CNA FINANCIAL CORP
Form 10-Q
July 30, 2018

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 June 30, 2018
OR
[ ]
TRANSITION
REPORT
PURSUANT
TO SECTION
13 OR 15(d)
OF THE
SECURITIES
EXCHANGE
ACT OF 1934
For the transition period from _____ to _____
Commission File Number 1-5823

CNA FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	36-6169860
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
151 N. Franklin Chicago, Illinois (Address of principal executive offices)	60606 (Zip Code)

(312) 822-5000
(Registrant's telephone number, including area code)

333 S. Wabash, Chicago, Illinois 60604
(Former name, former address and former fiscal year, if changed since last report)
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 [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes [x] No [ ]
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer [x]	Accelerated filer [ ]	Non-accelerated filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]	Emerging growth company [ ]

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. [ ]
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [x]
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at July 26, 2018
Common Stock, Par value $2.50	271,395,494

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PART I. Financial Information
Item 1. Condensed Consolidated Financial Statements
CNA Financial Corporation
Condensed Consolidated Statements of Operations (Unaudited)

Periods ended June 30	Three Months		Six Months	
(In millions, except per share data)	2018	2017	2018	2017
Revenues				
Net earned premiums	$1,815	$1,734	$3,600	$3,379
Net investment income	506	475	996	1,020
Net realized investment (losses) gains:				
Other-than-temporary impairment losses	—	(2)	(6)	(4)
Other net realized investment (losses) gains	(1)	52	17	90
Net realized investment (losses) gains	(1)	50	11	86
Non-insurance warranty revenue (Note J)	248	98	486	191
Other revenues	6	9	16	20
Total revenues	2,574	2,366	5,109	4,696
Claims, Benefits and Expenses				
Insurance claims and policyholders' benefits	1,327	1,280	2,666	2,573
Amortization of deferred acquisition costs	359	312	655	617
Non-insurance warranty expense (Note J)	225	72	441	142
Other operating expenses	298	292	601	568
Interest	35	40	70	83
Total claims, benefits and expenses	2,244	1,996	4,433	3,983
Income before income tax	330	370	676	713
Income tax expense	(60)	(98)	(115)	(181)
Net income	$270	$272	$561	$532
Basic earnings per share	$0.99	$1.01	$2.07	$1.96
Diluted earnings per share	$0.99	$1.00	$2.06	$1.96
Dividends declared per share	$0.30	$0.25	$2.60	$2.50
Weighted Average Outstanding Common Stock and Common Stock Equivalents				
Basic	271.5	271.1	271.5	271.0
Diluted	272.4	271.9	272.4	271.9

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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CNA Financial Corporation
Condensed Consolidated Statements of Comprehensive Income (Loss) (Unaudited)

Periods ended June 30	Three Months		Six Months	
(In millions)	2018	2017	2018	2017
Comprehensive Income (Loss)				
Net income	$270	$272	$561	$532
Other Comprehensive (Loss) Income, Net of Tax				
Changes in:				
Net unrealized gains on investments with other-than-temporary impairments	(1)	—	(10)	(4)
Net unrealized gains on other investments	(159)	77	(588)	144
Net unrealized gains on investments	(160)	77	(598)	140
Foreign currency translation adjustment	(52)	42	(40)	53
Pension and postretirement benefits	7	5	17	12
Other comprehensive (loss) income, net of tax	(205)	124	(621)	205
Total comprehensive income (loss)	$65	$396	$(60)	$737

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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CNA Financial Corporation
Condensed Consolidated Balance Sheets

(In millions, except share data)	June 30, 2018 (Unaudited)	December 31, 2017
Assets		
Investments:		
Fixed maturity securities at fair value (amortized cost of $37,928 and $38,215)	$ 39,795	$ 41,487
Equity securities at fair value (cost of $762 and $659)	773	695
Limited partnership investments	2,363	2,369
Other invested assets	48	44
Mortgage loans	865	839
Short term investments	1,308	1,436
Total investments	45,152	46,870
Cash	288	355
Reinsurance receivables (less allowance for uncollectible receivables of $29 and $29)	4,535	4,261
Insurance receivables (less allowance for uncollectible receivables of $44 and $44)	2,598	2,292
Accrued investment income	396	411
Deferred acquisition costs	673	634
Deferred income taxes	296	137
Property and equipment at cost (less accumulated depreciation of $234 and $274)	347	326
Goodwill	147	148
Other assets (Note A)	3,426	1,133
Total assets	$ 57,858	$ 56,567
Liabilities		
Insurance reserves:		
Claim and claim adjustment expenses	$ 21,990	$ 22,004
Unearned premiums	4,410	4,029
Future policy benefits	10,667	11,179
Short term debt	30	150
Long term debt	2,679	2,708
Other liabilities (includes $100 and $143 due to Loews Corporation) (Note A)	6,667	4,253
Total liabilities	46,443	44,323
Commitments and contingencies (Notes C and F)		
Stockholders' Equity		
Common stock ($2.50 par value; 500,000,000 shares authorized; 273,040,243 shares issued; 271,391,107 and 271,205,390 shares outstanding)	683	683
Additional paid-in capital	2,179	2,175
Retained earnings	9,216	9,414
Accumulated other comprehensive (loss) income	(605)	32
Treasury stock (1,649,136 and 1,834,853 shares), at cost	(58)	(60)
Total stockholders’ equity	11,415	12,244
Total liabilities and stockholders' equity	$ 57,858	$ 56,567

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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CNA Financial Corporation
Condensed Consolidated Statements of Cash Flows (Unaudited)
Six months ended June 30

(In millions)	2018	2017
Cash Flows from Operating Activities		
Net income	$561	$532
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Deferred income tax expense	15	122
Trading portfolio activity	(13)	(11)
Net realized investment gains	(11)	(86)
Equity method investees	(15)	42
Net amortization of investments	(30)	(21)
Depreciation and amortization	41	43
Changes in:		
Receivables, net	(587)	(195)
Accrued investment income	15	1
Deferred acquisition costs	(43)	(41)
Insurance reserves	563	262
Other assets	(178)	(118)
Other liabilities	(11)	(45)
Other, net	47	30
Total adjustments	(207)	(17)
Net cash flows provided by operating activities	354	515
Cash Flows from Investing Activities		
Dispositions:		
Fixed maturity securities - sales	4,781	3,142
Fixed maturity securities - maturities, calls and redemptions	1,306	1,770
Equity securities	25	22
Limited partnerships	93	100
Mortgage loans	68	17
Purchases:		
Fixed maturity securities	(5,608)	(4,840)
Equity securities	(127)	(8)
Limited partnerships	(72)	(47)
Mortgage loans	(94)	(72)
Change in other investments	(6)	(3)
Change in short term investments	135	81
Purchases of property and equipment	(76)	(68)
Other, net	14	17
Net cash flows provided by investing activities	439	111

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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Six months ended June 30		
(In millions)	2018	2017
Cash Flows from Financing Activities		
Dividends paid to common stockholders	$(706)	$(676)
Repayment of debt	(150)	—
Other, net	1	(1)
Net cash flows used by financing activities	(855)	(677)
Effect of foreign exchange rate changes on cash	(5)	5
Net change in cash	(67)	(46)
Cash, beginning of year	355	271
Cash, end of period	$288	$225

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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CNA Financial Corporation
Condensed Consolidated Statements of Stockholders' Equity (Unaudited)
Six months ended June 30

(In millions)	2018	2017
Common Stock		
Balance, beginning of period	$683	$683
Balance, end of period	683	683
Additional Paid-in Capital		
Balance, beginning of period	2,175	2,173
Stock-based compensation	4	(6)
Balance, end of period	2,179	2,167
Retained Earnings		
Balance, beginning of period, as previously reported	9,414	9,359
Cumulative effect adjustments from changes in accounting guidance, net of tax	(50)	—
Balance, beginning of period, as adjusted	9,364	9,359
Dividends paid to common stockholders	(709)	(680)
Net income	561	532
Balance, end of period	9,216	9,211
Accumulated Other Comprehensive (Loss) Income		
Balance, beginning of period, as previously reported	32	(173)
Cumulative effect adjustments from changes in accounting guidance, net of tax	(16)	—
Balance, beginning of period, as adjusted	16	(173)
Other comprehensive (loss) income	(621)	205
Balance, end of period	(605)	32
Treasury Stock		
Balance, beginning of period	(60)	(73)
Stock-based compensation	2	8
Balance, end of period	(58)	(65)
Total stockholders' equity	$11,415	$12,028

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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CNA Financial Corporation
Notes to Condensed Consolidated Financial Statements (Unaudited)
Note A. General
Basis of Presentation
The Condensed Consolidated Financial Statements include the accounts of CNA Financial Corporation (CNAF) and its subsidiaries. Collectively, CNAF and its subsidiaries are referred to as CNA or the Company. Loews Corporation (Loews) owned approximately 89% of the outstanding common stock of CNAF as of June 30, 2018.
The accompanying Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). Intercompany amounts have been eliminated. Certain financial information that is normally included in annual financial statements prepared in accordance with GAAP, including certain financial statement notes, is not required for interim reporting purposes and has been condensed or omitted. These statements should be read in conjunction with the Consolidated Financial Statements and notes thereto included in CNAF's Annual Report on Form 10-K filed with the Securities and Exchange Commission for the year ended December 31, 2017, including the summary of significant accounting policies in Note A. The preparation of Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the Condensed Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.
The interim financial data as of June 30, 2018 and for the three and six months ended June 30, 2018 and 2017 is unaudited. However, in the opinion of management, the interim data includes all adjustments, including normal recurring adjustments, necessary for a fair statement of the Company's results for the interim periods. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year.
Recently Adopted Accounting Standards Updates (ASU)
ASU 2014-09: In May 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-09, Revenue Recognition (Topic 606): Revenue from Contracts with Customers. The standard excludes from its scope the accounting for insurance contracts, financial instruments, and certain other agreements that are governed under other GAAP guidance. The updated guidance requires an entity to recognize revenue as performance obligations are met, in an amount that reflects the consideration the entity is entitled to receive for the transfer of the promised goods or services.
On January 1, 2018, the Company adopted the updated guidance using the modified retrospective method applied to all contracts which were not completed as of the date of adoption, with the cumulative effect recognized as an adjustment to the opening balance of Retained earnings. Prior period amounts have not been adjusted and continue to be reported in accordance with the previous accounting guidance.
Under the new guidance, revenue on warranty products and services will be recognized more slowly compared to the historic revenue recognition pattern. In addition, for warranty products in which the Company acts as the principal in the transaction, Non-insurance warranty revenue and Non-insurance warranty expense are increased to reflect the gross amount paid by consumers, including the retail seller’s markup which is considered a commission to the Company's agent. This gross-up of revenue and expense also resulted in an increase to Other assets and Other liabilities on the Company's Condensed Consolidated Balance Sheets as the revenue and expense are recognized over the actuarially determined expected claims emergence pattern.

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The cumulative effect changes to the Condensed Consolidated Balance Sheet for the adoption of the updated guidance on January 1, 2018 were as follows:

(In millions)	Balance as of December 31, 2017	Adjustments Due to Adoption of Topic 606	Balance as of January 1, 2018
Other assets	$ 1,133	$ 1,882	$ 3,015
Other liabilities	4,253	1,969	6,222
Deferred income taxes	137	21	158
Retained earnings	9,414	(66)	9,348

The impact of adoption on the Condensed Consolidated Statements of Operations and Balance Sheet was as follows:

Periods ended June 30, 2018	Three Months			Six Months		
(In millions)	Prior to Adoption	Effect of Adoption	As Reported	Prior to Adoption	Effect of Adoption	As Reported
Statement of operations:						
Non-insurance warranty revenue	$ 105	$ 143	$ 248	$ 206	$ 280	$ 486
Total revenues	2,431	143	2,574	4,829	280	5,109
Non-insurance warranty expense	80	145	225	158	283	441
Total claims, benefits and expenses	2,099	145	2,244	4,150	283	4,433
Income before income tax	332	(2)	330	679	(3)	676
Income tax expense	(61)	1	(60)	(116)	1	(115)
Net income	271	(1)	270	563	(2)	561
Balance sheet[(1)] at June 30, 2018:						
Other assets				$ 3,228	$ 198	$ 3,426
Other liabilities				6,466	201	6,667
Deferred income taxes				295	1	296
Retained earnings				9,218	(2)	9,216

(1) The Prior to Adoption amounts presented include the cumulative effect adjustment at adoption.

See Note J to the Condensed Consolidated Financial Statements for additional information regarding non-insurance revenues from contracts with customers.

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ASU 2016-01: In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The updated accounting guidance requires changes to the reporting model for financial instruments. The guidance primarily changes the model for equity securities by requiring changes in the fair value of equity securities (except those accounted for under the equity method of accounting, those without readily determinable fair values and those that result in consolidation of the investee) to be recognized through the income statement. The Company adopted the updated guidance on January 1, 2018 and recognized a cumulative effect adjustment that increased beginning Retained earnings by $28 million, net of tax. Prior period amounts have not been adjusted and continue to be reported in accordance with the previous accounting guidance.

For the three and six months ended June 30, 2018, the Company recognized $10 million and $25 million in pretax losses within Net realized investment gains (losses) for the change in fair value of non-redeemable preferred stock and $2 million and $2 million in pretax gains within Net investment income for the change in fair value of common stock as a result of this change. For the three and six months ended June 30, 2017, there was less than a $1 million decrease and a $1 million decrease in the fair value of common stock and a $2 million increase and a $7 million increase in the fair value of non-redeemable preferred stock recognized in Other comprehensive income. The Company's non-redeemable preferred stock contain characteristics of debt securities, are priced similarly to bonds, and are held primarily for income generation through periodic dividends. While recognition of gains and losses on these securities are no longer discretionary, management does not consider the changes in fair value of non-redeemable preferred stock to be reflective of our primary operations. As such, the changes in the fair value of these securities are recorded through Net realized investments gains (losses). The company owns certain common stock with the intention of holding the securities primarily for market appreciation and as such, the changes in the fair value of these securities are recorded through Net investment income.

ASU 2017-07: In March 2017, the FASB issued ASU No. 2017-07, Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The updated accounting guidance requires changes to the presentation of the components of net periodic benefit cost on the income statement by requiring service cost to be presented with other employee compensation costs and other components of net periodic pension cost to be presented outside of any subtotal of operating income. The ASU also stipulates that only the service cost component of net benefit cost is eligible for capitalization. The Company adopted the updated guidance effective January 1, 2018. The guidance was applied on a prospective basis for capitalization of service costs and on a retrospective basis for the presentation of the service cost and other components of net periodic benefit costs in the Company's Condensed Consolidated Statements of Operations and in its disclosures. The Company expanded the related footnote disclosure, Note G to the Condensed Consolidated Financial Statements, to disclose the amount of service cost and non-service cost components of net periodic benefit cost and the line items in the Condensed Consolidated Statements of Operations in which such amounts are reported. The change limiting the costs eligible for capitalization is not material to the Company’s results of operations or financial position.

ASU 2018-02: In February 2018, the FASB issued ASU No. 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. GAAP requires the remeasurement of deferred tax assets and liabilities due to a change in the tax rate to be included in Net income, even if the related income tax effects were originally recognized in Accumulated other comprehensive income (AOCI). The ASU allows a reclassification from AOCI to Retained earnings for stranded tax effects resulting from the new U.S. Federal corporate income tax rate enacted on December 22, 2017. The Company early adopted the updated guidance effective January 1, 2018 and elected to reclassify the stranded income tax effects relating to the reduction in the Federal corporate income tax rate from AOCI to Retained earnings at the beginning of the period of adoption. The net impact of the accounting change resulted in a $12 million increase in AOCI and a corresponding decrease in Retained earnings. The $12 million increase in AOCI is comprised of a $142 million increase in net unrealized gains (losses) on investments partially offset by a $130 million decrease in unrecognized pension and postretirement benefits.

The Company releases tax effects from AOCI utilizing the security-by-security approach for Net unrealized gains (losses) on investments with Other-than-temporary impairment (OTTI) losses and Net unrealized gains (losses) on other investments. For Pension and postretirement benefits, tax effects from AOCI are released at enacted tax rates based on the pre-tax adjustments to pension liabilities or assets recognized within OCI.

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Accounting Standards Pending Adoption

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842): Accounting for Leases. The updated accounting guidance requires lessees to recognize on the balance sheet assets and liabilities for the rights and obligations created by the majority of leases, including those historically accounted for as operating leases. The guidance is effective for interim and annual periods beginning after December 15, 2018. The Company is currently evaluating the effect the updated guidance will have on the Company's financial statements. It is expected that assets and liabilities will increase based on the present value of remaining lease payments for leases in place at the adoption date; however, this is not expected to be material to the Company's results of operations or financial position.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The updated accounting guidance requires changes to the recognition of credit losses on financial instruments not accounted for at fair value through net income. The guidance is effective for interim and annual periods beginning after December 15, 2019. The Company is currently evaluating the effect the guidance will have on the Company's financial statements, but expects the primary changes to be the use of the expected credit loss model for its mortgage loan portfolio and reinsurance receivables and the use of the allowance method rather than the write-down method for credit losses within the available-for-sale fixed maturities portfolio. The expected credit loss model will require a financial asset to be presented at the net amount expected to be collected. The allowance method for available-for-sale debt securities will allow the Company to record reversals of credit losses if the estimate of credit losses declines.

Income Tax Reform Update

On December 22, 2017, H.R.1, “An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018,” was signed into law (Tax Reform Legislation).

Shortly after enactment, the Securities and Exchange Commission Staff issued Staff Accounting Bulletin No. 118 (SAB 118) to provide guidance on accounting for the Tax Reform Legislation impacts when the measurements of the income tax effects are complete, incomplete, or incomplete but for which a provisional amount can be estimated. SAB 118 permits the recognition of provisional amounts, and adjustments to provisional amounts, in subsequent reporting periods within the one year measurement period.

The Company has reflected the following incomplete but reasonably estimated provisional items in Deferred income taxes on the Condensed Consolidated Balance Sheet at June 30, 2018. The effects of the adjustments to the Company’s provisional amounts for the three and six months ended June 30, 2018 did not impact income tax expense.

- The Company has recalculated its insurance reserves and the transition adjustment from existing law.
- The Company has recalculated amounts under special accounting method provisions for recognizing income for Federal income tax purposes no later than for financial accounting purposes and the transition adjustment from existing law.
- The Company has not recorded current or deferred taxes with respect to the international provisions since it does not expect to have inclusions in U.S. taxable income for certain earnings of foreign subsidiaries in future years.

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Note B. Earnings (Loss) Per Share

Earnings (loss) per share is based on the weighted average number of outstanding common shares. Basic earnings (loss) per share excludes the impact of dilutive securities and is computed by dividing Net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

For the three and six months ended June 30, 2018, approximately 835 thousand and 929 thousand potential shares attributable to exercises or conversions into common stock under stock-based employee compensation plans were included in the calculation of diluted earnings per share. For those same periods, approximately 445 thousand and 2 thousand potential shares attributable to exercises or conversions into common stock under stock-based employee compensation plans were not included in the calculation of diluted earnings per share, because the effect would have been antidilutive.

For the three and six months ended June 30, 2017, approximately 847 thousand and 915 thousand potential shares attributable to exercises or conversions into common stock under stock-based employee compensation plans were included in the calculation of diluted earnings per share. For those same periods, less than 1 thousand potential shares attributable to exercises or conversions into common stock under stock-based employee compensation plans were not included in the calculation of diluted earnings per share, because the effect would have been antidilutive.

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Note C. Investments

The significant components of Net investment income are presented in the following table.

Periods ended June 30	Three Months		Six Months	
(In millions)	2018	2017	2018	2017
Fixed maturity securities	$444	$457	$890	$912
Equity securities	12	2	22	3
Limited partnership investments	40	16	70	106
Mortgage loans	14	8	25	15
Short term investments	6	3	12	6
Trading portfolio	3	4	5	6
Other	3	—	3	1
Gross investment income	522	490	1,027	1,049
Investment expense	(16)	(15)	(31)	(29)
Net investment income	$506	$475	$996	$1,020

During the three and six months ended June 30, 2018, $2 million and $1 million of Net investment income was recognized due to the change in fair value of common stock still held as of June 30, 2018.

Net realized investment gains (losses) are presented in the following table.

Periods ended June 30	Three Months		Six Months	
(In millions)	2018	2017	2018	2017
Net realized investment gains (losses):				
Fixed maturity securities:				
Gross realized gains	$37	$56	$106	$105
Gross realized losses	(33)	(12)	(84)	(29)
Net realized investment gains (losses) on fixed maturity securities	4	44	22	76
Equity securities	(10)	—	(25)	—
Derivatives	4	(3)	9	(2)
Short term investments and other	1	9	5	12
Net realized investment gains (losses)	$(1)	$50	$11	$86

During the three and six months ended June 30, 2018, $10 million and $25 million of Net realized investment losses were recognized due to the change in fair value of non-redeemable preferred stock still held as of June 30, 2018.

The components of OTTI losses recognized in earnings by asset type are presented in the following table.

Periods ended June 30	Three Months		Six Months	
(In millions)	2018	2017	2018	2017
Fixed maturity securities available-for-sale:				
Corporate and other bonds	$ —	$ 2	$ 5	$ 4
Asset-backed	—	—	1	—
OTTI losses recognized in earnings	$ —	$ 2	$ 6	$ 4

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The following tables present a summary of fixed maturity and equity securities.

June 30, 2018 [1] (In millions)	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Unrealized OTTI Losses (Gains)
Fixed maturity securities available-for-sale:					
Corporate and other bonds	$ 17,883	$ 938	$ 203	$ 18,618	$ —
States, municipalities and political subdivisions	10,856	1,161	8	12,009	—
Asset-backed:					
Residential mortgage-backed	4,961	72	85	4,948	(25)
Commercial mortgage-backed	2,082	23	33	2,072	—
Other asset-backed	1,557	9	9	1,557	—
Total asset-backed	8,600	104	127	8,577	(25)
U.S. Treasury and obligations of government-sponsored enterprises	127	3	3	127	—
Foreign government	436	6	5	437	—
Redeemable preferred stock	9	1	—	10	—
Total fixed maturity securities available-for-sale	37,911	2,213	346	39,778	$ (25)
Total fixed maturity securities trading	17			17	
Total fixed maturity securities	$ 37,928	$ 2,213	$ 346	$ 39,795	

December 31, 2017 (In millions)	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Unrealized OTTI Losses (Gains)
Fixed maturity securities available-for-sale:					
Corporate and other bonds	$ 17,210	$ 1,625	$ 28	$ 18,807	$ —
States, municipalities and political subdivisions	12,478	1,551	2	14,027	(11)
Asset-backed:					
Residential mortgage-backed	5,043	109	32	5,120	(27)
Commercial mortgage-backed	1,840	46	14	1,872	—
Other asset-backed	1,083	16	5	1,094	—
Total asset-backed	7,966	171	51	8,086	(27)
U.S. Treasury and obligations of government-sponsored enterprises	111	2	4	109	—
Foreign government	437	9	2	444	—
Redeemable preferred stock	10	1	—	11	—
Total fixed maturity securities available-for-sale	38,212	3,359	87	41,484	$ (38)
Total fixed maturity securities trading	3			3	
Equity securities available-for-sale:					
Common stock	21	7	1	27	
Preferred stock	638	31	1	668	
Total equity securities available-for-sale	659	38	2	695	
Total fixed maturity and equity securities	$ 38,874	$ 3,397	$ 89	$ 42,182	

(1) As of January 1, 2018, the Company adopted ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The change in fair value of equity securities is now recognized through the income statement. See Note A to the Condensed Consolidated Financial Statements for additional information.

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The net unrealized gains on investments included in the tables above are recorded as a component of AOCI. When presented in AOCI, these amounts are net of tax and any required Shadow Adjustments. To the extent that unrealized gains on fixed income securities supporting certain products within the Life & Group segment would result in a premium deficiency if realized, a related increase in Insurance reserves is recorded, net of tax, as a reduction of net unrealized gains through Other comprehensive income (loss) (Shadow Adjustments). As of June 30, 2018 and December 31, 2017, the net unrealized gains on investments included in AOCI were correspondingly reduced by Shadow Adjustments of $1,186 million and $1,411 million.

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The following tables present the estimated fair value and gross unrealized losses of fixed maturity and equity securities in a gross unrealized loss position by the length of time in which the securities have continuously been in that position.

June 30, 2018 (1) (In millions)	Less than 12 Months Estimated Fair Value	Less than 12 Months Gross Unrealized Losses	12 Months or Longer Estimated Fair Value	12 Months or Longer Gross Unrealized Losses	Total Estimated Fair Value	Total Gross Unrealized Losses
Fixed maturity securities available-for-sale:						
Corporate and other bonds	$6,963	$ 192	$193	$ 11	$7,156	$ 203
States, municipalities and political subdivisions	723	8	3	—	726	8
Asset-backed:						
Residential mortgage-backed	3,183	68	344	17	3,527	85
Commercial mortgage-backed	913	16	228	17	1,141	33
Other asset-backed	632	6	27	3	659	9
Total asset-backed	4,728	90	599	37	5,327	127
U.S. Treasury and obligations of government-sponsored enterprises	49	1	19	2	68	3
Foreign government	178	3	40	2	218	5
Total	$12,641	$ 294	$854	$ 52	$13,495	$ 346

December 31, 2017 (In millions)	Less than 12 Months Estimated Fair Value	Less than 12 Months Gross Unrealized Losses	12 Months or Longer Estimated Fair Value	12 Months or Longer Gross Unrealized Losses	Total Estimated Fair Value	Total Gross Unrealized Losses
Fixed maturity securities available-for-sale:						
Corporate and other bonds	$1,354	$ 21	$168	$ 7	$1,522	$ 28
States, municipalities and political subdivisions	72	1	85	1	157	2
Asset-backed:						
Residential mortgage-backed	1,228	5	947	27	2,175	32
Commercial mortgage-backed	403	4	212	10	615	14
Other asset-backed	248	3	18	2	266	5
Total asset-backed	1,879	12	1,177	39	3,056	51
U.S. Treasury and obligations of government-sponsored enterprises	49	2	21	2	70	4
Foreign government	166	2	4	—	170	2
Total fixed maturity securities available-for-sale	3,520	38	1,455	49	4,975	87
Equity securities available-for-sale:						
Common stock	7	1	—	—	7	1
Preferred stock	93	1	—	—	93	1
Total equity securities available-for-sale	100	2	—	—	100	2
Total	$3,620	$ 40	$1,455	$ 49	$5,075	$ 89

(1) As of January 1, 2018, the Company adopted ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The change in fair value of equity securities is now recognized through the income statement. See Note A to the Condensed Consolidated Financial Statements for additional information.

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Based on current facts and circumstances, the Company believes the unrealized losses presented in the June 30, 2018 securities in a gross unrealized loss position table above are not indicative of the ultimate collectibility of the current amortized cost of the securities, but rather are attributable to changes in interest rates, credit spreads and other factors. The Company has no current intent to sell securities with unrealized losses, nor is it more likely than not that it will be required to sell prior to recovery of amortized cost; accordingly, the Company has determined that there are no additional OTTI losses to be recorded as of June 30, 2018.

The following table presents the activity related to the pretax credit loss component reflected in Retained earnings on fixed maturity securities still held as of June 30, 2018 and 2017 and for which a portion of an OTTI loss was recognized in Other comprehensive income (loss).

Periods ended June 30	Three Months		Six Months	
(In millions)	2018	2017	2018	2017
Beginning balance of credit losses on fixed maturity securities	$25	$32	$27	$36
Reductions for securities sold during the period	(4)	(2)	(6)	(6)
Ending balance of credit losses on fixed maturity securities	$21	$30	$21	$30

Contractual Maturity

The following table presents available-for-sale fixed maturity securities by contractual maturity.

	June 30, 2018		December 31, 2017	
(In millions)	Cost or Amortized Cost	Estimated Fair Value	Cost or Amortized Cost	Estimated Fair Value
Due in one year or less	$1,301	$ 1,322	$1,135	$ 1,157
Due after one year through five years	8,211	8,421	8,165	8,501
Due after five years through ten years	16,138	16,240	16,060	16,718
Due after ten years	12,261	13,795	12,852	15,108
Total	$37,911	$ 39,778	$38,212	$ 41,484

Actual maturities may differ from contractual maturities because certain securities may be called or prepaid. Securities not due at a single date are allocated based on weighted average life.

Derivative Financial Instruments

The Company holds an embedded derivative on a funds withheld liability with a notional value of $161 million and $167 million as of June 30, 2018 and December 31, 2017 and a fair value of $4 million and $(3) million as of June 30, 2018 and December 31, 2017. The embedded derivative on the funds withheld liability is accounted for separately and reported with the funds withheld liability in Other liabilities on the Condensed Consolidated Balance Sheets.

Investment Commitments

As of June 30, 2018, the Company had committed approximately $551 million to future capital calls from various third-party limited partnership investments in exchange for an ownership interest in the related partnerships.

As of June 30, 2018, the Company had mortgage loan commitments of $15 million representing signed loan applications received and accepted.

The Company invests in various privately placed debt securities, including bank loans, as part of its overall investment strategy and has committed to additional future purchases, sales and funding. Purchases and sales of privately placed debt securities are recorded once funded. As of June 30, 2018, the Company had commitments to purchase or fund additional amounts of $272 million and sell $111 million under the terms of such securities.

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Note D. Fair Value

Fair value is the price that would be received upon sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following fair value hierarchy is used in selecting inputs, with the highest priority given to Level 1, as these are the most transparent or reliable.

Level 1 - Quoted prices for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets.

Level 3 - Valuations derived from valuation techniques in which one or more significant inputs are not observable.

Prices may fall within Level 1, 2 or 3 depending upon the methodology and inputs used to estimate fair value for each specific security. In general, the Company seeks to price securities using third-party pricing services. Securities not priced by pricing services are submitted to independent brokers for valuation and, if those are not available, internally developed pricing models are used to value assets using a methodology and inputs the Company believes market participants would use to value the assets. Prices obtained from third-party pricing services or brokers are not adjusted by the Company.

The Company performs control procedures over information obtained from pricing services and brokers to ensure prices received represent a reasonable estimate of fair value and to confirm representations regarding whether inputs are observable or unobservable. Procedures may include i) the review of pricing service methodologies or broker pricing qualifications, ii) back-testing, where past fair value estimates are compared to actual transactions executed in the market on similar dates, iii) exception reporting, where period-over-period changes in price are reviewed and challenged with the pricing service or broker based on exception criteria, iv) deep dives, where the Company performs an independent analysis of the inputs and assumptions used to price individual securities and v) pricing validation, where prices received are compared to prices independently estimated by the Company.

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Assets and Liabilities Measured at Fair Value

Assets and liabilities measured at fair value on a recurring basis are presented in the following tables. Corporate bonds and other includes obligations of the U.S. Treasury, government-sponsored enterprises and foreign governments and redeemable preferred stock.

June 30, 2018 (In millions)	Level 1	Level 2	Level 3	Total Assets/Liabilities at Fair Value
Assets				
Fixed maturity securities:				
Corporate bonds and other	$166	$18,949	$94	$ 19,209
States, municipalities and political subdivisions	—	12,008	1	12,009
Asset-backed	—	8,304	273	8,577
Total fixed maturity securities	166	39,261	368	39,795
Equity securities:				
Common stock	85	—	4	89
Non-redeemable preferred stock	67	604	13	684
Total equity securities	152	604	17	773
Short term and other	167	1,050	—	1,217
Total assets	$485	$40,915	$385	$ 41,785
Liabilities				
Other liabilities	$—	$(4)	$—	$ (4)
Total liabilities	$—	$(4)	$—	$ (4)

December 31, 2017 (In millions)	Level 1	Level 2	Level 3	Total Assets/Liabilities at Fair Value
Assets				
Fixed maturity securities:				
Corporate bonds and other	$128	$19,148	$98	$ 19,374
States, municipalities and political subdivisions	—	14,026	1	14,027
Asset-backed	—	7,751	335	8,086
Total fixed maturity securities	128	40,925	434	41,487
Equity securities:				
Common stock	23	—	4	27
Non-redeemable preferred stock	68	584	16	668
Total equity securities	91	584	20	695
Short term and other	396	958	—	1,354
Total assets	$615	$42,467	$454	$ 43,536
Liabilities				
Other liabilities	$—	$3	$—	$ 3
Total liabilities	$—	$3	$—	$ 3

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The tables below present a reconciliation for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3).

Level 3 (In millions)	Corporate bonds and other	States, municipalities and political subdivisions	Asset-backed	Equity securities	Derivative financial instruments	Total
Balance as of April 1, 2018	$ 100	$ 1	$ 279	$ 18	$ —	$ 398
Total realized and unrealized investment gains (losses):						
Reported in Net realized investment gains (losses)	—	—	—	(1)	—	(1)
Reported in Net investment income	—	—	—	—	—	—
Reported in Other comprehensive income	(1)	—	(1)	—	—	(2)
Total realized and unrealized investment gains (losses)	(1)	—	(1)	(1)	—	(3)
Purchases	2	—	41	—	—	43
Sales	(5)	—	—	—	—	(5)
Settlements	(2)	—	(6)	—	—	(8)
Transfers into Level 3	—	—	13	—	—	13
Transfers out of Level 3	—	—	(53)	—	—	(53)
Balance as of June 30, 2018	$ 94	$ 1	$ 273	$ 17	$ —	$ 385
Unrealized gains (losses) on Level 3 assets and liabilities held as of June 30, 2018 recognized in Net income (loss)	$ —	$ —	$ —	$ (1)	$ —	$ (1)

Level 3 (In millions)	Corporate bonds and other	States, municipalities and political subdivisions	Asset-backed	Equity securities	Derivative financial instruments	Life settlement contracts	Total
Balance as of April 1, 2017	$ 121	$ 1	$ 256	$ 19	$ —	$ 46	$ 443
Total realized and unrealized investment gains (losses):							
Reported in Net realized investment gains (losses)	—	—	1	—	—	—	1
Reported in Other revenues	—	—	—	—	—	—	—
Reported in Other comprehensive income	—	—	1	1	—	—	2
Total realized and unrealized investment gains (losses)	—	—	2	1	—	—	3
Purchases	—	—	13	—	—	—	13
Sales	—	—	—	(1)	—	(45)	(46)
Settlements	(11)	—	(7)	—	—	—	(18)
Transfers into Level 3	—	—	24	—	—	—	24
Transfers out of Level 3	(10)	—	(70)	—	—	—	(80)
Balance as of June 30, 2017	$ 100	$ 1	$ 218	$ 19	$ —	$ 1	$ 339
Unrealized gains (losses) on Level 3 assets and liabilities held as of June 30, 2017 recognized in Net income (loss)	$ —	$ —	$ —	$ —	$ —	$ —	$ —

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Level 3 (In millions)	Corporate bonds and other	States, municipalities and political subdivisions	Asset-backed	Equity securities	Derivative financial instruments	Total
Balance as of January 1, 2018	$ 98	$ 1	$ 335	$ 20	$ —	$454
Total realized and unrealized investment gains (losses):						
Reported in Net realized investment gains (losses)	(1)	—	7	(3)	—	3
Reported in Net investment income	—	—	—	—	—	—
Reported in Other comprehensive income	(1)	—	(6)	—	—	(7)
Total realized and unrealized investment gains (losses)	(2)	—	1	(3)	—	(4)
Purchases	2	—	71	—	—	73
Sales	(5)	—	(72)	—	—	(77)
Settlements	(4)	—	(12)	—	—	(16)
Transfers into Level 3	5	—	13	—	—	18
Transfers out of Level 3	—	—	(63)	—	—	(63)
Balance as of June 30, 2018	$ 94	$ 1	$ 273	$ 17	$ —	$385
Unrealized gains (losses) on Level 3 assets and liabilities held as of June 30, 2018 recognized in Net income (loss)	$ —	$ —	$ —	$ (3)	$ —	$(3)

Level 3 (In millions)	Corporate bonds and other	States, municipalities and political subdivisions	Asset-backed	Equity securities	Derivative financial instruments	Life settlement contracts	Total
Balance as of January 1, 2017	$ 130	$ 1	$ 199	$ 19	$ —	$ 58	$407
Total realized and unrealized investment gains (losses):							
Reported in Net realized investment gains (losses)	—	—	1	—	1	—	2
Reported in Other revenues	—	—	—	—	—	6	6
Reported in Other comprehensive income	1	—	3	2	—	—	6
Total realized and unrealized investment gains (losses)	1	—	4	2	1	6	14
Purchases	5	—	51	1	—	—	57
Sales	(1)	—	—	(3)	(1)	(58)	(63)
Settlements	(25)	—	(13)	—	—	(5)	(43)
Transfers into Level 3	—	—	52	—	—	—	52
Transfers out of Level 3	(10)	—	(75)	—	—	—	(85)
Balance as of June 30, 2017	$ 100	$ 1	$ 218	$ 19	$ —	$ 1	$339
Unrealized gains (losses) on Level 3 assets and liabilities held as of June 30, 2017 recognized in Net income (loss)	$ —	$ —	$ —	$ —	$ —	$ —	$—

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Securities may be transferred in or out of levels within the fair value hierarchy based on the availability of observable market information and quoted prices used to determine the fair value of the security. The availability of observable market information and quoted prices varies based on market conditions and trading volume. During the three months ended June 30, 2018, there were no transfers between Level 1 and Level 2. During the six months ended June 30, 2018, there were $29 million of transfers from Level 2 to Level 1 and no transfers from Level 1 to Level 2. During the three and six months ended June 30, 2017 there were no transfers between Level 1 and Level 2. The Company's policy is to recognize transfers between levels at the beginning of quarterly reporting periods.

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Valuation Methodologies and Inputs

The following section describes the valuation methodologies and relevant inputs used to measure different financial instruments at fair value, including an indication of the level in the fair value hierarchy in which the instruments are generally classified.

Fixed Maturity Securities

Level 1 securities include highly liquid and exchange traded bonds and redeemable preferred stock, valued using quoted market prices. Level 2 securities include most other fixed maturity securities as the significant inputs are observable in the marketplace. All classes of Level 2 fixed maturity securities are valued using a methodology based on information generated by market transactions involving identical or comparable assets, a discounted cash flow methodology, or a combination of both when necessary. Common inputs for all classes of fixed maturity securities include prices from recently executed transactions of similar securities, marketplace quotes, benchmark yields, spreads off benchmark yields, interest rates and U.S. Treasury or swap curves. Specifically for asset-backed securities, key inputs include prepayment and default projections based on past performance of the underlying collateral and current market data. Fixed maturity securities are primarily assigned to Level 3 in cases where broker/dealer quotes are significant inputs to the valuation and there is a lack of transparency as to whether these quotes are based on information that is observable in the marketplace. Level 3 securities also include private placement debt securities whose fair value is determined using internal models with inputs that are not market observable.

Equity Securities

Level 1 securities include publicly traded securities valued using quoted market prices. Level 2 securities are primarily valued using pricing for similar securities, recently executed transactions and other pricing models utilizing market observable inputs. Level 3 securities are primarily priced using broker/dealer quotes and internal models with inputs that are not market observable.

Short Term and Other Invested Assets

Securities that are actively traded or have quoted prices are classified as Level 1. These securities include money market funds and treasury bills. Level 2 primarily includes commercial paper, for which all inputs are market observable. Fixed maturity securities purchased within one year of maturity are classified consistent with fixed maturity securities discussed above. Short term investments as presented in the tables above differ from the amounts presented on the Condensed Consolidated Balance Sheets because certain short term investments, such as time deposits, are not measured at fair value.

As of June 30, 2018 and December 31, 2017, there were approximately $42 million and $39 million of overseas deposits within other invested assets, which can be redeemed at net asset value in 90 days or less. Overseas deposits are excluded from the fair value hierarchy because their fair value is recorded using the net asset value per share (or equivalent) practical expedient.

Life Settlement Contracts

The Company sold its life settlement contracts to a third party in 2017. The valuation of the life settlement contracts was based on the terms of sale. The contracts were classified as Level 3 as there was not an active market for life settlement contracts.

Derivative Financial Investments

Level 2 investments primarily include the embedded derivative on the funds withheld liability. The embedded derivative on funds withheld liability is valued using the change in fair value of the assets supporting the funds withheld liability, which are fixed maturity securities valued with observable inputs.

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Significant Unobservable Inputs

The following tables present quantitative information about the significant unobservable inputs utilized by the Company in the fair value measurements of Level 3 assets. Valuations for assets and liabilities not presented in the tables below are primarily based on broker/dealer quotes for which there is a lack of transparency as to inputs used to develop the valuations. The quantitative detail of these unobservable inputs is neither provided nor reasonably available to the Company.

June 30, 2018	Estimated Fair Value (In millions)	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
Fixed maturity securities	$ 130	Discounted cash flow	Credit spread	1% - 12% (3%)

December 31, 2017	Estimated Fair Value (In millions)	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
Fixed maturity securities	$ 136	Discounted cash flow	Credit spread	1% - 12% (3%)

For fixed maturity securities, an increase to the credit spread assumptions would result in a lower fair value measurement.

Financial Assets and Liabilities Not Measured at Fair Value

The carrying amount and estimated fair value of the Company's financial assets and liabilities which are not measured at fair value on the Condensed Consolidated Balance Sheets are presented in the following tables.

June 30, 2018	Carrying Amount	Estimated Fair Value			
(In millions)		Level 1	Level 2	Level 3	Total
Assets					
Mortgage loans	$ 865	$ —	$ —	$ 850	$ 850
Note receivable	34				