant to which any of the Transferred Companies holds any Leased Real Property, including the right to all

security deposits and other amounts and instruments held by or on behalf of any of the Transferred Companies thereunder.

(pp) "Liberty Mutual Names and Marks" means the Name and Source Identifiers of Seller and its Affiliates.

(qq) "LIBOR" means a rate per annum equal to the three-month London Interbank Offered Rate as published in The Wall Street Journal, Eastern Edition, in effect on the Closing Date.

(rr) "Lien" means, as to any asset, any mortgage, pledge, deed of trust, hypothecation, right of others, claim, security interest, encumbrance, burden, title defect, title retention agreement, lease, sublease, license, occupancy agreement, easement, covenant, condition, encroachment, voting trust agreement, interest, option, right of first offer, negotiation or refusal, proxy, lien, charge or other restrictions or limitations of any nature whatsoever.

(ss) "Loss" and/or "Losses" shall (x) mean losses, liabilities, damages, costs, out-of-pocket expenses (including reasonable attorneys' fees), interest and penalties, but shall not include, in the absence of fraud, any measure of indirect, punitive or consequential damages, except to the extent actually awarded to a Governmental Authority or third party, and (y) be determined as to quantum without reference to any qualifications as to "materiality", "in all material respects" or "Business Material Adverse Effect" in the breached representation, warranty or covenant giving rise to such Losses.

(tt) "Name and Source Identifiers" means trade, corporate or business names, trademarks, service marks, domain names, acronyms, tag-lines, slogans, and logos.

(uu) "Ordinary Course of Business" means, with respect to any Person, the ordinary course of such Person's business consistent with such Person's past practices (including with respect to quantity and frequency).

(vv) "Organizational Documents" means the articles of incorporation, certificate of incorporation, charter, bylaws, articles of formation, certificate of formation, operating agreement, certificate of limited partnership, partnership agreement and all other similar documents, instruments or certificates executed, adopted or filed in connection with the creation, formation or organization of a Person, including any amendments thereto.

(ww) “Permits” means all licenses, permits, franchises, orders, approvals, registrations, authorizations and qualifications with Governmental Authorities.

(xx) “Permitted Lien” means, as to any asset, each of the following: (i) Liens for Taxes, assessments and governmental charges or levies not yet due and payable or due and payable but not delinquent or which are being contested in good faith; (ii) Liens imposed by Applicable Law; (iii) materialmen’s, mechanics’, carriers’, workmen’s and repairmen’s liens and other similar liens arising in the Ordinary Course of Business; (iv) pledges or deposits to secure obligations under workers’ compensation laws or similar legislation or to secure public or statutory obligations; (v) Liens related to deposits required by the insurance regulatory authority of any applicable jurisdiction; and (vi) minor survey exceptions, reciprocal easement agreements and other customary encumbrances on title to real property.

(yy) “Person” means any individual, corporation, partnership, firm, joint venture, association, joint-stock company, limited liability company, trust, unincorporated organization, governmental, judicial or regulatory body, business unit, division or other entity.

(zz) “Post-Closing Tax Period” means any Tax period beginning after the Closing and, with respect to a Tax period that begins on or before the Closing and ends thereafter, the portion of such Tax period beginning after the completion of the Closing.

(aaa) “Pre-Closing Tax Period” means any Tax period ending on or before the Closing Date and, with respect to a Tax period that begins on or before the Closing and ends thereafter, the portion of such Tax period ending at the completion of the Closing Date.

(bbb) “Purchase Price” means the GAAP Tangible Equity at Closing, plus $45,000,000.

(ccc) “Purchaser Disclosure Letter” means the disclosure letter delivered by Purchaser to Seller concurrently with entering into this Agreement.

(ddd) “Purchaser Material Adverse Effect” means a material adverse effect on the assets, liabilities, results of operations or financial condition of Purchaser and its Subsidiaries taken as a whole or on the ability of Purchaser and its Affiliates to perform their respective obligations under this Agreement and the Ancillary Agreements.

(eee) “Rate Lock Agreement” means that certain Rate Lock Agreement dated as of December 15, 2004 by and between SCL and LMIC, as amended.

(fff) “Representatives” as to any Person, means such Person’s directors, officers, employees, Affiliates, representatives (including financial advisors, attorneys, accountants and auditors) or agents.

(ggg) “SAP” means, as to any insurance entity, the statutory accounting principles prescribed or permitted by the Governmental Authority responsible for the regulation of insurance companies in the jurisdiction in which such entity is domiciled, consistently applied.

(hhh) “Securities Act” means the Securities Act of 1933, as amended, together with the rules and regulations thereunder.

(iii) “Seller Disclosure Letter” means the disclosure letter delivered by Seller to Purchaser concurrently with entering into this Agreement.

(jjj) “Seller Group” means Seller and its Affiliates, excluding any Transferred Company.

(kkk) “Seller Insurance Company” means LMIC.

(lll) “Straddle Period” means any Tax period that includes, but does not end on, the Closing Date.

(mmm) “Subsidiary” means, with respect to any Person, any corporation, limited liability company, partnership, association, or other business entity of which (a) if a corporation, a majority of the total voting power of shares of stock entitled (without regard to the occurrence of any contingency) to vote in the election of directors, managers, or trustees thereof is at the time owned or controlled, directly or indirectly, by that Person or one or more of the other Subsidiaries of that Person or a combination thereof or (b) if a limited liability company, partnership, association, or other business entity (other than a corporation), a majority of the partnership or other similar ownership interests thereof is at the time owned or controlled, directly or indirectly, by that Person or one or more Subsidiaries of that Person or a combination thereof and for this purpose, a Person or Persons own a majority ownership interest in such a business entity (other than a corporation) if such Person or Persons shall be allocated a majority of such business entity’s gains or losses or shall be or control any managing director or general partner of such business entity (other

than a corporation). The term “Subsidiary” shall include all Subsidiaries of such Subsidiary.

(nnn) “Tax” (or “Taxes” as the context may require) means any tax, however denominated, imposed by any federal, state, local, municipal, territorial or provincial or foreign government or any agency or political subdivision of any such government (a “Taxing Authority”), including any net income, alternative or add-on minimum tax, gross income, gross receipts, premium, sales, use, gains, goods and services, production, documentary, recording, social security, unemployment, disability, workers’ compensation, estimated, ad valorem, value added, transfer, franchise, profits, license, withholding, payroll, employment, excise, severance, stamp, capital stock, occupation, personal or real property, environmental or windfall profit tax, premiums, custom, duty or other tax, governmental fee or other like assessment or charge (but not including any guaranty fund assessment), together with any interest, penalty, addition to tax or additional amount imposed by any Taxing Authority relating to the assessment or collection thereof.

(ooo) “Tax Return” means any return or report (including any election, declaration, disclosure, schedule, estimate or information return) or amended return or report required to be supplied to a Taxing Authority relating to Taxes.

(ppp) “Transaction Agreements” means, collectively, this Agreement and the Ancillary Agreements.

(qqq) “Transferred Companies” means the Purchased Companies and the Transferred Subsidiaries.

(rrr) “Transferred Insurance Company” means a Transferred Company that is an insurance company.

(sss) “Transferred Non-Insurance Company” means a Transferred Company that is not an insurance company.

(ttt) “Transition Services Agreement” means the Transition Services Agreement to be entered into by and between Seller and Purchaser as of the Closing Date, the principal terms of which are set forth in Exhibit A hereto.

(uuu) “Transitional Trademark License Agreement” means the Transitional Trademark License Agreement substantially in the form of Exhibit B hereto to be executed at the Closing.

(www) "Transferred Shares" means the SHSI Shares and the SCL Membership Interests.

(xxx) "Transferred Subsidiary" means any Subsidiary of the Purchased Companies, including but not limited to, Heritage Summit Healthcare, LLC, a Florida limited liability company, Bridgefield Employers Insurance Company, a Florida corporation, and Bridgefield Casualty Insurance Company, a Florida corporation.

Section 1.2 Other Definitions.

Term	**Section in which Term is Defined**
"Acquisition Proposal"	Section 5.12
"AFG"	Preamble
"Agreement"	Preamble
"Annual Statutory Statements"	Section 3.19
"Audited Financial Statements"	Section 3.19
"Balance Sheet Date"	Section 3.19
"Balance Sheet Reserves"	Section 3.20
"Claims Notice"	Section 10.2(a)
"Closing"	Section 2.2
"Closing Conditions"	Section 2.2
"Closing Date"	Section 2.2
"Closing Statement"	Section 2.4(b)
"Company Insurance Policies"	Section 3.27(a)
"Deductible"	Section 10.5(a)
"Dispute Notice"	Section 2.4(c)
"Disputed Item"	Section 2.4(c)
"Enforceability Exceptions"	Section 3.2
"Equity Interests"	Recitals
"Estimated Closing Statement"	Section 2.4(a)
"Estimated GAAP Tangible Equity"	Section 2.4(a)
"Estimated Purchase Price"	Section 2.3(e)
"Financial Statements"	Section 3.19
"HSR Filing"	Section 5.13
"Indemnified Party"	Section 10.2(a)

"Indemnifying Party"	Section 10.2(a)

Term	Section in which Term is Defined
"Insurance Filings"	Section 3.10(a)
"Intercompany Agreements"	Section 3.11(i)
"LCS"	Recitals
"LMIC"	Recitals
"Material Contract"	Section 3.11
"New Benefit Plans"	Section 5.10(c)
"Orders"	Section 3.5(a)
"Outside Date"	Section 11.1(b)
"Policy Forms"	Section 3.10(c)
"Prior Year Reserve Release"	Section 3.18(d)
"Producers"	Section 3.14(a)
"Pro Forma Balance Sheet"	Section 3.19
"Purchased Company" or "Purchased Companies"	Recitals
"Purchased Company Securities"	Section 3.3(b)
"Purchaser"	Preamble
"Purchaser Awards"	Section 5.10(g)
"Purchaser Indemnified Parties"	Section 10.1(a)
"Regulatory Reports"	Section 3.10(b)
"Reinsurance Agreements"	Section 3.17(a)
"Resolution Period"	Section 2.4(d)
"Retained Employee"	Section 5.10(b)
"Seller"	Preamble
"Seller Awards"	Section 5.10(g)
"Seller Indemnified Parties"	Section 10.1(b)
"SCL"	Recitals
"SCL Membership Interests"	Recitals
"SHSI"	Recitals
"SHSI Shares"	Recitals
"Subsidiary Securities"	Section 3.4(b)
"Tax Accountant"	Section 6.4(d)

"Tax Matters"	Section 6.5(a)

Term	Section in which Term is Defined
"Third-Party Approvals"	Section 5.6(a)
"Third Party Claim"	Section 10.2(a)
"Transaction Consultant"	Section 2.4(e)
"Transferred Employees"	Section 5.10(a)
"Unassigned Agreement"	Section 5.6(b)
"Unresolved Items"	Section 2.4(e)
"WARN"	Section 5.10(j)

Section 1.3 Other Definitional Provisions.

(a) For purposes of this Agreement, the words "hereof," "herein," "hereby" and other words of similar import refer to this Agreement as a whole unless otherwise indicated.

(b) Whenever the singular is used herein, the same shall include the plural, and whenever the plural is used herein, the same shall include the singular, where appropriate.

(c) The term "including" means "including but not limited to."

(d) The use of the word "or" is not intended to be exclusive unless expressly indicated otherwise.

(e) Whenever used in this Agreement, the masculine gender shall include the feminine and neutral genders.

(f) All references herein to Articles, Sections, Subsections, Paragraphs, Exhibits and Schedules shall be deemed references to Articles and Sections and Subsections and Paragraphs of, and Exhibits and Schedules to, this Agreement unless the context shall otherwise require.

(g) Any reference herein to any statute, agreement or document, or any section thereof, shall, unless otherwise expressly provided, be a reference to such statute, agreement, document or section as amended, modified or supplemented (including any successor section) and in effect from time to time.

(h) All terms defined in this Agreement shall have the defined meaning when used in any Exhibit, Schedule, Ancillary Agreement, disclosure letter, certificate or other documents attached hereto or made or delivered

pursuant hereto unless otherwise defined therein, except where otherwise defined.

ARTICLE II
PURCHASE AND SALE OF EQUITY INTERESTS

Section 2.1 Consideration. Upon the terms and subject to the conditions of this Agreement, at the Closing, Seller shall cause LMIC and LCS to sell the Equity Interests to Purchaser, and Purchaser shall purchase the Equity Interests from LMIC and LCS, for the Purchase Price that is paid to Seller, subject to adjustment as set forth in Section 2.4.

Section 2.2 Closing. The closing (the "Closing") of the transactions contemplated hereby will take place at the offices of Debevoise & Plimpton LLP, 919 Third Avenue, New York, NY, at 10:00 a.m., Eastern time, on the third Business Day following the day on which the last of the conditions set forth in Article VII and Article VIII other than those conditions that by their terms are to be satisfied at the Closing, but subject to the satisfaction or waiver of those conditions at such time) (the "Closing Conditions") is satisfied or waived by the party or parties entitled to waive the same or such other date as Seller and Purchaser may mutually agree, provided that, the Purchaser may require that the Closing take place effective as of 12:01 a.m. on the first Business Day of the month following the month in which the last of the Closing Conditions is satisfied or waived by the party or parties entitled to waive the same, so long as the satisfaction or waiver of the last of the Closing Conditions results in a Closing Date within the last five (5) Business Days of the end of any month. To the extent the satisfaction or waiver of the last of the Closing Conditions results in a Closing Date within the first five (5) Business Days of the month, then the Closing shall occur on the third Business Day after the last of the Closing Conditions is satisfied or waived by the party or parties entitled to waive the same but shall be deemed by the Parties to be effective for accounting purposes as of 12:01 a.m. on the first Business Day of such month. The day on which the Closing takes place pursuant to this Section is referred to herein as the "Closing Date."

Section 2.3 Transactions at Closing. Upon the terms and subject to the conditions and limitations set forth in this Agreement, at the Closing each of the following shall occur:

(a) Seller shall cause LMIC or LCS, as applicable, to deliver to Purchaser certificates representing all of the Transferred Shares, accompanied by stock powers duly executed in blank or duly executed instruments of transfer;

(b) Seller shall deliver to Purchaser, and Purchaser shall deliver to Seller, duly executed counterparts of each of the Ancillary Agreements;

(c) Seller and Purchaser shall, or shall cause their respective Affiliates to, execute and deliver such other agreements, instruments or documents as are necessary or appropriate to give effect to the transactions contemplated by this Agreement and the Ancillary Agreements; and

(d) Immediately prior to Closing, Seller shall have terminated all intercompany reinsurance agreements with Affiliates of Seller except with respect to any intercompany reinsurance agreements set forth in Section 3.17(a)(4) of the Seller Disclosure Letter. At Closing, the Estimated Closing Statement shall reflect that such intercompany reinsurance arrangements have been terminated and such pooling arrangements unwound, and the reserves associated with the termination of such intercompany reinsurance arrangements funded with cash or short term government issued securities acceptable in writing to Purchaser. The capital and surplus of the Transferred Insurance Companies should reflect the capital and surplus of each such Transferred Insurance Company without regard to the internal reinsurance and pooling arrangements with Seller and its Affiliates.

(e) Purchaser shall pay to Seller an amount of cash equal to the Estimated Purchase Price by wire transfer of immediately available funds to an account designated in writing by Seller at least three (3) Business Days prior to the Closing Date. The "Estimated Purchase Price" shall be the amount of the GAAP Tangible Equity estimated by the Seller in good faith as of the Closing Date, plus forty-five million dollars ($45,000,000). For the avoidance of doubt, (i) the amount equal to $262,500 which represents 50% of the forfeited long-term incentive awards set forth in Section 5.10(h) shall be reflected in the calculation of GAAP Tangible Equity, but no other amounts in respect of any forfeited long-term incentive awards shall be reflected in the calculation of GAAP Tangible Equity, and (ii) any amounts payable by Purchaser pursuant to Section 5.10(i) shall be excluded from the calculation of GAAP Tangible Equity.

Section 2.4 Closing and Post-Closing Adjustments.

(a) Not later than the fifth Business Day prior to the Closing Date, Seller shall deliver to Purchaser a statement which shall be in the form attached hereto as Schedule 2.4(a) (the "Estimated Closing Statement"), setting forth an estimated calculation in reasonable detail of the GAAP Tangible Equity as of the Closing Date (the "Estimated GAAP Tangible Equity"), together with a

certification of a senior officer of Seller that the Estimated Closing Statement was estimated in good faith and based upon GAAP and the Books and Records.

(b) Seller shall, on or before the date that is sixty (60) calendar days after the Closing Date, deliver to Purchaser a statement (the "Closing Statement") consisting of a calculation in reasonable detail of GAAP Tangible Equity as of the Closing Date, in the same format as the Estimated Closing Statement, together with a certification of a senior officer of Seller to the same effect with respect to the Closing Statement as the certification of Seller's senior officer delivered with respect to the Estimated Closing Statement.

(c) The Closing Statement shall become final, binding and conclusive upon Seller and Purchaser on the sixtieth day following Purchaser's receipt of the Closing Statement, unless prior to such sixtieth day Purchaser delivers to Seller a written notice (a "Dispute Notice") stating that Purchaser believes the Closing Statement contains errors that would result in an adjustment to the Purchase Price in excess of $1,000,000 or was not prepared in accordance with GAAP, and specifying in reasonable detail each item that Purchaser disputes (each, a "Disputed Item"), the amount in dispute for each Disputed Item and the reasons supporting Purchaser's positions.

(d) If Purchaser delivers a Dispute Notice, then Seller and Purchaser shall seek in good faith to resolve the Disputed Items during the thirty-day period beginning on the date Seller receives the Dispute Notice (the "Resolution Period"). If Seller and Purchaser reach agreement with respect to any Disputed Items, Seller shall revise the Closing Statement to reflect such agreement.

(e) If Purchaser and Seller are unable to resolve all of the Disputed Items during the Resolution Period, then Purchaser and Seller shall jointly engage and submit the unresolved Disputed Items (the "Unresolved Items") to PricewaterhouseCoopers LLP (the "Transaction Consultant"). The Transaction Consultant shall act as an arbitrator to determine, based solely on presentations by Purchaser and Seller and not by independent review, only the Unresolved Items still in dispute and shall be limited to those adjustments, if any, required to be made for the Closing Statement to comply with the provisions of this Agreement. Purchaser and Seller shall agree, promptly after the Transaction Consultant has been appointed, on procedures governing the resolution of any dispute by the Transaction Consultant, provided that if Purchaser and Seller fail to agree on such procedures, the dispute resolution procedures of the American Arbitration Association shall govern. Purchaser and Seller shall use their reasonable best efforts to cause the Transaction Consultant to issue its written determination regarding the Unresolved Items within thirty days after such items

are submitted for review. The Transaction Consultant shall make a determination with respect to the Unresolved Items only and in a manner consistent with this Section 2.4 and GAAP, and in no event shall the Transaction Consultant's determination of the Unresolved Items be for an amount that is outside the range of Purchaser's and Seller's disagreement. Each of Purchaser and Seller shall use its reasonable best efforts to furnish to the Transaction Consultant such work papers and other documents and information pertaining to the Unresolved Items as the Transaction Consultant may reasonably request. The determination of the Transaction Consultant shall be final, binding and conclusive upon Purchaser and Seller absent manifest error, and Seller shall revise the Closing Statement to reflect such determination upon receipt thereof. The fees, expenses and costs of the Transaction Consultant shall be borne equally by Purchaser and Seller.

(f) Each party shall use its reasonable best efforts to provide promptly to the other parties all information and reasonable access to employees as such other parties shall reasonably request in connection with review of the Estimated Closing Statement, the Closing Statement or the Dispute Notice, as the case may be, including all work papers of the accountants who audited, compiled or reviewed such statements or notices (subject to the requesting party and its representatives entering into any undertakings required by the other party's accountants in connection therewith), and shall otherwise cooperate in good faith with such other parties to arrive at a final determination of the Closing Statement.

(g) In the event that the GAAP Tangible Equity as of the Closing Date (as reflected on the Closing Statement as finally determined pursuant to this Section 2.4) is greater than the Estimated GAAP Tangible Equity, Purchaser shall, within three (3) Business Days of the determination thereof, transfer to Seller the amount of such excess, together with interest thereon from and including the Closing Date but not including the date of such transfer, computed at LIBOR, by wire transfer of immediately available funds to an account or accounts designated by Seller.

(h) In the event that the GAAP Tangible Equity as of the Closing Date (as reflected on the Closing Statement as finally determined pursuant to this Section 2.4) is less than the Estimated GAAP Tangible Equity, Seller shall, within three (3) Business Days of the determination thereof, transfer to Purchaser the amount of such differential, together with interest thereon from and including the Closing Date but not including the date of such transfer, computed at LIBOR, by wire transfer of immediately available funds to an account designated by Purchaser.

Section 2.5 Allocation of Purchase Price. The Purchase Price, as adjusted as set forth in Section 2.4, shall be allocated for all tax purposes among the Transferred Shares and the assets of the Transferred Companies that are treated as disregarded entities for U.S. federal Income Tax purposes as provided in Section 2.5 of the Seller Disclosure Letter.

ARTICLE III
REPRESENTATIONS AND WARRANTIES OF SELLER

Except as set forth in the Seller Disclosure Letter, Seller hereby represents and warrants to Purchaser as of the Contract Date and as of the Closing Date (except where another date is specified, in which case the relevant representation and warranty is made only as of such specified date) as follows:

Section 3.1 Organization, Qualification and Corporate Power.

(a) Seller and each Transferred Company: (a) is duly organized and validly existing under the laws of its respective jurisdiction of organization, and such jurisdiction is listed in Section 3.1(a)(1) of the Seller Disclosure Letter; (b) has all requisite power and authority to carry on its business as it is now being conducted and to own, lease and operate its properties and assets; and (c) is duly qualified or licensed to do business as a foreign company in good standing in each jurisdiction in which the conduct of its business or the ownership, leasing or operation of its properties or assets or the nature of the business conducted by it makes such qualification necessary, except, in the case of clauses (b) and (c), where the failure to have such power and authority or to be so qualified would not, individually or in the aggregate, reasonably be expected to have a Business Material Adverse Effect and each such jurisdiction is listed in Section 3.1(a)(2) of the Seller Disclosure Letter.

(b) Seller has made available to Purchaser (i) true and complete copies of the Organizational Documents of each Transferred Company, as amended to the Contract Date, and (ii) true and complete copies of the stock transfer books and minute books or similar records of each Transferred Company.

(c) Section 3.1(c) of the Seller Disclosure Letter lists the name of and all titles held by each director and officer of each Transferred Company as of the date of this Agreement.

Section 3.2 Authorization. Seller has all requisite corporate power and authority to execute and deliver, and to perform its obligations under, this Agreement, and as of the date on which each Ancillary Agreement to which

Seller or any of its respective Affiliates (as applicable) is to be executed and delivered pursuant to the terms hereof, Seller or such applicable Affiliate, as applicable, will have all requisite corporate or equivalent power and authority to execute and deliver, and to perform its obligations under, each of the Ancillary Agreements to be so executed and delivered by it. The execution and delivery by Seller of this Agreement, and by the applicable Affiliate of Seller of the relevant Ancillary Agreements, and the performance by Seller or such Affiliates of its and their respective obligations under such agreements, have been duly authorized by Seller's board of directors and by all other necessary corporate action on the part of Seller, or by the applicable Affiliate's board of directors and by all other necessary corporate or company action on the part of such Affiliate, as the case may be. This Agreement has been duly executed and delivered by Seller, and each of the Ancillary Agreements to be executed by an Affiliate of Seller will, on the date such Ancillary Agreement is to be executed and delivered pursuant to the terms hereof, be duly executed and delivered by such Affiliate, and, subject to the due execution and delivery by the other parties to such agreements, this Agreement and the Ancillary Agreements will, upon due execution and delivery, be valid and binding obligations of such Seller or such Affiliate (as applicable), enforceable against Seller or such Affiliate in accordance with their respective terms, subject to:

(a) bankruptcy, insolvency, reorganization, fraudulent transfer, moratorium and other similar laws now or hereafter in effect relating to or affecting the rights of creditors of insurance companies or creditors' rights generally; and

(b) general principles of equity (regardless of whether considered in a proceeding at law or in equity).

Clauses (a) and (b) are referred to herein as the "Enforceability Exceptions."

Section 3.3 Capitalization; Title to Shares.

(a) The number of membership interests or shares of authorized capital stock, as applicable, of each of the Purchased Companies, and, in the case of the SHSI Shares, the par value thereof, is set forth in Section 3.3(a) of the Seller Disclosure Letter. The SCL Membership Interests and SHSI Shares are the only membership interests or shares of SCL and SHSI, respectively, that are issued and outstanding. The Equity Interests have been duly authorized and validly issued and are fully paid and non-assessable. LCS owns the SCL Membership Interests and LMIC owns the SHSI Shares, in each case beneficially and of record and free and clear of any Lien.

(b) Except as set forth in Section 3.3(b) of the Seller Disclosure Letter, there are no outstanding (i) phantom stock, equity party participation or shares of capital stock of or other voting or membership interests in any of the Purchased Companies, (ii) securities of any of the Purchased Companies convertible into or exercisable or exchangeable for shares of capital stock of or other voting or membership interests in such Purchased Company, (iii) options or other rights or agreements, commitments or understandings of any kind to acquire from any of the Purchased Companies, or other obligation of Seller, LCS, LMIC, any Purchased Company or any of their Affiliates to issue, transfer or sell, any shares of capital stock of or other voting or membership interests in any of the Purchased Companies or securities convertible into or exercisable or exchangeable for shares of capital stock of or other voting or membership interests in any of the Purchased Companies, (iv) voting trusts, proxies or other similar agreements or understandings to which Seller, LCS, LMIC, any of the Purchased Companies or any of their Affiliates is a party or by which Seller, LCS, LMIC, any of the Purchased Companies or any of their Affiliates is bound with respect to the voting of any shares of capital stock of or other voting or membership interests in any of the Purchased Companies or (v) contractual obligations or commitments of any character restricting the transfer of, or requiring the registration for sale of, any shares of capital stock of or other voting or membership interests in any of the Purchased Companies (the items in clauses (i), (ii) and (iii) being referred to collectively as the "Purchased Company Securities"). There are no outstanding obligations of any of the Purchased Companies or any of their respective Transferred Subsidiaries to repurchase, redeem or otherwise acquire any Purchased Company Securities.

Section 3.4 Subsidiaries; Ownership Interests.

(a) The authorized, issued and outstanding shares of capital stock of, and other voting or equity interests in, each of the Transferred Subsidiaries, the respective jurisdictions of formation of the Transferred Subsidiaries and each Purchased Company's direct or indirect ownership interest in each of the Transferred Subsidiaries are identified in Section 3.4(a) of the Seller Disclosure Letter.

(b) All of the outstanding shares of capital stock of and other voting or membership interests in each Transferred Subsidiary have been duly authorized and validly issued, fully paid and nonassessable and are owned beneficially and of record by one of the Purchased Companies or one of the Transferred Subsidiaries as set forth in Section 3.4(a) of the Seller Disclosure Letter, free and clear of any Liens other than Permitted Liens. Except as set forth in Section 3.4(b) of the Seller Disclosure Letter, there are no outstanding (i) phantom stock,

equity participation or shares of capital stock of or other voting or membership interests in any Transferred Subsidiary, (ii) securities of any of the Purchased Companies or any of their respective Affiliates convertible into or exercisable or exchangeable for shares of capital stock of or other voting or membership interests in any of the Transferred Subsidiaries or (iii) options or other rights or agreements, commitments or understandings of any kind to acquire from any of the Purchased Companies or any of their respective Affiliates, or other obligation of any of the Purchased Companies or any of their respective Affiliates to issue, transfer or sell, any shares of capital stock of or other voting or membership interests in any Transferred Subsidiary or securities convertible into or exercisable or exchangeable for shares of capital stock of or other voting or membership interests in any Transferred Subsidiary (the items in clauses (i), (ii) and (iii) being referred to collectively as the "Subsidiary Securities"). There are no outstanding obligations of any of the Purchased Companies or any of their respective Affiliates to repurchase, redeem or otherwise acquire any Subsidiary Securities.

(c) Except (i) for investment assets acquired in the Ordinary Course of Business or (ii) as set forth in Section 3.4(c) of the Seller Disclosure Letter, none of the Transferred Companies owns any shares of capital stock of or other voting or membership interests in (including any securities exercisable or exchangeable for or convertible into shares of capital stock of or other voting or membership interests in) any other Person.

Section 3.5 Litigation. Except as set forth in Section 3.5 of the Seller Disclosure Letter, as of the Contract Date, there are no:

(a) outstanding orders, writs, determinations, awards, decrees, injunctions, judgments or written agreements by or with any arbitrator or Governmental Authority ("Orders") applicable to any of the Transferred Companies or any of their respective properties or assets or the Business; or

(b) Actions pending or, to the Knowledge of Seller, threatened against any of the Transferred Companies, at law or in equity, before or by any Governmental Authority or before any arbitrator of any kind other than Actions involving claims under or in connection with Insurance Contracts in the Ordinary Course of Business.

Section 3.6 No Conflict or Violation. Except as set forth in Section 3.6 of the Seller Disclosure Letter, the execution, delivery and performance by Seller of this Agreement and by Seller or the applicable Affiliate of Seller of the Ancillary Agreements to which they may become a

party, and the consummation of the transactions contemplated hereby and thereby in accordance with the respective terms and conditions hereof and thereof will not:

(a) violate any provision of Organizational Documents of Seller, LMIC, LCS, any of the Transferred Companies or such Affiliate;

(b) violate, conflict with or result in the breach of any of the terms of, give any contracting party other than Seller, LMIC, LCS, the Transferred Companies or such Affiliate the right to terminate, or constitute (or with notice or lapse of time or both, constitute) a default under, any Material Contract or Reinsurance Agreement;

(c) violate any Order, or any agreement with, or condition imposed by, any Governmental Authority binding upon Seller, LMIC, LCS, any of the Transferred Companies or such Affiliate in connection with the Business;

(d) subject to obtaining the consents and approvals, making the filings and giving the notices referred to in Section 3.7 hereof, violate any Applicable Law; or

(e) result in a breach or violation of any of the terms or conditions of, constitute a default under, or otherwise cause an impairment or revocation of, any material Permit related to the Business;

except, in the case of Subsections (b)-(e) of this Section 3.6, for such breaches, conflicts, modifications, terminations, violations, defaults, impairments or revocations that may result from facts or circumstances relating to Purchaser or its Affiliates.

Section 3.7 Governmental Consents. The execution, delivery and performance by Seller of this Agreement, and by Seller or the applicable Affiliate of Seller of any Ancillary Agreement, and the consummation of the transactions contemplated hereby and thereby in accordance with the respective terms hereof and thereof, do not require Seller, LMIC, LCS, or such Affiliate to obtain any consent or approval from, or make any filing with, or give any notice to, any Governmental Authority, except (a) filings required under the HSR Act, (b) filings required by applicable Insurance Laws, (c) as set forth in Section 3.7 of the Seller Disclosure Letter, or (d) such consents, approvals, filings or notices the failure of which to be obtained, made or given, as the case may be, would, individually or in the aggregate, reasonably be expected to have a Business Material Adverse Effect.

Section 3.8 Compliance with Laws. Except as set forth in Section 3.8 of the Seller Disclosure Letter and subject to Section 3.10(e), since January 1, 2010, (a) each Transferred Company and, to the Knowledge of Seller and solely to the extent reasonably likely to adversely affect the operations of the Business from and after the Closing, the Seller Insurance Company, has complied in all material respects with all Applicable Laws and no Action has been filed or commenced against any of them, or threatened, alleging any failure to so comply, and (b) none of the Transferred Companies and, to the Knowledge of Seller and solely to the extent reasonably likely to adversely affect the operations of the Business from and after the Closing, the Seller Insurance Company (i) have received, any written notice or other written communication from any Governmental Authority regarding any actual or alleged violation of, or failure on the part of, the Transferred Companies to comply with any Applicable Laws or Governmental Orders applicable to them or their assets, properties or businesses (including any Insurance Laws), or (ii) is a party to, or bound by, any Governmental Order. None of the Transferred Companies is relying on any exemption from or deferral of any Law or Permit that would not be available to the Transferred Companies after Purchaser acquires the Equity Interests.

Section 3.9 Permits. Section 3.9 of the Seller Disclosure Letter lists all material Permits with respect to the Business or held by the Transferred Companies. Except as set forth in Section 3.9 of the Seller Disclosure Letter, the Transferred Companies hold all Permits required under Applicable Law in order to conduct the Business as currently conducted, and all such Permits are valid and in full force and effect. There is no Action, or to the Knowledge of Seller, investigation, that would reasonably be expected to lead to the revocation, amendment, failure to renew, limitation, suspension, or restriction of any Permit.

Section 3.10 Insurance Matters.

(a) Since January 1, 2011, each Transferred Company has filed all reports, statements, registrations, filings or submissions required to be filed with any Insurance Regulator under Insurance Laws governing insurance holding company systems, as to transactions between affiliated entities, extraordinary dividends, acquisitions of control, annual and quarterly financial statements, and other matters governed by such Insurance Laws governing holding company systems (collectively, the "Insurance Filings"), and all such Insurance Filings were true, complete and accurate in all material respects when filed.

(b) Seller has made available to Purchaser copies of all reports on financial examination, market conduct reports and other reports delivered by any Governmental Authority in respect of the Business since January 1, 2011 (collectively, the "Regulatory Reports") and no deficiencies have been asserted by any such Governmental Authority with respect to such Regulatory Reports that have not been cured or otherwise resolved.

(c) To the Knowledge of Seller, the Insurance Contracts are, and since January 1, 2011 have been, to the extent required under Applicable Law, written on forms (the "Policy Forms") approved by the applicable Insurance Regulator or filed and not objected to by such Insurance Regulator within the period provided for objection. No violations or deficiencies have been asserted by any Insurance Regulator with respect to any such Policy Form filings which have not been cured or otherwise resolved.

(d) None of the Transferred Companies is "commercially domiciled" under the Applicable Laws of any jurisdiction other than its respective jurisdiction of organization.

(e) Notwithstanding any of the representations and warranties contained elsewhere in this Agreement, (i) except as expressly stated therein, the representations and warranties in Section 3.8 shall not be read to cover compliance with Insurance Laws, and (ii) except where otherwise specifically noted, the representations and warranties contained in this Section 3.10 are the sole and exclusive representations and warranties made by Seller relating to the Insurance Filings, the Regulatory Reports and the Policy Forms.

Section 3.11 Contracts. Section 3.11 of the Seller Disclosure Letter lists the following contracts (written or oral) and other agreements (x) to which any Transferred Company is a party or to which any Transferred Company or any of its respective assets is bound or subject, or, to the Knowledge of Seller and solely to the extent reasonably likely to affect the operations of the Business from and after the Closing, (y) has been entered into by Seller or any of its Affiliates on behalf of and for the sole benefit of any of the Transferred Companies and to which any of the Transferred Companies are legally bound (each, a "Material Contract"):

(a) Any agreement (or group of related agreements) for the lease of personal property to or from any Person providing for lease payments in excess of $50,000 per annum;

(b) Any agreement (or group of related agreements) for the purchase or sale of products or the furnishing or receipt of services, the performance of which will extend over a period of more than one year or involve consideration in excess of $50,000;

(c) Any agreement concerning a partnership, joint venture, limited liability company, strategic alliance or other similar agreement or arrangement (including any agreement providing for joint research, development or marketing);

(d) Any agreement (or group of related agreements) under which it has created, incurred, assumed, or guaranteed any indebtedness for borrowed money, or any capitalized lease obligation, in excess of $50,000 or under which it has imposed a Lien on any of its assets, tangible or intangible;

(e) Any agreement that (i) limits the freedom of any Transferred Company to engage in any line or type of business in any particular geographic area or any particular medium, to compete with any Person, to solicit for employment, hire or obtain the services of any Person, (ii) contains exclusivity obligations or restrictions binding on any Transferred Company or that would be binding on Purchaser or any of its Affiliates after the Closing, or (iii) provides for a preferred or “most favored nations” status for any party thereto;

(f) Any agreement granting a right of first refusal or first offer or similar rights to any Person;

(g) Any agreement with Key Non-Affiliated Entities;

(h) Any agreement or license relating in whole or in part to the Intellectual Property of the Transferred Companies (including, without limitation, any agreement or license under which a Transferred Company has the right to use any Intellectual Property owned or held by a third party) which is material to the business, financial condition or results of operations of the Business (other than standard licenses for software that are commercially available to the public in the Ordinary Course of Business);

(i) Any contract between a Transferred Company, on the one hand, and Seller or any of its Affiliates (other than a Transferred Company), on the other hand (the “Intercompany Agreements”);

(j) Any agreement with any Governmental Authority;

(k) Other than transactions in Investments Assets, any agreement under which any Transferred Company has advanced or loaned any Person an amount exceeding $50,000; or

(l) Any other material agreement (or group of related agreements) not made in the Ordinary Course of Business.

Seller has delivered to Purchaser a correct and complete copy of each written agreement listed in Section 3.11 of the Seller Disclosure Letter and a written summary setting forth the material terms and conditions of each oral agreement referred to in Section 3.11 of the Seller Disclosure Letter. With respect to each such agreement: (i) the agreement is a legal, valid, and binding obligation of the Transferred Company party thereto and is enforceable against such party in accordance with its terms and is in full force and effect in all material respects; (ii) neither the applicable Transferred Company, nor, to the Knowledge of Seller, any other party to such agreement is in material breach or in default under the agreement (or alleged to be in material breach of or in default under the agreement); (iii) no event has occurred that with notice or lapse of time would constitute a material breach or default thereunder by any Transferred Company party to such agreement, or permit termination, modification, or acceleration of such agreement; (iv) no Transferred Company party thereto has provided any notice of any intention to terminate the agreement; and (v) the applicable Transferred Company has not repudiated any material provision of the agreement.

Section 3.12 Internal Controls

(a) Each Transferred Company and, to the Knowledge of Seller and solely to the extent reasonably likely to affect the operations of the Business from and after the Closing, the Seller Insurance Company, maintains internal accounting controls which provide reasonable assurance that (i) transactions are executed only with management’s authorization; and (ii) transactions are recorded as necessary to maintain accountability for its assets and permit preparation of (A) in the case of the Transferred Insurance Companies, its financial and statutory statements in conformity in all material respects with SAP and (B) in the case of Transferred Companies that are not Transferred Insurance Companies, its financial statements in conformity in all material respects with GAAP.

(b) Since January 1, 2010, neither the Transferred Companies and, to the Knowledge of Seller and solely to the extent reasonably likely to affect the operations of the Business from and after the Closing, the Seller Insurance Company, any of their respective directors or officers nor any of their respective

non-officer or director employees, auditors, accountants or Representatives has received any written non-frivolous complaint, allegation, assertion or claim (other than those that have been resolved without finding of material liability or improper conduct), regarding (i) the accounting, reserving or auditing practices, procedures, methodologies or methods of the Transferred Companies or the Seller Insurance Company or their respective internal accounting controls, including any complaint, allegation, assertion or claim that any Transferred Company or the Seller Insurance Company has engaged in questionable accounting, reserving or auditing practices; (ii) any significant deficiency or material weakness in the design or operation of any Transferred Company's internal controls over financial reporting which is reasonably likely to adversely affect such Transferred Company's or the Seller Insurance Company's ability to record, process, summarize and report financial information; or (iii) any fraud, whether or not material, that involves management or other employees of any Transferred Company or the Seller Insurance Company.

Section 3.13 Power of Attorney. There are no outstanding powers of attorney executed on behalf of any Transferred Company.

Section 3.14 Appointments and Licenses.

(a) Except as set forth in Section 3.14(a) of the Seller Disclosure Letter, since January 1, 2011, each Transferred Non-Insurance Company and, to the Knowledge of Seller, each other Person performing the duties of insurance producer, agency, agent, managing general agent, third party administrator, wholesaler, broker, service provider, solicitor, adjuster, marketer, underwriter, distributor or customer representative for the Business (collectively, "Producers") was duly licensed and appointed as an insurance producer, agency, agent, managing general agent, third party administrator, broker, service provider, solicitor or adjuster, as applicable (for the type of business written, sold or produced by such Producer at the time such Producer wrote, sold or produced business or performed such other act for or on behalf of the Transferred Companies or other Affiliate of Seller that may require a producer's, agency's, agent's, managing general agent's, third party administrator's, service provider's, solicitor's, broker's or other insurance license), as may be required by any Applicable Law. Since January 1, 2011, each Transferred Non-Insurance Company has marketed and sold all insurance policies and other insurance products, and provided services, in compliance in all material respects with all Applicable Laws.

(b) Seller does not own, directly or indirectly, (i) shares of capital stock of or other voting or membership interests in any of the Key Non-

Affiliated Entities, (ii) securities of any of the Key Non-Affiliated Entities convertible into or exercisable or exchangeable for shares of capital stock of or other voting or membership interests in such Key Non-Affiliated Entity, or (iii) options or other rights or agreements, commitments or understandings of any kind to acquire any shares of capital stock of or other voting or membership interests in any of the Key Non-Affiliated Entities or securities convertible into or exercisable or exchangeable for shares of capital stock of or other voting or membership interests in any of the Key Non-Affiliated Entities.

Section 3.15 Employees, Labor Matters, etc.

(a) Seller has made available to Purchaser a true and complete list of all Business Employees as of the date of this Agreement, including, to the extent permitted by Applicable Law, the title or position, hire date, current annual base compensation rate, commission, bonus or other incentive-based compensation, and work location.

(b) As of the date of this Agreement, no senior executive of the Transferred Companies or key group of Business Employees has communicated to Seller any plans to terminate employment with the Transferred Companies during the next twelve (12) months. No Transferred Company is a party to or bound by any collective bargaining agreement or similar agreement with any labor organization covering Business Employees, nor has any of them experienced any strike or material grievance, claim of unfair labor practices, or other collective bargaining dispute within the past five (5) years. No Transferred Company has committed any unfair labor practice with respect to the Business. Seller has no Knowledge of any organizational effort being made or threatened within the past five (5) years by or on behalf of any labor union with respect to Business Employees. Within the past three (3) years, no Transferred Company has implemented any plant closing or layoff of employees with respect to the Business requiring notice under the WARN Act, and no such action will be implemented without advance notification to, and the written consent of, Purchaser.

(c) The Transferred Companies are not and have not been, with respect to the Business: (A) “contractors” or “subcontractors” (as defined by Executive Order 11246), (B) required to comply with Executive Order 11246, or (C) required to maintain an affirmative action plan.

(d) Except as set forth in Section 3.15(d) of the Seller Disclosure Letter, none of the Transferred Companies has received with respect to the Business (i) notice of any unfair labor practice charge or complaint with respect

to it which is still pending before the National Labor Relations Board or any other Governmental Authority against it, (ii) notice of any charge or complaint with respect to it before the Equal Employment Opportunity Commission or any other Governmental Authority responsible for the prevention of unlawful employment practices which is still pending, (iii) notice of the intent of any Governmental Authority responsible for the enforcement of labor, employment, wages and hours of work, child labor, immigration, or occupational safety and health laws to conduct an investigation with respect to it or notice that such investigation is in progress in either case which is still pending, or (iv) notice of any Action pending in any forum by or on behalf of any present or former employee of any Transferred Company, any applicant for employment or classes of the foregoing alleging breach of any express or implied contract of employment, any Applicable Law governing employment or the termination thereof or other discriminatory, wrongful or tortious conduct in connection with the employment relationship.

(e) All compensation, including wages, commissions and bonuses, required to be paid as of the date of this Agreement to employees, independent contractors or consultants of the Transferred Companies have been timely paid. Except as set forth in Section 3.15(e) of the Seller Disclosure Letter, the Transferred Companies are in material compliance with all Applicable Laws respecting employment and employment practices, terms and conditions of employment and wages and hours. All individuals characterized and treated by the Transferred Companies as independent contractors or consultants are properly treated as independent contractors under all Applicable Laws, and all employees classified as exempt under the Fair Labor Standards Act and state and local wage and hour laws are properly classified.

(f) Notwithstanding any of the representations and warranties contained elsewhere in this Agreement, except where otherwise specifically noted, the representations and warranties contained in this Section 3.15 are the sole and exclusive representations and warranties made by Seller relating to employees and labor matters.

Section 3.16 Employee Benefit Plans and Related Matters; ERISA.

(a) Disclosure. Section 3.16(a)(1) of the Seller Disclosure Letter lists all Company Benefit Plans. For any Company Benefit Plan that is sponsored by the Seller or its Affiliates, Seller has made available to Purchaser complete and correct copies of each such Company Benefit Plan. Except as set forth on Section 3.16(a)(2) of the Seller Disclosure Letter no Company Benefit Plan is

sponsored or maintained solely by the Transferred Companies or provides benefits solely to the Business Employees.

(b) Qualification. Each Company Benefit Plan intended to be qualified under Section 401(a) of the Code, and the trust (if any) forming a part thereof, has received a favorable determination letter from the IRS, or with respect to a prototype plan, can rely on an opinion letter from the IRS to the prototype plan sponsor, to the effect that such Company Benefit Plan is so qualified and the plan and the trust related thereto are exempt from federal income taxes under Sections 401(a) and 501(a), respectively, of the Code, and, there are no existing circumstances or events that would reasonably be expected to result in any revocation of, or a change to, such determination letter or the unavailability of reliance on such opinion letter from the IRS, as applicable, nor has such revocation or unavailability been threatened. Nothing has occurred with respect to any Company Benefit Plan that has subjected or could reasonably be expected to subject Transferred Companies or, with respect to any period on or after the Closing, Purchaser or any of its Affiliates, to any material liability under ERISA or to Tax, penalty, or any material Liability under the Code.

(c) The execution, delivery and performance of this Agreement by Seller and the consummation by Seller of the transactions contemplated by this Agreement will not (alone or in combination with any other event) result in a material increase in the amount of compensation or benefits payable to or in respect of any current or former employee, officer, director or independent contractor of any of the Transferred Companies. No material payment or material deemed payment by the Transferred Companies will arise or be made as a result (alone or in combination with any other event) of the execution, delivery and performance of this Agreement by Seller, or the consummation by Seller of the transactions contemplated by this Agreement, that would not be deductible pursuant to Section 280G of the Code.

(d) Notwithstanding any of the representations and warranties contained elsewhere in this Agreement, except where otherwise specifically noted, the representations and warranties contained in this Section 3.16 are the sole and exclusive representations and warranties made by Seller relating to employee benefit plans and related matters.

Section 3.17 Reinsurance.

(a) Section 3.17(a)(1) of the Seller Disclosure Letter sets forth a complete and accurate list of all reinsurance and retrocession agreements to which any Transferred Insurance Company is a party (including any terminated

or expired treaty or agreement, but not including agreements that have been fully commuted) (collectively, the "Reinsurance Agreements"), true and correct copies of which have been made available to Purchaser. Section 3.17(a)(1) of the Seller Disclosure Letter also sets forth the effective date of each such Reinsurance Agreement , the termination date of any Reinsurance Agreement that has a definite termination date and indicates whether such Reinsurance Agreement will be terminated or commuted on or after the Contract Date and prior to the Closing Date. All reinsurance premiums due under the Reinsurance Agreements have been paid in full or are adequately accrued or reserved for by the Pro Forma Balance Sheet. No Transferred Insurance Company is in default and, to the Knowledge of Seller, no other party to any Reinsurance Agreement is in default, in each case, as to any material provision of any such Reinsurance Agreement, except as is being contested in good faith. Except as set forth in Section 3.17(a)(2) of the Seller Disclosure Letter, there are no pending or, to the Knowledge of Seller, threatened, Actions before any Governmental Authority or arbitrator with respect to any Reinsurance Agreements. Except as set forth in Section 3.17(a)(3) of the Seller Disclosure Letter, each Transferred Insurance Company was entitled to take credit in its most recent annual statutory statement in accordance with SAP for that portion of such Reinsurance Agreement as to which credit was taken in such statement. The transactions contemplated by the Transaction Agreements will not affect the obligations (if any) of the other parties to the Reinsurance Agreements to make payments to the applicable Transferred Insurance Company party thereto. Section 3.17(a)(4) of the Seller Disclosure Letter sets forth a complete and accurate list of the intercompany Reinsurance Agreements with Affiliates that will not be terminated and commuted prior to the Closing Date.

(b) Except as set forth in Section 3.17(b) of the Seller Disclosure Letter, neither the Seller nor any of its Affiliates (including the Transferred Companies) has received any written notice from any party to a Reinsurance Agreement that any material amount of reinsurance ceded thereunder will be in dispute.

(c) Section 3.17(c) of the Seller Disclosure Letter sets forth a correct and complete list of all Liens, collateral or security arrangements, including by means of a credit for reinsurance trust or letter of credit, to or for the benefit of any cedent under any Reinsurance Agreement.

Section 3.18 Absence of Certain Changes. Except as set forth in Section 3.18 of the Seller Disclosure Letter, since the Balance Sheet Date, (i) each Transferred Company has conducted the Business in the Ordinary Course of Business, and (ii) there has not occurred any event or events that, individually

or in the aggregate, have resulted in, or would reasonably be expected to result in, a Business Material Adverse Effect. Without limiting the generality of the foregoing, since that date:

(a) No Transferred Company has sold, leased, transferred, or assigned any material assets outside the Ordinary Course of Business;

(b) No Transferred Company has entered into any Material Contracts or any other material agreement, contract, lease, or license in connection with the Business outside the Ordinary Course of Business;

(c) No Transferred Company has accelerated, terminated, made material modifications to, waived or released any material rights or claims under, or canceled any Material Contract or Reinsurance Agreement outside the Ordinary Course of Business;

(d) None of the Transferred Companies has made any change in, to the extent applicable, its underwriting, reinsurance, claim processing and payment, selling, marketing, reserving, investing, financial accounting or investment policies, guidelines, practices or principles (other than (x) any change required by Applicable Law, GAAP or SAP, (y) in respect of underwriting or claims administration, in the Ordinary Course of Business, or (z) any prior year reserve release of up to $2.7 million in the aggregate (the "Prior Year Reserve Release"));

(e) No Transferred Company has entered into any new line of business;

(f) No Transferred Company has incurred any Lien (other than Permitted Liens) upon any material assets;

(g) No Transferred Company has made any capital expenditures in excess of $50,000, individually or in excess of $200,000 in the aggregate;

(h) Other than Investment Assets, no Transferred Company has made any material capital investment in, or any material loan to, any other Person;

(i) No Transferred Company has guaranteed the obligations of any other Person or created, incurred, or assumed more than $50,000 in aggregate indebtedness for borrowed money and capitalized lease obligations;

(j) No Transferred Company has transferred, assigned, or granted any license or sublicense of any material rights under or with respect to any Intellectual Property;

(k) There has been no change made or authorized in the Organizational Documents of any Transferred Company;

(l) No Transferred Company has issued, delivered, transferred, sold, pledged or otherwise disposed of or encumbered any capital stock of any Transferred Company or any securities convertible into or exchangeable for any such capital stock, or granted any options, warrants, or other rights to purchase or obtain (including upon conversion, exchange, or exercise) any such capital stock;

(m) No Transferred Company has declared, set aside, or paid any dividend or made any distribution with respect to its capital stock (whether in cash or in kind) or redeemed, purchased, or otherwise acquired any shares (or other applicable units) of its capital stock or other securities, and none of the Transferred Companies have effected any recapitalization, reclassification, stock split or like change in the capitalization of any Transferred Company;

(n) No Transferred Company has settled or compromised or agreed to the dismissal of any Action or threatened Action (in each case, except in the case of the Transferred Insurance Companies for claims under any Insurance Contracts within applicable policy limits), other than settlements or compromises that involved solely cash payments of less than $50,000 in the aggregate; and

(o) No Transferred Company has committed to any of the foregoing.

Section 3.19 Financial Statements. Seller has made available to Purchaser complete copies of (A) the audited financial statements of SCL at and for the periods ended December 31, 2010, 2011 and 2012 (such audited financial statements, collectively, the "Audited Financial Statements"), (B) unaudited statutory statements of each of the Transferred Insurance Companies at and for the periods ended December 31, 2010, 2011 and 2012 (the "Annual Statutory Statements") and (C) the unaudited *pro forma* balance sheet of the Business as of September 30, 2013 (such date, the "Balance Sheet Date", and such balance sheet, the "Pro Forma Balance Sheet", and together with the Audited Financial Statements and the Annual Statutory Statements, the "Financial Statements"). The Pro Forma Balance Sheet is included in Section 3.19 of the Seller Disclosure Letter; and the Financial Statements have been prepared in accordance with the respective accounting principles identified in

Section 3.19 of the Seller Disclosure Letter and, in the case of the Pro Forma Balance Sheet, give effect to the termination of certain reinsurance arrangements and the execution of a new Reinsurance Agreement, and (in the case of the Audited Financial Statements and the Annual Statutory Statements) presented fairly in all material respects in accordance with such accounting principles the financial position, results of operations and cash flows of the companies covered thereby at and for the respective periods indicated therein.

Section 3.20 Reserves. The reserves for payment of benefits, losses, claims and expenses under the Insurance Contracts reflected on the Pro Forma Balance Sheet, as of the Balance Sheet Date (the "Balance Sheet Reserves"), (i) were, in all material respects, determined in accordance with GAAP, consistently applied, (ii) were, in all material respects, fairly stated, (iii) satisfied, in all material respects, the requirements of Applicable Laws, and (iv) were computed in accordance with accepted loss reserving standards and principles and based on reasonable actuarial analysis and assumptions in accordance with generally accepted actuarial standards applied on a consistent basis; provided that notwithstanding anything to the contrary contained in this Agreement, Seller makes no representation, warranty, guaranty or covenant regarding, (1) the ultimate adequacy or sufficiency of, any reserves reflected in any financial statement, books, records or accounts of Seller or any of the Transferred Companies or (2) any inaccuracy in any forecasts, projections or similar materials that have been provided to Purchaser or any of its Affiliates or any of their respective directors, officers, employees, agents or representatives.

Section 3.21 Sufficiency of Assets.

(a) As of the Closing Date, the assets, properties and rights of the Transferred Companies, together with (i) the contracts, assets and obligations described in Section 3.21(a)(1) of the Seller Disclosure Letter which shall be contributed, transferred or assigned to SHSI or SCL, as applicable, prior to the Closing Date, (ii) the services contemplated to be provided to Purchaser or the Transferred Companies pursuant to the Ancillary Agreements (and the assets used to provide such services), and (iii) the services provided under Intercompany Agreements to be terminated as of the Closing, as described in Section 3.21(a)(2) of the Seller Disclosure Letter comprise all of the assets, properties and rights reasonably necessary to permit Purchaser to conduct the Business immediately following the Closing Date in the same manner as such Business is being conducted as of the date hereof. For the avoidance of doubt, Seller makes no representation or warranty in this Section 3.21 with respect to employees, which are exclusively addressed in Section 3.15 and Section 3.16.

(b) As of the Contract Date, each of the material assets and properties of the Transferred Companies, are free from defects (patent and latent), have been maintained in accordance with normal industry practice, are in good operating condition and repair (subject to normal wear and tear), and are suitable for the purposes for which it currently is used and proposed to be used, in each case, except as would not be, or would not reasonably be expected to be, materially adverse to the Transferred Companies.

Section 3.22 No Undisclosed Material Liabilities. No Transferred Company has any liabilities or obligations, in each case, of the type that would be required by SAP or GAAP to be specifically reflected on a balance sheet of the Business, other than: (i) liabilities set forth on the face of the Pro Forma Balance Sheet; and (ii) liabilities that have arisen after the Balance Sheet Date in the Ordinary Course of Business.

Section 3.23 Intercompany Accounts; Transactions with Affiliates.

(a) Section 3.23(a) of the Seller Disclosure Letter lists all inter-company balances as of the Balance Sheet Date between Seller or any of its respective Affiliates (other than the Transferred Companies), on the one hand, and any Transferred Company, on the other hand. Since the Balance Sheet Date, there has not been any accrual of liability by any Transferred Company to Seller or any of its respective Affiliates (other than a Transferred Company) or other transaction between a Transferred Company and Seller or any Affiliate of Seller (other than a Transferred Company), except in the Ordinary Course of Business.

(b) Section 3.23(b) of the Seller Disclosure Letter lists all Intercompany Agreements that will not be terminated on or prior to the Closing Date.

Section 3.24 Tax Matters.

(a) Except (x) as would not, individually or in the aggregate, reasonably be expected to have a Business Material Adverse Effect or (y) as set forth in Section 3.24 of the Seller Disclosure Letter:

(i) All Tax Returns required to be filed by or on behalf of the Transferred Companies have been duly and timely filed, and were complete and correct in all material respects when filed. All Taxes reflected on such Tax Returns, and all other Taxes required to be paid on or before the Closing Date by or with respect to, or which may be chargeable as a Lien upon the assets of, any Transferred Company, have

been, or prior to the Closing Date will be, duly and timely paid or are being contested in good faith by appropriate proceedings. All Taxes required to be withheld by any Transferred Company have been duly and timely withheld, such withheld Taxes have been either duly and timely paid to the proper Taxing Authority or properly set aside in accounts for such purpose and the Transferred Companies have complied in all material respects with all applicable Tax laws pertaining to Tax information reporting. A complete list of all federal, state and local Income Tax Returns filed or to be filed by the Transferred Companies for the 2011, 2012 and 2013 Tax years, including detail of Tax year, Taxing Authority, type of Tax, and filing entity is set forth in Section 3.24(a)(i) of the Seller Disclosure Letter.

(ii) (A) No written agreement waiving or extending, or having the effect of waiving or extending, the statute of limitations or the period of assessment or collection of any Taxes of any Transferred Company, and no written power of attorney with respect to any such Taxes that remains in effect has been filed or entered into with any Taxing Authority; (B) the time for filing any Tax Return of any Transferred Company has not been extended (other than through an automatic extension) to a date later than the Closing Date; (C) no Taxes of any Transferred Company are under audit, examination or investigation by any Taxing Authority; and (D) no Taxing Authority has asserted in writing any deficiency, claim or issue with respect to Taxes or any adjustment to Taxes against any Transferred Company with respect to any taxable period for which the period of assessment or collection remains open; and (E) there are no Liens for Taxes on any of the assets of the Transferred Companies other than Permitted Liens.

(b) SHSI and its Transferred Subsidiaries are members of an affiliated, combined or unitary group filing Consolidated or Combined Returns, (i) for U.S. federal Income Tax purposes and (ii) for state and local Income Tax purposes in the jurisdictions, if any, set forth in Section 3.24(b) of the Seller Disclosure Letter. None of the Transferred Companies (i) has received or applied for a Tax ruling or entered into a closing agreement pursuant to Section 7121 of the Code (or any predecessor provision or any similar provision of state or local law) that would be binding upon any Transferred Company after the Closing Date or (ii) has any liability for the Taxes of another Person (other than another Transferred Company) under Treasury Regulation Section 1.1502-6 or any similar provision of state, local or foreign law.

(c) None of the Transferred Companies will be required to include any item of income in, or exclude any item of deduction from, taxable income for any taxable period (or portion thereof) ending after the Closing Date, as a result of any (i) change in method of accounting for a taxable period ending on or prior to the Closing Date under Section 481 of the Code (or any corresponding provision of state, local or foreign income Tax law), (ii) installment sale or open transaction disposition made on or prior to the Closing Date, or (iii) any election under Section 108(i) of the Code (or similar provision of any state or local law). None of the Transferred Companies has "participated in a listed transaction" within the meaning of Treasury Regulations Section 1.6011-4(c) in any year for which the statute of limitations for the assessment or collection of Tax remains open.

(d) None of the Transferred Companies have constituted either a "distributing corporation" or a "controlled corporation" (within the meaning of Section 355(a)(1)(A) of the Code) in a distribution of stock qualifying for tax-free treatment under Section 355 of the Code (i) in the two years prior to the Closing Date or (ii) in a distribution which could otherwise constitute part of a "plan" or "series of related transactions" (within the meaning of Section 355(e) of the Code) in conjunction with the transactions contemplated by this Agreement.

(e) SCL and its Transferred Subsidiaries are each treated for federal tax purposes as a disregarded entity. None of SCL or its Transferred Subsidiaries has elected under Treasury Regulation Section 301.7701-3 with respect to its federal income tax classification.

(f) Notwithstanding any of the representations and warranties contained elsewhere in this Agreement, the representations and warranties contained in Section 3.16 and this Section 3.24, are the sole and exclusive representations and warranties relating to Tax matters.

Section 3.25 Intellectual Property. To the Knowledge of Seller, (a) the conduct of the Business does not infringe in any material respect the Intellectual Property rights of any Person and (b) none of the Intellectual Property owned by the Transferred Companies is being infringed in any material respect by any Person. To the Knowledge of Seller, all license fees due and owing with respect to software of other Intellectual Property licensed by the Transferred Companies have been paid in full.

Section 3.26 Real Property

(a) None of the Transferred Companies own any parcels of Real Property. Except as may be set forth in the Leases, the Transferred Companies have no outstanding options or obligations, rights of first offer or rights of first refusal to purchase any material real property.

(b) Section 3.26(b) of the Seller Disclosure Letter sets forth the address of each parcel of Leased Real Property, and a true and complete list of all Leases for each such Leased Real Property (including the date and name of the parties to such Lease document). Seller has delivered to Purchaser a true and complete copy in all material respects of each such Lease document (including any amendments, renewals, extensions, and guarantees related thereto). Except as set forth in Section 3.26(b) of the Seller Disclosure Letter, with respect to each of the Leases:

(i) each of the applicable Transferred Companies has a valid leasehold interest in the real property subject to a Lease included in the Leased Real Property, free and clear of all Liens, other than Permitted Liens;

(ii) such Lease is valid, binding, and in full force and effect;

(iii) the transactions contemplated by this Agreement do not require the consent of any other party to such Lease (except for those Leases for which lease consents set forth on Section 3.26(b) of the Seller Disclosure Letter are obtained), will not result in a breach of or default under such Lease;

(iv) to the Knowledge of Seller, neither the applicable Transferred Company nor any landlord party to the Lease has delivered or received any written notice of breach or default under such Lease in any material respect;

(v) the applicable Transferred Company has not subleased or licensed the Leased Real Property or any material portion thereof; and

(c) The Leased Real Property identified in Section 3.26(b) of the Seller Disclosure Letter comprise all of the material real property used in the business of the Transferred Companies.

(d) To the Knowledge of Seller, the Leased Real Property is in material compliance with all applicable building, zoning, subdivision, health and safety and other land use laws, including The Americans with Disabilities Act of

1990, as amended, affecting the Leased Real Property (collectively, the "Real Property Laws"). To the Knowledge of Seller, no Transferred Company has received any written notice of any material violation of any Real Property Law.

Section 3.27 Insurance Policies of the Transferred Companies.

(a) Section 3.27(a) of the Seller Disclosure Letter lists all material insurance policies (including fidelity bonds and other similar instruments, but excluding ceded Reinsurance Contracts) covering the Transferred Companies or the officers or directors thereof immediately following the Closing Date, in each case, as in effect on the Contract Date, other than insurance policies with Affiliates that will be terminated as of the Closing Date (the "Company Insurance Policies").

(b) All material premiums payable under the Company Insurance Policies either have been timely paid or adequate provisions for the payment thereof has been made. No written notice of cancellation or termination has been received by Seller or any Transferred Company with respect to any Company Insurance Policy.

Section 3.28 Brokers and Finders. No broker, finder or financial adviser has acted directly or indirectly as such for, or is entitled to any compensation from, Seller or any of its respective Affiliates in connection with this Agreement or the transactions contemplated hereby, except Bank of America Merrill Lynch, whose fees for services rendered in connection therewith will be paid by the Seller.

Section 3.29 Environmental, Health, and Safety Matters.

(a) Except as disclosed in Section 3.29(a) of the Seller Disclosure Letter, to the Knowledge of Seller, each of the Transferred Companies is, and since January 1, 2011 has been, in compliance, in each case in all material respects, with all Environmental, Health, and Safety Requirements.

(b) Without limiting the generality of the foregoing, each Transferred Company, has obtained and is in possession of, has for the past three (3) years complied, and is in compliance with, in each case in all material respects, all permits, licenses and other authorizations that are required pursuant to Environmental Health, and Safety Requirements for the occupation of its Leased Real Property and the operation of its Business.

(c) No Action is pending or, to the Knowledge of Seller, threatened against any Transferred Company arising under any Environmental, Health, and Safety Requirements. Since January 1, 2011, no Transferred Company has received any written notice, report or request for information regarding any actual or alleged violation of Environmental, Health, and Safety Requirements, or any liabilities or potential liabilities, or any claim based upon the release of or exposure to Hazardous Substances, including personal injury, wrongful death or property damage, including any investigatory, remedial, or corrective obligations, relating to any Transferred Company, their business, or their past or current facilities arising under Environmental, Health, and Safety Requirements, other than in connection with any such matter that has been resolved.

(d) To the Knowledge of Seller, there has been no release, discharge or disposal of Hazardous Substances by any Transferred Company at, on, under or from the Leased Real Property, or arising out of the operations of any Transferred Company, which, in each case, requires a material investigation or remediation by Seller or any of its Affiliates (including the Transferred Companies) under applicable Environmental, Health, and Safety Requirements or would otherwise reasonably be expected to result in the imposition of any material liability to any Transferred Company under any Environmental, Health, and Safety Requirements.

(e) To the Knowledge of Seller, there is no asbestos-containing material present in or on any Leased Real Property, in a condition constituting a violation of Environmental, Health, and Safety Requirements by any of the Transferred Companies, and since January 1, 2011, none of Seller or any of its Affiliates (including the Transferred Companies) has received a claim or demand relating to the presence of asbestos in or at any Leased Real Property.

(f) The representations and warranties set forth in this Section 3.29 are Seller's sole and exclusive representations and warranties regarding Environmental, Health and Safety matters.

Section 3.30 Guaranty Fund Assessments. The Transferred Insurance Companies have (i) timely paid or reserved for all guaranty association assessments that are due to any state guaranty association or other similar involuntary association or pool, and (ii) provided for all such assessments in the statutory statements to the extent necessary to be in conformity with SAP.

Section 3.31 Rating Agencies. Except as set forth in Section 3.31 of the Seller Disclosure Letter, as of the date of this Agreement, no rating agency has, to the Knowledge of Seller, indicated that it is considering the downgrade

of any rating assigned to any such Transferred Company or the placement of such Transferred Company on negative watch (other than any surveillance or review arising out of the transactions contemplated by this Agreement). Each such Transferred Company has as of the date of this Agreement the A.M. Best Company, Inc. and Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ratings set forth in Section 3.31 of the Seller Disclosure Letter.

Section 3.32 Portfolio Investments. All Investment Assets comply in all material respects with the applicable Insurance Laws and regulations of the respective state of domicile of the applicable Transferred Insurance Company. Except as set forth in Section 3.32 of the Seller Disclosure Letter, none of the Investment Assets is in default in the payment of principal or interest. Except as set forth in Section 3.32 of the Seller Disclosure Letter, as of the Contract Date, none of the Transferred Companies is a party to any derivative transaction which, pursuant to its terms and without any additional investment decision on the part of such Transferred Company, could result in an additional payment by such Transferred Company.

Section 3.33 Business Continuity. None of the material computer software, computer hardware (whether general or special purpose), telecommunications capabilities (including all voice, data and video networks) and other similar or related items of automated, computerized, and/or software systems and any other networks or systems and related services that are used by or relied on by the Transferred Companies in the conduct of the Business have experienced bugs, failures, breakdowns, or continued substandard performance in the past twelve (12) months that has caused, or would reasonably be expected to cause, a Business Material Adverse Effect.

Section 3.34 Data Privacy and Security. Since January 1, 2011, the conduct of the Business has complied in all material respects with and, as presently conducted, is in compliance in all material respects with, all Data Laws. Since January 1, 2011, neither the Seller nor any of its Affiliates (in the conduct of the Business) nor a Transferred Company in the conduct of any business has experienced any incidents involving personal information or other sensitive data that gave rise to any reporting requirements under applicable Data Laws, which, individually or in the aggregate, have resulted in, or would reasonably be expected to result in, a Business Material Adverse Effect.

Section 3.35 Actuarial Data. Seller has delivered to Purchaser data tables listed in Section 3.35 of the Seller Disclosure Letter for Purchaser's use in developing its independent projections of required loss, allocated loss

adjustment expense, and unallocated loss adjustment expense reserves in connection with the Business. With respect to each such data table, to the Knowledge of Seller, the data are accurate in all material respects. Notwithstanding the forgoing, no representation or warranty is made as to the accuracy of any actuarial analysis or estimates contained in the data tables listed in Section 3.35 of the Seller Disclosure Letter. The data tables delivered on the Contract Date do not reflect excess of loss workers' compensation reinsurance from an Affiliate of Seller with respect to 2009 and 2010; revised data tables reflecting such reinsurance will be delivered by Seller to Purchaser within five (5) Business Days following the Contract Date.

ARTICLE IV
REPRESENTATIONS AND WARRANTIES OF PURCHASER; OBLIGATIONS OF AFG

Except as set forth in the Purchaser Disclosure Letter, Purchaser, and, solely for the purpose of Section 4.6, AFG, hereby represent and warrant to Seller as of the Contract Date and as of the Closing Date (except where another date is specified, in which case the relevant representation and warranty is made only as of such specified date) as follows:

Section 4.1 Organization and Standing. Purchaser: (a) is duly incorporated and validly existing under the laws of its jurisdiction of incorporation; (b) has all requisite corporate power and authority to carry on its business as it is now being conducted and to own, lease and operate its properties and assets; and (c) is duly qualified or licensed to do business as a foreign corporation in good standing in each jurisdiction in which the conduct of its business or the ownership, leasing or operation of its properties or assets or the nature of the business conducted by it makes such qualification necessary, except, in the case of clauses (b) and (c), where the failure to have such power and authority or to be so qualified would not, individually or in the aggregate, reasonably be expected to have a Purchaser Material Adverse Effect.

Section 4.2 Authorization. Purchaser has all requisite corporate power and authority to execute and deliver, and to perform its obligations under, this Agreement, and as of the date on which each Ancillary Agreement to which Purchaser or an Affiliate of Purchaser (as applicable) is to be executed and delivered pursuant to the terms hereof, Purchaser or such applicable Affiliate, as applicable, will have all requisite corporate power and authority to execute and deliver, and to perform its obligations under, each of the Ancillary Agreements to be so executed and delivered by it. The execution and delivery by Purchaser of this Agreement, and by Purchaser or the applicable Affiliate of Purchaser, as

applicable, of the Ancillary Agreements to be so executed by Purchaser or such Affiliate, have been duly authorized by Purchaser's board of directors and by all other necessary corporate action on the part of Purchaser and its applicable Affiliates. This Agreement has been duly executed and delivered by Purchaser, and the Ancillary Agreements to be executed by Purchaser or an Affiliate of the Purchaser will, on the date such Ancillary Agreement is to be executed and delivered pursuant to the terms hereof, be duly executed and delivered by Purchaser or such Affiliate, and, subject to the due execution and delivery by the other parties to such agreements, this Agreement is, and the Ancillary Agreements executed by Purchaser or its applicable Affiliate will be, valid and binding obligations of Purchaser or such Affiliate, as applicable, enforceable against Purchaser or such Affiliate in accordance with their respective terms, subject to the Enforceability Exceptions.

Section 4.3 Actions and Proceedings. Except as disclosed in Section 4.3 of the Purchaser Disclosure Letter, there are no:

(a) outstanding Orders applicable to Purchaser or its properties or assets that, individually or in the aggregate, would reasonably be expected to have a Purchaser Material Adverse Effect; or

(b) Actions pending or threatened against Purchaser, at law or in equity, or before or by any Governmental Authority or arbitrator of any kind that would, individually or in the aggregate, reasonably be expected to have a Purchaser Material Adverse Effect.

Section 4.4 No Conflict or Violation. The execution, delivery and performance by Purchaser of this Agreement and the execution, delivery and performance by Purchaser or each of its applicable Affiliates of the Ancillary Agreements to which it is a party and the consummation of the transactions contemplated hereby and thereby in accordance with the respective terms and conditions hereof and thereof will not:

(a) violate any provision of the certificate of incorporation, bylaws or other Organizational Documents of Purchaser or such Affiliate;

(b) violate, conflict with or result in the breach of any of the terms of, result in any modification of the effect of, otherwise give any other contracting party the right to terminate, or constitute (or with notice or lapse of time or both, constitute) a default under, any material contract to which Purchaser is a party or by or to which any of its properties may be bound or subject;

(c) violate any Order, or any agreement with, or condition imposed by, any arbitrator or Governmental Authority binding upon Purchaser;

(d) subject to obtaining the consents and approvals, making the filings and giving the notices referred to in Section 4.5 hereof, violate any Applicable Law; or

(e) result in a breach or violation of any of the terms or conditions of, constitute a default under, or otherwise cause an impairment or revocation of, any Permit related to Purchaser's business;

except in the case of Subsections (a)-(e) of this Section 4.4, for such breaches, conflicts, modifications, terminations, violations, defaults, impairments or revocations that would not, individually or in the aggregate, reasonably be expected to have a Purchaser Material Adverse Effect.

Section 4.5 Governmental Consents. The execution, delivery and performance by Purchaser of this Agreement, and by Purchaser or the applicable Affiliate of Purchaser of any Ancillary Agreement to which it is a party, and the consummation of the transactions contemplated hereby and thereby in accordance with the respective terms hereof and thereof, do not require Purchaser or such Affiliate to obtain any consent or approval from, or make any filing with, or give any notice to, any Governmental Authority, except (a) filings required under the HSR Act, (b) as set forth in Section 4.5 of the Purchaser Disclosure Letter or (c) such consents, approvals, filings or notices the failure of which to be obtained, made or given, as the case may be, would not, individually or in the aggregate, reasonably be expected to have a Purchaser Material Adverse Effect.

Section 4.6 Sufficient Funds. AFG has, and at Closing Purchaser will have, sufficient funds to pay the Purchase Price, as it may be adjusted pursuant to the terms of Section 2.4, and to effect all other transactions contemplated by this Agreement and the Ancillary Agreements and to pay all fees and expenses of Purchaser related to the transactions contemplated by this Agreement and the Ancillary Agreements. Purchaser has provided Seller with a true and complete copy of (i) the audited GAAP financial statements of AFG as of December 31, 2012 (the "AFG Balance Sheet"), and (ii) a true and correct balance sheet of Purchaser as of September 30, 2013, and there has been no Purchaser Material Adverse Effect since such date.

Section 4.7 No Additional Representations; Inspection. Notwithstanding anything contained in this Agreement, any Ancillary

Agreement, the Seller Disclosure Letter or any of the Schedules or Exhibits hereto or thereto, Purchaser acknowledges and agrees that neither Seller nor any of its respective Affiliates, officers, directors, employees, advisors, agents, or other representatives is making or has made any representation or warranty whatsoever, express or implied, including any implied warranty of merchantability or suitability, as to the Transferred Companies or the Business, other than the representations and warranties expressly set forth in ARTICLE III and that the Transferred Companies and the Business are otherwise being sold "as is" and "where is." Without limiting the generality of the foregoing, neither Seller nor its respective Affiliates make any representations or warranties with respect to the success or profitability of the Business or the Transferred Companies, or otherwise with respect to the conduct of the Business following the Closing. In addition, Purchaser acknowledges and agrees that any estimates, forecasts, projections and predictions that have been provided or made available to Purchaser by or on behalf of Seller, including the Confidential Information Memorandum, the electronic data room and all management presentations established or provided in connection with the transactions contemplated by this Agreement, are not and shall not be deemed to be representations or warranties of Seller or any of its respective Affiliates and shall not form the basis, in whole or in part, for any claim against Seller or any of its respective Affiliates.

Section 4.8 Purchase For Investment; Investment Company. Purchaser is purchasing the Equity Interests for investment for its own account and not with a view to, or for sale in connection with, any distribution thereof. Purchaser (either alone or together with its advisors) has sufficient knowledge and experience in financial and business matters so as to be capable of evaluating the merits and risks of its investment in the Shares and is capable of bearing the economic risks of such investment. Purchaser acknowledges that the Equity Interests have not been registered under the Securities Act, or any state securities laws, and agrees that the Equity Interests may not be sold, transferred, offered for sale, pledged, hypothecated or otherwise disposed of without registration under the Securities Act, except pursuant to an exemption from such registration available under the Securities Act, and without compliance with foreign securities laws, in each case, to the extent applicable. Purchaser is not an investment company subject to registration and regulation under the Investment Company Act.

Section 4.9 Inspection. Purchaser acknowledges and agrees that it (i) has made its own inquiry and investigation into and, based thereon, has formed an independent judgment concerning the Transferred Companies and the Business, (ii) has been provided with adequate access to such information,

documents and other materials relating to the Transferred Companies and the Business as it has deemed necessary to enable it to form such independent judgment, (iii) has had such time as it deems necessary and appropriate to fully and completely review and analyze such information, documents and other materials and (iv) has been provided an opportunity to ask questions to Seller with respect to such information, documents and other materials and has received answers to such questions that it considers satisfactory. Purchaser and its Affiliates have made their investment decision with respect to the acquisition of the Business and the Equity Interests without reliance upon, any information, documents and other materials other than the representations and warranties contained in this Agreement.

Section 4.10 Brokers and Finders. No broker, finder or financial adviser has acted directly or indirectly as such for, or is entitled to any compensation from, Purchaser or its Affiliates in connection with this Agreement or the transactions contemplated hereby.

ARTICLE V
COVENANTS

Section 5.1 Preservation of Business, Conduct of Business. From the Contract Date through the Closing, except (a) as set forth in Section 5.1 of the Seller Disclosure Letter, (b) as contemplated by this Agreement or in furtherance of the transactions or other actions contemplated by this Agreement or the Ancillary Agreements (including the separation of the Business from the business of Seller and its Affiliates (other than the Transferred Companies)), (c) as required by Applicable Law, (d) to the extent consented to by Purchaser in writing, or (e) to the extent Purchaser fails to respond to a written request for consent within fifteen (15) Business Days after receipt of such request, (x) Seller shall cause each of the Transferred Companies and the Business to (i) operate in the Ordinary Course of Business, (ii) use commercially reasonable efforts to preserve intact the business of the Transferred Companies and the relationship of the Business with its policyholders (it being understood that no action by Seller or any of its respective Affiliates, as applicable, with respect to matters specifically addressed by any provision of Subsections (a) through (p) of this Section 5.1 shall be deemed to be a breach of the foregoing unless such action would constitute a breach of such provision of this Section 5.1), (iii) use commercially reasonable efforts to retain the services of officers and key employees, consultants, Producers and agents of the Business, and (iv) use commercially reasonable efforts to keep their business and properties

substantially intact, and (y) Seller shall cause the Transferred Companies not to do any of the following:

(a) (i) split, combine or reclassify any of the outstanding capital stock of, or issue or authorize the issuance of any other securities in respect of, in lieu of or in substitution for shares of, the outstanding capital stock of any Transferred Company, or (ii) purchase, redeem or otherwise acquire any shares of outstanding capital stock of any Transferred Company, or any rights, warrants or options to acquire any such shares;

(b) declare or pay any dividends or distributions on or in respect of any of the Equity Interests;

(c) transfer, issue, sell, pledge, encumber or dispose of, or authorize the transfer, issuance, sale, pledge, encumbrance or disposition of, any membership interests of or shares of capital stock or other securities of any of the Transferred Companies or grant options, warrants, calls or other rights to purchase or otherwise acquire any membership interests of or shares of capital stock or other securities of any of the Transferred Companies;

(d) amend the Organizational Documents of any Transferred Company;

(e) make any changes in the actuarial, underwriting, claims administration, actuarial reserving or accounting methods, policies, practices or principles of the Transferred Companies in effect on the date hereof (other than (x) any change required by Applicable Law, GAAP or SAP, (y) in respect of underwriting or claims administration, in the Ordinary Course of Business, or (z) the Prior Year Reserve Release);

(f) transfer, issue, sell, pledge, encumber or dispose of any assets of any of the Transferred Companies, other than (i) in the Ordinary Course of Business, including (A) treasury and cash management functions conducted in the Ordinary Course of Business, (B) Ordinary Course of Business reinsurance arrangements, or (C) dispositions of investments in a manner consistent with the respective investment policies of each Transferred Company, or (ii) any sale, assignment, transfer, lease, license or other disposition (including by way of reinsurance outside the Ordinary Course of Business) of any material assets of any of the Transferred Companies with a sale price that exceeds $25,000 individually or $100,000 in the aggregate or (iii) Permitted Liens;

(g) incur any indebtedness for borrowed money, or otherwise become responsible for any indebtedness of another Person;

(h) acquire any corporation, partnership, joint venture, association or other business organization or division thereof, or substantially all of the assets of any of the foregoing;

(i) enter into any settlement or release with respect to any Action or Order (except for claims under policies or contracts of insurance or reinsurance in the Ordinary Course of Business), unless such settlement or release (a) contemplates only the payment of money without ongoing limits on the conduct or operation of the Business, which payments of money shall not be in excess of $25,000 individually or $100,000 in the aggregate, (b) provides for a complete and unconditional release or dismissal with prejudice, and (c) does not include a statement or admission of fault, culpability or failure to act by or on behalf of the Transferred Company;

(j) abandon, modify, waive or terminate any material Permit;

(k) other than pursuant to its current terms, enter into, amend, terminate, renew or extend any Material Contract, Contract with Key Non-Affiliated Entities, Reinsurance Agreement or Lease, or enter into any contract that would be a Material Contract, Reinsurance Agreement or Lease if in effect on the Contract Date;

(l) acquire any owned real property (other than real estate acquired or held for investment purposes in the Ordinary Course of Business);

(m) other than actions taken in Ordinary Course of Business with respect to current or former employees of Seller and its Affiliates (including similarly situated Business Employees), (x) amend any Company Benefit Plan in any material respect in a manner affecting the Business Employees, (y) establish any new arrangement that would (if it were in effect on the date hereof) constitute a Company Benefit Plan that provides compensation or employee benefits to the Business Employees, or (y) take any action to increase the rate of compensation of the Business Employees;

(n) other than (x) actions taken in Ordinary Course of Business with respect to current or former employees of Seller and its Affiliates (including similarly situated Business Employees), (y) as provided for in any written agreements or Company Benefit Plans or (z) as required by Applicable Law, (i) other than bonuses already earned and payable under plans existing on the

Contract Date, grant any bonuses, whether monetary or otherwise, or increase in any wages, salary, severance, pension or other compensation or benefits in respect of the Business Employees, (ii) change the terms of employment for any Business Employee or terminate the employment of any Business Employees, in each case for which the aggregate costs and expenses of such action exceed $50,000, or (iii) accelerate the vesting or payment of any compensation or benefit for any Business Employee; provided, however, that nothing in this clause (n) is intended to limit the payments of any amounts that would ordinarily be paid such as payments from a long-term or short-term incentive program;

(o) issue, sell or grant options, warrants or rights to purchase or subscribe to, enter into any arrangement or contract with respect to the issuance or sale of, or redeem or repurchase any Purchased Company Securities or make any changes (by combination, reorganization or otherwise) in the capital structure of the Purchased Company (other than pursuant to the terms of the awards under a Company Benefit Plan); or

(p) agree or commit to do any of the foregoing.

Section 5.2 Reserve Balances. During the period between the Balance Sheet Date and the Closing Date, none of Seller, LMIC, LCS or the Transferred Companies shall take, or cause to be taken, any actions to record any favorable reserve development with respect to the reserves of the Transferred Insurance Companies (other than (i) any change required by Applicable Law, GAAP or SAP, (ii) Ordinary Course of Business reserve releases attributable to development of the in-force business of the Transferred Insurance Companies and (iii) the Prior Year Reserve Release) to the extent such actions would result in the difference between the Held Reserve and the Indicated Reserve as of the Closing Date as reflected in Section 5.2 of the Seller Disclosure Letter, as calculated by Seller's actuary in the same manner and applying consistent methodologies, as being less than the difference between the Held Reserve and the Indicated Reserve as of the Balance Sheet Date less the amount of the Prior Year Reserve Release.

Section 5.3 Access.

(a) During the period between the Contract Date and the Closing Date, Purchaser shall be entitled, through its employees and representatives and at its own expense, to make such examination of all premises, properties, books, records, contracts, and documents of or to extent principally pertaining to each Transferred Company or the Business as Purchaser may reasonably request. In addition, and subject to Section 5.4 of this Agreement, during the period between

the Contract Date and the Closing Date, (i) Purchaser shall be entitled through its employees and representatives and, at its own expense, to access such books, records, contracts and documents and make such examinations or interviews of Business Employees as Purchaser may reasonably request and only to the extent reasonably necessary to enable Purchaser to conduct business following Closing or to enable Purchaser to prepare its purchase accounting related to the transaction contemplated by this Agreement, and (ii) Seller shall permit all relevant Business Employees, as reasonably determined by Seller, to assist Purchaser with the preparation and delivery of appropriate presentations to third parties, including third-party reinsurers, as reasonably necessary to implement Purchaser's reasonably designed reinsurance program, after giving appropriate regard to matters of confidentiality in a form and substance satisfactory to Seller. Any investigation, examination or interview by Purchaser of employees of the Transferred Companies and its respective Affiliates or access or assistance pursuant to any of the provisions of this Section 5.3 shall be conducted or occur at reasonable times during normal business hours and upon reasonable prior notice to Seller with a representative of Seller present; provided, however, that such actions by Purchaser shall not unreasonably interfere with the normal operation of the Business. Notwithstanding any other provisions of this Section 5.3, Purchaser and Seller shall cooperate in implementing the provisions of this Section 5.3 so as not to prevent or interfere with Seller's compliance with Section 5.1 hereof.

(b) Following the Closing Date, Seller shall, and shall cause its Affiliates to: (i) allow Purchaser, upon reasonable prior notice and during normal business hours, through its employees and representatives, the right, at Purchaser's expense, to examine and make copies of any records retained by Seller in respect of the Transferred Companies for any reasonable business purpose, including, without limitation, the preparation or examination of Purchaser's Tax Returns, regulatory filings and financial statements, but only to the extent that such records of Seller constitute Books and Records; (ii) allow Purchaser to interview Seller's or its applicable Affiliate's employees for any reasonable purpose relating to the Business, including, without limitation, the preparation or examination of Tax Returns, regulatory and statutory filings and financial statements and the conduct of any litigation relating to the Business or otherwise, or the conduct of any regulatory, customer or other dispute resolution process and (iii) maintain such records for Purchaser's examination and copying until at least the sixth anniversary of the Closing Date, after which anniversary Seller may destroy such records in their discretion, provided that Seller and its Affiliates shall have no obligation to maintain or retain any books and records to the extent that electronic (to the extent that Purchaser has or had unrestricted

download capability to such electronic books and records) or paper copies or originals of such books and records are delivered to Purchaser or any of its Affiliates (including any of the Transferred Companies) at or prior to the Closing. Access to such employees and records shall not unreasonably interfere with the business operations of Seller or its respective Affiliates.

(c) Following the Closing Date, Purchaser shall, and shall cause its Affiliates to: (i) allow Seller, upon reasonable prior notice and during normal business hours, through their respective employees and representatives, the right to (A) examine and make copies, at Seller's expense, of the books and records of the Transferred Companies and (B) interview Purchaser's and its Affiliates' employees, in the case of either clause (i)(A) or (i)(B), in connection with the preparation or examination of Tax Returns, regulatory and statutory filings and financial statements, review of the Closing Statement, the conduct of any regulatory, customer or other dispute resolution process, to the extent related to the period prior to Closing; and (ii) maintain such books and records for Seller's examination and copying. Purchaser shall maintain and make available to Seller such books and records of the Transferred Companies for at least six (6) years after the Closing Date. Access to such employees and books and records shall not unreasonably interfere with the business operations of Purchaser or its Affiliates.

(d) Anything to the contrary in Section 5.3(a), (b) or (c) notwithstanding, the party granting access may withhold any document (or portions thereof) or information (i) that is subject to the terms of a non-disclosure agreement with a third party, (ii) that constitutes privileged attorney-client communications or attorney work product and the transfer of which, or the provision of access to which, as reasonably determined by such party's counsel, constitutes a waiver of any such privilege or (iii) if the provision of access to such document (or portion thereof) or information, as determined by such party's counsel, would reasonably be expected to conflict with Applicable Laws. Notwithstanding the foregoing, the party granting access shall provide Books and Records related to pending claims, compliance and regulatory matters, reinsurance and any other matter that is the subject of a pending matter, settlement or Order.

Section 5.4 Confidentiality.

(a) Without limiting any of the terms thereof, from the Contract Date until the Closing Date, the terms of the Confidentiality Agreement shall govern Purchaser's and its agents' and representatives' obligations with respect to all confidential information with respect to the Business, the Seller, the Transferred

Companies and their respective Affiliates and other related Persons, which has been provided or made available to them at any time, including during the period between the Contract Date and the Closing Date; and the terms of the Confidentiality Agreement are incorporated herein by reference. The Confidentiality Agreement shall continue in full force and effect until the Closing, at which time it shall automatically terminate.

(b) From and after the Closing: (i) Seller shall, and shall cause its respective Affiliates and representatives to, maintain in confidence any written, oral or other information to the extent relating to the Business obtained by virtue of Seller' ownership of the Business prior to the Closing; and (ii) Purchaser shall, and shall cause its Affiliates and representatives to, maintain in confidence any written, oral or other information of or relating to Seller or its respective Affiliates (other than information to the extent relating to the Business) obtained by virtue of its ownership of the Business from and after the Closing, except, in each case, to the extent that the applicable party is required to disclose such information by judicial or administrative process or pursuant to Applicable Law or such information can be shown to have been in the public domain through no fault of the applicable party. Notwithstanding the foregoing, after the Closing, Purchaser shall, and shall cause its Affiliates and representatives to, use commercially reasonable efforts to promptly (and in any event within six (6) months after the Closing) remove, erase, delete or otherwise destroy all information of or relating to Seller or its respective Affiliates (other than to the extent relating to the Business) (whether in print, electronic or other forms) in the possession of any Business Employee.

Section 5.5 Consents and Reasonable Efforts.

(a) Subject to the terms and conditions of this Agreement, each of Purchaser and Seller agrees to use its reasonable best efforts (i) to take, or cause to be taken, all actions, and to do, or cause to be done, all things necessary, proper or advisable to consummate and make effective, as soon as practicable and not more than 120 days after the Contract Date, the transactions contemplated by this Agreement and the Ancillary Agreements and (ii) to (A) lift or rescind any injunction or restraining order or other order adversely affecting the ability of the parties to consummate the transactions contemplated hereby and (B) defend any litigation or other proceeding seeking to enjoin, prevent or delay the consummation of the transactions contemplated hereby or seeking damages related thereto.

(b) Subject to the terms and conditions of this Agreement, each of Purchaser and Seller shall, and shall cause their respective Affiliates to, use their

reasonable best efforts (i) to take, or cause to be taken, all actions necessary, proper or advisable to comply promptly with all requirements with respect to the transactions contemplated by this Agreement and the Ancillary Agreements and, subject to the conditions set forth in Article VII and Article VIII, to consummate the transactions contemplated by this Agreement and the Ancillary Agreements and (ii) to obtain (and to cooperate with the other party to obtain) any consent, authorization, order or approval of, or any exemption by, any Governmental Authority and any other third party which is required to be obtained by Purchaser, Seller or any of their respective Affiliates in connection with the transactions contemplated by this Agreement, it being understood and agreed that, subject to Section 5.13, "reasonable best efforts" shall, with respect to the Purchaser, be deemed to include complying with any requirements of Applicable Law or of any Governmental Authority that may arise or be imposed in connection with the approval of the transactions contemplated hereby, provided that neither Seller, Purchaser nor any Affiliate shall be required to comply with any extraordinary requirements of a Governmental Authority that would materially and adversely interfere with the operations of the Business, taken as a whole.

(c) Without limiting the generality of the other provisions of this Section 5.5, Purchaser will promptly file appropriate "Form A's" with the applicable Governmental Authorities set forth in Section 3.7 of the Seller Disclosure Letter within twenty (20) Business Days from the Contract Date, and Purchaser and Seller and their respective applicable Affiliates will promptly (but in any event within twenty (20) Business Days from the Contract Date) file all documentary materials required with respect to other filings, notices, consents or approvals with or of any Governmental Authority in connection with the transactions contemplated by this Agreement and promptly file any additional information requested by any Governmental Authority as soon as practicable after receipt of a request therefor. Purchaser agrees promptly to provide, or cause to be provided, all information and documents that may be requested by any Governmental Authority relating to Purchaser or its Affiliates or its or their structure, businesses, operations, assets, liabilities or financial condition or any of its or their directors, officers, partners, members, or shareholders.

(d) To the extent necessary to ensure consistent reporting, the parties agree that they will consult with each other with respect to the obtaining of all consents or approvals of Governmental Authorities necessary or advisable to consummate the transactions contemplated by this Agreement and each party will keep the other apprised of the status of matters relating to such consents or approvals. Purchaser and Seller shall have the right to review in advance, and to

the extent practicable, and subject to any restrictions under Applicable Law, each will consult the other on, any material filing made with, or written materials submitted to, any third party or any Governmental Authority in connection with the transactions contemplated by this Agreement. Purchaser and Seller shall promptly furnish to each other copies of all such filings and written materials after their filing or submission, in each case subject to Applicable Laws.

(e) Purchaser and Seller shall, upon request, furnish each other with all information concerning themselves, their respective Affiliates, directors, officers and shareholders and such other matters as may be reasonably necessary or advisable in connection with the preparation of any statement, filing, notice or application made by or on their behalf to any Governmental Authority in connection with the transactions contemplated by this Agreement.

(f) Purchaser and Seller shall promptly advise each other upon receiving any communication from any Governmental Authority whose consent or approval is required for consummation of the transactions contemplated by this Agreement, including promptly furnishing each other copies of any written or electronic communications, and shall promptly advise each other when any such communication causes such party to believe that there is a reasonable likelihood that any such consent or approval will not be obtained or that the receipt of any such approval will be materially delayed or conditioned.

(g) None of Purchaser, on the one hand, or Seller or any Transferred Company, on the other hand, shall permit any of their officers or any other representatives or agents to participate in any live or telephonic meeting with any Governmental Authority in respect of any filings, investigation or other inquiry (other than routine, ministerial matters) relating to the transactions contemplated by this Agreement unless it consults with the other in advance and, to the extent permitted by Applicable Law and by such Governmental Authority, gives the other the opportunity to attend and participate in such meeting.

Section 5.6 Third-Party Consents.

(a) Seller and Purchaser shall, and shall cause their respective Affiliates to, cooperate and use commercially reasonable efforts to obtain, as promptly as possible but in no event later than the Closing, the consents, approvals and agreements of, or to give and make all notices and filings with the Persons listed in Section 5.6 of the Seller Disclosure Letter (the "Third-Party Approvals"); provided, in each case, that Seller and Purchaser shall bear equally the cost of obtaining any Third-Party Approval pursuant to this Section 5.6 up to $250,000, and Purchaser shall bear all such costs in excess of such amount. In

furtherance of the foregoing, Purchaser agrees to provide such assurances as to financial capability, resources and creditworthiness as may be reasonably requested by any Person whose consent, approval or agreement is sought hereunder. Notwithstanding the foregoing, the failure to obtain any Third-Party Approval shall not (x) constitute a failure to satisfy any condition set forth in Article VII or Article VIII or (y) otherwise relieve any Person from its obligation to consummate the transactions contemplated by this Agreement and the Ancillary Agreements.

(b) In the event and to the extent that Seller and Purchaser are unable to obtain any Third-Party Approval prior to the Closing, (i) Seller shall, for a period of up to twelve (12) months following the Closing, use commercially reasonable efforts in cooperation with Purchaser and its Affiliates (including the Transferred Companies) to provide or cause to be provided to Purchaser the benefits of any agreement for which Third-Party Approval has not been obtained (an "Unassigned Agreement"). If and when any Third-Party Approval shall be obtained, Seller shall promptly assign all of its rights and obligations under the Unassigned Agreement for which Third Party Approval has been obtained to Purchaser without the payment of further consideration and Purchaser shall, without the payment of any further consideration therefor, assume such rights and obligations and Seller shall be relieved of any and all obligation or liability hereunder and thereunder. Notwithstanding the foregoing, to the extent that Seller and Purchaser are unable to obtain any Third-Party Approval with respect to an agreement prior to the Closing, the parties hereto agree that from and after the Closing, Purchaser and the Transferred Companies shall not have any rights, or be entitled to any benefits, under such agreement until such time as such Third-Party Approval is obtained.

Section 5.7 Intercompany Balances; Certain Agreements.

(a) Seller shall, and shall cause its Affiliates to, take such actions and make such payments as may be necessary (including executing one or more releases in form and substance reasonably satisfactory to Purchaser) so that, immediately prior to the Closing, the Transferred Companies, on the one hand, and Seller and its Affiliates (other than the Transferred Companies), on the other hand, shall settle, discharge, offset, pay, repay in full, terminate or extinguish all Intercompany Obligations, regardless of their maturity, for the amount due, including any accrued and unpaid interest to but excluding the date of payment, fees and other amounts due or outstanding thereunder; provided, however, that if each such item is not paid in full in cash, the method of discharge must be reasonably satisfactory to Purchaser.

(b) On or prior to the Closing Date, Seller shall, and shall cause its Affiliates to, take such actions as may be necessary (including executing one or more instruments evidencing such termination and one or more releases, in each case, in form and substance reasonably satisfactory to Purchaser) to terminate and release the Transferred Companies from any and all liabilities and obligations arising in connection with all Intercompany Agreements

Section 5.8 Further Actions; Further Assurances.

(a) Each of the parties hereto shall execute such documents and other papers and perform such further acts as may be reasonably required to carry out the provisions hereof and the transactions contemplated hereby. Without limiting the covenants set forth in Section 5.5, each such party shall, at or prior to the Closing Date, use its reasonable best efforts to fulfill or obtain the fulfillment of the conditions precedent to the consummation of the transactions contemplated hereby, including the execution and delivery of any documents, certificates, instruments or other papers that are reasonably required for the consummation of the transactions contemplated hereby.

(b) On and after the Closing Date, Seller and Purchaser shall, and shall cause their respective Affiliates to, take all reasonable actions and execute any additional documents, instruments or conveyances of any kind which may be reasonably necessary to carry out any of the provisions hereof, so as to put Purchaser and its Affiliates in full possession and operating control of the Business and to effect fully the separation of the Business from the Seller.

Section 5.9 Expenses. Except as otherwise specifically provided in this Agreement or the Ancillary Agreements, the parties to this Agreement shall bear their respective expenses incurred in connection with the preparation, execution and performance of this Agreement and the Ancillary Agreements and the transactions contemplated hereby and thereby, including all fees and expenses of agents, representatives, counsel, investment bankers, actuaries and accountants.

Section 5.10 Employee Matters.

(a) Other than as set forth in Section 5.10(b), not less than twenty one (21) days prior to the expected Closing Date, Purchaser, or the appropriate Affiliate of the Purchaser, on behalf of the Transferred Companies, shall make offers of employment to eligible Business Employees, to be effective as of the Closing. Each such offer by Purchaser, or the appropriate Affiliate of the Purchaser, to a Business Employee shall provide the following terms and

conditions: (1) that such offer shall be effective as of the Closing; (2) that the initial work location immediately after the Closing shall be the same as immediately prior to the Closing and the initial job duties of the Business Employee immediately after the Closing shall be substantially similar as immediately prior to the Closing; (3) that the Business Employee's total annual cash compensation shall in the aggregate be substantially comparable to pre-Closing levels; (4) that the Business Employee shall be immediately eligible to participate in the fringe and employee benefit plans, programs and policies as Purchaser and its Affiliates provides to an eligible employee pursuant to the terms of such plan, program or policy; and (5) that such offer shall be deemed accepted unless affirmatively rejected by the Business Employee (each Business Employee who accepts or is deemed to have accepted such offer of employment (including pursuant to Section 5.10(b)), a "Transferred Employee"). Each such offer shall be subject to the screening procedures of Purchaser set forth in Section 5.10 of the Purchaser Disclosure Letter (for the avoidance of doubt, references in this Agreement to an "eligible" Business Employee means a Business Employee, subject to such screening procedures). Seller shall provide Purchaser with an updated list of the information described in Section 3.15(a) as reasonably requested by Purchaser in writing to enable Purchaser to make the offers of employment described in this Section 5.10(a). Notwithstanding the foregoing, an updated Section 3.15(a) of the Seller Disclosure Letter shall be provided to Purchaser no later than three (3) Business Days after the Contract Date and shall include the names of all Business Employees.

(b) Notwithstanding Section 5.10(a), Purchaser may, but shall not be obligated to, make an offer of employment to any Business Employee who is on short- or long-term disability, leave under the Family and Medical Leave Act or other leave approved (other than vacation) by the Transferred Companies as of immediately prior to the Closing (each, a "Retained Employee"). Each Retained Employee shall remain an employee of Seller and its Affiliates (other than the Transferred Companies), and neither Purchaser nor the Transferred Companies shall have or retain any liability or obligation in respect of the Retained Employee; provided, that if a Retained Employee is cleared for return to work to perform all essential job functions on or before the six (6) month anniversary of the Closing Date, Purchaser shall cause an offer of employment substantially consistent with the requirements of Section 5.10(a) to be made to such individual (if necessary, with reasonable accommodation). Any Retained Employee that accepts such an offer of employment shall be a Transferred Employee for purposes of this Agreement from and after his or her commencement of employment with Purchaser, the Transferred Companies or any of their Affiliates.

(c) For all purposes under the employee benefit plans, programs and arrangements established or maintained by Purchaser, the Transferred Companies and their respective Affiliates in which Business Employees may be eligible to participate after the Closing, (the "New Benefit Plans"), each Transferred Employee shall be credited with the same amount of service as was credited with the Transferred Companies and their Affiliates as of the Closing under similar or comparable Company Benefit Plans (only for purposes of eligibility to participate and vesting, but not for benefit accrual); provided, that such crediting shall not operate to duplicate any benefit or the funding of any benefit. In addition, and without limiting the generality of the foregoing, (i) with respect to any New Benefit Plans in which the Transferred Employees may be eligible to participate following the Closing, each Transferred Employee will be eligible to participate in such New Benefit Plans, based on the service credited pursuant to the first sentence of this Section 5.10(c), to the extent coverage under such New Benefit Plans replaces coverage under a similar or comparable Company Benefit Plan in which such Transferred Employee was eligible to participate immediately before such commencement of participation (such plans, collectively, the "Old Benefit Plans") and (ii) for purposes of each New Benefit Plan providing medical, dental, pharmaceutical, vision and/or life benefits to any Transferred Employee, Purchaser and the Transferred Companies shall cause all pre-existing condition exclusions and actively-at-work requirements of such New Benefit Plan to be waived for such Transferred Employee and his or her covered dependents, to the extent any such exclusions or requirements were waived or were inapplicable under any similar or comparable Company Benefit Plan; provided, to the extent dental, vision or life benefits are fully insured, only to the extent approved by the insurance carrier; provided further, that Purchaser shall use commercially reasonable efforts to obtain such consent. For each Business Employee enrolled in a New Benefit Plan providing medical coverage, Purchaser and the Transferred Companies shall cause any eligible expenses incurred by such Transferred Employee and his or her covered dependents during the portion of the plan year of the Old Benefit Plan ending on the date such Transferred Employee's participation in the corresponding New Benefit Plan begins to be taken into account for purposes of satisfying all deductible, and maximum out-of-pocket requirements applicable to such Transferred Employee and his or her covered dependents for the applicable plan year as if such amounts had been paid in accordance with such New Benefit Plan to the extent administratively practicable as determined in good faith by the Purchaser. For purposes of paid time off, each Transferred Employee will be provided payment by the Seller for the value of all accrued time through the Closing Date and, after the Closing Date, Transferred Employees will be provided with paid-time off pursuant to the terms of the Purchaser's program; provided, however, that (x) the

Transferred Employees will receive credit for all service with the Transferred Companies prior to and following the Closing Date and (y) in the event that a Transferred Employee received approval from Seller and its Affiliates of a vacation in the Ordinary Course of Business prior to the Closing Date, Purchaser shall, unless conflicting business demands require otherwise, advance the Transferred Employee the same number of paid vacation days so as to permit the Transferred Employee to take such vacation on a paid basis up to a maximum of five (5) days of paid vacation. For purposes of Transferred Employees who participate in the Seller's Savings Plan, the Purchaser shall cause the Purchaser's 401(k) plan to accept an elective direct rollover of the Transferred Employees' accounts under the Seller's Savings Plan which includes participant loans.

(d) Subject to any required enrollment and payment requirements, following the Closing Date Seller shall continue to honor eligibility for Company Benefit Plans providing post-retirement medical, dental and life insurance plans for all Transferred Employees who were eligible to retire from Seller and its Affiliates and receive the same as of the Closing. For purposes of determining the timing of commencement of the required enrollment procedures for such post-retirement benefits (but, for avoidance of doubt, not eligibility requirements), the date as of which the eligible Transferred Employee terminates service with Purchaser, the Transferred Companies and their Affiliates following the Closing Date shall be treated as the date as of which the Transferred Employee retired from service with Seller and its Affiliates; provided, however, that the Transferred Employee shall have notified Seller of the Transferred Employee's termination of employment with Purchaser, the Transferred Companies and their affiliates within 30 days of such termination of employment. Purchaser will not assume any liability associated with any of the Company Benefit Plans maintained by the Seller providing such benefits.

(e) With respect to any Transferred Employee whose employment is terminated by Purchaser, the Transferred Companies or any of their Affiliates (other than for cause) during the twelve-month period commencing immediately following the Closing Date, Purchaser shall provide, or shall cause its Affiliates to provide, severance benefits to such Transferred Employee, which shall be determined and payable in accordance with either (i) the severance benefit plan or arrangement maintained by Seller or any of its Affiliates for the benefit of such Transferred Employee immediately prior to the Closing Date or (ii) the severance benefit plan maintained for similarly situated employees of Purchaser and its Affiliates at the time of such Transferred Employee's termination of employment, whichever is more favorable to the Transferred Employee, in each

case taking into account all service with Seller, Purchaser and their respective Affiliates in determining the amount of severance benefits payable.

(f) No later than the later of the Closing Date and March 15, 2014, Seller shall cause eligible Business Employees to be paid amounts under Seller's and its Affiliates' annual bonus plans or other incentive plans, in each case with respect to performance periods completed prior to the date of payment, that are due or become due as a result of the transaction.

(g) Purchaser or its Affiliates shall grant and pay to Transferred Employees awards under an annual bonus plan maintained by Purchaser or its Affiliates subject to the achievement of performance goals and criteria determined by Purchaser ("Purchaser Awards"); provided that the performance period applicable to the Purchaser Awards shall begin as of January 1, 2014. The amount accrued by Seller from January 1, 2014 through and including the Closing Date in respect of the awards that Seller or its Affiliates' would have granted in the Ordinary Course of Business for the 2014 performance year under Seller's and its Affiliates' annual bonus plans for the performance period beginning in 2014 (collectively the "Seller Awards") shall be reflected in the calculation of GAAP Tangible Equity. The accrual will be based on the Seller Awards' target values, and will only be accrued to the extent Seller or its Affiliates have not made payment to the Transferred Employee in respect of the Seller Awards. No later than 5 Business Days prior to the Closing Date, Seller shall deliver to Purchaser a schedule detailing the names of the Transferred Employees who would have received Seller Awards, the amounts of such Seller Awards and the amounts accrued pursuant to this Section 5.10(g).

(h) On or as soon as reasonably practicable following the Closing Date, Purchaser or its Affiliates shall provide a compensatory arrangement to each Transferred Employee who forfeits one or more long-term incentive awards as a result of, or in connection with, the transactions contemplated by this Agreement, which compensatory arrangement shall provide an incentive opportunity for each such Transferred Employee to earn the value lost by the Transferred Employee in respect of such forfeited long-term incentive awards. An amount equal to $262,500 (which represents 50% of the amount of the forfeited long-term incentive awards) shall be reflected in the calculation of GAAP Tangible Equity. No later than 5 Business Days prior to the Closing Date, Seller shall deliver to Purchaser a schedule detailing the names of the Transferred Employees who will forfeit long-term incentive awards as a result of, or in connection with, the transactions contemplated by this Agreement, and the amounts of such awards that are so forfeited.

(i) Purchaser and Seller agree to the matters set forth on Section 5.10(i) of the Seller Disclosure Letter. For the avoidance of doubt, any amounts payable by Purchaser as set forth on Section 5.10(i) of the Seller Disclosure Letter shall be excluded from the calculation of GAAP Tangible Equity.

(j) Purchaser and its Affiliates shall not at any time prior to 90 days after the Closing Date effectuate a "plant closing" or a "mass layoff" as such terms are defined in the Worker Adjustment and Retraining Notification Act of 1988 ("WARN") or effectuate any similar triggering under any other applicable Law, affecting in whole or in part any site of employment, facility, operating unit directly related to the Business or Transferred Employee. Purchaser agrees to provide any required notice under WARN and any other Applicable Law and to otherwise comply with any such statute with respect to any "plant closing" or "mass layoff" (as defined in WARN) or any similar triggering event under any other Applicable Law occurring on or after the Closing or arising as a result of the transactions contemplated hereby

(k) The terms of this Section 5.10 shall not confer any rights or remedies upon any Transferred Employee or any Governmental Authority or any other Person other than the parties hereto. Nothing contained in this agreement shall constitute or be deemed to be an amendment to any Company Benefit Plan or any other compensation or benefit plan, program or arrangement. Nothing herein expressed or implied shall confer upon any Transferred Employee any rights or remedies, including without limitation, any right to employment or continued employment for any specified period of any nature or kind whatsoever.

(l) On or prior to the Closing Date, Seller shall pay in full all accrued and unpaid obligations to Transferred Employees for vacation, sick leave, and paid time off.

Section 5.11 Notice of Developments. From the date hereof until the Closing, Seller shall notify Purchaser in writing of: (i) any circumstance, event or action the existence, occurrence or taking of which that, to the Knowledge of Seller, has had, or would reasonably be expected to have, a Business Material Adverse Effect, (ii) any written notice or other communication from any Person alleging that the consent of such Person is required by this Agreement, (iii) any material communication from any Insurance Regulator with respect to the Transferred Companies or the Business; (iv) the resignation, or receipt of any written notice relating to the resignation, of any of the individuals set forth in Section 5.11 of the Seller Disclosure Letter; and (v) any material Action commenced or, to the Knowledge of Seller, threatened in writing against, the

Transferred Companies or the Business before any Governmental Authority or arbitrator, and Purchaser shall notify Seller in writing of any circumstance, event or action the existence, occurrence or taking of which that, to the Knowledge of Seller, has had, or would reasonably be expected to have, a Business Material Adverse Effect.

Section 5.12 Exclusivity. Seller will not (and Seller will cause each of LMIC, LCS and each Transferred Company not to) (i) solicit, initiate, or encourage the submission of any proposal or offer from any Person (other than Purchaser and its Affiliates) relating to the acquisition of all or any portion of the Business, including any capital stock or other voting securities, or any substantial portion of the assets, of any Transferred Company (whether structured as a merger, consolidation, share exchange, reinsurance transaction or otherwise) (an "Acquisition Proposal") or (ii) participate in any discussions or negotiations regarding, furnish any information with respect to, assist or participate in, or facilitate in any other manner any effort or attempt by any Person to do or seek any Acquisition Proposal. In the event that Seller or any of their Affiliates (including the Transferred Companies) receive an Acquisition Proposal, Seller shall promptly, but in no event later than forty-eight hours thereafter, notify Purchaser in writing of such proposal and provide a copy thereof (if in written or electronic form) or, if in oral form, a summary of the terms and conditions thereof.

Section 5.13 HSR. Seller and Purchaser shall, as promptly as practicable, but in no event later than twenty (20) calendar days following the execution and delivery of this Agreement, submit all filings required by the HSR Act (the "HSR Filing") and any other applicable Competition Law, as appropriate, and thereafter provide any supplemental information requested in connection therewith. Any such notification and report form and supplemental information will be in substantial compliance with the requirements of the HSR Act or other applicable Competition Law. Seller and Purchaser shall furnish to the other such necessary information and reasonable assistance as the other may request in connection with its preparation of any filing or submission that is necessary under the HSR Act or other applicable Competition Law. Seller and the Purchaser shall request early termination of the applicable waiting period under the HSR Act and any other applicable Competition Law. Seller and Purchaser shall each promptly inform the other party of any material communication received by such party from any Governmental Authority in respect of the HSR Filing or any Competition Law. Each of Seller and Purchaser shall (a) use its respective commercially reasonable efforts to comply as expeditiously as possible with all requests of any Governmental Authority for

additional information and documents, including information or documents requested under the HSR Act or other applicable Competition Law; (b) not (i) extend any waiting period under the HSR Act or any applicable Competition Law or (ii) enter into any agreement with any Governmental Authority not to consummate the transactions contemplated by this Agreement, except, in each case, with the prior consent of the Purchaser and Seller. Notwithstanding any of the foregoing, nothing in this Section 5.13 shall require, or be construed to require, Purchaser or any of its Affiliates to agree to (A) sell, hold, divest, discontinue or limit, before or after the Closing Date, any material assets, businesses or interests of any Purchaser, Seller, LMIC, LCS, any Transferred Company or any of their respective Affiliates; (B) any conditions relating to, or changes or restrictions in, the operations of any such assets, businesses or interests which, in either case, could reasonably be expected to materially and adversely impact the economic or business benefits to any Purchaser of the transactions contemplated by this Agreement; or (C) any material modification or waiver of the terms and conditions of this Agreement.

Section 5.14 Non-Solicitation. For a period of eighteen (18) months following the Closing Date Seller shall not, and shall cause its Affiliates not to, directly or indirectly or through any other Person, (a) solicit for employment or hire any Person who is at the time of solicitation, or within the three (3) month period prior thereto has been, employed by the Transferred Companies or otherwise employed on behalf of the Business, or (b) solicit for employment or hire any Person who is at the time of such solicitation, or within the three (3) month period prior thereto has been, employed by any of the Key Non-Affiliated Entities. For a period of two (2) years following the Closing Date, Seller shall not, and shall cause its Affiliates not to, directly or indirectly through any other Person, (x) solicit any of the Key Non-Affiliated Entities for the purpose of diverting the soliciting agent services work performed pursuant to the Contracts with Key Non-Affiliated Entities, or (y) make use of any Books and Records or undertake any directed effort to intentionally solicit any policyholder or Producer of the Business to transfer their policy from a Transferred Company to an Affiliate of Seller, subject to Applicable Laws. This prohibition on Seller’s ability to solicit in-force business from a Transferred Company specifically restricts advertisements, offers, commission programs, discounts, communications and promotions which are targeted to the Transferred Companies’ policyholders or their Producers. Nevertheless, nothing in this Section shall prohibit Seller from accepting business from any Producer where the business is proposed to Seller or its affiliates at the Producer’s independent initiation. Nothing in this Section 5.14 shall restrict the solicitation or hiring of any person (i) by means of a general solicitation or advertisement

that is not intentionally targeted at employees of the Transferred Companies or Persons otherwise employed on behalf of the Business, provided that, and solely for the purpose of this subsection (i), Seller may not hire any of the individuals set forth in Section 5.14 of the Seller Disclosure Letter even if they respond to such solicitation or advertisement, or (ii) whose employment has been terminated by Purchaser, the Transferred Companies or their Affiliates.

Section 5.15 Removal of "Liberty Mutual" Identifiers.

(a) Subject to the terms and conditions of the Transitional Trademark License Agreement, as soon as reasonably practicable after the Closing Date, but in no event later than fifteen (15) days after the Closing Date, Purchaser shall cause the Transferred Companies to cease using the Liberty Mutual Names and Marks as an identifier in the conduct of the Business as conducted by Purchaser; provided that in the event Purchaser or any Transferred Company is required to obtain the approval of any Governmental Authority set forth in Section 5.15 of the Purchaser Disclosure Letter prior to taking the actions contemplated in this Section 5.15, Purchaser and/or such Transferred Companies shall make all necessary filings within five (5) days of the Closing Date and use their reasonable best efforts to seek all such approvals as promptly as practicable after the Closing Date. Purchaser shall take all actions contemplated in this Section 5.15 as soon as reasonably practicable after obtaining the approvals referred to in this Section 5.15, but in no event later than five (5) Business Days after the date such approvals are received.

(b) Notwithstanding any other provisions in this Section 5.15, commencing as soon as reasonably practicable following the Contract Date, Purchaser and Seller shall cooperate and use commercially reasonable efforts to take all steps necessary to implement at the earliest practicable date the actions contemplated in Section 5.15(a).

Section 5.16 Ancillary Agreements. During the period prior to the Closing Date, the parties shall negotiate the services to be provided pursuant to the Transition Services Agreement, the Transitional Trademark License Agreement, and any other Ancillary Agreement, in good faith.

Section 5.17 Insurance Policies. From and after the Closing Date, the Transferred Companies and their assets will cease to be insured by any insurance policies or any self-insured programs of Seller or Seller's Affiliates. With respect to events or circumstances relating to the Business that occurred or existed prior to the Closing Date and that are covered by third party insurance policies of Seller or its Affiliates, Purchaser may request Seller or its Affiliates

to make claims under such policies and to remit to Purchaser any recoveries in respect of such claims, provided that Purchaser agrees to reimburse Seller or its Affiliates for either any retentions or deductibles or any retroactive or prospective premium adjustments associated with such coverage.

Section 5.18 Information Technologies. As soon as practicable following the Closing Date, Seller shall, and shall cause its Affiliates to, transfer to Purchaser all servers, laptops, data storage devices, UPS and mobile devices used exclusively by the Transferred Companies prior to the Contract Date, except for any such equipment located in Seller's Kansas City Data Center, provided that Purchaser shall, and shall cause the Transferred Companies to, promptly remove all software and data, including but not limited to, all information and images, relating to Seller and its Affiliates (other than the Transferred Companies) prior to the termination of the Transition Services Agreement by re-imaging all such devices with a Purchaser image. Purchaser hereby agrees to indemnify, defend and hold Seller and its Affiliates harmless from and against any Losses arising out of any third-Person claim as a result of or in connection with the failure of any Transferred Company to promptly remove all such aforementioned software and data from such servers, laptops and mobile devices by re-imaging prior to the termination of the Transition Services Agreement.

Section 5.19 Reinsurance. Prior to the Closing Date, Seller shall cause one of its Affiliates (other than a Transferred Insurance Company) to enter into a workers' compensation excess of loss reinsurance agreement with the Transferred Insurance Companies, the terms and conditions of which shall be substantially similar to the terms and conditions of the workers' compensation excess of loss reinsurance agreement entered into between Peerless Insurance Company and the Transferred Insurance Companies on January 1, 2009 and January 1, 2010, except with respect to reinsurance premiums.

ARTICLE VI
TAX MATTERS

Section 6.1 Seller's Responsibility for Taxes. From and after the Closing, Seller shall bear and pay, reimburse, indemnify and hold harmless Purchaser from and against any and all (a) Consolidated Income Tax Liabilities and (b) Taxes attributable to any Pre-Closing Tax Period imposed on any Transferred Company or for which any Transferred Company may be liable as

transferee, successor, by contract or otherwise, in each case, other than (i) Taxes imposed as a result of any transaction that occurs on the Closing Date after effective time of the Closing, (ii) Taxes arising as a result of Purchaser's making or causing to be made, without the prior written consent of Seller, any election under Section 338 of the Code (or any similar provision of state, local or foreign law) in respect of any Transferred Company and (iii) Taxes that are reflected in the Closing Statement. With respect to any Straddle Period, any liability for Taxes shall be apportioned between the Pre-Closing Period and the remaining portion of such Straddle Period (i) in the case of real and personal property Taxes on a per diem basis and (ii) in the case of all other Taxes, on the basis of a closing of the books as of the end of the effective time of the Closing, provided that exemptions, allowances or deductions that are calculated on an annual basis (including, but not limited to, depreciation and amortization deductions) shall be allocated between the Pre-Closing Tax Period and the remaining portion of such Straddle Period in proportion to the number of days in each such portion.

Section 6.2 Purchaser's Responsibility for Taxes. Purchaser shall bear and pay, reimburse, indemnify and hold harmless Seller and its Affiliates from and against all liabilities for Taxes relating to any Transferred Company, excluding Taxes for which Seller is responsible under Section 6.1.

Section 6.3 Refunds; Post-Closing Date Losses. Purchaser and Seller shall each be entitled to receive and retain any refund or other reimbursement in respect of Taxes for which such party is responsible under Section 6.1, Section 6.2 or Section 6.7, as the case may be, and Purchaser and Seller, as the case may be, shall promptly (a) notify the other party of the receipt by them or any of their Affiliates of any refund or other reimbursement to which the other party is entitled hereunder and (b) pay over such refund or other reimbursement (net of any reasonable costs attributable to the receipt of such refund or other reimbursement) to the other party. Neither Purchaser nor any Transferred Company shall, to the extent permitted by applicable Tax law, carryback to a Pre-Closing Tax Period any item of loss, deduction or credit or any net operating loss, net capital loss or other tax credit or benefit that is attributable to, arises from or relates to any Post-Closing Tax Period.

Section 6.4 Tax Returns.

(a) Seller shall be responsible for preparing all Tax Returns of the Transferred Companies for all tax periods ending on or prior to the Closing Date; provided, however, if any such Tax Return described in this Section 6.4(a) relates to a Tax for which Purchaser is responsible under Section 6.2, not later than (i) thirty (30) days prior to the due date for filing such Tax Return by

Seller, Seller shall provide Purchaser with a copy of such Tax Return for Purchaser's approval in the case of an Income Tax Return, and (ii) twenty (20) days prior to the due date for filing such Tax Return in the case of all other Tax Returns required to be filed by Seller. Seller shall prepare all Tax Returns pursuant to this Section 6.4(a) in a manner consistent with past practices unless otherwise required by law. Tax Returns (including amended Tax Returns) for the Transferred Companies for the tax period ending on the Closing Date shall be prepared in all material respects in a manner consistent with the current and deferred tax calculations that support the Closing Statement.

(b) Purchaser shall be responsible for preparing and filing all other Tax Returns relating to the business or assets of the Transferred Companies; provided, however, that in the case of any such Tax Return with respect to a Pre-Closing Tax Period or a Straddle Period, not later than (i) thirty (30) days prior to the due date for filing such Tax Return by Purchaser, Purchaser shall provide Seller with a copy of relevant portions of the draft of such Tax Return for Seller's approval in the case of an Income Tax Return, and (ii) twenty (20) days prior to the due date for filing such Tax Return in the case of all other Tax Returns required to be filed by Purchaser.

(c) Without the prior written consent of Seller, Purchaser shall not, and shall not permit any of its Affiliates to, amend any Tax Returns or make or change any Tax elections or accounting methods, in each case with respect to any Transferred Company relating to a Pre-Closing Tax Period or a Straddle Period, except to the extent required by applicable Tax law. Upon a determination by Purchaser or any such Affiliate that such amendment or making or changing of any Tax elections or accounting methods is so required, Purchaser shall promptly notify Seller of such determination.

(d) In the event of any disagreement between Purchaser and Seller regarding any Tax Return furnished to Seller or Purchaser for approval under either Section 6.4(a) or Section 6.4(b) that cannot be resolved by the fifteenth day prior to the due date for such Tax Return, such disagreement shall be resolved by an accounting firm of international reputation mutually agreeable to Purchaser and Seller (the "Tax Accountant"), and any such determination by the Tax Accountant shall be final. The fees and expenses of the Tax Accountant shall be borne equally by Purchaser and Seller. If the Tax Accountant does not resolve any differences between Purchaser and Seller with respect to such Tax Return at least five days prior to the due date therefor, such Tax Return shall be filed as prepared by Purchaser or Seller and amended to reflect the Tax Accountant's resolution.

Section 6.5 Tax Contests.

(a) Purchaser or Seller, as the case may be, shall notify the other party within twenty days after receipt by such party or any of its Affiliates of written notice of any pending federal, state, local or foreign Tax audit or examination or notice of deficiency or other adjustment, assessment or redetermination relating to Taxes for which such other party or its Affiliates may be responsible under Section 6.1, Section 6.2 or Section 6.7 ("Tax Matters").

(b) Seller shall have the sole right to control, contest, resolve and defend against any Tax Matters relating to Taxes of any Transferred Company for which Seller is obligated to indemnify Purchaser under Section 6.1 or that would otherwise reasonably be expected to result in a claim for indemnification against Seller pursuant to this Agreement. Subject to such control, Purchaser and its representatives shall be permitted, at Purchaser's expense, to be present at, and participate in any administrative or judicial proceeding with respect to Tax Matters other than any Tax Matters relating to any Consolidated Income Tax Liabilities or Consolidated or Combined Return.

(c) Subject to Section 6.5(d), Purchaser shall have the sole right to control all Tax Matters of any Transferred Company not controlled by Seller pursuant to Section 6.5(b). Subject to such control, Seller and its representatives shall be permitted, at Seller's expense, to be present at, and participate in, any administrative or judicial proceeding with respect to Tax Matters that would reasonably be expected to give rise to a liability for which Seller is responsible pursuant to Section 6.1 or that would otherwise reasonably be expected to result in a claim for indemnification against Seller pursuant to this Agreement.

(d) Purchaser shall not, and shall not permit its Affiliates to, concede, settle or compromise a Tax Matter (or portion thereof) controlled by Purchaser under Section 6.5(c) to the extent such concession, settlement or compromise could reasonably be expected to give rise to a liability for which Seller is responsible pursuant to Section 6.1 or otherwise result in a claim for indemnification against Seller pursuant to this Agreement without the consent of Seller, which consent shall not be unreasonably withheld, delayed or conditioned.

(e) Seller shall not, and shall not permit its Affiliates to, concede, settle or compromise a Tax Matter (or portion thereof) controlled by Seller under Section 6.5(b) to the extent such concession, settlement or compromise could reasonably be expected to increase the Taxes payable by Purchaser or any of its

Affiliates after the Closing Date without the consent of Purchaser, which consent shall not be unreasonably withheld, delayed or conditioned.

Section 6.6 Books and Records; Cooperation. Purchaser and Seller shall (and shall cause their respective Affiliates to) (a) provide the other party and its Affiliates with such assistance as may be reasonably requested in connection with the preparation of any Tax Return or any audit or other examination by any taxing authority or any judicial or administrative proceeding relating to Taxes, (b) retain (and provide the other party and its Affiliates with reasonable access to) all records or information that may be relevant to such Tax Return, audit, examination or proceeding, and (c) make employees available on a mutually convenient basis to provide assistance or information, provided that the foregoing shall be done in a manner so as not to interfere unreasonably with the conduct of the business of the parties.

Section 6.7 Transfer Taxes. All transfer, documentary, sales, use, stamp, registration, value added and other such Taxes and fees (including any penalties and interest) incurred in connection with the transactions contemplated by this Agreement (including any real property transfer tax and any similar Tax) shall be paid by one-half by Seller and one-half by Purchaser when due, and Seller and Purchaser will, at their own expense, file all necessary Tax Returns and other documentation with respect to all such Taxes and fees, and, if required by applicable law, Seller and Purchaser will, and will cause their respective Affiliates to, join in the execution of any such Tax Returns and other documentation filed by the other party.

Section 6.8 Tax Treatment of Indemnity Payments. To the extent permitted under applicable Tax law, the parties agree to treat any indemnity payment made under this Article VI or Article X as an adjustment to the Purchase Price for all federal, state, local and foreign Tax purposes, and the parties agree to, and shall cause their respective Affiliates to, file their Tax Returns accordingly.

Section 6.9 Tax Sharing Agreements. All Tax sharing arrangements and Tax indemnity arrangements relating to the Transferred Companies will terminate on the Closing Date and none of the Transferred Companies will have any liability thereunder commencing after the Closing Date.

Section 6.10 Certain Consolidated Return Elections. Seller shall make, or cause to be made, an election under Treasury Regulation Section 1.1502-36(d)(6) to the full extent necessary to avoid any attribute reduction in SHSI or any of its Transferred Subsidiaries pursuant to Treasury Regulation Section

1.1502-36(d). In the event of any such attribute reduction pursuant to Treasury Regulation Section 1.1502-36(d), Seller shall indemnify Purchaser in the amount of 35% of the attribute reduction when it occurs. In the event Seller elects under Treasury Regulation Section 1.1502-36(d)(6)(i)(B) to reattribute attributes of SHSI or any of its Transferred Subsidiaries to Seller, Seller shall indemnify Purchaser at the time of reattribution in an amount equal to 35% of the reattribution. Seller shall deliver to Purchaser for approval a copy of any election described in this Section 6.10, and, to the extent such election relates to a specific dollar amount of stock basis reduction, or provides for reattribution of attributes of Seller, supporting calculations under Treasury Regulation Section 1.1502-36(d), seventy-five days prior to the due date of the U.S. Federal Income Tax Consolidated or Combined Return for the year in which such election is made. Purchaser's approval of such election shall not be unreasonably withheld, delayed or conditioned.

Section 6.11 Deliveries to Purchaser. Seller shall, (a) on or before the date that is sixty (60) calendar days after the Closing Date, deliver to Purchaser calculations of stock tax basis, earnings and profits and tax attributes of the Transferred Companies and tax attributes of SHSI updated through the Closing Date, and (b) use its commercially reasonable effort to deliver to Purchaser copies of the Tax Returns for the Transferred Companies for the Tax period ending on the Closing Date, prepared on a stand-alone basis, not later than forty-five (45) days prior to the date such Tax Returns are to be filed with the IRS, and in any event not later than thirty (30) calendar days prior to such date, provided that, subject to other provisions of this Agreement, Seller shall have no additional liability to Purchaser with respect to any of the materials delivered to Purchaser pursuant to this Section 6.11.

Section 6.12 Overlap. To the extent of any inconsistency between this Article VI and Article X, this Article VI shall control as to matters relating to Taxes.

ARTICLE VII
CONDITIONS PRECEDENT TO THE OBLIGATION OF PURCHASER TO CLOSE

The obligations of Purchaser under this Agreement are subject to the satisfaction at or prior to the Closing of the following conditions, any one or more of which may be waived by Purchaser to the extent permitted by law:

Section 7.1 Representations, Warranties and Covenants.

(a) Seller shall have performed in all material respects its covenants and obligations under this Agreement required to be performed by it on or prior to the Closing Date, except to the extent that such covenants or obligations are qualified by the term "material," or contain terms such as "Business Material Adverse Effect," in which case Seller shall have performed and complied with all of such covenants (as so written, including the term "material" or "Material") in all respects through the Closing;

(b) the representations and warranties of Seller contained in ARTICLE III of this Agreement (without giving effect to any limitations as to "materiality" or "Business Material Adverse Effect" set forth therein) shall be true and correct at and as of the Closing Date with the same effect as though made at and as of such time (except for representations and warranties that are made as of a specific date which representations and warranties shall be true and correct at and as of such date), except where all failures to be so true and correct would not reasonably be expected, individually or in the aggregate, to have a Business Material Adverse Effect; and

(c) Purchaser shall have received a certificate signed by a duly authorized officer of Seller to the effect that the foregoing conditions have been satisfied.

Section 7.2 Other Agreements. Seller and its Affiliates shall have executed and delivered each Ancillary Agreement to which it is a party (other than those Ancillary Agreements to be executed and delivered after the Closing Date pursuant to the terms hereof).

Section 7.3 Reserved.

Section 7.4 Rate Lock Agreement. The Rate Lock Agreement shall have been terminated and any amounts advanced to LMIC thereunder shall be paid in cash by Seller to the appropriate Transferred Company.

Section 7.5 Governmental and Regulatory Consents and Approvals. All consents and approvals of Governmental Authorities listed in Section 3.7 of the Seller Disclosure Letter and Section 4.5 of the Purchaser Disclosure Letter shall have been obtained and shall be in full force and effect.

Section 7.6 Competition Law Notifications. The notifications of Purchaser and Seller pursuant to the HSR Act and other applicable Competition Laws shall have been made, all necessary consents shall have been obtained and

all waiting periods thereunder (and any extensions thereof) shall have expired or otherwise been terminated.

Section 7.7 Governmental Order. No Governmental Order shall have been issued and be in effect, and no Action shall be pending before any Governmental Authority or arbitrator which has the effect, or would have the effect if determined adversely, of (A) restraining or preventing consummation of any of the transactions contemplated by this Agreement or any of the Ancillary Agreements, or (B) causing any of the transactions contemplated by this Agreement or any of the Ancillary Agreements to be rescinded, or subject to rescission, following consummation.

Section 7.8 Resignations. Purchaser shall have received the resignations, effective as of the Closing, of each director and officer of the Transferred Companies, other than those directors and officers with respect to which Purchaser has notified Seller in writing at least five (5) Business Days prior to the Closing Date to not so resign.

Section 7.9 Other Deliverables.

(a) Seller shall have delivered to Purchaser copies of the certificate of incorporation or similar Organizational Documents of Seller, LCS, LMIC and each Transferred Company, certified as of a date that is no earlier than ten (10) Business Days prior to the Closing Date by the Secretary of State (or comparable officer) of the jurisdiction of each such Person's organization;

(b) Seller shall have delivered to Purchaser a certificate of good standing (or local law equivalent) for Seller, LCS, LMIC and each Transferred Company, issued as of a date that is no earlier than ten (10) Business Days prior to the Closing Date by the Secretary of State (or comparable officer) of the jurisdiction of each such Person's organization;

(c) Seller shall have delivered to Purchaser a certificate duly executed by the Secretary or an Assistant Secretary of Seller, dated the Closing Date, in form and substance reasonably satisfactory to Purchaser, as to: (A) no amendments to the certificate of incorporation or similar Organizational Document of Seller; (B) the bylaws of Seller; (C) the resolutions of the board of directors (or a duly authorized committee thereof) of Seller, LCS and LMIC authorizing the execution, delivery, and performance of this Agreement and each other Transaction Agreement to which Seller is a party, and (D) incumbency and specimen signatures of the officers of Seller executing this Agreement or any other agreement contemplated by this Agreement;

(d) The Books and Records, provided, however, to the extent that the Books and Records are in the possession of an Affiliate of Seller, the conditions set forth in this Section 7.9(d) shall be deemed satisfied so long as Seller shall use commercially reasonable efforts to provide such Books and Records promptly following the Closing Date; and

(e) One or more CDs including the Organizational Documents of each Transferred Company, as amended to the Contract Date, the Material Contracts and Reinsurance Agreements made available in the electronic data room.

ARTICLE VIII
CONDITIONS PRECEDENT TO THE OBLIGATION OF SELLER TO CLOSE

The obligations of Seller under this Agreement are subject to the satisfaction on or prior to the Closing of the following conditions, any one or more of which may be waived by them to the extent permitted by law:

Section 8.1 Representations, Warranties and Covenants.

(a) Purchaser shall have performed in all material respects its covenants and obligations under this Agreement required to be performed by it on or prior to the Closing Date, except to the extent that such covenants or obligations are qualified by the term "material," or contain terms such as "Purchaser Material Adverse Effect," in which case Purchaser shall have performed and complied with all of such covenants (as so written, including the term "material" or "Material") in all respects through the Closing;

(b) the representations and warranties of Purchaser contained in ARTICLE IV of this Agreement (without giving effect to any limitations as to "materiality" or "Purchaser Material Adverse Effect" set forth therein) shall be true and correct at and as of the Closing Date with the same effect as though made at and as of such time (except for representations and warranties that are made as of a specific date which representations and warranties shall be true and correct at and as of such date), except where all failures to be so true and correct would not reasonably be expected, individually or in the aggregate, to have a Purchaser Material Adverse Effect; and

(c) Seller shall have received a certificate signed by a duly authorized officer of Purchaser to the effect that the foregoing conditions have been satisfied.

Section 8.2 Other Agreements. Each of Purchaser and its applicable Affiliates shall have executed and delivered each Ancillary Agreement to which it is a party (other than those Ancillary Agreements to be executed and delivered after the Closing Date pursuant to the terms hereof).

Section 8.3 Governmental and Regulatory Consents and Approvals. All consents and approvals of Governmental Authorities listed in Section 3.7 of the Seller Disclosure Letter and Section 4.5 of the Purchaser Disclosure Letter shall have been obtained and shall be in full force and effect.

Section 8.4 Competition Law Notifications. The notifications of Purchaser and Seller pursuant to the HSR Act and other applicable Competition Laws shall have been made, all necessary consents shall have been obtained and all waiting periods thereunder (and any extensions thereof) shall have expired or otherwise been terminated.

Section 8.5 Governmental Order. No Governmental Order shall have been issued and be in effect, and no Action shall be pending before any Governmental Authority or arbitrator which has the effect, or would have the effect if determined adversely, of (A) restraining or preventing consummation of any of the transactions contemplated by this Agreement or any of the Ancillary Agreements, or (B) causing any of the transactions contemplated by this Agreement or any of the Ancillary Agreements to be rescinded, or subject to rescission, following consummation.

ARTICLE IX
SURVIVAL

Section 9.1 Survival of Representations, Warranties, Covenants and Certain Indemnities.

(a) The representations and warranties of Seller and Purchaser contained in this Agreement shall survive the Closing until the date that is eighteen (18) months following the Closing Date, except that the representations and warranties in Section 3.1, Section 3.2, Section 3.3, Section 3.4, Section 3.28, Section 4.1, Section 4.2, Section 4.7, Section 4.8 and Section 4.10 shall survive the Closing indefinitely and shall not terminate prior to the expiration of the applicable statute of limitations.

(b) Unless a specified period is set forth in this Agreement (in which event such specified period will control), covenants and agreements to be performed following the Closing shall survive the Closing and remain in effect until fully performed to the extent such covenants and agreements are to be performed following the Closing, and covenants and agreements to be fully performed at or prior to the Closing shall not survive the Closing.

(c) Notwithstanding anything to the contrary in this Section 9.1, any claims asserted in good faith with reasonable specificity (to the extent known at such time) and in writing by notice from the non-breaching party to the breaching party prior to the expiration date of the applicable survival period shall not thereafter be barred by the expiration of the relevant representation or warranty and such claims shall survive until finally resolved.

ARTICLE X
INDEMNIFICATION AND OTHER RIGHTS

Section 10.1 Obligation to Indemnify.

(a) Subject to the limitations on survival set forth in ARTICLE IX and to the limitations set forth in this ARTICLE X, Seller agrees to indemnify, defend and hold harmless Purchaser and its directors, officers, employees, Affiliates (including the Transferred Companies), successors and permitted assigns (collectively, the "Purchaser Indemnified Parties") from and against all Losses asserted against, imposed upon or incurred by any Purchaser Indemnified Party to the extent arising from:

(i) any breach of or inaccuracy in the representations and warranties made by Seller contained in ARTICLE III hereof or in any certificate or instrument delivered by or on behalf of Seller pursuant to this Agreement; or

(ii) any breach, nonfulfillment or default in the performance of any of the covenants, agreements or obligations of Seller contained in this Agreement.

(b) Subject to the limitations on survival set forth in ARTICLE IX and to the limitations set forth in this ARTICLE X, Purchaser agrees to indemnify, defend and hold harmless Seller and its respective directors, officers, employees, Affiliates, successors and permitted assigns (collectively, the "Seller Indemnified Parties") from and against all Losses asserted against, imposed upon or incurred by any Seller Indemnified Party to the extent arising from:

(i) any breach of or inaccuracy in the representations and warranties made by Purchaser contained in ARTICLE IV or in any certificate or instrument delivered by or on behalf of Purchaser pursuant to this Agreement;

(ii) any breach, nonfulfillment or default in the performance of any of the covenants, agreements or obligations of Purchaser or AFG contained in this Agreement; or

(iii) the ownership and operation of the Business from and after the Closing.

Section 10.2 Claims Notice.

(a) In the event that any Purchaser Indemnified Party or Seller Indemnified Party forms an intention to assert a claim for indemnification hereunder arising from a claim or demand made, or an Action or investigation instituted, by any Person not either a party to this Agreement or an Affiliate of a party to this Agreement that may result in a Loss for which indemnification may be claimed under this ARTICLE X (a "Third Party Claim"), such party seeking indemnification (the "Indemnified Party") shall, as promptly as practicable after forming such intention, give written notice (a "Claims Notice") to the other party (the "Indemnifying Party"). Such Claims Notice shall specify in detail the facts constituting the basis for, and the amount of, the claim asserted. The failure by any Indemnified Party to notify the Indemnifying Party as promptly as practicable shall relieve the Indemnifying Party of its indemnification obligations

except and only to the extent such failure or other actions taken by the Indemnified Party shall actually prejudice an Indemnifying Party; provided, however, that an Indemnifying Party shall have no obligation whatsoever to indemnify an Indemnified Party if a Claims Notice containing the information specified above is not received by the Indemnifying Party prior to the termination of the applicable periods described in Section 9.1.

(b) Subject to the provisions of this Section 10.2(b), upon receipt of a Claims Notice the Indemnifying Party shall have the right to assume the defense and control of Third Party Claims. In the event the Indemnifying Party exercises such right to assume the defense and control of a Third Party Claim, the Indemnified Party shall have the right but not the obligation reasonably to participate in (but not control) the defense of Third Party Claims with its own counsel and at its own expense, provided, however, that if the representation of the Indemnified Party and the Indemnifying Party by the same counsel creates a conflict of interest under applicable standards of professional conduct of attorneys or materially prejudices the defense or prosecution of the defenses available to the Indemnified Party, then the Indemnifying Party shall be liable for the reasonable fees and expenses of one separate counsel employed by the Indemnified Party. Notwithstanding the foregoing, the Indemnifying Party shall cooperate fully and in good faith with the Indemnified Party in the defense of any such Third Party Claim that (x) is asserted directly by or on behalf of a Person that is a Producer or customer of any Transferred Company, or (y) seeks an injunction or other equitable relief against the Indemnified Party. Any election by an Indemnifying Party to assume the defense of a Third Party Claim must be delivered by the Indemnifying Party to the Indemnified Party within fifteen (15) Business Days after receipt of the Indemnified Party's Claims Notice, and failure on the part of the Indemnifying Party to send such notice within such fifteen (15) Business Day period shall be deemed an election not to assume the defense of such Third Party Claim. If the Indemnifying Party elects to assume the defense of a Third Party Claim, then the Indemnified Party shall, and shall cause each of its directors, officers, employees, agents, representatives, Affiliates and permitted assigns to, cooperate fully with the Indemnifying Party in the defense of any such Third Party Claim, which cooperation shall include designating a liaison counsel to whom the Indemnifying Party may direct notices and other communications, using reasonable efforts to make witnesses available, and providing records and documents to the extent such witnesses, records and documents are relevant to the Third Party Claim.

(c) The Indemnified Party shall not consent to a settlement of, or the entry of any judgment arising from, any Third Party Claim without the consent

of the Indemnifying Party. The Indemnifying Party shall be authorized to consent to a settlement of, or the entry of any judgment arising from, any Third Party Claim as to which the Indemnifying Party has assumed the defense in accordance with the terms of Section 10.2(a), without the consent of any Indemnified Party, but only to the extent that such settlement or entry of judgment:

(i) provides solely for the payment of money,

(ii) does not impose an injunction or other equitable relief upon the Indemnified Party,

(iii) provides a complete and unconditional release of, or dismissal with prejudice of claims against, any Indemnified Party potentially affected by such Third Party Claim from all matters that were asserted in connection with such claims, and

(iv) does not include a statement or admission of fault, culpability or failure to act by or on behalf of the Indemnified Party.

Section 10.3 Procedures for Direct Claims. In the event any Indemnified Party shall form an intention to bring a claim that does not involve a Third Party Claim for indemnity against any Indemnifying Party, the Indemnified Party shall deliver written notice of such claim to the Indemnifying Party as promptly as practicable after forming such intention. Such notice shall specify in detail the facts constituting the basis for, and the amount of, the claim asserted. The failure by any Indemnified Party to notify the Indemnifying Party as promptly as practicable shall relieve the Indemnifying Party of its indemnification obligation except and only to the extent such failure or other action taken by the Indemnified Party shall actually prejudice the Indemnifying Party, provided, however, that an Indemnifying Party shall have no obligation whatsoever to indemnify an Indemnified Party if the written notice described in this Section 10.3 is not received by the Indemnifying Party prior to the termination of the applicable periods described in Section 9.1.

Section 10.4 Indemnification Payments. Any payment arising under this Article X shall be made by wire transfer of immediately available funds to such account or accounts as the Indemnified Party shall designate to the Indemnifying Party in writing; provided that such payments shall be made, without duplication, only to Purchaser or Seller, as the case may be.

Section 10.5 Limitations on Indemnification Obligations. In addition to any other limitations contained in ARTICLE IX and ARTICLE X hereof, the obligations of Seller and Purchaser to indemnify any Purchaser Indemnified Party or Seller Indemnified Party, as the case may be, are subject to, and limited by, the following:

(a) Seller shall be obligated to provide indemnification pursuant to Section 10.1(a)(i) only if the aggregate dollar amount of Losses with respect to all misrepresentations and breaches of warranty referred to in Section 10.1(a)(i) exceeds an amount equal to 1.5% of the Purchase Price as finally adjusted in accordance with Section 2.4 (the "Deductible"), and then only for the amount of Losses in excess of the Deductible; provided that Seller shall not be obligated to provide indemnification pursuant to Section 10.1(a)(i) if the dollar amount of any Loss resulting from a single claim or aggregated claims arising out of related facts, events or circumstances in connection with the breach of a representation or warranty is less than $15,000 and any such Loss or Losses shall not count towards the Deductible.

(b) The maximum aggregate liability of Seller for indemnification for all Losses pursuant to Section 10.1(a)(i) shall be an amount equal to 22.5% of the Purchase Price as finally adjusted in accordance with Section 2.4.

(c) Each Indemnified Party shall be obligated to use its reasonable best efforts to mitigate the amount of any Losses for which it is entitled to seek indemnification hereunder.

(d) The amount of any indemnification payments finally determined to be due to an Indemnified Party pursuant to this ARTICLE X or ARTICLE VI shall be calculated taking into account any Income Tax benefits actually recognized as a result of the Loss as to which such payment is made (net of any Income Tax detriment actually recognized in respect of the receipt of such payments) by such Indemnified Party. The Indemnified Party shall use its commercially reasonable efforts to contest any effort by a Governmental Authority to disallow any such net Income Tax benefits or to otherwise avoid such net Income Tax benefits becoming unavailable; notwithstanding the foregoing, to the extent any such net Income Tax benefit is subsequently finally determined to be disallowed or otherwise unavailable to the Indemnified Party, the Indemnified Party may recover the disallowed or unavailable amount from the Indemnifying Party.

(e) Upon making any indemnification payment, the Indemnifying Party will, to the extent of such payment, be subrogated to all rights of the

Indemnified Party against any third party in respect of the Loss to which the payment relates. Each such Indemnified Party and Indemnifying Party will duly execute upon request all instruments reasonably necessary to evidence and perfect the above-described subrogation rights.

(f) The amount of any Losses sustained by an Indemnified Party and owed by an Indemnifying Party shall be reduced by any amount to which such Indemnified Party actually receives with respect thereto under any insurance or reinsurance coverage, or from any other party alleged to be responsible therefor (taking into account any costs, expenses, and increased premiums incurred by the Indemnified Party or its Affiliates as a direct result of the pursuit or recovery of such amounts). The Indemnified Party shall use commercially reasonable efforts to collect any amounts available under such insurance or reinsurance coverage and from such other party alleged to have responsibility. If the Indemnified Party receives an amount under insurance or reinsurance coverage or from such other party with respect to Losses sustained at any time subsequent to any indemnification actually having been paid pursuant to this ARTICLE X, then such Indemnified Party shall promptly reimburse by that amount the applicable Indemnifying Party for any such indemnification payment actually made by such Indemnifying Party.

(g) Purchaser acknowledges and agrees that, notwithstanding anything to the contrary contained in ARTICLE III of this Agreement, Seller makes no representation, warranty, guaranty or covenant regarding, and shall have no obligation to indemnify Purchaser Indemnified Parties with respect to any Losses attributable to, (i) any changes in the level of risk-based capital that may be required to be held by any Transferred Company with respect to the liabilities and obligations arising under Insurance Contracts issued or assumed by such Transferred Company, or (ii) any change in Applicable Law, or in the interpretation, application or administration of Applicable Law, following the Closing Date.

(h) For the avoidance of doubt, Seller shall be under no obligation to indemnify any Purchaser Indemnified Party for any Losses to the extent reflected on the Closing Statement.

(i) Purchaser shall be obligated to provide indemnification pursuant to Section 10.1(b)(i) only if the aggregate dollar amount of Losses with respect to all misrepresentations and breaches of warranty referred to in Section 10.1(b)(i) exceeds an amount equal to 1.5% of the Purchase Price as finally adjusted in accordance with Section 2.4, and then only for the amount of Losses in excess of the Deductible; provided that Purchaser shall not be obligated to provide

indemnification pursuant to Section 10.1(b)(i) if the dollar amount of any Loss resulting from a single claim or aggregated claims arising out of related facts, events or circumstances in connection with the breach of a representation or warranty is less than $15,000 and any such Loss or Losses shall not count towards the Deductible.

Section 10.6 Exclusive Remedy. If the Closing occurs, the indemnities provided for in this ARTICLE X and in ARTICLE VI shall be the sole and exclusive remedy of the parties hereto and their respective officers, directors, employees, agents and Affiliates for any breach of or inaccuracy in any representation or warranty or any breach, nonfulfillment or default in the performance of any of the covenants or agreements contained in this Agreement, and the parties shall not be entitled to a rescission of this Agreement or to any further indemnification rights or claims of any nature whatsoever in respect thereof (including any common law rights of contribution), all of which the parties hereto hereby waive. The provisions of this Section 10.6 will not, however, prevent or limit a cause of action (a) under Section 12.10 to obtain an injunction or injunctions to prevent breaches of this Agreement and to enforce specifically the terms and provisions hereof, including but not limited to, the terms and provisions of Section 5.14, (b) under Section 2.4(e) to enforce any decision or determination of the Transaction Consultant or (c) arising out of fraud.

ARTICLE XI
TERMINATION PRIOR TO CLOSING

Section 11.1 Termination of Agreement. This Agreement may be terminated at any time prior to the Closing:

(a) by Seller or Purchaser in writing, if there shall be any Order of any Governmental Authority binding on Purchaser or Seller, which prohibits or restrains Purchaser or Seller from consummating the transactions contemplated hereby; provided that Purchaser or Seller, as the case may be, shall have used its commercially reasonable efforts to have any such Order lifted and the same shall not have been lifted by the Outside Date;

(b) by either of Seller or Purchaser in writing, if the Closing has not occurred on or before the last day of the month in which the 6-month anniversary of the Contract Date occurs (the "Outside Date") unless the absence of such occurrence shall be due to the failure of the party seeking to terminate this Agreement (or any of its Affiliates) materially to perform each of its obligations under this Agreement required to be performed by it on or prior to the Closing

Date; provided, however, that if the Closing hereunder has not occurred due solely to the failure of a party to receive a required consent or approval from a Governmental Authority, the parties agree to extend the Outside Date to the last day of the month that is three (3) months after the month in which the Outside Date occurs and to continue to use their respective reasonable best efforts to obtain such consent or approval;

(c) by Purchaser, if there has been any failure on the part of Seller to comply with or perform any of its respective agreements, covenants or obligations hereunder, including without limitations those set forth in ARTICLE VII hereof, and such failure has had or would reasonably be expected to have a Business Material Adverse Effect and such noncompliance or nonperformance shall not have been:

(i) cured or eliminated within fifteen (15) Business Days following receipt by Seller of written notice thereof from Purchaser; or

(ii) waived by Purchaser on or before the Closing Date;

(d) by Seller, if there has been any failure on the part of Purchaser to comply with or perform any of its agreements, covenants or obligations hereunder and such failure has had or could reasonably be expected to have a Purchaser Material Adverse Effect, and such noncompliance or nonperformance shall not have been:

(i) cured or eliminated by Purchaser within fifteen (15) Business Days following receipt by Purchaser of written notice thereof from Seller; or

(ii) waived by Seller on or before the Closing Date; or

(e) at any time on or prior to the Closing Date, by mutual written consent of Seller and Purchaser.

Section 11.2 Survival. If this Agreement is terminated as described above, this Agreement shall become null and void and of no further force and effect, except that:

(a) In the event of such a termination because of any intentional breach, the breaching party shall be liable to the other party for all Losses and damages arising directly from such breach; and

(b) the obligations arising under this Section 11.2 and the provisions of Sections 1.1, 1.2, 1.3, Section 12.1-Section 12.7 (inclusive), 12.10 and 12.12-12.16 (inclusive) hereof shall remain in full force and effect.

ARTICLE XII
MISCELLANEOUS

Section 12.1 Publicity. Except as may otherwise be required by Applicable Law, no release or announcement concerning this Agreement or the Ancillary Agreements or the transactions contemplated hereby or thereby shall be made by Purchaser without the prior written approval of Seller or by Seller without the prior written approval of Purchaser, which approval shall not be unreasonably withheld, conditioned or delayed. The parties hereto shall cooperate with each other in making any release or announcement.

Section 12.2 Confidentiality. In addition and subject to the covenants and limitations contained in Section 5.4 hereof, the parties agree that, other than as agreed or as required to implement the transactions contemplated hereby, the parties will keep confidential the terms and conditions of this Agreement and the Ancillary Agreements, including the Exhibits and Schedules hereto and thereto, and any written, oral or other information related to the negotiation hereof and thereof, except (a) as otherwise required by Applicable Law (including pursuant to the rules of any stock exchange or self-regulatory organization on which the securities of a relevant party are listed) or (b) disclosure to a Governmental Authority that is determined to be advisable in the reasonable judgment of the disclosing party.

Section 12.3 Notices. All notices, requests and other communications to any party hereunder shall be in writing (including facsimile transmission) and shall be given:

(a) if to Seller:

Liberty Mutual Group Inc.
175 Berkeley Street
Boston, MA 02116
Attention: Steven Zagoren

Liberty Mutual Group Inc.
175 Berkeley Street
Boston, MA 02116
Attention: Richard P. Quinlan, Senior Vice President and Deputy General Counsel

with a copy (which shall not constitute notice) to:

Debevoise & Plimpton LLP
919 Third Avenue
New York, NY 10022
Fax: (212) 909-6836
Telephone: (212) 909-6000
Attention: Nicholas F. Potter, Esq.

(b) if to Purchaser:

General Counsel
Great American Holding, Inc.
301 East Fourth Street
Cincinnati, OH 45202
Fax: (513) 369-5631
Telephone: (513) 369-5611
Attention: Vito C. Peraino, Esq., Senior Vice President

with a copy (which shall not constitute notice) to:

Office of Chief Financial Officer
American Financial Group, Inc.
301 East Fourth Street
Cincinnati, Ohio 45202
Fax: (513) 369-5631
Telephone: (513) 369-3696
Attention: Joseph E. (Jeff) Consolino, Executive Vice President and Chief Financial Officer

with a copy (which shall not constitute notice) to:

Keating Muething & Klekamp PLL
1 East Fourth Street, Suite 1400
Cincinnati, Ohio 45202
Fax: (513) 579-6457
Telephone: (513) 579-6456
Attention: D. Brock Denton, Esq.

or such other address or facsimile number as such party may hereafter specify for the purpose by notice to the other parties hereto. All such notices, requests and other communications shall be deemed received on the date of receipt by the recipient thereof if received prior to 5:00 p.m. on a Business Day in the place of

receipt. Otherwise, any such notice, request or communication shall be deemed to have been received on the next succeeding Business Day in the place of receipt.

Section 12.4 Entire Agreement. This Agreement (and the Ancillary Agreements, the Confidentiality Agreement and the other agreements contemplated hereby and thereby, and the Exhibits and Schedules hereto and thereto) contains the entire agreement among the parties with respect to the subject matter hereof and supersedes all prior agreements, written or oral, with respect thereto. Without limiting the generality of the foregoing sentence, the only representations and warranties made by the parties hereto with respect to the subject matter hereof are the representations and warranties contained in this Agreement and the Schedules and Exhibits hereto. Information disclosed to Purchaser in the Confidential Information Memorandum, the electronic data room, any management presentation or any other information provided to Purchaser or any of its Affiliates shall not form the basis for any claim against Seller or any of its respective Affiliates, officers, directors, employees, advisors, agents or representatives. The inclusion of any item in the schedules or exhibits hereto is not evidence of the materiality of such item for the purposes of this Agreement or any other purpose, and shall not be considered as evidence that such item was required to be disclosed therein.

Section 12.5 Waivers and Amendments; Non-Contractual Remedies; Preservation of Remedies. This Agreement and the Ancillary Agreements may be amended, superseded, canceled, renewed or extended, and the terms hereof may be waived, only by a written instrument signed by the parties hereto or thereto, as applicable, or, in the case of a waiver, in a written instrument signed by the party waiving compliance. No delay on the part of any party on exercising any right, power or privilege hereunder shall operate as a waiver thereof, nor shall any waiver on the part of any party of any right, power or privilege, nor any single or partial exercise of any such right, power or privilege, preclude any further exercise thereof or the exercise of any other such right, power or privilege. The rights and remedies herein provided are cumulative and, unless provided otherwise in this Agreement, including Section 10.6 hereof, or in the Ancillary Agreements, are not exclusive of any rights or remedies that any party may otherwise have at law or in equity.

Section 12.6 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware, without giving effect to its principles or rules of conflict of laws.

Section 12.7 Consent to Jurisdiction; Waiver of Jury Trial.

(a) All actions and proceedings arising out of or relating to this Agreement shall be heard and determined in the Chancery Court of the State of Delaware or, in the event that such court does not have subject matter jurisdiction over such action or proceeding, any federal court sitting in the State of Delaware, and the parties to this Agreement irrevocably submit to the exclusive jurisdiction of such courts (and, in the case of appeals, appropriate appellate courts therefrom) in any such action or proceeding and irrevocably waive the defense of an inconvenient forum to the maintenance of any such action or proceeding. The consents to jurisdiction set forth in this paragraph shall not constitute general consents to service of process in the State of Delaware and shall have no effect for any purpose except as provided in this paragraph and shall not be deemed to confer rights on any Person other than the parties hereto. Each of the parties to this Agreement consents to service being made through the notice procedures set forth in Section 12.3 and agrees that service of any process, summons, notice or document by registered mail (return receipt requested and first-class postage prepaid) to the respective addresses set forth in Section 12.3 shall be effective service of process for any suit or proceeding in connection with this Agreement or the transactions contemplated by this Agreement. The parties hereto agree that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by Applicable Law.

(b) EACH OF THE PARTIES TO THIS AGREEMENT IRREVOCABLY WAIVES ANY AND ALL RIGHTS TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATED TO THIS AGREEMENT.

Section 12.8 Seller Disclosure Letter and Purchaser Disclosure Letter. Disclosure of any fact or item in any section of the Seller Disclosure Letter or the Purchaser Disclosure Letter referenced by a particular paragraph or section in this Agreement shall, should the existence of the fact or item or its contents be relevant to any other paragraph or section and this relevance is apparent on the face of such disclosure, be deemed to be disclosed with respect to that other paragraph or section whether or not a specific cross-reference appears. Disclosure of any fact or item in any section of the Seller Disclosure Letter or the Purchaser Disclosure Letter shall not necessarily mean that such item or fact is material to the business or financial condition of (i) the Transferred Companies individually or taken as a whole or (ii) the Purchaser, as applicable.

Section 12.9 Binding Effect; Assignment. This Agreement and the Ancillary Agreements shall be binding upon and inure to the benefit of the parties and their respective successors, permitted assigns and legal representatives. Unless otherwise provided herein or in the Ancillary Agreements, neither this Agreement nor any Ancillary Agreement, nor any right or obligation hereunder or thereunder, may be assigned by any party (in whole or in part) without the prior written consent of the other parties hereto; provided, however, that with notice to Seller, Purchaser may assign its rights and obligations hereunder to an Affiliate, with the consent of Purchaser not to be unreasonably withheld, delayed or conditioned; provided, further, that no such assignment shall release Purchaser from any of its obligations hereunder.

Section 12.10 Severability. Any term or provision of this Agreement that is determined by a court of competent jurisdiction to be inoperative or unenforceable for any reason shall, as to that jurisdiction, be ineffective solely to the extent of such invalidity or unenforceability without rendering invalid or unenforceable the remaining terms and provisions of this Agreement or affecting the validity or enforceability of any of the terms or provisions of this Agreement in any other jurisdiction, so long as the economic or legal substance of the transactions contemplated hereby is not affected in any manner materially adverse to any party. If any provision of this Agreement is determined by a court of competent jurisdiction to be so broad as to be unenforceable, that provision shall be interpreted to be only so broad as is enforceable.

Section 12.11 Specific Performance. The parties agree that irreparable damage would occur if any provision of this Agreement were not performed in accordance with the terms hereof and that the parties shall be entitled to an injunction or injunctions to prevent breaches of this Agreement or to enforce specifically the performance of the terms and provisions hereof in any court specified in Section 12.7, in addition to any other remedy to which they are entitled at law or in equity. The parties hereby waive, in any action for specific performance, the defense of adequacy of a remedy at law and the posting of any bond or other security in connection therewith.

Section 12.12 Interpretation. This Agreement shall be interpreted and enforced in accordance with the provisions hereof without the aid of any canon, custom or rule of law requiring or suggesting constitution against the party causing the drafting of the provision in question.

Section 12.13 No Third Party Beneficiaries. Other than the rights granted to the Purchaser Indemnified Parties and the Seller Indemnified

Parties under ARTICLE X, nothing in this Agreement or the Ancillary Agreements is intended or shall be construed to give any Person, other than the parties hereto, their successors and permitted assigns, any legal or equitable right, remedy or claim under or in respect of this Agreement or the Ancillary Agreements or any provision contained herein or therein.

Section 12.14 Counterparts. This Agreement may be executed by the parties hereto in separate counterparts, each of which when so executed and delivered shall be an original, but all such counterparts shall together constitute one and the same instrument. Each counterpart may consist of a number of copies hereof each signed by less than all, but together signed by all, of the parties hereto.

Section 12.15 Headings. The headings in this Agreement are for reference only, and shall not affect the interpretation of this Agreement.

Section 12.16 Dollar References. All dollar references in this Agreement are to the currency of the United States.

IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first above written.

LIBERTY MUTUAL GROUP INC.

By: /s/ Steven M. Zagoren
Name: Steven M. Zagoren
Title: Vice President

GREAT AMERICAN HOLDING, INC.

By: /s/ Vito C. Peraino
Name: Vito C. Peraino
Title: Senior Vice President

AMERICAN FINANCIAL GROUP, INC.
(for the purpose of Section 4.6 only)

By: /s/ Joseph E. (Jeff) Consolino
Name: Joseph E. (Jeff) Consolino
Title: Executive Vice President
and Chief Financial Officer

Exhibit 12

AMERCIAN FINANCIAL GROUP, INC. AND SUBSIDIARIES

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES
(Dollars in Millions)

	Year ended December 31,				
	2013	2012	2011	2010	2009
Earnings before income taxes	$ 689	$ 537	$ 558	$ 694	$ 818
Undistributed equity in (earnings) losses of investee	—	(1)	1	3	2
Losses of managed investment entities attributable to noncontrolling interest	26	98	24	64	—
Fixed charges:					
Interest on annuities	531	541	510	444	435
Interest expense	71	75	74	69	59
Debt discount, expense and other fixed charges	1	12	13	11	9
Portion of rentals representing interest	19	16	18	14	13
EARNINGS	$ 1,337	$ 1,278	$ 1,198	$ 1,299	$ 1,336
Fixed charges:					
Interest on annuities	$ 531	$ 541	$ 510	$ 444	$ 435
Interest expense	71	75	74	69	59
Debt discount, expense and other fixed charges	1	12	13	11	9
Portion of rentals representing interest	19	16	18	14	13
FIXED CHARGES	$ 622	$ 644	$ 615	$ 538	$ 516
Ratio of Earnings to Fixed Charges	2.15	1.98	1.95	2.42	2.59
Earnings in Excess of Fixed Charges	$ 715	$ 634	$ 583	$ 761	$ 820

Exhibit 21

AMERICAN FINANCIAL GROUP, INC.

SUBSIDIARIES OF THE REGISTRANT

The following is a list of subsidiaries of AFG at December 31, 2013. All corporations are subsidiaries of AFG and, if indented, subsidiaries of the company under which they are listed.

Name of Company	Incorporated	Percentage of Ownership
American Money Management Corporation	Ohio	100
APU Holding Company	Ohio	100
American Premier Underwriters, Inc.	Pennsylvania	100
Republic Indemnity Company of America	California	100
Republic Indemnity Company of California	California	100
GAI Holding Bermuda Ltd.	Bermuda	100
GAI Indemnity, Ltd.	United Kingdom	100
Marketform Group Limited	United Kingdom	100
Marketform Holdings Limited	United Kingdom	100
Lavenham Underwriting Limited	United Kingdom	100
Marketform Limited	United Kingdom	100
Sampford Underwriting Limited	United Kingdom	100
Great American Financial Resources, Inc.	Delaware	100
Ceres Group, Inc.	Delaware	100
Continental General Corporation	Nebraska	100
Continental General Insurance Company	Ohio	100
Great American Life Insurance Company	Ohio	100
Annuity Investors Life Insurance Company	Ohio	100
Manhattan National Holding Corporation	Ohio	100
Manhattan National Life Insurance Company	Illinois	100
United Teacher Associates, Ltd.	Texas	100
United Teacher Associates Insurance Company	Texas	100
Great American Holding, Inc.	Ohio	100
American Empire Surplus Lines Insurance Company	Delaware	100
American Empire Insurance Company	Ohio	100
Mid-Continent Casualty Company	Ohio	100
Mid-Continent Assurance Company	Ohio	100
Oklahoma Surety Company	Ohio	100
Great American Insurance Company	Ohio	100
Brothers Property Corporation	Ohio	80
GAI Warranty Company	Ohio	100
GAI Warranty Company of Florida	Florida	100
Great American Alliance Insurance Company	Ohio	100
Great American Assurance Company	Ohio	100
Great American Casualty Insurance Company	Ohio	100
Great American Contemporary Insurance Company	Ohio	100
Great American E&S Insurance Company	Delaware	100
Great American Fidelity Insurance Company	Delaware	100
Great American Insurance Company of New York	New York	100
Great American Protection Insurance Company	Ohio	100
Great American Security Insurance Company	Ohio	100
Great American Spirit Insurance Company	Ohio	100
National Interstate Corporation	Ohio	52
Hudson Indemnity, Ltd.	Cayman Islands	100
National Interstate Insurance Company	Ohio	100
National Interstate Insurance Company of Hawaii, Inc.	Ohio	100
Triumphe Casualty Company	Ohio	100
Vanliner Insurance Company	Missouri	100
Professional Risk Brokers, Inc.	Illinois	100
Strategic Comp Holdings, LLC	Louisiana	100
Strategic Comp Services, LLC	Louisiana	100
Strategic Comp, LLC	Louisiana	100

The names of certain subsidiaries are omitted, as such subsidiaries in the aggregate would not constitute a significant subsidiary.

AMERICAN FINANCIAL GROUP, INC.

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the following Registration Statements and related Prospectuses of American Financial Group, Inc. of our reports dated February 28, 2014, with respect to the consolidated financial statements and schedules and the effectiveness of internal control over financial reporting of American Financial Group, Inc. and subsidiaries, included in this Annual Report (Form 10-K) for the year ended December 31, 2013.

Form	Registration Number	Description
S-8	33-58825	Stock Option Plan
S-8	33-58827	Employee Stock Purchase Plan
S-3	333-102567	Dividend Reinvestment Plan
S-8	333-117062	Non-employee Directors Compensation Plan
S-8	333-184913	Non-employee Directors Compensation Plan
S-8	333-14935	Retirement and Savings Plan
S-8	333-91945	Deferred Compensation Plan
S-8	333-125304	2005 Stock Incentive Plan
S-8	333-170343	2005 Stock Incentive Plan
S-8	333-184914	2005 Stock Incentive Plan
S-3	333-179867	Shelf Registration — Debt and Equity Securities
S-8	333-176192	2011 Equity Bonus Plan (formerly known as the 2011 Co-CEO Equity Bonus Plan)
S-8	333-184915	2011 Equity Bonus Plan (formerly known as the 2011 Co-CEO Equity Bonus Plan)

/s/ ERNST & YOUNG LLP

Cincinnati, Ohio
February 28, 2014

Exhibit 31(a)

AMERICAN FINANCIAL GROUP, INC.

SARBANES-OXLEY SECTION 302(a) CERTIFICATIONS

I, Carl H. Lindner III, certify that:

1. I have reviewed this annual report on Form 10-K of American Financial Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

February 28, 2014

By: /s/ Carl H. Lindner III
Carl H. Lindner III
Co-Chief Executive Officer

AMERICAN FINANCIAL GROUP, INC.

SARBANES-OXLEY SECTION 302(a) CERTIFICATIONS

I, S. Craig Lindner, certify that:

1. I have reviewed this annual report on Form 10-K of American Financial Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

February 28, 2014

By: /s/ S. Craig Lindner
S. Craig Lindner
Co-Chief Executive Officer

Exhibit 31(c)

AMERICAN FINANCIAL GROUP, INC.

SARBANES-OXLEY SECTION 302(a) CERTIFICATIONS

I, Joseph E. (Jeff) Consolino, certify that:

1. I have reviewed this annual report on Form 10-K of American Financial Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

February 28, 2014

By: /s/ Joseph E. (Jeff) Consolino
Joseph E. (Jeff) Consolino
Executive Vice President and Chief Financial Officer

Exhibit 32

AMERICAN FINANCIAL GROUP, INC.

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002

In connection with the filing with the Securities and Exchange Commission of the Annual Report of American Financial Group, Inc. (the "Company") on Form 10-K for the period ended December 31, 2013 (the "Report"), the undersigned officers of the Company, certify, pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that to the best of their knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

February 28, 2014	By: /s/ Carl H. Lindner III
Date	Carl H. Lindner III
	Co-Chief Executive Officer
February 28, 2014	By: /s/ S. Craig Lindner
Date	S. Craig Lindner
	Co-Chief Executive Officer
February 28, 2014	By: /s/ Joseph E. (Jeff) Consolino
Date	Joseph E. (Jeff) Consolino
	Executive Vice President and Chief Financial Officer

A signed original of this written statement will be retained by the Registrant and furnished to the Securities and Exchange Commission or its staff upon request.