TRAVELERS COMPANIES, INC.
Form 10-Q
October 22, 2008
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2008

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 001-10898

The Travelers Companies, Inc.

(Exact name of registrant as specified in its charter)

Minnesota	**41-0518860**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

385 Washington Street

St. Paul, MN 55102

(Address of principal executive offices) (Zip Code)

(651) 310-7911

(Registrant s telephone number, including area code)

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

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

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

The number of shares of the Registrant s Common Stock, without par value, outstanding at October 17, 2008 was 584,522,765.

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The Travelers Companies, Inc.

Quarterly Report on Form 10-Q

For Quarterly Period Ended September 30, 2008

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Item 1. FINANCIAL STATEMENTS

THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF INCOME (Unaudited)

(in millions, except per share data)

	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Revenues				
Premiums	**$ 5,448**	$ 5,416	**$ 16,145**	$ 16,038
Net investment income	**716**	929	**2,309**	2,879
Fee income	**120**	148	**315**	395
Net realized investment gains (losses)	**(170)**		**(196)**	142
Other revenues	**31**	33	**99**	72
Total revenues	**6,145**	6,526	**18,672**	19,526
Claims and expenses				
Claims and claim adjustment expenses	**3,871**	2,985	**9,984**	9,270
Amortization of deferred acquisition costs	**990**	956	**2,905**	2,740
General and administrative expenses	**1,001**	817	**2,718**	2,486
Interest expense	**95**	94	**276**	255
Total claims and expenses	**5,957**	4,852	**15,883**	14,751
Income before income taxes	**188**	1,674	**2,789**	4,775
Income tax expense (benefit)	**(26)**	476	**666**	1,237
Net income	**$ 214**	$ 1,198	**$ 2,123**	$ 3,538
Net income per share				
Basic	**$ 0.36**	$ 1.85	**$ 3.53**	$ 5.36
Diluted	**$ 0.36**	$ 1.81	**$ 3.47**	$ 5.22
Weighted average number of common shares outstanding				
Basic	**587.5**	648.4	**600.7**	658.9
Diluted	**598.0**	661.9	**612.3**	680.3

See notes to consolidated financial statements (unaudited).

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THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

(in millions)

	September 30, 2008 (Unaudited)	December 31, 2007
Assets		
Fixed maturities, available for sale at fair value (including $15 and $1,988 subject to securities lending) (amortized cost $62,897 and $64,152)	**$ 61,491**	$ 64,920
Equity securities, at fair value (cost $472 and $473)	**447**	488
Real estate	**830**	850
Short-term securities	**5,124**	5,186
Other investments	**3,307**	3,374
Total investments	**71,199**	74,818
Cash	**387**	271
Investment income accrued	**830**	861
Premiums receivable	**6,189**	6,142
Reinsurance recoverables	**15,108**	15,641
Ceded unearned premiums	**1,169**	1,123
Deferred acquisition costs	**1,854**	1,809
Deferred tax asset	**1,952**	1,207
Contractholder receivables	**6,877**	6,696
Goodwill	**3,366**	3,366
Other intangible assets	**716**	814
Other assets	**3,048**	2,476
Total assets	**$ 112,695**	$ 115,224
Liabilities		
Claims and claim adjustment expense reserves	**$ 57,027**	$ 57,700
Unearned premium reserves	**11,377**	11,227
Contractholder payables	**6,877**	6,696
Payables for reinsurance premiums	**766**	618
Debt	**6,331**	6,242
Other liabilities	**5,596**	6,125
Total liabilities	**87,974**	88,608
Shareholders equity		
Preferred Stock Savings Plan convertible preferred stock (0.3 shares issued and outstanding at both dates)	**92**	112
Common stock (1,750.0 shares authorized; 587.2 and 627.8 shares issued and outstanding)	**19,196**	18,990
Retained earnings	**12,690**	11,110
Accumulated other changes in equity from nonowner sources	**(932)**	670
Treasury stock, at cost (126.0 and 82.9 shares)	**(6,325)**	(4,266)
Total shareholders equity	**24,721**	26,616
Total liabilities and shareholders equity	**$ 112,695**	$ 115,224

See notes to consolidated financial statements (unaudited).

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THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY (Unaudited)

(in millions)

For the nine months ended September 30,	2008	2007
Convertible preferred stock savings plan		
Balance, beginning of year	**$ 112**	$ 129
Redemptions during period	**(20)**	(14)
Balance, end of period	**92**	115
Common stock		
Balance, beginning of year	**18,990**	18,530
Employee share-based compensation	**96**	219
Compensation amortization under share-based plans and other changes	**110**	131
Conversion of convertible notes		36
Balance, end of period	**19,196**	18,916
Retained earnings		
Balance, beginning of year	**11,110**	7,253
Net income	**2,123**	3,538
Dividends	**(538)**	(557)
Other	**(5)**	1
Balance, end of period	**12,690**	10,235
Accumulated other changes in equity from nonowner sources, net of tax		
Balance, beginning of year	**670**	452
Change in net unrealized gain on investment securities	**(1,438)**	(231)
Net change in unrealized foreign currency translation and other changes	**(164)**	74
Balance, end of period	**(932)**	295
Treasury stock (at cost)		
Balance, beginning of year	**(4,266)**	(1,229)
Treasury shares acquired share repurchase authorization	**(2,022)**	(1,947)
Net shares acquired related to employee share-based compensation plans	**(37)**	(78)
Balance, end of period	**(6,325)**	(3,254)
Total common shareholders equity	**24,629**	26,192
Total shareholders equity	**$ 24,721**	$ 26,307
Common shares outstanding		
Balance, beginning of year	**627.8**	678.3
Shares acquired share repurchase authorization	**(42.3)**	(37.0)
Net shares issued under employee share-based compensation plans	**1.7**	4.1
Shares issued pursuant to conversion of convertible notes		0.7
Balance, end of period	**587.2**	646.1
Summary of changes in equity from nonowner sources		
Net income	**$ 2,123**	$ 3,538
Other changes in equity from nonowner sources, net of tax	**(1,602)**	(157)
Total changes in equity from nonowner sources	**$ 521**	$ 3,381

See notes to consolidated financial statements (unaudited).

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THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)

(in millions)

For the nine months ended September 30,	**2008**	**2007**
Cash flows from operating activities		
Net income	**$ 2,123**	$ 3,538
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized investment (gains) losses	**196**	(142)
Depreciation and amortization	**627**	605
Deferred federal income tax expense	**49**	249
Amortization of deferred policy acquisition costs	**2,905**	2,740
Equity in income from other investments	**34**	(489)
Premiums receivable	**(47)**	(135)
Reinsurance recoverables	**533**	1,694
Deferred acquisition costs	**(2,950)**	(2,988)
Claims and claim adjustment expense reserves	**(673)**	(1,074)
Unearned premium reserves	**150**	363
Trading account activities	**5**	(3)
Loss on redemption of subordinated debentures		32
Excess tax benefits from share-based payment arrangements	**(8)**	(23)
Other	**(371)**	(428)
Net cash provided by operating activities	**2,573**	3,939
Cash flows from investing activities		
Proceeds from maturities of fixed maturities	**3,670**	3,957
Proceeds from sales of investments:		
Fixed maturities	**3,588**	3,681
Equity securities	**61**	77
Real estate	**25**	10
Other investments	**547**	1,153
Purchases of investments:		
Fixed maturities	**(6,635)**	(9,686)
Equity securities	**(103)**	(63)
Real estate	**(31)**	(69)
Other investments	**(527)**	(562)
Net (purchases) sales of short-term securities	**60**	(64)
Securities transactions in course of settlement	**(387)**	(331)
Other	**(267)**	(292)
Net cash provided by (used in) investing activities	**1**	(2,189)
Cash flows from financing activities		
Issuance of debt	**496**	2,461
Payment of debt	**(403)**	(1,956)
Dividends paid to shareholders	**(536)**	(557)
Issuance of common stock employee share options	**72**	192
Treasury stock acquired share repurchase authorization	**(2,055)**	(1,947)
Treasury stock acquired net employee share-based compensation	**(28)**	(39)
Excess tax benefits from share-based payment arrangements	**8**	23
Other		1
Net cash used in financing activities	**(2,446)**	(1,822)

Effect of exchange rate changes on cash		**(12)**		4
Net increase (decrease) in cash		**116**		(68)
Cash at beginning of period		**271**		459
Cash at end of period	**$**	**387**	$	391
Supplemental disclosure of cash flow information				
Income taxes paid	**$**	**832**	$	935
Interest paid	**$**	**248**	$	240

See notes to consolidated financial statements (unaudited).

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THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

Basis of Presentation

The interim consolidated financial statements include the accounts of The Travelers Companies, Inc. (together with its subsidiaries, the Company). These financial statements are prepared in conformity with U.S. generally accepted accounting principles (GAAP) and are unaudited. In the opinion of the Company s management, all adjustments necessary for a fair presentation have been reflected. Certain financial information that is normally included in annual financial statements prepared in accordance with GAAP, but that is not required for interim reporting purposes, has been omitted. Certain reclassifications have been made to the 2007 financial statements to conform to the 2008 presentation. The accompanying interim consolidated financial statements and related notes should be read in conjunction with the Company s consolidated financial statements and related notes included in the Company s 2007 Annual Report on Form 10-K.

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and claims and expenses during the reporting period. Actual results could differ from those estimates. All material intercompany transactions and balances have been eliminated.

Adoption of New Accounting Standards

Accounting for Uncertainty in Income Taxes

The Financial Accounting Standards Board (FASB) issued, in July 2006, FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109* (FIN 48) and, in May 2007, FASB Staff Position (FSP) FIN 48-1, *Definition of Settlement in FASB Interpretation No. 48* (FSP FIN 48-1). FIN 48 is intended to clarify the accounting for uncertainty in income taxes recognized in a company s financial statements and prescribes the recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

Under FIN 48, evaluation of a tax position is a two-step process. The first step is to determine whether it is more-likely-than-not that a tax position will be sustained upon examination, including the resolution of any related appeals or litigation based on the technical merits of that position. The second step is to measure a tax position that meets the more-likely-than-not threshold to determine the amount of benefit to be recognized in the financial statements. A tax position that meets the more-likely-than-not recognition threshold shall initially and subsequently be measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information.

Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent period in which the threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not criteria should be de-recognized in the first subsequent financial reporting period in which the threshold is no longer met.

The adoption of FIN 48 at January 1, 2007 and FSP FIN 48-1 at June 30, 2007 did not have a material effect on the Company s results of operations, financial position or liquidity.

The total amount of unrecognized tax benefits at January 1, 2007 was $339 million. Included in that balance were $101 million of unrecognized tax benefits that, if recognized, would affect the annual effective tax rate and $175 million of unrecognized tax benefits for which the ultimate deductibility is certain, but for which there is uncertainty about the timing of deductibility. Because of the impact of deferred tax accounting, the timing of such deductibility would not affect the annual effective tax rate other than for interest and penalties. The balance of unrecognized tax benefits at January 1, 2007 was comprised of $63 million of unrecognized tax benefits that, if recognized, would reduce goodwill.

The Company recognizes accrued interest and penalties, if any, related to unrecognized tax benefits in income taxes. The Company had approximately $35 million for the payment of interest accrued at January 1, 2007.

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THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES, Continued

Fair Value Measurements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure about fair value measurements. It applies to other pronouncements that require or permit fair value but does not require any new fair value measurements. The statement defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

FAS 157 establishes a fair value hierarchy to increase consistency and comparability in fair value measurements and disclosures. The hierarchy is based on the inputs used in valuation and gives the highest priority to quoted prices in active markets. The highest possible level should be used to measure fair value. FAS 157 is effective for fiscal years beginning after November 15, 2007.

In February 2008, FASB issued FSP FAS 157-2, *Effective Date of FASB Statement No. 157* (FSP FAS 157-2), which permits a one-year deferral of the application of FASB Statement No. 157, *Fair Value Measurements*, for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually).

The Company adopted FAS 157 and FSP FAS 157-2 effective January 1, 2008. Accordingly, the provisions of FAS 157 were not applied to goodwill and other intangible assets held by the Company and measured annually for impairment testing purposes only. The adoption of FAS 157, for all other assets and liabilities held by the Company, did not have a material effect on the Company s results of operations, financial position or liquidity. The Company will adopt FAS 157 for non-financial assets and non-financial liabilities on January 1, 2009 and does not expect the provisions to have a material effect on its results of operations, financial position or liquidity.

In October 2008, the FASB issued FSP FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market For That Asset Is Not Active* (FSP FAS 157-3), with an immediate effective date, including prior periods for which financial statements have not been issued. FSP FAS 157-3 amends FAS 157 to clarify the application of fair value in inactive markets and allows for the use of management s internal assumptions about future cash flows with appropriately risk-adjusted discount rates when relevant observable market data does not exist. The objective of FAS 157 has not changed and continues to be the determination of the price that would be received in an orderly transaction that is not a forced liquidation or distressed sale at the measurement date. The adoption of FSP FAS 157-3 in the third quarter did not have a material effect on the Company s results of operations, financial position or liquidity.

Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (FAS 159).FAS 159 permits an entity to irrevocably elect fair value on a contract-by-contract basis for new assets or liabilities within the scope of FAS 159 as the initial and subsequent measurement attribute for those financial assets and liabilities and certain other items including property and casualty insurance contracts. Entities electing the fair value option would be required to recognize changes in fair value in earnings and to expense up-front costs and fees associated with the item for which the fair value option is elected. Entities electing the fair value option are required to distinguish on the face of the statement of financial position the fair value of assets and liabilities for which the fair value option has been elected, and similar assets and liabilities measured using another measurement attribute. An entity can accomplish this by either reporting the fair value and non-fair-value carrying amounts as separate line items or aggregating those amounts and disclosing parenthetically the amount of fair value included in the aggregate amount.

FAS 159 is effective for fiscal years beginning after November 15, 2007. Upon adoption, an entity is permitted to elect the fair value option irrevocably for any existing asset or liability within the scope of the standard. The adjustment to reflect the difference between the fair value and the carrying amount would be accounted for as a cumulative-effect adjustment to retained earnings as of the date of initial adoption. Retrospective application would not be permitted. The Company did not elect the fair value option for assets and liabilities currently held upon its adoption of FAS 159 effective January 1, 2008. Therefore, FAS 159 did not have an impact on the Company s results of operations, financial position or liquidity.

THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES, Continued

Collateral Assignment Split-Dollar Life Insurance Arrangements

In March 2007, the FASB issued Emerging Issues Task Force Issue No. 06-10, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements* (EITF 06-10). EITF 06-10 provides guidance on the recognition and measurement of assets related to collateral assignment split-dollar life insurance arrangements. EITF 06-10 is effective for fiscal years beginning after December 15, 2007. The adoption of EITF 06-10 effective January 1, 2008 did not have a material effect on the Company s results of operations, financial position or liquidity.

Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards

In June 2007, the FASB issued Emerging Issues Task Force Issue No. 06-11, *Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards* (EITF 06-11). EITF 06-11 requires that realized income tax benefits related to dividend payments that are charged to retained earnings and paid to employees holding equity shares, nonvested equity share units and outstanding equity share options should be recognized as an increase in additional paid-in capital. EITF 06-11 shall be applied to share-based payment awards that are declared in fiscal years beginning after December 15, 2007. The adoption of EITF 06-11 effective January 1, 2008 did not have a material effect on the Company s results of operations, financial position or liquidity.