

ALLEGHANY CORP /DE  
Form 10-Q  
May 06, 2008

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

(MARK ONE)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
FOR QUARTERLY PERIOD ENDED MARCH 31, 2008**

**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 1-9371**

**ALLEGHANY CORPORATION**

**EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER**

**DELAWARE**

**STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION**

**51-0283071**

**I.R.S. EMPLOYER IDENTIFICATION NO.**

**7 TIMES SQUARE TOWER, 17TH FLOOR, NY, NY 10036**

**ADDRESS OF PRINCIPAL EXECUTIVE OFFICES, INCLUDING ZIP CODE**

**212-752-1356**

**REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE**

**NOT APPLICABLE**

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  NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A LARGE ACCELERATED FILER, AN ACCELERATED FILER, A NON-ACCELERATED FILER, OR A SMALLER REPORTING COMPANY. SEE THE DEFINITIONS OF LARGE ACCELERATED FILER, ACCELERATED FILER AND SMALLER REPORTING COMPANY IN RULE 12B-2 OF THE EXCHANGE ACT. (CHECK ONE):

LARGE ACCELERATED  
FILER

ACCELERATED  
FILER

NON-ACCELERATED  
FILER

SMALLER REPORTING  
COMPANY

(DO NOT CHECK IF A SMALLER REPORTING COMPANY)

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A SHELL COMPANY (AS DEFINED IN RULE 12B-2 OF THE EXCHANGE ACT).

YES  NO

INDICATE THE NUMBER OF SHARES OUTSTANDING OF EACH OF THE ISSUER'S CLASSES OF COMMON STOCK, AS OF THE LAST PRACTICABLE DATE.

8,342,448 SHARES AS OF April 30, 2008



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**CONSOLIDATED STATEMENTS OF EARNINGS**  
**AND COMPREHENSIVE INCOME**  
**FOR THE THREE MONTHS ENDED**  
**MARCH 31, 2008 AND 2007**

(dollars in thousands, except share and per share amounts)  
(unaudited)

	<b>2008</b>	<b>2007</b>
<b>Revenues</b>		
Net premiums earned	\$ 297,466	\$ 271,571
Net investment income	41,341	45,169
Realized capital gains	74,712	50,141
Other income	136	8,725
Total revenues	413,655	375,606
<b>Costs and expenses</b>		
Loss and loss adjustment expenses	155,195	122,604
Commissions, brokerage and other underwriting expenses	84,056	71,278
Other operating expenses	15,212	13,166
Corporate administration	9,948	8,004
Interest expense	226	723
Total costs and expenses	264,637	215,775
Earnings before income taxes and minority interest	149,018	159,831
Income taxes	43,615	51,056
Earnings before minority interest	105,403	108,775
Minority interest, net of tax	6,682	2,357
Net earnings	\$ 98,721	\$ 106,418
<b>Changes in other comprehensive income</b>		
Change in unrealized gains, net of deferred taxes	\$ 1,061	\$ 27,273
Less: reclassification for gains realized in net earnings, net of taxes	(48,563)	(32,592)
Other	(5)	13

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Comprehensive income	\$ 51,214	\$ 101,112
Net earnings	\$ 98,721	\$ 106,418
Preferred dividends	4,305	4,306
Net earnings available to common stockholders	\$ 94,416	\$ 102,112
Basic earnings per share of common stock *	\$ 11.33	\$ 12.32
Diluted earnings per share of common stock *	\$ 10.57	\$ 11.42
Dividends per share of common stock	*	*
Average number of outstanding shares of common stock **	8,329,657	8,288,807

\* Adjusted to reflect the common stock dividend declared in February 2008.

\*\* In February 2008 and 2007, Alleghany declared a stock dividend consisting of one share of Alleghany common stock for every fifty shares outstanding.

See accompanying Notes to Unaudited Consolidated Financial Statements.

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**ALLEGHANY CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(dollars in thousands, except share amounts)

	<b>March 31, 2008 (unaudited)</b>	<b>December 31, 2007</b>
<b>Assets</b>		
Investments		
Available for sale securities at fair value:		
Equity securities (cost: 2008 \$678,773; 2007 \$695,429)	\$1,065,598	\$1,180,092
Debt securities (cost: 2008 \$3,043,531; 2007 \$2,981,236)	3,081,689	3,010,378
Short-term investments	549,244	424,494
	4,696,531	4,614,964
Other invested assets	195,040	193,272
Total investments	4,891,571	4,808,236
Cash	52,253	65,115
Premium balances receivable	198,598	201,066
Reinsurance recoverables	993,767	967,533
Ceded unearned premium reserves	233,514	242,891
Deferred acquisition costs	89,305	89,437
Property and equipment at cost, net of accumulated depreciation and amortization	20,905	21,518
Goodwill and other intangibles, net of amortization	217,945	214,995
Current taxes receivable		2,646
Other assets	129,797	119,609
	\$6,827,655	\$6,733,046
<b>Liabilities and Stockholders Equity</b>		
Losses and loss adjustment expenses	\$2,680,776	\$2,580,056
Unearned premiums	789,269	818,979
Reinsurance payable	86,033	78,379
Net deferred tax liabilities	27,467	57,733
Subsidiaries debt	5,000	5,000
Current taxes payable	43,045	
Minority interest	105,971	99,135
Other liabilities	251,739	299,889
Total liabilities	3,989,300	3,939,171

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Preferred stock (shares authorized: 2008 and 2007 outstanding 2008 1,131,819; 2007 1,131,819)	1,132,000; issued and	299,480	299,480
Common stock (shares authorized: 2008 and 2007 outstanding 2008 8,339,579; 2007 8,322,348)	22,000,000; issued and	8,176	8,159
Contributed capital		688,610	689,435
Accumulated other comprehensive income		281,125	328,632
Treasury stock, at cost (2008 5,334 shares; 2007 none)		(1,811)	
Retained earnings		1,562,775	1,468,169
Total stockholders' equity		2,838,355	2,793,875
		\$6,827,655	\$6,733,046
<b>Shares of Common Stock Outstanding *</b>		8,334,245	8,322,348

\* Adjusted to reflect the common stock dividend declared in February 2008.

See accompanying Notes to Unaudited Consolidated Financial Statements.

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**ALLEGHANY CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE THREE MONTHS ENDED**

**MARCH 31, 2008 AND 2007**

(dollars in thousands)

(unaudited)

	<b>2008</b>	<b>2007</b>
<b>Cash flows from operating activities</b>		
Net earnings	\$ 98,721	\$ 106,418
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	5,085	2,269
Net realized capital (gains) losses	(74,712)	(50,141)
(Increase) decrease in other assets	4,747	495
(Increase) decrease in reinsurance receivable, net of reinsurance payable	(18,580)	44,558
(Increase) decrease in premium balances receivable	2,468	12,656
(Increase) decrease in ceded unearned premium reserves	9,377	18,856
(Increase) decrease in deferred acquisition costs	132	(1,684)
Increase (decrease) in other liabilities and current taxes	(12,348)	28,395
Increase (decrease) in unearned premiums	(29,710)	(34,560)
Increase (decrease) in losses and loss adjustment expenses	100,720	3,438
Net adjustments	(12,821)	24,282
Net cash provided by operating activities	85,900	130,700
<b>Cash flows from investing activities</b>		
Purchase of investments	(354,989)	(319,724)
Sales of investments	272,111	76,091
Maturities of investments	117,693	55,664
Purchases of property and equipment	(455)	(1,005)
Net change in short-term investments	(125,439)	15,594
Acquisition of insurance companies, net of cash acquired	(2,639)	
Other, net	1,072	(2,905)
Net cash (used in) provided by investing activities	(92,646)	(176,285)
<b>Cash flows from financing activities</b>		
Treasury stock acquisitions	(1,811)	
Principal payments on long-term debt		(80,000)
Decrease in notes receivable		91,535
Convertible preferred stock dividends paid	(4,305)	(4,306)
Tax benefit on stock options exercised		1,062
Other, net		2,222
Net cash provided by (used in) financing activities	(6,116)	10,513

Net (decrease) increase in cash	(12,862)	(35,072)
Cash at beginning of period	65,115	68,332
Cash at end of period	\$ 52,253	\$ 33,260

**Supplemental disclosures of cash flow information**

Cash paid during the period for:

Interest	\$ 33	\$ 506
Income taxes paid (refunds received)	\$ 2,325	\$ 1,390

See accompanying Notes to Unaudited Consolidated Financial Statements.

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**Notes to Unaudited Consolidated Financial Statements**

**Alleghany Corporation and Subsidiaries**

***1. Principles of Financial Statement Presentation***

This report should be read in conjunction with the Annual Report on Form 10-K for the year ended December 31, 2007 (the 2007 10-K ) of Alleghany Corporation ( Alleghany ).

Alleghany, a Delaware corporation, is engaged in the property and casualty and surety insurance business through its wholly-owned subsidiary Alleghany Insurance Holdings LLC ( AIHL ). AIHL s insurance business is conducted through its wholly-owned subsidiaries RSUI Group, Inc. ( RSUI ), Capitol Transamerica Corporation and Platte River Insurance Company (collectively CATA ) and AIHL s majority-owned subsidiaries Employers Direct Corporation ( EDC ), of which AIHL owns approximately 98 percent and Darwin Professional Underwriters, Inc. ( Darwin ), of which AIHL owns approximately 55 percent. AIHL Re LLC ( AIHL Re ), a captive reinsurance subsidiary of AIHL, is available to provide reinsurance to Alleghany operating units and affiliates. In addition, Alleghany owns approximately 32.9 percent of the outstanding shares of common stock of Homesite Group Incorporated ( Homesite ), a national, full-service, mono-line provider of homeowners insurance, and this investment is reflected in Alleghany s financial statements in other invested assets. Alleghany also owns and manages properties in the Sacramento, California region through its subsidiary Alleghany Properties Holdings LLC ( Alleghany Properties ) and conducts corporate investment and other activities at the parent level, including the holding of strategic equity investments. These strategic equity investments are available to support the internal growth of subsidiaries and for acquisitions of, and substantial investments in, operating companies.

The financial statements contained in this Report on Form 10-Q are unaudited, but reflect all adjustments which, in the opinion of management, are necessary to a fair statement of results of the interim periods covered thereby. All adjustments are of a normal and recurring nature except as described herein.

The accompanying consolidated financial statements include the results of Alleghany and its wholly-owned and majority-owned subsidiaries, and have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ). All significant inter-company balances and transactions have been eliminated in consolidation.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those reported results to the extent that those estimates and assumptions prove to be inaccurate.

Certain prior year amounts have been reclassified to conform to the 2008 presentation. In the 2007 second quarter, Alleghany determined that it had incorrectly classified operating payments made from its investing accounts as an investing cash flow activity in its consolidated statements of cash flows. These operating payment amounts should have been classified as outflows from operating activities. As a result, for the three-month period ended March 31, 2007, cash outflows in the amount of \$11.6 million were reclassified from cash flows used in investing

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activities to cash flows used in operating activities. This correction is not material to Alleghany's consolidated financial statements.

***2. Recent Accounting Pronouncements***

In September 2006, FASB Statement No. 157, *Fair Value Measurements* (SFAS 157), was issued. SFAS 157 provides guidance for using fair value to measure assets and liabilities. SFAS 157 does not expand the use of fair value in any new circumstances. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Alleghany has adopted the provisions of SFAS 157 as of January 1, 2008, and the implementation did not have a material impact on its results of operations and financial condition. See Note 7.

At its September 2006 meeting, the Emerging Issues Task Force reached a consensus with respect to Issue No. 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. This Issue addresses split-dollar life insurance, which is defined as an arrangement in which the employer and an employee share the cash surrender value and/or death benefits of the insurance policy. Additional information regarding this Issue can be found in Note 1.p. to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K. Alleghany has adopted the provisions of this Issue as of January 1, 2008, and the implementation did not have a material impact on its results of operations and financial condition.

In February 2007, FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*, was issued. This Statement permits entities to choose to measure many financial instruments and certain other items at fair value, at specified election dates, with unrealized gains and losses reported in earnings at each subsequent reporting date. This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS 157. Alleghany has adopted the provisions of this Statement as of January 1, 2008, and the implementation did not have any impact on its results of operations and financial condition.

In December 2007, FASB Statements No. 141 (revised 2007), *Business Combinations* (SFAS 141R), and No. 160, *Noncontrolling Interests in Consolidated Financial Statements* (SFAS 160), were issued. SFAS 141R replaces FASB Statement No. 141, *Business Combinations*. SFAS 141R requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose additional information regarding the nature and financial effect of the business combination. SFAS 160 requires all entities to report noncontrolling (minority) interests in subsidiaries in the same way as equity in the consolidated financial statements. SFAS 160 also requires disclosure, on the face of the consolidated statement of income, of the amounts of consolidated net income attributable to the parent and to the noncontrolling interest. Alleghany will adopt SFAS 141R and SFAS 160 for all business combinations initiated after December 31, 2008. Alleghany will also reclassify its minority interest liabilities as a separate component of shareholders' equity after December 31, 2008.

**Table of Contents****3. Earnings Per Share of Common Stock**

The following is a reconciliation of the income and share data used in the basic and diluted earnings per share computations for the three months ended March 31, 2008 and 2007 (in thousands, except share amounts):

	2008	2007
Net earnings	\$ 98,721	\$ 106,418
Preferred dividends	4,305	4,306
Income available to common stockholders for basic earnings per share	94,416	102,112
Preferred dividends	4,305	4,306
Effect of other dilutive securities	73	68
Income available to common stockholders for diluted earnings per share	\$ 98,794	\$ 106,486
Weighted average shares outstanding applicable to basic earnings per share	8,329,657	8,288,807
Preferred stock	997,969	998,023
Effect of other dilutive securities	20,993	40,459
Adjusted weighted average shares outstanding applicable to diluted earnings per share	9,348,619	9,327,289

Contingently issuable shares of 47,294 and 59,486 were potentially available during the 2008 and 2007 first quarters, respectively, but were not included in the computations of diluted earnings per share because the impact was anti-dilutive to the earnings per share calculation.

Earnings per share by quarter may not equal the amount for the full year due to rounding.

**4. Commitments and Contingencies****(a) Leases**

Alleghany leases certain facilities, furniture and equipment under long-term lease agreements.

**(b) Litigation**

Alleghany's subsidiaries are parties to pending litigation and claims in connection with the ordinary course of their businesses. Each such subsidiary makes provisions for estimated losses to be incurred in such litigation and claims, including legal costs. In the opinion of management such provisions are adequate.

**(c) Asbestos and Environmental Exposure**

AIHL's reserve for unpaid losses and loss adjustment expenses includes \$22.7 million of gross reserves and \$22.6 million of net reserves at March 31, 2008 and \$22.9 million of gross reserves and \$22.7 million of net reserves at December 31, 2007, for various liability coverages related to asbestos and environmental impairment claims that arose from reinsurance assumed by a subsidiary of CATA between 1969 and 1976. This subsidiary exited this business in 1976. Although Alleghany is unable at this time to determine whether additional reserves, which could have a material impact upon its results of operations, may be necessary in the future, Alleghany believes that CATA's asbestos and environmental reserves are adequate at March 31, 2008. Additional information concerning CATA's asbestos and environmental exposure can be found in Note 13 to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K.

**Table of Contents****(d) Indemnification Obligations**

On July 14, 2005, Alleghany completed the sale of its world-wide industrial minerals business, World Minerals, Inc. ( World Minerals ), to Imerys USA, Inc. (the Purchaser ), a wholly-owned subsidiary of Imerys, S.A., pursuant to a Stock Purchase Agreement, dated as of May 19, 2005, by and among the Purchaser, Imerys, S.A. and Alleghany (the Stock Purchase Agreement ). Pursuant to the Stock Purchase Agreement, Alleghany undertook certain indemnification obligations, including a general indemnification for breaches of representations and warranties set forth in the Stock Purchase Agreement (the Contract Indemnification ) and a special indemnification (the Products Liability Indemnification ) related to products liability claims arising from events that occurred during pre-closing periods, including the period of Alleghany ownership (the Alleghany Period ).

The representations and warranties to which the Contract Indemnification applies survive for a two-year period (until July 14, 2007 with the exception of certain representations and warranties such as those related to environmental, real estate and tax matters, which survive for periods longer than two years) and generally, except for tax and certain other matters, apply only to aggregate losses in excess of \$2.5 million, up to a maximum of approximately \$123.0 million. The Stock Purchase Agreement provides that Alleghany has no responsibility for products liability claims arising in respect of events occurring after the closing, and that any products liability claims involving both pre-closing and post-closing periods will be apportioned on an equitable basis. Additional information concerning the Contract Indemnification and Products Liability Indemnification can be found in Note 13 to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K.

Based on Alleghany s experience to date and other analyses, Alleghany established a \$600 thousand reserve in connection with the Products Liability Indemnification for the Alleghany Period. Such reserve was \$410 thousand at March 31, 2008.

**(e) Equity Holdings Concentration**

At March 31, 2008, Alleghany had a concentration of market risk in its available-for-sale equity securities portfolio of common stock of Burlington Northern Santa Fe Corporation ( Burlington Northern ), a railroad holding company, amounting to \$368.9 million. During the first three months of 2008, Alleghany sold approximately 1.0 million shares of Burlington Northern common stock, resulting in a pre-tax gain of \$78.1 million.

At March 31, 2008, Alleghany also had a concentration of market risk in its available-for-sale equity securities portfolio with respect to the common stock of certain energy sector businesses amounting to \$321.4 million.

***5. Segment of Business***

Information related to Alleghany s reportable segment is shown in the table below. Property and casualty insurance and surety operations are conducted by AIHL through its insurance operating units RSUI, CATA, EDC, and Darwin. In addition, AIHL Re is a wholly-owned subsidiary of AIHL that is available to provide reinsurance to Alleghany s insurance operating units and affiliates.

Alleghany s reportable segment is reported in a manner consistent with the way management evaluates the businesses. As such, insurance underwriting activities are evaluated separately from investment activities. Net realized capital gains are not considered relevant in evaluating investment performance on an annual basis. Segment accounting policies are the same as those

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described in Note 1 to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K. The primary components of corporate activities are Alleghany Properties, AIHL's investment in Homesite, corporate investment and other activities at the parent level, including strategic equity investments. Such strategic equity investments are available to support the internal growth of subsidiaries and for acquisitions of, and substantial investments in, operating companies.

(in millions)	For the three months ended March 31,	
	2008	2007
<b>Revenues:</b>		
AIHL insurance group:		
Net premiums earned		
RSUI	\$ 177.9	\$ 166.6
CATA	46.8	47.3
Darwin	52.0	40.0
EDC	20.6	
AIHL Re	0.2	17.7
	297.5	271.6
Net investment income	37.6	37.1
Net realized capital gains (losses)	(3.4)	(5.8)
Other income	0.1	0.1
Total insurance group	331.8	303.0
Corporate activities:		
Net investment income (1)	3.7	8.1
Net realized capital gains (2)	78.1	55.9
Other income		8.6
Total	\$ 413.6	\$ 375.6
<b>Earnings before income taxes and minority interest:</b>		
AIHL insurance group:		
Underwriting profit (loss) (3)		
RSUI	\$ 38.6	\$ 50.3
CATA	4.2	7.0
Darwin	18.4	2.8
EDC	(3.1)	
AIHL Re	0.2	17.6
	58.3	77.7
Net investment income	37.6	37.1
Net realized capital gains (losses)	(3.4)	(5.8)
Other income, less other expenses	(14.6)	(12.0)

Total insurance group	77.9	97.0
Corporate activities:		
Net investment income (1)	3.7	8.1
Net realized capital gains (2)	78.1	55.9
Other income		8.6
Corporate administration and other expenses	10.6	9.1
Interest expense	0.2	0.7
Total	\$149.0	\$159.8

(1) Includes (\$0.2) million and \$2.9 million for the three months ended March 31, 2008 and 2007, respectively, of Alleghany's equity in earnings of Homesite, net of purchase accounting adjustments (See Note 16 to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K).



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- (2) Principally reflects net realized capital gains from the sale of Burlington Northern common stock in the 2008 first quarter and 2007 first quarter.
  
- (3) Represents net premiums earned less loss and loss adjustment expenses and underwriting expenses, all as determined in accordance with GAAP, and does not include net investment income and other income or net realized capital gains. Underwriting expenses represent commission and brokerage expenses and that portion of salaries, administration and other operating expenses directly attributable to underwriting activities, whereas the remainder constitutes other

expenses.

#### **6. Reinsurance**

As discussed in the 2007 10-K, RSUI reinsures its property lines of business through a program consisting of surplus share treaties, facultative placements, per risk and catastrophe excess of loss treaties. RSUI's catastrophe reinsurance program (which covers catastrophe risks including, among others, windstorms and earthquakes) and per risk reinsurance program run on an annual basis from May 1 to the following April 30 and thus expired on April 30, 2008. RSUI has placed substantially all of its catastrophe reinsurance program for the 2008-2009 period. Under the new program, RSUI's catastrophe reinsurance program provides coverage in two layers for \$400.0 million of losses in excess of a \$100.0 million net retention after application of the surplus share treaties, facultative reinsurance and per risk covers. The first layer provides coverage for \$100.0 million of losses, before a 33.15 percent co-participation by RSUI, in excess of the \$100.0 million net retention, and the second layer provides coverage for \$300.0 million of losses, before a 5 percent co-participation by RSUI, in excess of \$200.0 million. The renewed program is substantially similar to the expired program. In addition, RSUI's property per risk reinsurance program for the 2008-2009 period provides RSUI with reinsurance for \$90.0 million of losses in excess of \$10.0 million net retention per risk after application of the surplus share treaties and facultative reinsurance, which is substantially similar to the expired program. As discussed in Note 5(d) to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K, RSUI reinsures its other lines of business through quota share treaties, except for professional liability lines where RSUI retains all of such business.

As discussed in Note 5(e) to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K, Darwin reinsures all of its lines of business through a program consisting of a variety of excess of loss treaties. In April 2008, Darwin substantially completed the renewal of its main reinsurance program. For Darwin's medical lines of business, the new program provides coverage for \$15.0 million of losses, before a 15 percent co-participation by Darwin, in excess of a \$1.0 million net retention. For Darwin's non-medical lines of business, the new program provides coverage in three layers, with the ultimate premium varying depending upon the profitability of the business reinsured. The first layer covers all non-medical lines of business (other than (i) publicly traded, financial institutions and healthcare directors and officers liability and (ii) managed care and financial institutions errors and omissions liability) for \$1.0 million of losses before a 25 percent co-participation by Darwin, in excess of a \$1.0 million net retention. The second and third layers provide coverage for all covered non-medical lines of business, with the second layer providing coverage for \$3.0 million of losses, before a 25 percent co-participation by Darwin, in excess of a \$2.0 million net retention, and the third layer providing coverage for \$15.0 million of losses, before a 15 percent co-participation by Darwin, in excess of \$5.0 million. In addition to its main reinsurance program, Darwin has placed a number of specific excess of loss treaties covering classes of business where the underwriting has been delegated to a program manager, with Darwin's net retentions varying from \$0.35 million to \$1.4 million.

AIHL Re and Homesite entered into a reinsurance agreement, effective April 1, 2007, whereby AIHL Re provided \$20.0 million of excess-of-loss reinsurance coverage to Homesite under its

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catastrophe reinsurance program. This reinsurance coverage expired on March 31, 2008, and AIHL Re is not participating in Homesite's catastrophe reinsurance program for the 2008-2009 period.

**7. Fair Value of Financial Instruments**

The estimated carrying values and fair values of Alleghany's financial instruments as of March 31, 2008 and December 31, 2007 are as follows (in millions):

	March 31, 2008		December 31, 2007	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Assets</b>				
Investments*	\$ 4,710.6	\$ 4,710.6	\$ 4,626.3	\$ 4,626.3
<b>Liabilities</b>				
Subsidiaries' debt**	\$ 5.0	\$ 5.0	\$ 5.0	\$ 5.0

\* For purposes of this table, investments include available-for-sale securities as well as investments in partnerships carried at fair value that are included in other invested assets. Investments exclude Alleghany's investments in Homesite and partnerships that are accounted for under the equity-method, which are included in other invested assets. The fair value of short-term investments approximates amortized cost. The fair value of all other categories of investments is discussed below.

\*\* The carrying value of the subsidiaries debt is estimated to approximate fair value.

As previously noted, SFAS 157 was issued in September 2006 and adopted by Alleghany as of January 1, 2008. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are not adjusted for transaction costs. In addition, SFAS 157 establishes a three-tiered hierarchy for inputs used in measuring fair value of financial instruments that emphasizes the use of observable inputs over the use of unobservable inputs by requiring that the observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing a financial instrument. Unobservable inputs are inputs that reflect one's belief about the assumptions market participants would use in pricing a financial instrument based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1 Valuations are based on unadjusted quoted prices in active markets for identical, unrestricted assets. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these assets does not involve any meaningful degree of judgment. An active market is defined as a market where transactions for the financial instrument occur with sufficient frequency and volume to provide pricing information on an ongoing basis. For Alleghany, assets utilizing Level 1 inputs generally include common stocks and U.S. Government debt securities, where valuations are based on quoted market prices.

Level 2 Valuations are based on quoted market prices where such markets are not deemed to be sufficiently active. In such circumstances, additional valuation metrics will be used which involve direct or indirect observable market inputs. For Alleghany, assets utilizing Level 2 inputs generally include debt securities other than debt issued by the U.S. Government, and preferred stocks. Third-party dealer quotes are typically used for these types of fixed income securities. In developing such quotes, dealers will use the terms of the security and market-based inputs. Terms of the security include coupon,

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maturity date, and any special provisions that may, for example, enable the investor, at his election, to redeem the security prior to its scheduled maturity date. Market-based inputs include the level of interest rates applicable to comparable securities in the market place and current credit rating(s) of the security.

Level 3 Valuations are based on inputs that are unobservable and significant to the overall fair value measurement. Valuation under Level 3 generally involves a significant degree of judgment. For Alleghany, assets utilizing Level 3 inputs include partnership investments carried at fair value. The fair value of Alleghany's investments in partnerships carried at fair value is predicated on valuations of the underlying assets provided by general partner of the entity in which such investment was held. In developing their valuations, the general partner will often utilize third-party dealer quotes that include valuations based on unobservable market inputs.

The estimated fair values of Alleghany's invested assets by balance sheet caption and level as of March 31, 2008 are as follows (in millions):

	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Equity securities	\$ 1,022.1	\$ 43.5	\$	\$ 1,065.6
Debt securities	171.4	2,890.3	20.0	3,081.7
Short-term investments	543.2	6.0		549.2
Other invested assets*			14.1	14.1
Investments (excluding Homesite)	\$ 1,736.7	\$ 2,939.8	\$ 34.1	\$ 4,710.6

\* The carrying value of partnership investments of \$14.1 million increased by \$2.7 million from the December 31, 2007 carrying value of \$11.4 million, due principally to \$2.0 million of additional investments and a net \$0.7 million increase in estimated fair value during the period.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

References to the Company, Alleghany, we, us, and our in Items 2, 3 and 4 of Part I, as well as in Part II, of this Form 10-Q refer to Alleghany Corporation and its consolidated subsidiaries unless the context otherwise requires.

AIHL refers to our insurance holding company subsidiary Alleghany Insurance Holdings LLC. RSUI refers to our subsidiary RSUI Group, Inc. and its subsidiaries. AIHL Re refers to our subsidiary AIHL Re LLC. CATA refers to our subsidiary Capitol Transamerica Corporation and its subsidiaries and also includes the results and operations of Platte River Insurance Company unless the context otherwise requires. EDC refers to our subsidiary Employers Direct Corporation and its subsidiaries. Darwin refers to our majority-owned subsidiary Darwin Professional Underwriters, Inc. and its subsidiaries. Unless the context otherwise requires, references to AIHL include the operations of RSUI, CATA, EDC, Darwin and AIHL Re. Alleghany Properties refers to our subsidiary Alleghany Properties Holdings LLC and its subsidiaries.

**Cautionary Statement Regarding Forward-Looking Information**

*Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures About Market Risk contain disclosures which are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements include all statements that do not relate solely to historical or current facts, and can be identified by the use of words such as may, will, expect, project, estimate, anticipate, plan, believe, potential, should, continue or the negative versions of those words or other comparable words. These forward-looking statements are based upon our current plans or expectations and are subject to a number of uncertainties and risks that could significantly affect current plans, anticipated actions and our future financial condition and results. These statements are not guarantees of future performance, and we have no specific intention to update these statements. The uncertainties and risks include, but are not limited to, risks relating to our insurance operating units such as*

*significant weather-related or other natural or human-made catastrophes and disasters;*

*the cyclical nature of the property and casualty industry;*

*the long-tail and potentially volatile nature of certain casualty lines of business written by our insurance operating units;*

*the cost and availability of reinsurance;*

*exposure to terrorist acts;*

*the willingness and ability of our insurance operating units' reinsurers to pay reinsurance recoverables owed to our insurance operating units;*

*changes in the ratings assigned to our insurance operating units;*

*claims development and the process of estimating reserves;*

*legal and regulatory changes;*

*the uncertain nature of damage theories and loss amounts;*

*increases in the levels of risk retention by our insurance operating units; and*

*adverse loss development for events insured by our insurance operating units in either the current year or prior year.*

*Additional risks and uncertainties include general economic and political conditions, including the effects of a prolonged U.S. or global economic downturn or recession; changes in costs;*

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*variations in political, economic or other factors; risks relating to conducting operations in a competitive environment; effects of acquisition and disposition activities, inflation rates or recessionary or expansive trends; changes in interest rates; changes in market prices of our significant equity investments; extended labor disruptions, civil unrest or other external factors over which we have no control; and changes in our plans, strategies, objectives, expectations or intentions, which may happen at any time at our discretion. As a consequence, current plans, anticipated actions and future financial condition and results may differ from those expressed in any forward-looking statements made by us or on our behalf.*

**Critical Accounting Estimates**

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, or GAAP, requires us to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period covered by the financial statements. Critical accounting estimates are defined as those estimates that are important to the presentation of our financial condition and results of operations and require us to exercise significant judgment.

We review our critical accounting estimates and assumptions quarterly. These reviews include evaluating the adequacy of reserves for unpaid losses and loss adjustment expenses and the reinsurance allowance for doubtful accounts, analyzing the recoverability of deferred tax assets, assessing goodwill for impairment and evaluating the investment portfolio for other-than-temporary declines in estimated fair value. Actual results may differ from the estimates used in preparing the consolidated financial statements.

Readers are encouraged to review our Report on Form 10-K for the year ended December 31, 2007, or the 2007 10-K, for a more complete description of our critical accounting estimates.

**Business Overview**

We are engaged, through AIHL and its subsidiaries, primarily in the property and casualty and surety insurance business. In addition, AIHL Re, a captive reinsurance subsidiary of AIHL, is available to provide reinsurance to our insurance operating units and affiliates. We also own and manage properties in the Sacramento, California region through our subsidiary Alleghany Properties and conduct corporate investment and other activities at the parent level, including the holding of strategic equity investments. Our primary sources of revenues and earnings are our insurance operations and investments.

The profitability of our insurance operating units, and as a result, our profitability, is primarily impacted by the adequacy of premium rates, as well as the cost of reinsurance, level of catastrophe losses, intensity of competition and investment returns. The ultimate adequacy of premium rates is not known with certainty at the time a property casualty insurance policy is issued because premiums are determined before claims are reported. The adequacy of premium rates is affected mainly by the severity and frequency of claims, which are influenced by many factors, including natural disasters, regulatory measures and court decisions that define and expand the extent of coverage and the effects of economic inflation on the amount of compensation due for injuries or losses.



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With respect to reinsurance, as part of their overall risk and capacity management strategy, our insurance operating units purchase reinsurance for certain amounts of risk underwritten by them, especially catastrophe risks. The reinsurance programs purchased by our insurance operating units are generally subject to annual renewal. Market conditions beyond their control determine the availability and cost of the reinsurance protection they purchase, which may affect the level of businesses written and thus their profitability.

Catastrophe losses, or the absence thereof, have also had a significant impact on our results. For example, pre-tax catastrophe losses, net of reinsurance and reinsurance reinstatement premiums, at our insurance operating units were \$48.9 million in 2007, \$18.0 million in 2006 and \$330.8 million in 2005. The incidence and severity of catastrophes in any short period of time are inherently unpredictable. Catastrophes can cause losses in a variety of our property and casualty lines, and most of our past catastrophe-related claims have resulted from severe storms. Although we experienced minimal catastrophe losses in 2007 and 2006, it is possible that a catastrophic event or multiple catastrophic events could produce significant losses and have a material adverse effect on our financial condition and results of operations in the future.

The profitability of our insurance operating units is impacted by price competition. Historically, the financial performance of the property and casualty insurance industry has tended to fluctuate in cyclical periods of price competition and excess underwriting capacity, known as a soft market, followed by periods of high premium rates and shortages of underwriting capacity. Although an individual insurance company's financial performance is dependent on its own specific business characteristics, the profitability of most property and casualty insurance companies tends to follow this cyclical market pattern. As discussed in more detail below, our insurance operating units experienced increased pricing competition in certain of their lines of business during 2006, this competitive environment continued and increased during 2007 and increased even more during the 2008 first quarter, resulting in a decrease in pricing over that time. The impact of this price competition cannot be fully quantified in advance, but it is possible that this price competition, to the extent the loss costs of our insurance operating units exceed premiums, could have a material adverse effect on the results of our insurance operating units in the future.

Finally, profitability is also affected by our investment income. Our invested assets, which are derived primarily from our own capital and cash flow from our insurance operating units, are invested principally in fixed income securities, although we also invest in equity securities. The return on fixed income securities is primarily impacted by general interest rates and the credit quality and duration of the securities.

The following discussion and analysis presents a review of our results for the three months ended March 31, 2008 and 2007. You should read this review in conjunction with the consolidated financial statements and other data presented in this Form 10-Q as well as Management's Discussion and Analysis of Financial Condition and Results of Operation and Risk Factors contained in our 2007 10-K. Our results for the first three months of 2008 are not indicative of operating results in future periods.

**Table of Contents****Consolidated Results of Operations**

The following table summarizes our consolidated revenues, costs and expenses and earnings for the three months ended March 31, 2008 and 2007.

(in thousands)	Three months ended March	
	2008	31, 2007
<b>Revenues</b>		
Net premiums earned	\$ 297,466	\$ 271,571
Net investment income	41,341	45,169
Net realized capital gains	74,712	50,141
Other income	136	8,725
Total revenues	413,655	375,606
<b>Costs and expenses</b>		
Loss and loss adjustment expenses	155,195	122,604
Commissions, brokerage and other underwriting expenses	84,056	71,278
Other operating expenses	15,212	13,166
Corporate administration	9,948	8,004
Interest expense	226	723
Total costs and expenses	264,637	215,775
Earnings before income taxes and minority interest	149,018	159,831
Income taxes	43,615	51,056
Earnings before minority interest	105,403	108,775
Minority interest, net of tax	6,682	2,357
Net earnings	\$ 98,721	\$ 106,418
<b>Revenues:</b>		
AIHL	\$ 331,848	\$ 303,051
Corporate activities (1)	81,807	72,555
<b>Earnings before income taxes and minority interest:</b>		
AIHL	\$ 77,927	\$ 97,039
Corporate activities (1)	71,091	62,792
(1) Corporate activities consist of Alleghany Properties, Homesite and corporate		

activities at the  
parent level.

Our earnings before income taxes and minority interest in the first three months of 2008 decreased from the corresponding 2007 period, primarily reflecting increases in loss and loss adjustment expenses and commissions, brokerage and other underwriting expenses as well as a decrease in other income, partially offset by an increase in net premiums earned and substantially higher net realized capital gains. The increase in loss and loss adjustment expenses and commissions, brokerage and other underwriting expenses primarily reflects the inclusion in the 2008 first quarter of EDC's results and an increase in RSUI's loss and loss adjustment expenses. The decrease in other income for the 2008 first quarter from the corresponding 2007 period primarily reflects a pre-tax gain of approximately \$7.2 million realized in the 2007 first quarter on sales of real property by Alleghany Properties, compared with immaterial sales activity during the 2008 first quarter. The increase in net premiums earned primarily reflects growth at Darwin and the inclusion of EDC's results. The increase in net realized capital gains in the first three months of 2008 primarily reflects increased sales of common stock of Burlington Northern Santa Fe Corporation, or Burlington Northern during the 2008 first quarter, compared with the corresponding 2007 period.

The effective tax rate on net earnings before income taxes and minority interest was 29.3 percent for the 2008 first quarter, compared with 31.9 percent for the corresponding 2007 period, reflecting an increase in tax exempt income in the 2008 period.

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The increase in minority interest expense in the 2008 first quarter from the corresponding 2007 period reflects a substantial increase in earnings from Darwin.

**AIHL Operating Unit Pre-Tax Results**

(in millions, except ratios)

<b>Three months ended March 31, 2008</b>	RSUI	AIHL Re	CATA	EDC (1)	Darwin	AIHL
Gross premiums written	\$ 255.1	\$ 0.2	\$ 47.8	\$ 23.3	\$ 80.0	\$ 406.4
Net premiums written	\$ 152.4	\$ 0.2	\$ 46.0	\$ 21.1	\$ 58.0	\$ 277.7
Net premiums earned (2)	\$ 177.9	\$ 0.2	\$ 46.8	\$ 20.6	\$ 52.0	\$ 297.5
Loss and loss adjustment expenses	94.5		23.5	17.2	20.0	155.2
Underwriting expenses (3)	44.8		19.1	6.5	13.6	84.0
Underwriting profit (loss) (4)	\$ 38.6	\$ 0.2	\$ 4.2	\$ (3.1)	\$ 18.4	\$ 58.3
Net investment income (2)						37.6
Net realized capital losses (2)						(3.4)
Other income (2)						0.1
Other expenses (3)						(14.7)
Earnings before income taxes and minority interest						\$ 77.9
Loss ratio (5)	53.1%		50.2%	83.8%	38.4%	52.2%
Expense ratio (6)	25.2%	18.3%	40.9%	31.4%	26.3%	28.3%
Combined ratio (7)	78.3%	18.3%	91.1%	115.2%	64.7%	80.5%
<b>Three months ended March 31, 2007</b>						
Gross premiums written	\$ 288.9		\$ 52.7		\$ 74.3	\$ 415.9
Net premiums written	\$ 156.4		\$ 50.6		\$ 48.9	\$ 255.9
Net premiums earned (2)	\$ 166.6	\$ 17.7	\$ 47.3		\$ 40.0	\$ 271.6
Loss and loss adjustment expenses	76.4		20.7		25.5	122.6
Underwriting expenses (3)	39.9	0.1	19.6		11.7	71.3
Underwriting profit (4)	\$ 50.3	\$ 17.6	\$ 7.0		\$ 2.8	\$ 77.7
Net investment income (2)						37.1
Net realized capital losses (2)						(5.8)
Other income (2)						0.1
Other expenses (3)						(12.1)
						\$ 97.0

Earnings before income taxes and  
minority interest

Loss ratio (5)	45.9%		43.8%	63.7%	45.1%
Expense ratio (6)	24.0%	0.3%	41.5%	29.1%	26.2%
Combined ratio (7)	69.9%	0.3%	85.3%	92.8%	71.3%

(1) Includes the results of EDC, net of purchase accounting adjustments, commencing July 18, 2007. See Note 9 to the Notes to the Consolidated Financial Statements set forth in Item 8 of our 2007 10-K.

(2) Represent components of total revenues.

(3) Underwriting expenses represent commission and brokerage expenses and that portion of salaries, administration and other operating expenses directly attributable to underwriting activities, whereas the remainder constitutes other expenses.

- (4) Represents net premiums earned less loss and loss adjustment expenses and underwriting expenses, all as determined in accordance with GAAP, and does not include net investment income and other income or net realized capital gains. Underwriting profit does not replace net income determined in accordance with GAAP as a measure of profitability; rather, we believe that underwriting profit, which does not include net investment income and other income or net realized capital gains, enhances the understanding of AIHL s insurance operating units operating results by highlighting net income attributable to their underwriting performance. With the addition of net investment

income and other income and net realized capital gains, reported pre-tax net income (a GAAP measure) may show a profit despite an underlying underwriting loss. Where underwriting losses persist over extended periods, an insurance company's ability to continue as an ongoing concern may be at risk. Therefore, we view underwriting profit as an important measure in the overall evaluation of performance.

- (5) Loss and loss adjustment expenses divided by net premiums earned, all as determined in accordance with GAAP.
- (6) Underwriting expenses divided by net premiums earned, all as determined in accordance with GAAP.

- (7) The sum of the loss ratio and expense ratio, all as determined in accordance with GAAP, representing the percentage of each premium dollar an insurance company has to spend on losses (including loss adjustment expenses) and underwriting expenses.



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Discussion of individual AIHL operating unit results follows, and AIHL investment results are discussed below under Investments.

**RSUI**

The decrease in gross premiums written by RSUI in the 2008 first quarter from the corresponding 2007 period primarily reflects continuing and increasing pricing competition, particularly in RSUI's general liability and property lines of business. RSUI's net premiums earned in both property and casualty lines of business increased in the 2008 first quarter from the corresponding 2007 period. The increase in property premiums earned is due primarily to reduced reinsurance limits being purchased and reduced rates paid for catastrophe and per risk reinsurance coverage renewed at May 1, 2007. The increase in casualty premiums earned primarily reflects the growth of RSUI's binding authority line of business which writes small, specialized coverages pursuant to underwriting authority arrangements with managing general agents.

The increase in RSUI's loss and loss adjustment expenses in the 2008 first quarter from the corresponding 2007 period primarily reflects higher property losses, including a single loss of approximately \$10.0 million arising from a factory explosion. The increase in RSUI's underwriting expenses in the 2008 first quarter from the corresponding 2007 period primarily reflects higher incurred commission expenses primarily resulting from the non-renewal of RSUI's professional liability quota share reinsurance treaty which expired in April 2007, as well as lower ceding commissions on RSUI's property surplus share reinsurance arrangements. RSUI's 2008 first quarter underwriting profit decreased from the corresponding 2007 period, primarily reflecting an increase in property losses. Rates at RSUI in the 2008 first quarter, compared with the corresponding 2007 period, reflect overall industry trends of downward pricing as a result of increased competition, with decreased rates in all of RSUI's lines of business.

As discussed in our 2007 10-K, RSUI reinsures its property lines of business through a program consisting of surplus share treaties, facultative placements, per risk and catastrophe excess of loss treaties. RSUI's catastrophe reinsurance program (which covers catastrophe risks including, among others, windstorms and earthquakes) and per risk reinsurance program run on an annual basis from May 1 to the following April 30 and thus expired on April 30, 2008. RSUI has placed substantially all of its catastrophe reinsurance program for the 2008-2009 period. Under the new program, RSUI's catastrophe reinsurance program provides coverage in two layers for \$400.0 million of losses in excess of a \$100.0 million net retention after application of the surplus share treaties, facultative reinsurance and per risk covers. The first layer provides coverage for \$100.0 million of losses, before a 33.15 percent co-participation by RSUI, in excess of the \$100.0 million net retention, and the second layer provides coverage for \$300.0 million of losses, before a 5 percent co-participation by RSUI, in excess of \$200.0 million. The renewed program is substantially similar to the expired program. In addition, RSUI's property per risk reinsurance program for the 2008-2009 period provides RSUI with reinsurance for \$90.0 million of losses in excess of \$10.0 million net retention per risk after application of the surplus share treaties and facultative reinsurance, which is substantially similar to the expired program. As discussed in the 2007 10-K, RSUI reinsures its other lines of business through quota share treaties, except for professional liability lines where RSUI retains all of such business.

**Table of Contents****AIHL Re**

AIHL Re was formed in June 2006 as a captive reinsurance subsidiary of AIHL to provide catastrophe reinsurance coverage for AIHL's insurance operating units and affiliates. AIHL Re and Homesite entered into a reinsurance agreement, effective April 1, 2007, whereby AIHL Re provided \$20.0 million of excess-of-loss reinsurance coverage to Homesite under its catastrophe reinsurance program. This reinsurance coverage expired on March 31, 2008, and AIHL Re is not participating in Homesite's catastrophe reinsurance program for the 2008-2009 period. In connection with the expiration of the agreement, the trust funds established to secure AIHL Re's obligations to make payments to Homesite under such reinsurance agreement were dissolved and the \$20.0 million in such funds was disbursed to AIHL Re in April 2008. AIHL Re's underwriting profit in the 2008 first quarter reflects the absence of catastrophe losses during the period. AIHL Re's underwriting profit in the 2007 first quarter reflects the absence of catastrophe losses during the period when AIHL Re was participating on RSUI's catastrophe reinsurance program. AIHL Re's participation on such RSUI catastrophe reinsurance program expired in April 2007.

**CATA**

CATA's net premiums earned in the 2008 first quarter decreased from the corresponding 2007 period, primarily reflecting continuing and increasing pricing competition in CATA's property and casualty (including in excess and surplus markets) and commercial surety lines of business. The increase in loss and loss adjustment expenses in the 2008 first quarter from the corresponding 2007 period primarily reflects a net \$1.5 million release of prior year loss reserves during the 2008 period, compared with a \$3.4 million release of primarily casualty and surety prior year loss reserves during the 2007 period. The \$1.5 million net reserve release during the 2008 first quarter reflects a release of primarily casualty and surety prior year loss reserves, partially offset by a strengthening of property prior year loss reserves. The increase in loss and loss adjustment expenses described above was the primary cause for the decrease in CATA's underwriting profit in the 2008 first quarter from the corresponding 2007 period.

Rates at CATA in the 2008 first quarter, compared with the corresponding 2007 period, reflect overall industry trends of downward pricing as a result of increased competition, with decreased rates in CATA's property and casualty and commercial surety lines of business.

**EDC**

AIHL's results include the results of EDC, net of purchase accounting adjustments, commencing July 18, 2007. See Note 16 to the Notes to the Consolidated Financial Statements set forth in Item 8 of our 2007 10-K. EDC's net premiums earned in the first three months of 2008 reflect increased competition and decreasing rates in its California workers' compensation business. Loss and loss adjustment expenses in the first three months of 2008 reflect the exposure of EDC's underlying book of business, relatively flat trends in loss costs and the favorable impact of reduced estimated unallocated loss adjustment expenses.

**Darwin**

The increase in net premiums earned in the 2008 first quarter from the corresponding 2007 period primarily reflects an increase in gross premiums written as a result of growth in Darwin's errors & omissions and medical malpractice lines of business, as well as a \$3.7 million reduction

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in ceded premiums related to a release of prior year loss reserves during the 2008 first quarter. The decrease in loss and loss adjustment expenses in the 2008 first quarter from the corresponding 2007 period primarily reflects favorable loss emergence (resulting in a release in the 2008 first quarter of \$11.7 million of prior year reserves, compared with a release of \$0.8 million in the 2007 first quarter), partially offset by the impact of the increase in net premiums earned.

The decrease in loss and loss adjustment expenses and increase in net premiums earned described above were the primary reasons for the increase in Darwin's underwriting profit in the 2008 first quarter from the corresponding 2007 period. Darwin experienced increased competition and decreased rates across all of its lines of business during the 2008 first quarter, compared with the corresponding 2007 period.

As discussed in the 2007 10-K, Darwin reinsures all of its lines of business through a program consisting of a variety of excess of loss treaties. In April 2008, Darwin substantially completed the renewal of its main reinsurance program. For Darwin's medical lines of business, the new program provides coverage for \$15.0 million of losses, before a 15 percent co-participation by Darwin, in excess of a \$1.0 million net retention. For Darwin's non-medical lines of business, the new program provides coverage in three layers, with the ultimate premium varying depending upon the profitability of the business reinsured. The first layer covers all non-medical lines of business (other than (i) publicly traded, financial institutions and healthcare directors and officers, or D&O, liability and (ii) managed care and financial institutions errors and omissions liability) for \$1.0 million of losses before a 25 percent co-participation by Darwin, in excess of a \$1.0 million net retention. The second and third layers provide coverage for all covered non-medical lines of business, with the second layer providing coverage for \$3.0 million of losses, before a 25 percent co-participation by Darwin, in excess of a \$2.0 million net retention, and the third layer providing coverage for \$15.0 million of losses, before a 15 percent co-participation by Darwin, in excess of \$5.0 million. In addition to its main reinsurance program, Darwin has placed a number of specific excess of loss treaties covering classes of business where the underwriting has been delegated to a program manager, with Darwin's net retentions varying from \$0.35 million to \$1.4 million.

**Reserve Review Process**

AIHL's insurance operating units periodically analyze liabilities for unpaid losses and loss adjustment expenses, or LAE, established in prior years and adjust their expected ultimate cost, where necessary, to reflect positive or negative development in loss experience and new information, including, for certain catastrophic events, revised industry estimates of the magnitude of a catastrophe. Adjustments to previously recorded liabilities for unpaid losses and LAE, both positive and negative, are reflected in our financial results in the periods in which these adjustments are made and are referred to as prior year reserve development. The following table presents the reserves established in connection with the losses and LAE of AIHL's insurance operating units on a gross and net basis by line of business. These reserve amounts represent the accumulation of estimates of ultimate losses (including for claims incurred but not yet reported, or IBNR) and LAE.

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<i>( in millions)</i>	<i>Property</i>	<i>Casualty(1)</i>	<i>CMP(2)</i>	<i>Surety</i>	<i>Workers</i>		<i>Total</i>
					<i>Comp(3)</i>	<i>All Other(4)</i>	
<b><i>At March 31, 2008</i></b>							
Gross loss and LAE reserves	\$ 330.4	\$ 1,986.5	\$ 83.4	\$ 22.6	\$ 190.4	\$ 67.5	\$ 2,680.8
Reinsurance recoverables on unpaid losses	(132.1)	(771.4)	(3.3)	(1.3)	(10.1)	(43.9)	(962.1)
Net loss and LAE reserves	\$ 198.3	\$ 1,215.1	\$ 80.1	\$ 21.3	\$ 180.3	\$ 23.6	\$ 1,718.7
<b><i>At December 31, 2007</i></b>							
Gross loss and LAE reserves	\$ 332.1	\$ 1,883.6	\$ 85.0	\$ 20.6	\$ 187.4	\$ 71.4	\$ 2,580.1
Reinsurance recoverables on unpaid losses	(126.4)	(732.3)	(1.1)	(0.3)	(8.8)	(46.4)	(915.3)
Net loss and LAE reserves	\$ 205.7	\$ 1,151.3	\$ 83.9	\$ 20.3	\$ 178.6	\$ 25.0	\$ 1,664.8

(1) Primarily consists of excess and umbrella, D&O liability, professional liability, general liability and medical malpractice liability.

(2) Commercial multiple peril.

(3) Workers compensation amounts include

EDC, net of purchase accounting adjustments (See Note 16 to the Notes to the Consolidated Financial Statements set forth in Item 8 of our 2007 10-K). Such adjustments include a minor reduction of gross and net loss and LAE for acquisition-date discounting, as required under purchase accounting.

- (4) Primarily consists of loss and LAE reserves for discontinued lines of business and loss reserves acquired in connection with prior acquisitions for which the sellers provided loss reserve guarantees. The loss and LAE reserves are ceded 100 percent to the sellers. Additional information regarding the loss reserve guarantees can be found in

Note 5 to the  
Notes to the  
Consolidated  
Financial  
Statements set  
forth in Item 8  
of our 2007  
10-K Report.

*Changes in Loss and LAE Reserves between March 31, 2008 and December 31, 2007*

**Gross Reserves.** The increase in gross loss and LAE reserves at March 31, 2008 from December 31, 2007 primarily reflects increases in casualty gross loss and LAE reserves, partially offset by modest decreases in other gross loss and LAE reserves. The increase in casualty gross loss and LAE reserves primarily reflects anticipated loss reserves on current accident year gross premiums earned and limited gross paid loss activity for the current and prior casualty accident years, primarily at RSUI and Darwin. The decrease in other reserves is due primarily to a reduction in loss reserves acquired in connection with prior acquisitions which are ceded 100 percent to the sellers.

**Net Reserves.** The increase in net loss and LAE reserves at March 31, 2008 from December 31, 2007 primarily reflects increases in casualty net loss and LAE reserves, partially offset by modest decreases in property and CMP net loss and LAE reserves. The increase in casualty net loss and LAE reserves primarily reflects anticipated loss reserves on current accident year premiums earned and limited net paid loss activity for the current and prior casualty accident years, primarily at RSUI and Darwin. Such increases for Darwin were partially offset by an \$11.7 million release of prior year reserves in the 2008 first quarter. The decrease in net property loss and LAE reserves is mainly due to loss payments made by RSUI on 2004 and 2005 hurricane related losses, principally Hurricane Katrina. The decrease in net CMP loss and LAE reserves is due to reduced premium volume and release of prior year reserves in the 2008 first quarter.

**Table of Contents****Reinsurance Recoverables**

At March 31, 2008, AIHL had total reinsurance recoverables of \$993.8 million, consisting of \$962.1 million of ceded outstanding losses and LAE and \$31.7 million of recoverables on paid losses. Approximately 91.3 percent of AIHL's reinsurance recoverables balance at March 31, 2008 was due from reinsurers having an A.M. Best financial strength rating of A (Excellent) or higher.

**Corporate Activities Results from Operations**

Corporate activities recorded a pre-tax gain of \$71.1 million on revenues of \$81.8 million in the 2008 first quarter, compared with a pre-tax gain of \$62.8 million on revenues of \$72.5 million in the corresponding 2007 period. The results for such 2008 and 2007 periods primarily reflect net realized capital gains at the parent level of \$78.1 million and \$55.9 million, respectively, resulting from the sale of approximately 1.0 million shares and approximately 0.8 million shares, respectively, of Burlington Northern common stock. In addition, the 2007 results also benefited from the sale by Alleghany Properties of certain real estate holdings during the first three months of 2007 which generated a pre-tax gain of approximately \$7.2 million, compared with immaterial sales activity during the comparable 2008 period.

The decrease in net investment income for corporate activities in the 2008 first quarter from the corresponding 2007 period reflects: (i) a loss of \$0.2 million of our share of earnings in Homesite, net of purchase accounting adjustments, in the 2008 period, compared with a gain of \$2.9 million in the 2007 period; (ii) a loss of \$1.0 million from parent-level partnership investments in the 2008 period, compared with a minimal gain in the 2007 period; (iii) lower average investment yields during the first three months of 2008; and (iv) lower average fixed income assets during the 2008 first quarter due to capital contributions made by parent to AIHL in connection with AIHL's acquisition of EDC in July 2007.

**Investments**

On a consolidated basis, our invested asset portfolio was approximately \$4.9 billion as of March 31, 2008, an increase of 1.7 percent from approximately \$4.8 billion at December 31, 2007. At March 31, 2008, the average duration of our debt securities portfolio was 4.4 years, compared with 4.3 years at December 31, 2007.

The invested asset portfolio generated net investment income of \$41.3 million in the 2008 first quarter, of which \$37.6 million was generated by AIHL and \$3.7 million was generated by corporate activities. These amounts were \$45.2 million, \$37.1 million, and \$8.1 million, respectively, for the corresponding 2007 period. The slight increase in AIHL's net investment income in the 2008 first quarter compared with the corresponding 2007 period was due principally to the net positive effect from the acquisition of EDC and strong underwriting cash flow, largely offset by lower average investment yields during the 2008 first quarter.

The sales within our invested asset portfolio generated net realized capital gains of \$74.7 million in the 2008 first quarter, comprised of \$3.4 million of net losses at AIHL and \$78.1 million of net gains generated by corporate activities. These amounts were \$50.1 million, (\$5.8) million, and \$55.9 million, respectively, for the comparable 2007 period. As noted above, the net realized capital gains for corporate activities in both the 2008 and 2007 periods were due primarily to the sale of Burlington Northern common stock. As of March 31, 2008, we held approximately 4.0 million shares of Burlington Northern common stock with an aggregate market

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value at that date of approximately \$368.9 million. Net realized capital losses in the 2008 first quarter and the 2007 first quarter, respectively, consisted of \$15.1 million and \$6.6 million, respectively, of unrealized losses related to AIHL's investment portfolio that were deemed to be other than temporary, partially offset by \$11.7 million and \$0.8 million, respectively, of net realized capital gains on the sale of securities by AIHL. The \$15.1 million of unrealized losses relates to AIHL's common stock holdings in the financial services sector, whereas the \$6.6 million related to AIHL's mortgage- and asset-backed bond holdings. As of March 31, 2008, our equity portfolio had a net unrealized gain of \$386.8 million, comprised of gross unrealized gains of \$442.6 million and gross unrealized losses of \$55.8 million. As of December 31, 2007, the comparable figures were \$484.7 million, \$513.7 million and \$29.0 million, respectively. As of March 31, 2008 and December 31, 2007, no equity security was in a continuous unrealized loss position for twelve months or more.

**Financial Condition**

Stockholders' equity increased to \$2,838.4 million as of March 31, 2008, compared with \$2,793.9 million as of December 31, 2007, representing an increase of 1.6 percent, due to net earnings in the first three months of 2008, partially offset by a net decrease in unrealized losses on our investment portfolio during the first three months of 2008.

In February 2008, Alleghany announced that its Board of Directors had authorized the purchase of shares of Alleghany common stock, at such times and at prices as management may determine advisable, up to an aggregate of \$300.0 million. During the first quarter of 2008, we had purchased an aggregate of 5,334 shares of our common stock for approximately \$1.8 million, at an average price per share of \$339.50. As of March 31, 2008 and December 31, 2007, we had 8,334,245 and 8,322,348 shares of our common stock outstanding, respectively, adjusted to reflect the common stock dividend declared in February 2008 and payable in April 2008.

We and our subsidiaries have adequate internally generated funds and unused credit facilities to provide for the currently foreseeable needs of its and their businesses, respectively.

**Recent Accounting Pronouncements**

In September 2006, FASB Statement No. 157, Fair Value Measurements (SFAS 157), was issued. SFAS 157 provides guidance for using fair value to measure assets and liabilities. SFAS 157 does not expand the use of fair value in any new circumstances. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We have adopted the provisions of SFAS 157 as of January 1, 2008, and the implementation did not have a material impact on our results of operations and financial condition. See Note 7.

At its September 2006 meeting, the Emerging Issues Task Force reached a consensus with respect to Issue No. 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements. This Issue addresses split-dollar life insurance, which is defined as an arrangement in which the employer and an employee share the cash surrender value and/or death benefits of the insurance policy. Additional information regarding this Issue can be found in Note 1.p. to the Notes to the Consolidated Financial Statements set forth in Item 8 of the 2007 10-K. We have adopted the provisions of this Issue as of January 1, 2008, and the implementation did not have a material impact on our results of operations and financial condition.



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In February 2007, FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*, was issued. This Statement permits entities to choose to measure many financial instruments and certain other items at fair value, at specified election dates, with unrealized gains and losses reported in earnings at each subsequent reporting date. This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS 157. We have adopted the provisions of this Statement as of January 1, 2008, and the implementation did not have any impact on our results of operations and financial condition.

In December 2007, FASB Statements No. 141 (revised 2007), *Business Combinations* (SFAS 141R), and No. 160, *Noncontrolling Interests in Consolidated Financial Statements* (SFAS 160), were issued. SFAS 141R replaces FASB Statement No. 141, *Business Combinations*. SFAS 141R requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose additional information regarding the nature and financial effect of the business combination. SFAS 160 requires all entities to report noncontrolling (minority) interests in subsidiaries in the same way as equity in the consolidated financial statements. SFAS 160 also requires disclosure, on the face of the consolidated statement of income, of the amounts of consolidated net income attributable to the parent and to the noncontrolling interest. We will adopt SFAS 141R and SFAS 160 for all business combinations initiated after December 31, 2008. We will also reclassify its minority interest liabilities as a separate component of shareholders' equity after December 31, 2008.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Market risk is the risk of loss from adverse changes in market prices and rates, such as interest rates, foreign currency exchange rates and commodity prices. The primary market risk related to our non-trading financial instruments is the risk of loss associated with adverse changes in interest rates.

The table below presents a sensitivity analysis of our consolidated debt securities as of March 31, 2008. Sensitivity analysis is defined as the measurement of potential change in future earnings, fair values or cash flows of market sensitive instruments resulting from one or more selected hypothetical changes in interest rates. In this sensitivity analysis model, we use fair values to measure its potential change, and a +/- 300 basis point range of change in interest rates to measure the hypothetical change in fair value of the financial instruments included in the analysis. The change in fair value is determined by calculating hypothetical March 31, 2008 ending prices based on yields adjusted to reflect a +/- 300 basis point range of change in interest rates, comparing these hypothetical ending prices to actual ending prices, and multiplying the difference by the par outstanding.

Subsidiary debt as of March 31, 2008 of \$5.0 million is not presented in the table below as it is not material to our analysis of sensitivity to interest rates given the amount and terms of this debt. See Note 7 to the Notes to the Consolidated Financial Statements set forth in Item 8 of our 2007 10-K for more information regarding such subsidiary debt.

**Table of Contents**At March 31, 2008 ( in millions)

	-300	-200	-100	0	100	200	300
Interest rate shifts							
Debt securities, fair value	\$ 3,484.2	\$ 3,351.0	\$ 3,217.6	\$ 3,081.7	\$ 2,945.8	\$ 2,813.3	\$ 2,684.5
Estimated change in fair value	\$ 402.5	\$ 269.3	\$ 135.9		\$ (135.9)	\$ (268.4)	\$ (397.2)

This sensitivity analysis provides only a limited, point-in-time view of the market risk of the financial instruments discussed above. The actual impact of changes in equity prices and market interest rates on the financial instruments may differ significantly from those shown in the sensitivity analysis. The sensitivity analysis is further limited because it does not consider any actions we could take in response to actual and/or anticipated changes in interest rates.

**ITEM 4. CONTROLS AND PROCEDURES.**

We carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer, or CEO, and our chief financial officer, or CFO, of the effectiveness of design and operation of our disclosure controls and procedures as of the end of the period covered by this report on Form 10-Q pursuant to Rule 13a-15(e) or 15d-15(e) promulgated under the Securities Exchange Act of 1934, or Exchange Act. Based on that evaluation, our management, including our CEO and CFO, concluded that our disclosure controls and procedures were effective as of that date to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and timely reported as specified in the U.S. Securities and Exchange Commission's rules and forms. Additionally, as of the end of the period covered by this report on Form 10-Q, there have been no changes in internal control over financial reporting during the period covered by this report on Form 10-Q that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION****ITEM 1A. RISK FACTORS.**

There are no material changes from the risk factors set forth in Part I, Item 1A, Risk Factors, of our 2007 10-K. Please refer to that section for disclosures regarding the risks and uncertainties related to our businesses.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.****(c) Issuer Purchases of Equity Securities.**

The following table summarizes our common stock repurchases for the quarter ended March 31, 2008.

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Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1)
January 1, 2008 through January 31, 2008		\$		
February 1, 2008 through February 28, 2008		\$		
March 1, 2008 through March 31, 2008	5,334	\$ 339.50	5,334	\$ 298,200,000
Total		\$ 339.50		

(1) On February 26, 2008, we announced that our Board of Directors had authorized the purchase of shares of our common stock, at such times and at prices as management may determine advisable, up to an aggregate of \$300.0 million. As of March 31, 2008, we had purchased the number of shares set forth in the table for aggregate consideration of \$1.8 million.

**ITEM 6. EXHIBITS.**

Exhibit

Number	Description
10.1	Letter Agreement, dated April 15, 2008, between Alleghany and Weston M. Hicks, filed as Exhibit 10.1 to Alleghany's Current Report on Form 8-K filed on April 21, 2008, is incorporated herein by reference.
31.1	Certification of the Chief Executive Officer of the Company pursuant to Rule 13a-14(a) or Rule 15(d)-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of the Chief Financial Officer of the Company pursuant to Rule 13a-14(a) or Rule 15(d)-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. This exhibit shall not be deemed filed as a part of this report on Form 10-Q.
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. This exhibit shall not be deemed filed as a part of this report on Form 10-Q.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ALLEGHANY CORPORATION  
Registrant

Date: May 6, 2008

/s/ Roger B. Gorham  
Roger B. Gorham  
Senior Vice President  
(and chief financial officer)

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