Item 8. Financial Statements and Supplementary Data

RESPONSIBILITY FOR FINANCIAL STATEMENTS

We have prepared the consolidated financial statements of Cincinnati Financial Corporation and our subsidiaries for the year ended December 31, 2006, in accordance with accounting principles generally accepted in the United States of America (GAAP).

We are responsible for the integrity and objectivity of these financial statements. The amounts, presented on an accrual basis, reflect our best estimates and judgment. These statements are consistent in all material aspects with other financial information in the Annual Report on Form 10-K. Our accounting system and related internal controls are designed to assure that our books and records accurately reflect the company's transactions in accordance with established policies and procedures as implemented by qualified personnel.

Our board of directors has established an audit committee of independent outside directors. We believe these directors are free from any relationships that could interfere with their independent judgment as audit committee members.

The audit committee meets periodically with management, our independent registered public accounting firm and our internal auditors to discuss how each is handling responsibilities. The audit committee reports on their findings to the board of directors. The audit committee recommends to the board the annual appointment of the independent registered public accounting firm. The audit committee reviews with this firm the scope of the audit assignment and the adequacy of internal controls and procedures.

Deloitte & Touche LLP, our independent registered public accounting firm, audited the consolidated financial statements of Cincinnati Financial Corporation and subsidiaries for the year ended December 31, 2006. Their report is on Page 80. Deloitte's auditors met with our audit committee to discuss the results of their examination. They have the opportunity to present their opinions about the adequacy of internal controls and the quality of financial reporting without management present.

MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Cincinnati Financial Corporation and its subsidiaries is responsible for establishing and maintaining adequate internal controls, designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America (GAAP). The 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 GAAP and that receipts and expenditures of the company are being made only in accordance with authorizations of management and the 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.

All internal control systems, no matter how well designed, have inherent limitations, including the possibility of human error and the circumvention of overriding controls. Accordingly, even effective internal control can provide only reasonable assurance with respect to financial statement preparation and presentation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

The company's management assessed the effectiveness of the company's internal control over financial reporting as of December 31, 2006, as required by Section 404 of the Sarbanes Oxley Act of 2002. Management's assessment is based on the criteria established in the Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and was designed to provide reasonable assurance that the company maintained effective internal control over financial reporting as of December 31, 2006. The assessment led management to conclude that, as of December 31, 2006, the company's internal control over financial reporting was effective based on those criteria.

The company's independent registered public accounting firm has issued an attestation report on our internal control over financial reporting as of December 31, 2006, and the company's management assessment of our internal control over financial reporting. This report appears below.

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU
Chairman and Chief Executive Officer

/S/ Kenneth W. Stecher

Kenneth W. Stecher
Chief Financial Officer, Executive Vice President, Secretary and Treasurer
(Principal Accounting Officer)

February 23, 2007

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of Cincinnati Financial Corporation:

We have audited the consolidated balance sheets of Cincinnati Financial Corporation and subsidiaries (the company) as of December 31, 2006 and 2005, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2006. Our audits also included the financial statement schedules listed in the Index at Item 15(c). We also have audited management's assessment, included in the Management's Annual Report on Internal Control Over Financial Reporting report, that the company maintained effective internal control over financial reporting as of December 31, 2006, based on the criteria established in the Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The company's management is responsible for these financial statements and financial statement schedules, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on these financial statements and financial statement schedules, an opinion on management's assessment, and an opinion on the effectiveness of the company's internal control over financial reporting 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 and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. 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 the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the 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, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the company as of December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein. Also, in our opinion, management's assessment that the company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Furthermore, in our opinion, the company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in Note 1 to the Consolidated Financial Statements, the company adopted the provisions of Statement of Financial Accounting Standards No. 123(R), Share Based Payment, on January 1, 2006, and the recognition and related disclosure provisions of Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension Plans and Other Postretirement Benefit Plans on December 31, 2006.

/S/ Deloitte & Touche LLP
Cincinnati, Ohio
February 23, 2007

Cincinnati Financial Corporation and Subsidiaries

Consolidated Balance Sheets

(Dollars in millions except per share data)	**December 31, 2006**	December 31, 2005
ASSETS		
Investments		
Fixed maturities, at fair value (amortized cost: 2006—$5,739; 2005—$5,387)	**$ 5,805**	$ 5,476
Equity securities, at fair value (cost: 2006—$2,621; 2005—$2,128)	**7,799**	7,106
Short-term investments, at fair value (amortized cost: 2006—$95; 2005—$75)	**95**	75
Other invested assets	**60**	45
Total investments	**13,759**	12,702
Cash and cash equivalents	**202**	119
Investment income receivable	**121**	117
Finance receivable	**108**	105
Premiums receivable	**1,128**	1,116
Reinsurance receivable	**683**	681
Prepaid reinsurance premiums	**13**	14
Deferred policy acquisition costs	**453**	429
Land, building and equipment, net, for company use (accumulated depreciation: 2006—$261; 2005—$232)	**193**	168
Other assets	**58**	66
Separate accounts	**504**	486
Total assets	**$ 17,222**	$ 16,003
LIABILITIES		
Insurance reserves		
Loss and loss expense reserves	**$ 3,896**	$ 3,661
Life policy reserves	**1,409**	1,343
Unearned premiums	**1,579**	1,559
Other liabilities	**533**	455
Deferred income tax	**1,653**	1,622
Note payable	**49**	0
6.125% senior notes due 2034	**371**	371
6.9% senior debentures due 2028	**28**	28
6.92% senior debentures due 2028	**392**	392
Separate accounts	**504**	486
Total liabilities	**10,414**	9,917
Commitments and contingent liabilities (Note 15)	—	—
SHAREHOLDERS' EQUITY		
Common stock, par value—$2 per share; (authorized: 2006—500 million shares, 2005—500 million shares; issued: 2006—196 million shares, 2005—194 million shares)	**391**	389
Paid-in capital	**1,015**	969
Retained earnings	**2,786**	2,088
Accumulated other comprehensive income	**3,379**	3,284
Treasury stock at cost (2006—23 million shares, 2005—20 million shares)	**(763)**	(644)
Total shareholders' equity	**6,808**	6,086
Total liabilities and shareholders' equity	**$ 17,222**	$ 16,003

Accompanying notes are an integral part of this statement.

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(In millions except per share data)	Years ended December 31,		
	2006	2005	2004
REVENUES			
Earned premiums			
Property casualty	**$ 3,163**	$ 3,058	$ 2,919
Life	**115**	106	101
Investment income, net of expenses	**570**	526	492
Realized investment gains and losses	**684**	61	91
Other income	**18**	16	11
Total revenues	**4,550**	3,767	3,614
BENEFITS AND EXPENSES			
Insurance losses and policyholder benefits	**2,128**	1,911	1,846
Commissions	**630**	627	615
Other operating expenses	**354**	302	270
Taxes, licenses and fees	**77**	72	75
Increase in deferred policy acquisition costs	**(21)**	(19)	(30)
Interest expense	**53**	51	38
Total benefits and expenses	**3,221**	2,944	2,814
INCOME BEFORE INCOME TAXES	**1,329**	823	800
PROVISION (BENEFIT) FOR INCOME TAXES			
Current	**404**	188	171
Deferred	**(5)**	33	45
Total provision for income taxes	**399**	221	216
NET INCOME	**$ 930**	$ 602	$ 584
PER COMMON SHARE			
Net income—basic	**$ 5.36**	$ 3.44	$ 3.30
Net income—diluted	**5.30**	3.40	3.28

Accompanying notes are an integral part of this statement.

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In millions)	Years ended December 31,		
	2006	2005	2004
COMMON STOCK			
Beginning of year	**$ 389**	$ 370	$ 352
5% stock dividend	**0**	18	18
Stock options exercised	**2**	1	0
End of year	**391**	389	370
PAID-IN CAPITAL			
Beginning of year	**969**	618	306
5% stock dividend	**0**	341	312
Stock loan	**0**	0	(3)
Stock options exercised	**28**	9	3
Share-based compensation	**17**	0	0
Other	**1**	1	0
End of year	**1,015**	969	618
RETAINED EARNINGS			
Beginning of year	**2,088**	2,057	1,986
Net income	**930**	602	584
5% stock dividend	**0**	(359)	(330)
Dividends declared	**(232)**	(212)	(183)
End of year	**2,786**	2,088	2,057
ACCUMULATED OTHER COMPREHENSIVE INCOME			
Beginning of year	**3,284**	3,787	4,084
Other comprehensive income, net	**127**	(503)	(297)
Cumulative effect of change in accounting for pension obligations	**(32)**	0	0
End of year	**3,379**	3,284	3,787
TREASURY STOCK			
Beginning of year	**(644)**	(583)	(524)
Purchase	**(120)**	(63)	(66)
Reissued	**1**	2	7
End of year	**(763)**	(644)	(583)
Total shareholders' equity	**$ 6,808**	$ 6,086	$ 6,249
COMMON STOCK - NUMBER OF SHARES OUTSTANDING			
Beginning of year	**174**	167	160
5% stock dividend	**0**	9	8
Shares issued	**1**	0	0
Purchase of treasury shares	**(2)**	(2)	(1)
End of year	**173**	174	167
COMPREHENSIVE INCOME			
Net income	**$ 930**	$ 602	$ 584
Other comprehensive income, net	**127**	(503)	(297)
Total comprehensive income	**$ 1,057**	$ 99	$ 287

Accompanying notes are an integral part of this statement.

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	Years ended December 31,		
	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	**$ 930**	$ 602	$ 584
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation, amortization and other non-cash items	**38**	33	28
Realized gains on investments	**(684)**	(61)	(91)
Share-based compensation	**17**	0	0
Interest credited to contract holders	**31**	28	24
Changes in:			
Investment income receivable	**(3)**	(10)	(8)
Premiums and reinsurance receivable	**(13)**	2	(118)
Deferred policy acquisition costs	**(21)**	(19)	(30)
Other assets	**17**	5	(13)
Loss and loss expense reserves	**235**	112	134
Life policy reserves	**81**	84	109
Unearned premiums	**20**	20	93
Other liabilities	**(5)**	(17)	83
Deferred income tax	**(5)**	33	45
Current income tax	**(23)**	(7)	(17)
Net cash provided by operating activities	**615**	805	823
CASH FLOWS FROM INVESTING ACTIVITIES			
Sale of fixed maturities	**110**	243	175
Call or maturity of fixed maturities	**343**	466	664
Sale of equity securities	**859**	104	536
Collection of finance receivables	**35**	34	32
Purchase of fixed maturities	**(753)**	(1,297)	(1,718)
Purchase of equity securities	**(689)**	(219)	(148)
Change in short-term investments, net	**(15)**	(4)	(71)
Investment in buildings and equipment, net	**(52)**	(44)	(33)
Investment in finance receivables	**(41)**	(45)	(46)
Collection of negotiated settlement-software cost recovery	**0**	0	9
Change in other invested assets, net	**(11)**	(9)	(1)
Net cash used in investing activities	**(214)**	(771)	(601)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from 6.125% senior notes	**0**	0	371
Debt issuance costs from 6.125% senior notes	**0**	0	(4)
Payment of cash dividends to shareholders	**(228)**	(204)	(177)
Purchase of treasury shares	**(120)**	(61)	(59)
Increase in notes payable	**49**	0	(183)
Proceeds from stock options exercised	**27**	11	3
Contract holder funds deposited	**32**	87	93
Contract holder funds withdrawn	**(78)**	(54)	(51)
Excess tax benefits on share-based compensation	**2**	0	0
Other	**(2)**	0	0
Net cash used in financing activities	**(318)**	(221)	(7)
Net increase (decrease) in cash and cash equivalents	**83**	(187)	215
Cash and cash equivalents at beginning of year	**119**	306	91
Cash and cash equivalents at end of year	**$ 202**	$ 119	$ 306
Supplemental disclosures of cash flow information:			
Interest paid (net of capitalized interest: 2006—$2; 2005—$1; 2004—$0)	**$ 53**	$ 51	$ 34
Income taxes paid	**429**	195	188
Non-cash activities:			
Conversion of fixed maturity to equity security and fixed maturity investments	**$ 50**	$ 42	$ 23
Equipment acquired under capital lease obligations	**12**	0	0

Accompanying notes are an integral part of this statement.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

We underwrite insurance through four companies that market through local independent insurance agents. Our products include a broad range of business and personal policies, as well as life and disability income insurance and annuities. We also provide finance/leasing products and asset management services through our CFC Investment Company and CinFin Capital Management Company subsidiaries.

Basis of Presentation

Our consolidated financial statements include the accounts of the parent company and our wholly owned subsidiaries. We present our statements in accordance with accounting principles generally accepted in the United States of America (GAAP). In consolidating our accounts, we have eliminated significant intercompany balances and transactions.

In accordance with GAAP, we have made estimates and assumptions that affect the amounts we report and discuss in the consolidated financial statements and accompanying notes. Actual results could differ from our estimates.

Earnings per Share

Net income per common share is based on the weighted average number of common shares outstanding during each of the respective years. We calculate net income per common share (diluted) assuming the exercise of stock options. We have adjusted shares and earnings per share to reflect all stock splits and dividends prior to December 31, 2006, including the 5 percent stock dividend paid April 26, 2005.

Share-based Compensation

We grant qualified and non-qualified stock options (share-based compensation) under our plans. These stock options are granted to associates at an exercise price that is not less than market price at the date of grant and are exercisable over 10 year periods. Prior to January 1, 2006, we accounted for those plans under the recognition and measurement provisions of APB Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations, as permitted by the Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation. No stock-based employee compensation cost was recognized in the Statement of Income for the years ended December 31, 2005 and 2004, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. Effective January 1, 2006, we adopted the fair value recognition provisions of SFAS No. 123(R), Share Based Payment, using the modified-prospective-transition method. We have elected to use the alternative method for determining the beginning balance of the additional paid-in capital pool, as described in FASB Staff Position 123(R)-3. See Note 16, Page 100, for more information regarding our share-based compensation.

Property Casualty Insurance

Property casualty policy written premiums are deferred and recorded as earned premiums on a pro rata basis over the terms of the policies. We record as unearned premium the portion of written premiums that apply to unexpired policy terms. The expenses associated with issuing insurance policies – primarily commissions, premium taxes and underwriting costs – are deferred and amortized over the terms of policies.

Certain property casualty policies are not booked before the effective date. An actuarial estimate is made to determine the amount of unbooked written premiums. The majority of the estimate is unearned and does not have a material impact on earned premium.

We establish reserves to cover the expected cost of claims – or losses – and our expenses related to investigating, processing and resolving claims. Although determining the appropriate amount of reserves including reserves for catastrophe losses is inherently uncertain, we base our decisions on past experience and current facts. Reserves are based on claims reported prior to the end of the year and estimates of unreported claims. We take into account the fact that we may recover some of our costs through salvage and subrogation. We regularly review and update reserves using the most current information available. Any resulting adjustments are reflected in current year insurance losses and policyholder benefits.

The Cincinnati Insurance Companies actively market property casualty insurance policies in 32 states. Our 10 largest states generated 70.0 percent and 69.7 percent of total property casualty premiums in 2006 and 2005. Ohio, our largest state, accounted for 22.0 percent and 22.5 percent of total earned premiums in 2006 and 2005. Agencies in Georgia, Illinois, Indiana, Michigan, North Carolina, Pennsylvania and Virginia each contributed between 4 percent and 10 percent of premium volume in 2006. No single agency relationship accounted for more than 1.2 percent of the company's total agency direct earned premiums in 2006.

Policyholder Dividends

Certain workers' compensation policies include the possibility of an insured earning a return of a portion of their premium, called a policyholder dividend. The dividend is generally calculated by determining the profitability of a policy year along with the associated premium. We reserve for all probable future policyholder dividend payments.

Life and Health Insurance

We offer several types of life and health insurance and we account for each according to the duration of the contract. Short-duration contracts are written to cover claims that arise during a short, fixed term of coverage. We generally have the right to change the amount of premium charged or cancel the coverage at the end of each contract term. Group life insurance is an example. We record premiums for short-duration contracts similarly to property casualty contracts.

Long-duration contracts are written to provide coverage for an extended period of time. Traditional long-duration contracts require policyholders to pay scheduled gross premiums, generally not less frequently than annually, over the term of the coverage. Premiums for these contracts are recognized as revenue when due. Whole life insurance is an example. Some traditional long-duration contracts have premium payment periods shorter than the period over which coverage is provided. For these contracts the excess of premium over the amount required to pay expenses and benefits is recognized over the term of the coverage rather than over the premium payment period. Ten-pay whole life insurance is an example.

We establish a liability for traditional long-duration contracts as we receive premiums. The amount of this liability is the present value of future expenses and benefits less the present value of future net premiums. Net premium is the portion of gross premium required to provide for all expenses and benefits. We estimate future expenses and benefits and net premium using assumptions for expected expenses, mortality, morbidity, withdrawal rates and investment income. We include a provision for adverse deviation, meaning we allow for some uncertainty in making our assumptions. We establish our assumptions when the contract is issued and we generally maintain those assumptions for the life of the contract. We use both our own experience and industry experience, adjusted for historical trends, in arriving at our assumptions for expected mortality, morbidity and withdrawal rates. We use our own experience and historical trends for setting our assumption for expected expenses. We base our assumption for expected investment income on our own experience, adjusted for current economic conditions.

When we issue a traditional long-duration contract, we capitalize acquisition costs. Acquisition costs are costs which vary with, and are primarily related to, the production of new business. We then charge these deferred policy acquisition costs to expenses over the premium paying period of the contract and we use the same assumptions that we use when we establish the liability for the contract.

Universal life contracts are long-duration contracts for which contractual provisions are not fixed, unlike whole life insurance. Universal life contracts allow policyholders to vary the amount of premium, within limits, without our consent. However we may vary the mortality and expense charges, within limits, and the interest crediting rate used to accumulate policy values. We do not record universal life premiums as revenue. Instead we recognize as revenue the mortality charges, administration charges and surrender charges when received. Some of our universal life contracts assess administration charges in the early years of the contract that are compensation for services we will provide in the later years of the contract. These administration charges are deferred and are recognized over the period when we provide those future services.

For universal life long-duration contracts we maintain a liability equal to the policyholder account value. There is no provision for adverse deviation. Some of our universal life policies contain no-lapse guarantee provisions. For these policies, we establish a reserve in addition to the account balance, based on expected no-lapse guarantee benefits and expected policy assessments.

When we issue a universal life long-duration contract we capitalize acquisition costs. We then charge these capitalized costs to expenses over the term of coverage of the contract. When we charge deferred policy acquisition costs to expenses, we use assumptions based on our best estimates of long-term experience. We review and modify these assumptions on a regular basis.

Separate Accounts

We issue life contracts with guaranteed minimum returns, referred to as bank-owned life insurance contracts (BOLIs). We legally segregate and record as separate accounts the assets and liabilities for some of our BOLIs, based on the specific contract provisions. We guarantee minimum investment returns, account values and death benefits for our separate account BOLIs. Our other BOLIs are general account products.

We carry the assets of separate account BOLIs at fair value. The liabilities on separate account BOLIs primarily are the contract holders' claims to the related assets and are carried at the fair value of the assets. If the BOLI asset value is projected below the value we guaranteed, a liability is established by a charge to the company's earnings.

Generally, investment income and realized investment gains and losses of the separate accounts accrue directly to the contract holder and we do not include them in the Consolidated Statements of Income. Revenues and expenses related to separate accounts consist of contractual fees and mortality, surrender and expense risk charges. Also, each separate account BOLI includes a negotiated gain and loss sharing arrangement with the company. A percentage of each separate account's realized gain and loss representing contract fees and assessments accrues to us and is transferred from the separate account to our general account and is recognized as revenue or expense.

Reinsurance

We reduce risk and uncertainty by buying property casualty and life reinsurance. Reinsurance contracts do not relieve us from our duty to policyholders, but rather help protect our financial strength to perform that duty. We estimate loss amounts recoverable from our reinsurers based on the reinsurance policy terms. Historically, our claims with reinsurers have been paid. We do not have an allowance for uncollectible reinsurance.

We also serve in a limited way as a reinsurer for other insurance companies, reinsurers and involuntary state pools. We record our transactions for such assumed reinsurance based on reports provided to us by the ceding reinsurer.

Cash and Cash Equivalents

Cash and cash equivalents include cash and money market funds.

Investments

Our portfolio investments are primarily in publicly traded fixed-maturity, equity and short-term investments, classified as available for sale at fair value in the consolidated financial statements. Fixed-maturity investments (taxable bonds, tax-exempt bonds and redeemable preferred stocks) and equity investments (common and non-redeemable preferred stocks) are classified as available for sale and recorded at fair value in the consolidated financial statements. Short-term investments are classified as available for sale and recorded at amortized cost, which approximates fair value, in the consolidated financial statements. The number of fixed-maturity securities trading below 100 percent of book value can be expected to fluctuate as interest rates rise or fall. Because of our strong surplus and long-term investment horizon, we intend to hold fixed-maturity investments until maturity, regardless of short-term fluctuations in fair values.

We include unrealized gains and losses on investments, net of taxes, in shareholders' equity as accumulated other comprehensive income. Realized gains and losses on investments are recognized in net income on a specific identification basis.

Investment income consists mainly of interest and dividends. We record interest on an accrual basis and record dividends at the ex-dividend date. We amortize premiums and discounts on fixed-maturity securities using the effective interest method.

Facts and circumstances sometimes warrant investment write-downs. We record such other-than-temporary declines as realized investment losses.

Fair Value Disclosures

We primarily base fair value for investments in equity and fixed-maturity securities (including redeemable preferred stock and assets held in separate accounts) on quoted market prices or on data provided by an outside resource that supplies global securities pricing. When a price is not available from these sources, as the case of securities that are not publicly traded, we determine the fair value using quotes from independent brokers. The fair value of investments priced by independent brokers is less than 1 percent of the fair value of our total investment portfolio.

We estimate fair value for liabilities under investment-type insurance contracts (annuities) using discounted cash flow calculations. We base the calculations on interest rates offered on contracts of similar nature and maturity. We base fair value for long-term senior notes and notes payable on the quoted market prices for such notes.

Derivative Financial Instruments and Hedging Activities

Some of our investments contain embedded options. These investments include convertible debt and convertible preferred stock. We calculate fair value and account for the embedded options separately. The changes in fair values of embedded derivates are recognized in net income in the period they occur.

In 2006, CFC Investment Company, our commercial leasing and financing subsidiary, replaced $49 million of intercompany debt with borrowings against one of our short-term lines of credit to improve cash flow for the parent company. During the third quarter, we entered into an interest-rate swap to manage the variability of interest payments for certain variable-rate debt obligations ($49 million notional amount). Under this interest-rate swap contract, we have agreed to pay a fixed rate of interest for a three-year period. The contract is intended to be a hedge against changes in the amount of future cash flows associated with the related interest

payments for our short-term line of credit. The interest-rate swap contract is reflected at fair value in our consolidated balance sheet.

SFAS No. 133, as amended, requires changes in the fair value of the company's derivative financial instruments to be recognized periodically as realized gains or losses on the consolidated statement of income or as a component of accumulated other comprehensive income in shareholders' equity, respectively. We recognized a $324,000 pretax realized investment loss due to the decline in the fair value of the interest rate swap prior to qualifying for hedge accounting treatment.

In October, we completed the necessary requirements for the interest-rate swap to qualify for hedge accounting treatment under SFAS No. 133. We expect that the interest-rate swap will be a highly effective hedge and that future changes in the fair value of the interest-rate swap will be recorded as a component of accumulated other comprehensive income. We do not expect any significant amounts to be reclassified into earnings in the next 12 months. The fair value of the company's interest rate swap was $430,000 at December 31, 2006.

Securities Lending Program

In 2006, we began actively participating in a securities lending program under which certain fixed-maturity securities from our investment portfolio are loaned to other institutions for short periods of time. We require collateral in excess of the market value of the loaned securities. The collateral is invested in accordance with our guidelines in high-quality, short-duration instruments to generate additional investment income. The market value of the loaned securities is monitored on a daily basis and additional collateral is added or refunded as the market value of the loaned securities changes. The securities lending collateral is recognized as an asset, and classified as securities lending collateral, with a corresponding liability for the obligation to return the collateral.

We maintain the right and ability to redeem the fixed-maturity securities loaned on short notice and continue to earn interest on the securities. We maintain effective control over the securities that we have loaned, which are classified as invested assets on our consolidated balance sheets. Interest income on collateral, net of fees, was $697,000 for the twelve months ended December 31, 2006. At December 31, 2006, we had no securities on loan and held no collateral. We recalled our securities on loan prior to year end for statutory reporting reasons. We have continued the securities lending program in 2007.

Lease/Finance

Our CFC Investment Company subsidiary provides auto and equipment direct financing (leases and loans) to commercial and individual clients. We generally transfer ownership of the property to the client as the terms of the leases expire. Our lease contracts contain bargain purchase options. We record income over the financing term using the interest method.

We capitalize and amortize lease or loan origination costs over the life of the financing using the interest method. These costs may include, but are not limited to: finder fees, broker fees, filing fees and the cost of credit reports.

Asset Management

Our CinFin Capital Management subsidiary generates revenue from management fees. We set those fees based on the market value of assets under management, and we record our revenue as it is earned.

Land, Building and Equipment

We record building and equipment at cost less accumulated depreciation. Certain equipment held under capital leases also is classified as property and equipment with the related lease obligations recorded as liabilities. Our depreciation is based on estimated useful lives (ranging from three years to 39½ years) using straight-line and accelerated methods. Depreciation expense recorded in 2006, 2005 and 2004 was $38 million, $33 million and $30 million, respectively. We monitor land, building and equipment for potential impairments. Potential impairments may include a significant decrease in the market values of the assets, considerable cost overruns on projects or a change in legal factors or business climate, or other factors that indicate that the carrying amount may not be recoverable.

We capitalize costs for internally developed computer software during the application development stage. These costs generally consist of external consulting, payroll and payroll-related costs.

Income Taxes

We calculate deferred income tax liabilities and assets using tax rates in effect for the time when temporary differences in book and taxable income are estimated to reverse. We recognize deferred income taxes for numerous temporary differences between our taxable income and book-basis income and other changes in shareholders' equity. Such temporary differences relate primarily to unrealized gains on investments and differences in the recognition of deferred acquisition costs and insurance reserves. We charge deferred income taxes associated with unrealized appreciation (except the amounts related to the effect of income tax rate

changes) to shareholders' equity in accumulated other comprehensive income. We charge deferred taxes associated with other differences to income.

New Accounting Pronouncements

SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of SFAS Nos. 133 and 140

In February 2006, Financial Accounting Standards Board (FASB) issued SFAS No. 155. This accounting standard permits fair value re-measurement for any hybrid financial instrument containing an embedded derivative that otherwise would require bifurcation; clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133; establishes a requirement to evaluate interests in securitized financial assets to identify them as freestanding derivatives or as hybrid financial instruments containing an embedded derivative requiring bifurcation; clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument pertaining to a beneficial interest other than another derivative financial instrument. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year beginning after September 15, 2006.

We adopted SFAS No. 155 on January 1, 2007, to permit fair value re-measurement for our hybrid financial instruments that contain embedded derivatives that required bifurcation under the original provisions of SFAS No. 133. The adoption is not expected to have a material impact on our results of operations or financial position.

SFAS No. 157, Fair Value Measurements

In September 2006, FASB issued SFAS No. 157, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The provisions of SFAS No. 157 are effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We currently are evaluating the timing and impact of adopting SFAS No. 157 on our financial position.

SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of SFAS Nos. 87, 88, 106, and 132(R)

In September 2006, FASB issued SFAS No. 158, which requires that we recognize the over-funded or under-funded status of our defined benefit plans as an asset or liability. SFAS No. 158 is effective as of December 31, 2006, with changes in the funded status recognized through accumulated other comprehensive income in the year in which they occur.

The adoption of SFAS No. 158 resulted in an increase in liabilities of approximately $32 million on an after-tax basis with a corresponding reduction in accumulated other comprehensive income and shareholders' equity. SFAS No. 158 did not change the amount of net periodic benefit expense recognized in an entity's results of operations.

SAB No. 108, Considering the Effects of Prior Year Misstatements when Qualifying Misstatements in Current Year Financial Statements

In September 2006, the SEC issued Staff Accounting Bulletin (SAB) No. 108 to address diversity in practice in quantifying financial statement misstatements. SAB 108 requires that we quantify misstatements based on their impact on each of our financial statements and related disclosures. SAB 108 is effective as of December 31, 2006, allowing a one-time transitional cumulative effect adjustment to retained earnings as of January 1, 2006, for errors that were not previously deemed material, but are material under the guidance in SAB No. 108.The impact of adopting SAB No. 108 did not result in a material effect on our results of operations and financial position.

Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of SFAS No. 109

In July 2006, FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes. FIN 48 is an interpretation of SFAS No. 109, Accounting for Income Taxes. This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109. This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. This Interpretation is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 as of January 1, 2007, as required. In the first quarter of 2007, we will record a cumulative effect adjustment of a change in accounting principle as prescribed by FIN 48. We do not expect FIN 48 to have a material effect on our results or operations or financial position.

SOP 05-1, Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts

In October 2005, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 05-1, which provides accounting guidance for deferred policy acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in SFAS No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments. SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights or coverages that occurs by the exchange of a contract for a new contract, or by amendment, endorsement or rider to a contract, or by the election of a feature or coverage within a contract. Internal replacement contracts are those that are substantially changed from the replaced contract and are accounted for as an extinguishment of the replaced contract. Nonintegrated contract features are accounted for as separately issued contracts. Modifications resulting from the election of a feature or coverage within a contract or from an integrated contract feature generally do not result in an internal replacement contract subject to SOP 05-1 provided certain conditions are met. The provisions of SOP 05-1 are effective for internal replacements occurring in fiscal years beginning after December 15, 2006. We do not expect this statement to have a material impact on our results of operations or financial position.

Reclassifications

We have reclassified certain prior-year amounts to conform with current-year classifications.

2. INVESTMENTS

(In millions)	Years ended December 31, 2006	2005	2004
Investment income summarized by investment category:			
Interest on fixed maturities	**$ 300**	$ 280	$ 252
Dividends on equity securities	**262**	244	239
Other investment income	**15**	8	6
Total	**577**	532	497
Less investment expenses	**7**	6	5
Total	**$ 570**	$ 526	$ 492
Realized investment gains and losses summary:			
Fixed maturities:			
Gross realized gains	**$ 27**	$ 36	$ 36
Gross realized losses	**(2)**	(1)	(20)
Other-than-temporary impairments	**(1)**	(1)	(5)
Equity securities:			
Gross realized gains	**656**	40	101
Gross realized losses	**(5)**	(6)	(30)
Other-than-temporary impairments	**0**	0	(1)
Embedded derivatives	**7**	(7)	10
Other	**2**	0	0
Total	**$ 684**	$ 61	$ 91
Change in unrealized investment gains and losses and other summary:			
Fixed maturities	**$ (23)**	$ (198)	$ (6)
Equity securities	**200**	(575)	(448)
Adjustment to deferred acquisition costs and life policy reserves	**2**	6	3
Other	**2**	18	(6)
Income taxes on above	**(54)**	246	160
Total	**$ 127**	$ (503)	$ (297)

At December 31, 2006, contractual maturity dates for fixed-maturity and short-term investments were:

(In millions)	Amortized cost	Fair value	% of Fair value
Maturity dates occurring:			
Less than one year	$ 203	$ 204	3.5 %
One year through five years	787	802	13.6
After five years through ten years	2,860	2,865	48.5
After ten years through twenty years	1,729	1,763	29.9
Over twenty years	255	266	4.5
Total	$ 5,834	$ 5,900	100.0 %

Actual maturities may differ from contractual maturities when there is a right to call or prepay obligations with or without call or prepayment penalties.

At December 31, 2006, investments with book value of $64 million and fair value of $66 million were on deposit with various states in compliance with regulatory requirements.

The following table analyzes cost or amortized cost, gross unrealized gains, gross unrealized losses and fair value for our investments:

(In millions) At December 31,	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
2006				
Fixed maturities:				
States, municipalities and political subdivisions	**$ 2,382**	**$ 40**	**$ 6**	**$ 2,416**
Convertibles and bonds with warrants attached	**264**	**17**	**3**	**278**
Public utilities	**140**	**4**	**2**	**142**
United States government	**5**	**0**	**0**	**5**
Government-sponsored enterprises	**995**	**0**	**23**	**972**
Foreign government	**3**	**0**	**0**	**3**
All other corporate bonds and short-term investments	**2,045**	**61**	**22**	**2,084**
Total	**$ 5,834**	**$ 122**	**$ 56**	**$ 5,900**
Equity securities	**$ 2,621**	**$ 5,181**	**$ 3**	**$ 7,799**
2005				
Fixed maturities:				
States, municipalities and political subdivisions	$ 2,083	$ 48	$ 14	$ 2,117
Convertibles and bonds with warrants attached	270	17	9	278
Public utilities	139	5	1	143
United States government	5	0	0	5
Government-sponsored enterprises	992	0	19	973
Foreign government	3	0	0	3
All other corporate bonds and short-term investments	1,970	89	27	2,032
Total	$ 5,462	$ 159	$ 70	$ 5,551
Equity securities	$ 2,128	$ 4,986	$ 8	$ 7,106

This table reviews unrealized losses and fair values by investment category and by length of time securities have been in a continuous unrealized loss position:

(In millions)	Less than 12 months		12 months or more		Total	
At December 31,	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
2006						
Fixed maturities:						
States, municipalities and political subdivisions	**$ 190**	**$ 1**	**$ 589**	**$ 5**	**$ 779**	**$ 6**
Convertibles and bonds with warrants attached	**6**	**0**	**43**	**3**	**49**	**3**
Public utilities	**4**	**0**	**54**	**2**	**58**	**2**
United States government	**3**	**0**	**1**	**0**	**4**	**0**
Government-sponsored enterprises	**1**	**0**	**970**	**23**	**971**	**23**
Foreign government	**3**	**0**	**0**	**0**	**3**	**0**
All other corporate bonds and short-term investments	**88**	**2**	**726**	**20**	**814**	**22**
Total	**295**	**3**	**2,383**	**53**	**2,678**	**56**
Equity securities:	**39**	**2**	**11**	**1**	**50**	**3**
Total	**$ 334**	**$ 5**	**$ 2,394**	**$ 54**	**$ 2,728**	**$ 59**
2005						
Fixed maturities:						
States, municipalities and political subdivisions	$ 754	$ 8	$ 173	$ 6	$ 927	$ 14
Convertibles and bonds with warrants attached	73	3	39	6	112	9
Public utilities	44	1	6	0	50	1
United States government	1	0	0	0	1	0
Government-sponsored enterprises	607	8	354	11	961	19
All other corporate bonds and short-term investments	387	11	284	16	671	27
Total	1,866	31	856	39	2,722	70
Equity securities:	59	2	47	6	106	8
Total	$ 1,925	$ 33	$ 903	$ 45	$ 2,828	$ 78

At December 31, 2006, 482 fixed-maturity investments with a total unrealized loss of $53 million and three equity securities with a total unrealized loss of $1 million had been in that position for 12 months or more. All were trading between 70 percent to less than 100 percent of book value.

At December 31, 2005, 177 fixed-maturity investments with a total unrealized loss of $39 million and three equity securities with a total unrealized loss of $6 million had been in that position for 12 months or more. All were trading between 70 percent to less than 100 percent of book value.

Investments in companies that exceed 10 percent of our shareholders' equity at December 31 include:

(In millions)	2006		2005	
	Cost	Fair value	Cost	Fair value
Issuers:				
Fifth Third Bancorp common stock	**$ 283**	**$ 2,979**	$ 283	$ 2,745
Exxon Mobil Corporation common stock	**133**	**687**	133	503
Alltel Corporation common stock and fixed maturity	**0**	**0**	122	807

We sold 12,700,164 shares of our holdings of Alltel Corporation common stock in January 2006 and 475,000 shares in December 2005. The sale contributed $647 million and $27 million to our 2006 and 2005 pretax realized gains. The sale contributed $412 million and $15 million to net income in 2006 and 2005, respectively.

3. DEFERRED ACQUISITION COSTS

This table summarizes components of our deferred policy acquisition costs asset:

(In millions)	At December 31,		
	2006	2005	2004
Deferred policy acquisition costs asset at beginning of year	**$ 429**	$ 400	$ 372
Capitalized deferred policy acquisition costs	**706**	683	657
Amortized deferred policy acquisition costs	**(685)**	(664)	(626)
Amortized shadow deferred policy acquisition costs	**3**	10	(3)
Deferred policy acquisition costs asset at end of year	**$ 453**	$ 429	$ 400

4. PROPERTY CASUALTY LOSS AND LOSS EXPENSES

This table summarizes activity in the reserve for loss and loss expenses:

(In millions)	Years ended December 31,		
	2006	2005	2004
Gross loss and loss expense reserves, January 1	**$ 3,629**	$ 3,514	$ 3,386
Less reinsurance receivable	**518**	537	541
Net loss and loss expense reserves, January 1	**3,111**	2,977	2,845
Net incurred loss and loss expenses related to:			
Current accident year	**2,124**	1,972	1,949
Prior accident years	**(116)**	(160)	(196)
Total incurred	**2,008**	1,812	1,753
Net paid loss and loss expenses related to:			
Current accident year	**819**	772	804
Prior accident years	**944**	906	817
Total paid	**1,763**	1,678	1,621
Net loss and loss expense reserves, December 31	**3,356**	3,111	2,977
Plus reinsurance receivable	**504**	518	537
Gross loss and loss expense reserves, December 31	**$ 3,860**	$ 3,629	$ 3,514

We base property casualty loss and loss expenses reserve estimates on our experience and on information gathered from internal analyses and our appointed actuary. When reviewing reserves, we analyze historical data and estimate the effect of various other factors, such as industry loss frequency and severity and premium trends; past, present and anticipated product pricing; anticipated premium growth; other quantifiable trends; and projected ultimate loss ratios.

Because of changes in estimates of insured events in prior years, we decreased the provision for loss and loss expenses by $116 million, $160 million and $196 million in calendar years 2006, 2005 and 2004. These decreases are partly due to the effects of settling reported (case) and unreported (IBNR) reserves established in prior years for amounts less than expected.

The reserve for loss and loss expenses in the consolidated balance sheets also includes $36 million, $32 million and $35 million at December 31, 2006, 2005 and 2004, respectively, for certain life and health losses.

5. LIFE POLICY RESERVES

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

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

Here is a summary of our life policy reserves:

(In millions)	At December 31, 2006	2005
Ordinary/traditional life	**$ 453**	$ 419
Universal life	**396**	376
Annuities	**537**	523
Other	**23**	25
Total	**$ 1,409**	$ 1,343

At both December 31, 2006 and 2005, the fair value associated with the annuities shown above was approximately $563 million.

6. NOTES PAYABLE

We had two lines of credit with commercial banks amounting to $125 million with an outstanding balance of $49 million at year-end 2006. We had no compensating balance requirement on short-term debt for either 2006 or 2005. We had two lines of credit with commercial banks amounting to $125 million with no outstanding balance at year-end 2005. Interest rates charged on such borrowings ranged from 5.90 percent to 6.03 percent during 2006.

The company's subsidiary, CFC Investment Company, entered into an interest-rate swap agreement during 2006, which expires in three years, to hedge future cash flows (thereby obtaining a fixed interest rate of 5.985 percent) related to certain variable rate debt obligations. This swap is reflected at fair value in the consolidated balance sheets and the unrealized loss, net of tax, at December 31, 2006, of $69,000 is a component of shareholders' equity in accumulated other comprehensive income. The company does not expect any significant amounts to be reclassified into earnings as a result of interest rate changes in the next 12 months.

7. SENIOR DEBT

This table summarizes the principal amounts of our long-term debt excluding unamortized discounts:

(In millions) Interest rate	Year of issue		At December 31, 2006	2005
6.90%	1998	Senior debentures, due 2028	**$ 28**	$ 28
6.92%	2005	Senior debentures, due 2028	**392**	392
6.125%	2004	Senior notes, due 2034	**375**	375
		Total	**$ 795**	$ 795

The fair value of our senior debt approximated $850 million at year-end 2006 and $870 million at year-end 2005. None of the notes are encumbered by rating triggers.

8. SHAREHOLDERS' EQUITY AND DIVIDEND RESTRICTIONS

Our insurance subsidiary declared dividends to the parent company of $275 million in 2006, $275 million in 2005 and $175 million in 2004. State of Ohio regulatory requirements restrict the dividends insurance subsidiaries can pay. Generally, the most Ohio-domiciled insurance subsidiaries can pay without prior regulatory approval is the greater of 10 percent of statutory surplus or 100 percent of statutory net income for the prior calendar year up to the amount of statutory unassigned surplus as of the end of the prior calendar year. Dividends exceeding these limitations may be paid only with approval of the Ohio Department of Insurance. During 2007, the total dividends that our lead insurance subsidiary may pay to our parent company without regulatory approval will be approximately $572 million.

As of December 31, 2006, 11.6 million shares of common stock were available for future stock option grants.

Declared cash dividends per share were $1.34, $1.21 and $1.04 for the years ended December 31, 2006, 2005 and 2004, respectively.

Accumulated Other Comprehensive Income

The change in unrealized gains and losses on investments and derivatives included:

(In millions)	Years ended December 31,								
		2006			2005			2004	
	Before tax	Income tax	Net	Before tax	Income tax	Net	Before tax	Income tax	Net
Accumulated unrealized gains (losses) on securities available for sale at January 1	**$ 5,060**	**$ 1,776**	**$ 3,284**	$ 5,809	$ 2,022	$ 3,787	$ 6,269	$ 2,183	$ 4,086
Net unrealized gains (losses)	**880**	**298**	**582**	(692)	(226)	(466)	(372)	(131)	(241)
Reclassification adjustment for (gains) losses included in net income	**(701)**	**(245)**	**(456)**	(61)	(21)	(40)	(91)	(31)	(60)
Adjustment to deferred acquisition costs and life policy reserves	**2**	**1**	**1**	4	1	3	3	1	2
Effect on other comprehensive income	**181**	**54**	**127**	(749)	(246)	(503)	(460)	(161)	(299)
Accumulated unrealized gains (losses) on securities available for sale at December 31	**$ 5,241**	**$ 1,830**	**$ 3,411**	$ 5,060	$ 1,776	$ 3,284	$ 5,809	$ 2,022	$ 3,787
Accumulated unrealized gains (losses) on derivatives used in cash flow hedging relationships at January 1	**$ 0**	**$ 0**	**$ 0**	$ 0	$ 0	$ 0	$ (3)	$ (1)	$ (2)
Net unrealized gains (losses)	**0**	**0**	**0**	0	0	0	0	0	0
Reclassification adjustment for (gains) losses included in net income	**0**	**0**	**0**	0	0	0	3	1	2
Effect on other comprehensive income	0	0	0	0	0	0	3	1	2
Accumulated unrealized gains (losses) on derivatives used in cash flow hedging relationships at December 31	**$ 0**	**$ 0**	**$ 0**	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Accumulated unrealized losses for pension obligations at January 1	**$ 0**	**$ 0**	**$ 0**	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Cumulative effect of change in accounting for pension obligations	**(49)**	**(17)**	**(32)**	0	0	0	0	0	0
Accumulated unrealized losses for pension obligations at December 31	**$ (49)**	**$ (17)**	**$ (32)**	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Accumulated other comprehensive income at January 1	**$ 5,060**	**$ 1,776**	**$ 3,284**	$ 5,809	$ 2,022	$ 3,787	$ 6,266	$ 2,182	$ 4,084
Other comprehensive income (loss)	**181**	**54**	**127**	(749)	(246)	(503)	(457)	(160)	(297)
Cumulative effect of change in accounting for pension obligations	**(49)**	**(17)**	**(32)**	0	0	0	0	0	0
Accumulated other comprehensive income at December 31	**$ 5,192**	**$ 1,813**	**$ 3,379**	$ 5,060	$ 1,776	$ 3,284	$ 5,809	$ 2,022	$ 3,787

9. REINSURANCE

Our statements of income include earned property casualty premiums on assumed and ceded business:

(In millions)	Years ended December 31,		
	2006	2005	2004
Direct earned premiums	**$ 3,296**	$ 3,209	$ 3,062
Assumed earned premiums	**26**	28	32
Ceded earned premiums	**(158)**	(179)	(175)
Net earned premiums	**$ 3,164**	$ 3,058	$ 2,919

Our statements of income include incurred property casualty loss and loss expenses on assumed and ceded business:

(In millions)	Years ended December 31,		
	2006	2005	2004
Direct incurred loss and loss expenses	$ **2,072**	$ 1,898	$ 1,870
Assumed incurred loss and loss expenses	**13**	40	17
Ceded incurred loss and loss expenses	**(77)**	(126)	(134)
Net incurred loss and loss expenses	$ **2,008**	$ 1,812	$ 1,753

10. INCOME TAXES

Here is a summary of the major components of our net deferred tax liability:

(In millions)	At December 31,	
	2006	2005
Deferred tax liabilities:		
Unrealized gains on investments and derivatives	**$ 1,824**	$ 1,788
Deferred acquisition costs	**142**	135
Other	**36**	32
Total	**2,002**	1,955
Deferred tax assets:		
Loss and loss expense reserves	**190**	179
Unearned premiums	**109**	108
Life policy reserves	**22**	26
Other	**28**	20
Total	**349**	333
Net deferred tax liability	**$ 1,653**	$ 1,622

The provision for federal income taxes is based upon a consolidated income tax return for the company and subsidiaries. As of December 31, 2006, we had no capital loss carry forwards.

The differences between the statutory income tax rates and our effective income tax rates are as follows:

	Years ended December 31,		
	2006	2005	2004
Tax at statutory rate	**35.0 %**	35.0 %	35.0 %
Increase (decrease) resulting from:			
Tax-exempt municipal bonds	**(2.2)**	(3.2)	(2.5)
Dividend exclusion	**(3.9)**	(5.7)	(5.7)
Other	**1.1**	0.7	0.2
Effective rate	**30.0 %**	26.8 %	27.0 %

Filed tax returns for calendar years 2000 through 2005 are currently open with the Internal Revenue Service. As of December 31, 2005, federal income taxes had not been provided for on our life insurance subsidiary's Policyholder Surplus Account (PSA), which totaled $14 million as of December 31, 2005 and 2004.
The American Jobs Creation Act of 2004 suspended for a two-year period beginning January 1, 2005, the tax liability of a stock life insurance company on distributions made from the PSA. In July 2006, the company's life insurance subsidiary declared and paid a $14 million dividend, eliminating its PSA balance as of December 31, 2006.

11. NET INCOME PER COMMON SHARE

Basic earnings per share are computed based on the weighted average number of shares outstanding. Diluted earnings per share are computed based on the weighted average number of common and dilutive potential common shares outstanding. We have adjusted shares and earnings per share to reflect all stock splits and dividends prior to December 31, 2006.

Here are calculations for basic and diluted earnings per share:

(In millions)	Years ended December 31, 2006	2005	2004
Numerator:			
Net income—basic and diluted	**$ 930**	$ 602	$ 584
Denominator:			
Weighted-average common shares outstanding	**173,423,395**	175,062,669	176,476,722
Effect of stock options	**2,027,946**	2,053,457	1,900,126
Adjusted weighted-average shares	**175,451,341**	177,116,126	178,376,848
Earnings per share:			
Basic	**$ 5.36**	$ 3.44	$ 3.30
Diluted	**5.30**	3.40	3.28
Number of anti-dilutive option shares	**1,336,150**	0	264,602
Exercise price of anti-dilutive option shares	**$ 45.26**	—	$ 41.14

The only current source of dilution of our common shares is outstanding stock options to purchase shares of common stock. The above table shows the number of anti-dilutive options shares at year-end 2006, 2005 and 2004. We did not include these options in the computation of net income per common share (diluted) because their exercise would have an anti-dilutive effect.

12. Pension Plan

We sponsor a defined contribution plan (401(k) savings plan) and a defined benefit pension plan covering substantially all employees. We do not contribute to the 401(k) plan but we do pay all operating expenses. Benefits for the defined benefit pension plan are based on years of credited service and compensation level. Contributions are based on the frozen entry age actuarial cost method. We also maintain a supplemental retirement plan (SERP) with liabilities of approximately $5 million to $9 million at year-end 2006 and 2005. The SERP is included in the obligation and expense amounts. Our pension expense is composed of several components that are determined using the projected unit credit actuarial cost method and are based on certain actuarial assumptions.

Key assumptions used in developing the 2006 net pension obligation were a 5.75 percent discount rate and rates of compensation increases ranging from 4 percent to 6 percent. To determine the discount rate, the plan's particular liability characteristics – the amounts, timing and interest sensitivity of expected benefit payments – were evaluated and then matched to a yield curve based on actual high-quality corporate bonds across a full maturity spectrum. Once the plan's projected cash flows matched the yield curve, a present value was developed, which was then calibrated to a single-equivalent discount rate. That discount rate, when applied to a single sum, would generate the necessary cash flows to pay benefits when due. It was increased by 0.25 percentage points in 2006 due to market interest rates conditions. We based the rates of compensation increase on the company's historical data, which led us to lower the range from the 5 percent to 7 percent used in previous years.

Key assumptions used in developing the 2006 net pension expense were a 5.50 percent discount rate, an 8 percent expected return on plan assets and rates of compensation increases ranging from 5 percent to 7 percent. The 8 percent return on plan assets assumption is based partially on the fact that substantially all of the investments held by the pension plan are common stocks that pay annual dividends. We believe this rate is representative of the expected long-term rate of return on these assets. These assumptions were consistent with the prior year, except that the discount rate was reduced by 0.25 percentage points due to market interest rate conditions.

Benefit obligation activity using an actuarial measurement date at December 31 follows:

(In millions)	Qualified Pension Plan		Supplemental Pension Plan		Totals	
	2006	2005	**2006**	2005	**2006**	2005
Change in projected benefit obligation:						
Benefit obligation at beginning of year	**$ 235**	$ 199	**$ 9**	$ 5	**$ 244**	$ 204
Service cost	**16**	13	**0**	0	**16**	13
Interest cost	**14**	12	**0**	1	**14**	13
Plan amendments	**0**	0	**0**	3	**0**	3
Actuarial loss	**11**	18	**0**	0	**11**	18
Benefits paid	**(10)**	(7)	**(4)**	0	**(14)**	(7)
Projected benefit obligation at end of year	**$ 266**	$ 235	**$ 5**	$ 9	**$ 271**	$ 244
Accumulated benefit obligation	**$ 200**	$ 165	**$ 4**	$ 6	**$ 204**	$ 171
Change in plan assets:						
Fair value of plan assets at beginning of year	**$ 173**	158	**0**	0	**$ 173**	$ 158
Actual return on plan assets	**35**	12	**0**	0	**35**	12
Employer contributions	**10**	10	**4**	0	**14**	10
Benefits paid	**(10)**	(7)	**(4)**	0	**(14)**	(7)
Fair value of plan assets at end of year	**$ 208**	$ 173	**$ 0**	$ 0	**$ 208**	$ 173
Funded (unfunded) status:						
Funded (unfunded) status at end of year	**$ (58)**	$ (62)	**$ (5)**	$ (9)	**$ (63)**	$ (71)

The accumulated benefit obligation was $204 million and $171 million at December 31, 2006 and 2005, respectively. The fair value of our stock comprised $29 million (14 percent of total plan assets) at December 31, 2006, and $29 million (17 percent of total plan assets) at December 31, 2005.

At December 31, 2005 there were no amounts recognized in accumulated other comprehensive income for the plans. A reconciliation follows of the funded status at the end of the measurement period to the amounts recognized in the statement of financial position at December 31, 2006:

(In millions)	Qualified Pension Plan	Supplemental Pension Plan	Total
Amounts recognized in the statement of financial position consist of:			
Noncurrent liability	$ (58)	$ (5)	$ (63)
Total	$ (58)	$ (5)	$ (63)
Amounts recognized in accumulated other comprehensive income not yet recognized as a component of net periodic benefit cost consist of:			
Net actuarial loss/(gain)	$ 40	$ (1)	$ 39
Prior service cost	6	4	10
Total	$ 46	$ 3	$ 49

The projected benefit obligation and fair value of plan assets for pension plans with a projected benefit obligation in excess of plan assets at December 31 follows:

(In millions)	Qualified Pension Plan		Supplemental Pension Plan		Total	
	2006	2005	**2006**	2005	**2006**	2005
Projected benefit obligation in excess of plan assets:						
Projected benefit obligation at end of year	**$ 266**	$ 235	**$ 5**	$ 9	**$ 271**	$ 244
Fair value of plan assets at end of year	**208**	173	**0**	0	**208**	173

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for pension plans with an accumulated benefit obligation in excess of plan assets at December 31 follows:

(In millions)	Supplemental Pension Plan	
	2006	2005
Accumulated benefit obligation in excess of plan assets:		
Projected benefit obligation at end of year	**$ 5**	$ 9
Accumulated benefit obligation at end of year	**4**	6
Fair value of plan assets at end of year	**0**	0

The weighted-average assumptions used to determine benefit obligations at December 31 follows:

	2006	2005
Discount rate	**5.75 %**	5.50 %
Rate of compensation increase	**4-6**	5-7

We evaluate our pension plan assumptions annually and update them as necessary. The discount rate assumptions for our benefit obligation track with Moody's Aa bond yield, and yearly adjustments reflect any

changes to those bond yields. Compensation increase assumptions reflect historical calendar year compensation increases.

Here are the components of our net periodic benefit cost at December 31:

(In millions)	Qualified Pension Plan			Supplemental Pension Plan			Total		
	2006	2005	2004	**2006**	2005	2004	**2006**	2005	2004
Service cost	**$ 16**	$ 13	$ 11	**$ 0**	$ 0	$ 0	**$ 16**	$ 13	$ 11
Interest cost	**14**	12	10	**0**	1	0	**14**	13	10
Expected return on plan assets	**(14)**	(13)	(12)	**0**	0	0	**(14)**	(13)	(12)
Amortization of actuarial gain, prior service cost and transition asset	**2**	1	0	**1**	0	0	**3**	1	0
Net periodic benefit cost	**$ 18**	$ 13	$ 9	**$ 1**	$ 1	$ 0	**$ 19**	$ 14	$ 9

Here is a summary of the weighted-average assumptions we use to determine our net expense for the plan:

	Qualified Pension Plan			Supplemental Pension Plan		
	2006	2005	2004	**2006**	2005	2004
Discount rate	**5.50 %**	5.75 %	6.00 %	**5.50 %**	5.75 %	6.00 %
Expected return on plan assets	**8.00**	8.00	8.00	**NA**	NA	NA
Rate of compensation increase	**5-7**	5-7	5-7	**5-7**	5-7	5-7

Our pension plan asset allocations by category are:

	At December 31,	
	2006	2005
Asset category:		
Equity securities	**94 %**	93 %
Fixed maturities	**4**	5
Cash and cash equivalents	**2**	2
Total	**100 %**	100 %

We expect to contribute approximately $10 million to our pension plan in 2007 with a target allocation of 90 percent equity securities and 10 percent fixed maturities and cash.

We expect to make the following benefit payments, which reflect expected future service:

(In millions) For the years ended December 31,	Qualified Pension Plan	Supplemental Pension Plan	Total
2007	$ 9	$ 0	$ 9
2008	12	2	14
2009	13	0	13
2010	10	2	12
2011	15	0	15
Years 2012-2016	108	1	109

The estimated costs that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next year are as follows:

(In millions)	Qualified Pension Plan	Supplemental Pension Plan	Total
Actuarial (gain)/loss	$ 2	$ (1)	$ 1
Prior service cost	0	1	1
Total	$ 2	$ 0	$ 2

The incremental effect of applying SFAS No. 158 on individual line items in the statement of financial position at December 31, 2006, follows:

(In millions)	Qualified Pension Plan			Supplemental Pension Plan			Total		
	Without FAS 158	With FAS 158	Increase/ (Decrease)	Without FAS 158	With FAS 158	Increase/ (Decrease)	Without FAS 158	With FAS 158	Increase/ (Decrease)
Other liabilities	$ 12	$ 58	$ 46	$ 2	$ 5	$ 3	$ 14	$ 63	$ 49
Deferred income tax	(4)	(20)	(16)	(1)	(2)	(1)	(5)	(22)	(17)
Accumulated other comprehensive income	0	(30)	(30)	0	(2)	(2)	0	(32)	(32)

13. STATUTORY ACCOUNTING INFORMATION

Insurance companies use statutory accounting practices (SAP) as prescribed by regulatory authorities. The three primary differences between SAP and GAAP are:

- policy acquisition costs are expensed when incurred,
- life insurance reserves are based upon different actuarial assumptions and
- deferred income taxes are valued and established using a different basis.

Statutory net income and capital and surplus determined in accordance with SAP prescribed or permitted by insurance regulatory authorities for four legal entities, our insurance subsidiary and its three insurance subsidiaries, are as follows:

(In millions)	SAP Net Income Years ended December 31,			Capital and Surplus At December 31,	
	2006	2005	2004	**2006**	2005
The Cincinnati Insurance Company	**$ 572**	$ 517	$ 588	**$ 4,723**	$ 4,220
The Cincinnati Casualty Company	**15**	13	9	**282**	263
The Cincinnati Indemnity Company	**2**	2	2	**62**	63
The Cincinnati Life Insurance Company	**28**	21	28	**479**	451

Statutory capital and surplus for our insurance subsidiary, The Cincinnati Insurance Company, includes capital and surplus of its three insurance subsidiaries.

14. TRANSACTIONS WITH AFFILIATED PARTIES

We paid certain officers and directors, or insurance agencies of which they are shareholders, commissions of approximately $7 million, $6 million and $11 million on premium volume of approximately $40 million, $41 million and $76 million for 2006, 2005 and 2004, respectively.

15. COMMITMENTS AND CONTINGENT LIABILITIES

Legal issues are part of the normal course of business for all companies. As such, we have various litigation and claims against us in process and pending. Having analyzed those claims with our legal counsel, we believe the outcomes of normal insurance matters will not have a material effect on our consolidated financial position, results of operations or cash flows. We further believe that the outcomes of non-insurance matters will be covered by insurance coverage or will not have a material effect on our consolidated financial position, results of operations or cash flows.

In June 2004 we discovered some uncertainty regarding the status of the Cincinnati Financial Corporation holding (parent) company under the Investment Company Act of 1940. Several tests and enumerated exemptions determine whether a company meets the definition of an investment company under the Investment Company Act. In particular, one test states that a company may be an investment company if it owns investment securities with a value greater than 40 percent of its total assets (excluding assets of its subsidiaries), a level which the holding company exceeded between 1991 and August 2004.

On June 28, 2004, Cincinnati Financial Corporation filed an application with the SEC formally requesting an exemption for the holding company under Section 3(b)(2) of the Investment Company Act. Section 3(b)(2) specifically permits the SEC to exempt entities primarily engaged in business other than that of investing, reinvesting, owning, holding or trading in securities. Cincinnati Financial Corporation alternatively asked the SEC for relief pursuant to Section 6(c) of the Investment Company Act, which would exempt it from all the provisions of the Act because doing so is necessary or appropriate in the public interest, consistent with the protection of investors and consistent with the purposes intended by the Investment Company Act.

Following its SEC filing, the holding company transferred investment securities to our subsidiary, The Cincinnati Insurance Company, in August 2004, lowering the holding company's ratio of investment securities to holding-company-only assets below 40 percent. We have maintained that ratio below the 40 percent level since the time of the transfer.

Because the ratio is below 40 percent, we believe the SEC staff is not actively considering the application.

We strongly believe the holding company is, and has been, outside the intended scope of the Investment Company Act because the company is, and has been, primarily engaged in the business of property casualty and life insurance through its subsidiaries. As a registered investment company, the holding company would not be permitted to operate its business as it currently operates, nor would a registered investment company be permitted to have many of the relationships that the holding company has with its affiliated companies.

To increase certainty that regulation under the Investment Company Act would not apply to the company in the future, our operations are limited by the constraint that investment securities held at the holding company level should remain below the 40 percent threshold described above. Efforts to stay below the threshold could result in:

- A need to dispose of otherwise desirable investment securities, possibly under undesirable conditions. Such dispositions could result in a lower return on investment because of market value fluctuations. Dispositions also could result in loss of investment income that we may be unable to replace in a timely fashion. If we were unable to manage the timing of the dispositions, we also might realize unnecessary capital gains, which would increase our annual tax payment.
- Limited opportunities to purchase equity securities that hold the potential for market value appreciation. Historically, the holding company has successfully invested in equity securities that provided both income

and capital appreciation, contributing to long-term growth in book value. Constraining our ability to pursue this strategy and invest in equity securities could hamper book value growth over the long term.

- Maintenance of a greater portion of our portfolio of equity securities at our insurance subsidiary. As a result of the transfer of assets to ensure compliance with the 40 percent threshold, the holding company now is more reliant on that subsidiary for cash to fund parent-company obligations, including shareholder dividends and interest on long-term debt.

Although we intend to manage assets to stay below the 40 percent threshold, events beyond our control, including significant appreciation in the value of certain investment securities, could result in the holding company exceeding the 40 percent threshold. While we believe that even in such circumstances the company would not be an investment company because it is primarily engaged in the business of insurance through its subsidiaries, the SEC, among others, could disagree with this position.

If it were determined that the holding company is an unregistered investment company, the holding company might be unable to enforce contracts with third parties, and third parties could seek rescission of transactions with the holding company undertaken during the period that it was an unregistered investment company, subject to equitable considerations set forth in the Investment Company Act. In addition, the holding company could become subject to monetary penalties or injunctive relief, or both, in an action brought by the SEC.

16. EQUITY COMPENSATION PLANS

As a result of adopting SFAS No. 123(R) on January 1, 2006, our income before income taxes for the year ended December 31, 2006, was reduced by $17 million. Our net income for the year ended December 31, 2006, was reduced by $14 million. If we had continued to account for stock-based compensation under APB Opinion No. 25, there would have been no effect on net income. The weighted-average grant-date fair value of options granted during 2006 and 2005 was $10.09 and $12.49, respectively. The total intrinsic value of options exercised during the years ended December 31, 2006, 2005 and 2004, was $22 million, $9 million and $6 million, respectively. The total intrinsic value of options vested during the years ended December 31, 2006, 2005 and 2004, was $10 million, $12 million and $11 million. (Intrinsic value is the market price less the exercise price.)

Under the modified-prospective-transition method, in 2006, we recognized:

- compensation cost for all stock options granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123(R)
- compensation cost for all non-vested stock options granted prior to January 1, 2006, that vested during 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123 and
- compensation cost for all non-vested stock options that have nonsubstantive vesting requirements, such as those to associates who are eligible for retirement.

Results for prior periods have not been retrospectively adjusted for SFAS No. 123(R). As of December 31, 2006, we had $14 million of unrecognized total compensation cost related to non-vested stock options. That cost will be recognized over a weighted-average period of 1.7 years. SFAS No. 123(R) also requires us to classify certain tax benefits related to share-based compensation deductions as cash from financing activities. As of December 31, 2006, these tax benefits totaled $2 million.

In determining the share-based compensation amounts for 2006, the fair value of each option granted in 2006 was estimated on the date of grant using the binomial option-pricing model with the following weighted average assumptions used for grants in 2006: dividend yield of 3.22 percent; expected volatility ranging from 20.25 to 27.12 percent; risk-free interest rates ranging from 4.5 to 4.61 percent; and expected lives of five to seven years.

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS No. 123 to options granted under our stock option plans prior to our adoption of SFAS No. 123(R) on January 1, 2006. For purposes of this pro forma disclosure, the fair value of each option was estimated on the date of grant using the binomial option-pricing model with the following weighted-average assumptions used for grants in:

- 2005 – Dividend yield of 2.66 percent; expected volatility of 25.61 percent; risk-free interest rate of 4.62 percent; and expected lives of 10 years.
- 2004 – Dividend yield of 2.40 percent; expected volatility of 25.65 percent; risk-free interest rate of 4.37 percent; and expected lives of 10 years.

(In millions except per share data)		Years ended December 31, 2005	2004
Net income	As reported	$ 602	$ 584
Stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects		13	12
	Pro forma	$ 589	$ 572
Net income per common share—basic	As reported	$ 3.44	$ 3.30
	Pro forma	3.36	3.24
Net income per common share—diluted	As reported	$ 3.40	$ 3.28
	Pro forma	3.32	3.21

Here is a summary of options information:

(Dollars in millions, shares in thousands)	Shares	Weighted-average exercise	Aggregate intrinsic value
2006			
Outstanding at beginning of year	**10,589**	**$ 33.70**	
Granted/reinstated	**1,372**	**45.26**	
Exercised	**(1,084)**	**24.93**	
Forfeited/revoked	**(210)**	**36.16**	
Outstanding at end of period	**10,667**	**36.03**	**$ 99**
Options exercisable at end of period	**7,985**	$ **33.70**	**$ 93**
Weighted-average fair value of options granted during the period		**10.09**	
2005			
Outstanding at beginning of year	9,698	$ 32.05	
Granted/reinstated	1,504	41.62	
Exercised	(467)	24.18	
Forfeited/revoked	(146)	35.89	
Outstanding at end of period	10,589	33.70	$ 116
Options exercisable at end of period	7,794	$ 31.69	$ 101
Weighted-average fair value of options granted during the period		12.49	
2004			
Outstanding at beginning of year	8,791	$ 30.63	
Granted/reinstated	1,439	38.81	
Exercised	(397)	24.02	
Forfeited/revoked	(135)	34.29	
Outstanding at end of period	9,698	32.05	$ 98
Options exercisable at end of period	7,050	$ 30.50	$ 82
Weighted-average fair value of options granted during the period		11.18	

Cash received from the exercise of options was $27 million, $11 million and $10 million for the years ended December 31, 2006, 2005 and 2004, respectively. The tax benefit realized on options exercised was $3 million for the year ended December 31, 2006, and less than $1 million for the years ended December 31, 2005 and 2004.

Options outstanding and exercisable consisted of the following at December 31, 2006:

(Shares in thousands)	Options outstanding			Options exercisable	
Range of exercise prices	Shares	Weighted-average remaining contractual life	Weighted-average exercise price	Shares	Weighted-average exercise price
$15.00 to $19.99	2	0.11 yrs	$ 19.34	2	$ 19.34
$20.00 to $24.99	161	0.28 yrs	20.60	161	20.60
$25.00 to $29.99	944	3.01 yrs	27.07	944	27.07
$30.00 to $34.99	4,571	4.19 yrs	32.66	4,571	32.66
$35.00 to $39.99	1,968	5.31 yrs	38.44	1,535	38.34
$40.00 to $44.99	1,685	6.94 yrs	41.54	757	41.45
$45.00 to $49.99	1,336	9.08 yrs	45.26	15	45.26
Total	10,667	5.28 yrs	36.03	7,985	33.70

The weighted-average remaining contractual life for exercisable awards as of December 31, 2006, was 4.24 years. As of December 31, 2006, 11.6 million shares of common stock were available for future stock option grants. We currently issue new shares for option exercises.

17. SEGMENT INFORMATION

We operate primarily in two industries, property casualty insurance and life insurance. We regularly review four different reporting segments to make decisions about allocating resources and assessing performance:

- Commercial lines property casualty insurance
- Personal lines property casualty insurance
- Life insurance
- Investment operations

We report as "Other" the non-investment operations of the parent company, CFC Investment Company and CinFin Capital Management Company (excluding client investment activities), as well as other income of our insurance subsidiary.

Revenues come primarily from unaffiliated customers:

- All three insurance segments record revenues from insurance premiums earned. Life insurance segment revenues also include separate account investment management fees.
- Our investment operations' revenues are pretax net investment income plus realized investment gains and losses.
- Other revenues are primarily finance/lease income.

Income or loss before income taxes for each segment is reported based on the nature of that business area's operations:

- Income before income taxes for the insurance segments is defined as underwriting income or loss.
  - For commercial lines and personal lines insurance segments, we calculate underwriting income or loss by recording premiums earned minus loss and loss expenses and underwriting expenses incurred.
  - For the life insurance segment, we calculate underwriting income or loss by recording premiums earned and separate account investment management fees, minus contract holder benefits and expenses incurred, plus investment interest credited to contract holders.
- Income before income taxes for the investment operations segment is net investment income plus realized investment gains and losses for all fixed-maturity and equity security investments of the entire company, minus investment interest credited to contract holders of the life insurance segment.
- Loss before income taxes for the Other category is primarily due to interest expense from debt of the parent company and operating expenses of our headquarters.

Identifiable assets are used by each segment in its operations. We do not separately report the identifiable assets for the commercial or personal lines segments because we do not use that measure to analyze the segments. We include all fixed-maturity and equity security investment assets, regardless of ownership, in the investment operations segment.

This table summarizes segment information:

(In millions)	Years ended December 31, 2006	2005	2004
Revenues:			
Commercial lines insurance			
Commercial casualty	**$ 831**	$ 759	$ 686
Commercial property	**491**	467	440
Commercial auto	**453**	457	450
Workers' compensation	**366**	328	313
Specialty packages	**141**	137	133
Surety and executive risk	**93**	80	80
Machinery and equipment	**27**	26	24
Total commercial lines insurance	**2,402**	2,254	2,126
Personal lines insurance			
Personal auto	**385**	433	451
Homeowner	**289**	282	256
Other personal lines	**88**	89	86
Total personal lines insurance	**762**	804	793
Life insurance	**118**	110	104
Investment operations	**1,254**	587	583
Other	**15**	12	8
Consolidated eliminations	**(1)**	0	0
Total	**$ 4,550**	$ 3,767	$ 3,614
Income (loss) before income taxes:			
Insurance underwriting results:			
Commercial lines insurance	**$ 208**	$ 285	$ 338
Personal lines insurance	**(27)**	45	(40)
Life insurance	**(1)**	7	2
Investment operations	**1,200**	536	537
Other	**(51)**	(50)	(37)
Total	**$ 1,329**	$ 823	$ 800
Identifiable assets:			
Property casualty insurance	**$ 2,220**	$ 2,167	
Life insurance	**886**	845	
Investment operations	**13,820**	12,774	
Other	**296**	217	
Total	**$ 17,222**	$ 16,003	

QUARTERLY SUPPLEMENTARY DATA (UNAUDITED)

This table includes unaudited quarterly financial information for the years ended December 31, 2006 and 2005:

(Dollars in millions except per share data)	Quarter 1st	2nd	3rd	4th	Full year
2006					
Revenues	**$ 1,607**	**$ 981**	**$ 967**	**$ 995**	**$ 4,550**
Income before income taxes	**834**	**175**	**148**	**172**	**1,329**
Net income	**552**	**132**	**115**	**130**	**930**
Net income per common share—basic	**3.17**	**0.77**	**0.67**	**0.75**	**5.36**
Net income per common share—diluted	**3.13**	**0.76**	**0.66**	**0.75**	**5.30**
2005					
Revenues	$ 916	$ 940	$ 944	$ 967	$ 3,767
Income before income taxes	195	215	151	261	823
Net income	144	158	117	183	602
Net income per common share—basic	0.82	0.90	0.67	1.04	3.44
Net income per common share—diluted	0.81	0.89	0.66	1.03	3.40

Note: The sum of the quarterly reported amounts may not equal the full year as each is computed independently.

First-quarter and full-year 2006 – The company sold its holdings in Alltel Corporation common stock in the first quarter of 2006. The sale contributed $647 million to revenues and $412 million, or $2.35 per share, to net income.