ALLEGHANY CORP /DE
Form 10-K/A
March 11, 2009

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K/A
Amendment No. 1

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2008

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission file number 1-9371

ALLEGHANY CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**51-0283071**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
7 Times Square Tower, New York, New York (Address of principal executive offices)	10036 (Zip Code)

Registrant s telephone number, including area code:
(212) 752-1356

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $1.00 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
Not applicable

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

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

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 þ No o

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

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

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

Indicate by check mark whether the registrant is a shell company.

Yes o No þ

As of June 30, 2008, the aggregate market value (based upon the closing price of these shares on the New York Stock Exchange) of the shares of Common Stock of Alleghany Corporation held by non-affiliates was $2,161,992,492.

As of February 20, 2009, 8,273,891 shares of Common Stock were outstanding.

EXPLANATORY NOTE

Alleghany Corporation (the Company) is filing this Amendment No.1 (this Amendment) to its Annual Report on Form 10-K for the year ended December 31, 2008, as originally filed with the Securities and Exchange Commission on February 27, 2009 (the Form 10-K Report), for the sole purpose of (i) adding to Part II, Item 8, Financial Statements and Supplementary Data, the report of KPMG LLP dated February 25, 2009 with respect to the effectiveness of the Company s internal control over financial reporting as of December 31, 2008, which appears on page 46 below (the Attestation Report), and the reference to the Attestation Report in the audit report of KPMG LLP dated February 25, 2009, which appears on page 45 below, and (ii) adding to Part II, Item 9A, Controls and Procedures, under the subheading, Management s Annual Report on Internal Control over Financial Reporting, a statement that KPMG LLP has issued the Attestation Report, which appears on page 47 below.

As required by Rule 12b-15 under the Securities Exchange Act of 1934, as amended, new certifications of our principal executive officer and principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, are filed as exhibits to this Amendment.

Other than as set forth above, this Amendment does not modify or update any of the other disclosure contained in the Form 10-K Report and does not reflect events occurring after the filing of the Form 10-K Report on February 27, 2009.

Item 8. Financial Statements and Supplementary Data.

Index to Consolidated Financial Statements

Alleghany Corporation and Subsidiaries

ALLEGHANY CORPORATION AND SUBSIDIARIES
Consolidated Balance Sheets

	December 31, **2008**	December 31, 2007
	(in thousands, except share amounts)	
Assets		
Investments		
Available-for-sale securities at fair value:		
Equity securities (cost: 2008 $463,207; 2007 $691,429)	**$ 629,518**	$ 1,176,412
Debt securities (amortized cost: 2008 $2,781,829; 2007 $2,541,488)	**2,760,019**	2,564,717
Short-term investments	**636,197**	316,897
	4,025,734	4,058,026
Other invested assets	**250,407**	193,272
Total investments	**4,276,141**	4,251,298
Cash	**18,125**	57,646
Premium balances receivable	**154,022**	170,080
Reinsurance recoverables	**1,056,438**	1,018,673
Ceded unearned premium reserves	**185,402**	221,203
Deferred acquisition costs	**71,753**	75,623
Property and equipment at cost, net of accumulated depreciation and amortization	**23,310**	19,735
Goodwill and other intangibles, net of amortization	**151,223**	207,540
Current taxes receivable	**14,338**	4,116
Net deferred tax assets	**130,293**	
Assets of discontinued operations		812,119
Other assets	**100,783**	104,079
	$ 6,181,828	$ 6,942,112
Liabilities and Stockholders Equity		
Losses and loss adjustment expenses	**$ 2,578,590**	$ 2,379,701
Unearned premiums	**614,067**	699,409
Reinsurance payable	**53,541**	57,380
Net deferred tax liabilities		71,594
Liabilities of discontinued operations		663,417
Other liabilities	**288,941**	286,284
Total liabilities	**3,535,139**	4,157,785
Preferred stock		
	299,429	299,480

(shares authorized: 2008 and 2007 1,132,000; shares issued and outstanding: 2008 1,131,619; 2007 1,131,819)		
Common stock		
(shares authorized: 2008 and 2007 22,000,000; issued and outstanding 2008 8,349,284; 2007 8,322,348)	**8,349**	8,159
Contributed capital	**742,863**	689,435
Accumulated other comprehensive income	**87,249**	328,632
Treasury stock, at cost (2008 76,513 shares; 2007 none)	**(24,290)**	
Retained earnings	**1,533,089**	1,458,621
Total stockholders equity	**2,646,689**	2,784,327
	$ 6,181,828	$ 6,942,112

See accompanying Notes to Consolidated Financial Statements.

ALLEGHANY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Earnings and Comprehensive Income

	Years Ended December 31,		
	2008	2007	2006
	(in thousands, except per share amounts)		
Revenues			
Net premiums earned	**$ 948,652**	$ 974,321	$ 877,750
Net investment income	**130,184**	146,082	127,935
Net realized capital (losses) gains	**(92,168)**	92,766	28,212
Other income	**2,432**	15,427	26,435
Total revenues	**989,100**	1,228,596	1,060,332
Costs and expenses			
Loss and loss adjustment expenses	**570,019**	449,052	410,335
Commissions, brokerage and other underwriting expenses	**286,573**	257,198	215,533
Other operating expenses	**34,861**	55,604	47,361
Corporate administration	**35,895**	32,987	41,667
Interest expense	**700**	1,476	5,626
Total costs and expenses	**928,048**	796,317	720,522
Earnings from continuing operations, before income taxes	**61,052**	432,279	339,810
Income taxes	**20,485**	144,737	98,863
Earnings from continuing operations	**40,567**	287,542	240,947
Discontinued operations			
Operations (including a gain on disposal of $141,688 in 2008)	**164,193**	24,976	14,998
Income taxes (including tax on the gain on disposal of $49,591 in 2008)	**56,789**	13,448	8,042
Earnings from discontinued operations, net of tax	**107,404**	11,528	6,956
Net earnings	**$ 147,971**	$ 299,070	$ 247,903
Changes in other comprehensive income			
Change in unrealized (losses) gains, net of deferred taxes of $(145,368), $60,778 and $23,227 for 2008, 2007 and 2006, respectively	**$ (269,969)**	$ 112,874	$ 43,136
Less: reclassification for (losses) gains realized in net earnings, net of taxes of $(15,198), $32,458 and $9,878 for 2008, 2007 and 2006, respectively	**28,225**	(60,280)	(18,346)
Other	**361**	167	(106)
Comprehensive income	**$ (93,412)**	$ 351,831	$ 272,587

Net earnings	**$ 147,971**	$ 299,070	$ 247,903
Preferred dividends	**17,218**	17,223	8,994
Net earnings available to common stockholders	**$ 130,753**	$ 281,847	$ 238,909
Basic earnings per share of common stock: *			
Continuing operations	**$ 2.81**	$ 32.53	$ 27.95
Discontinued operations	**12.92**	1.39	0.84
Basic earnings per share	**$ 15.73**	$ 33.92	$ 28.79
Diluted earnings per share of common stock: *			
Continuing operations	**$ 2.81**	$ 30.85	$ 27.23
Discontinued operations	**12.92**	1.23	0.78
Diluted earnings per share	**$ 15.73**	$ 32.08	$ 28.01

* Amounts reflect subsequent common stock dividends.

See accompanying Notes to Consolidated Financial Statements.

ALLEGHANY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Changes in Stockholders Equity

	Three Years Ended December 31, 2008						
	Preferred Stock	Common Stock	Contributed Capital	Accumulated Other Comprehensive Income	Treasury Stock	Retained Earnings	Total Stockholders Equity
	(in thousands, except share amounts)						
Balance at December 31, 2005 (8,388,721 shares of common stock issued; none in treasury)*	$	$ 7,905	$ 591,164	$ 254,397	$	$ 1,040,920	$ 1,894,386
Add (deduct):							
Net earnings						247,903	247,903
Other comprehensive loss, net of tax:							
Retirement plans				(3,316)			(3,316)
Change in unrealized appreciation of investments, net				24,790			24,790
Comprehensive income				21,474		247,903	269,377
Dividends paid		22	6,759		37,542	(53,431)	(9,108)
Stock based compensation			19,302				19,302
Treasury stock purchase					(39,185)		(39,185)
Gain on sale of subsidiary stock			9,473				9,473
Issuance of preferred stock	299,527		(9,105)				290,422
Other, net		32	9,622		1,643		11,297
Balance at December 31, 2006 (8,280 848 shares of common stock issued; none in treasury)*	299,527	7,959	627,215	275,871		1,235,392	2,445,964
Add (deduct):							
Net earnings						299,070	299,070
Other comprehensive loss, net of tax:							
Retirement plans				167			167
Change in unrealized appreciation of				52,594			52,594

investments, net							
Comprehensive income				52,761		299,070	351,831
Dividends paid		159	58,315			(75,840)	(17,366)
Stock based compensation			1,144				1,144
Other, net	(47)	41	2,761			(1)	2,754
Balance at December 31, 2007 (8,322,348 shares of common stock issued; none in treasury)*	299,480	8,159	689,435	328,632		1,458,621	2,784,327
Add (deduct):							
Net earnings						147,971	147,971
Other comprehensive loss, net of tax:							
Retirement plans				361			361
Change in unrealized appreciation of investments, net				(241,744)			(241,744)
Comprehensive income				(241,383)		147,971	(93,412)
Dividends paid		163	55,988			(73,501)	(17,350)
Stock based compensation			2,941				2,941
Treasury stock purchase					(24,290)		(24,290)
Adjust gain on sale of subsidiary stock			(9,473)				(9,473)
Other, net	(51)	27	3,972			(2)	3,946
Balance at December 31, 2008 (8,349,284 shares of common stock issued; 76,513 in treasury)	**$ 299,429**	**$ 8,349**	**$ 742,863**	**$ 87,249**	**$ (24,290)**	**$ 1,533,089**	**$ 2,646,689**

* Amounts reflect subsequent common stock dividends.

See accompanying Notes to Consolidated Financial Statements.

ALLEGHANY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Cash Flows

	Years Ended December 31,		
	2008	2007	2006
	(in thousands)		
Cash flows from operating activities			
Net earnings	**$ 147,971**	$ 299,070	$ 247,903
Earnings from discontinued operations, net	**107,404**	11,528	6,956
Earnings from continuing operations	**40,567**	287,542	240,947
Adjustments to reconcile earnings from continuing operations to net cash provided by operating activities:			
Depreciation and amortization	**25,674**	16,275	11,674
Net realized capital (gains) losses	**92,168**	(92,766)	(28,212)
(Increase) decrease in other assets	**(37,117)**	(2,515)	(29,191)
(Increase) decrease in reinsurance receivable, net of reinsurance payable	**(41,604)**	116,257	482,467
(Increase) decrease in premium balances receivable	**17,671**	27,318	9,424
(Increase) decrease in ceded unearned premium reserves	**35,801**	90,098	43,294
(Increase) decrease in deferred acquisition costs	**3,870**	(8,286)	(12,736)
Increase (decrease) in other liabilities and current taxes	**(24,928)**	46,224	80,115
Increase (decrease) in unearned premiums	**(86,955)**	(102,873)	(4,880)
Increase (decrease) in losses and loss adjustment expenses	**198,889**	(25,469)	(342,936)
Net adjustments	**183,469**	64,263	209,019
Net cash provided by operating activities from continuing operations	**224,036**	351,805	449,966
Net cash provided by operating activities from discontinued operations	**106,510**	127,355	103,769
Net cash provided by operating activities	**330,546**	479,160	553,735
Cash flows from investing activities			
Purchase of investments	**(1,564,024)**	(1,336,433)	(1,436,265)
Sales of investments	**1,149,434**	824,305	298,408
Maturities of investments	**325,970**	284,666	283,095
Purchases of property and equipment	**(9,760)**	(4,884)	(4,251)
Net change in short-term investments	**(320,111)**	79,974	196,628
Other, net	**3,700**	4,640	9,270
Acquisition of majority- and minority-owned companies, net of cash acquired	**(50,816)**	(186,743)	(120,670)
Net cash provided by investing activities from continuing operations	**(465,607)**	(334,475)	(773,785)

Net cash provided by investing activities from discontinued operations	**151,607**	(152,076)	(91,998)
Net cash (used in) provided by investing activities	**(314,000)**	(486,551)	(865,783)
Cash flows from financing activities			
Proceeds from issuance of convertible preferred stock, net of issuance costs			290,422
Proceeds from issuance of subsidiary common stock, net of issuance costs			86,288
Treasury stock acquisitions	**(25,068)**		(39,186)
Principal payments on long-term debt		(80,000)	
Proceeds from repayment of note receivable		91,536	
Convertible preferred stock dividends paid	**(17,350)**	(17,367)	(8,342)
Tax benefit on stock based compensation	**2,330**	1,063	1,034
Other, net	**2,133**	3,626	2,406
Net cash provided by (used in) financing activities from continuing operations	**(37,955)**	(1,142)	332,622
Net cash provided by (used in) financing activities from discontinued operations	**(5,000)**	5,316	301
Net cash provided by (used in) financing activities	**(42,955)**	4,174	332,923
Cash flows of discontinued operations			
Operating activities	**(106,510)**	(127,355)	(103,769)
Investing activities	**88,398**	152,076	91,998
Financing activities	**5,000**	(5,316)	(301)
Net cash provided by (used in) discontinued operations	**(13,112)**	19,405	(12,072)
Net cash provided by (used in) continuing operations	**(39,521)**	16,188	8,803
Cash at beginning of period	**57,646**	41,458	32,655
Cash at end of period	**$ 18,125**	$ 57,646	$ 41,458
Supplemental disclosures of cash flow information			
Cash paid during the period for:			
Interest	**$ 200**	$ 505	$ 4,350
Income taxes paid (refunds received)	**$ 179,984**	$ 191,680	$ 105,282

See accompanying Notes to Consolidated Financial Statements.

ALLEGHANY CORPORATION AND SUBSIDIARIES
Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Principles

a. Principles of Financial Statement Presentation

Alleghany Corporation, a Delaware corporation, which together with its subsidiaries is referred to as Alleghany unless the context otherwise requires, 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 (Platte River) (collectively, CATA unless the context otherwise requires) and AIHL s majority-owned subsidiary, Employers Direct Corporation (EDC), of which AIHL owns approximately 98.5 percent. AIHL Re LLC (AIHL Re), a captive reinsurance subsidiary of AIHL, has, in the past, been available to provide reinsurance to Alleghany operating units and affiliates. In addition, Alleghany owns approximately 33 percent of the outstanding shares of common stock of Homesite Group Incorporated (Homesite), a national, full-service, mono-line provider of homeowners insurance, and approximately 40 percent of ORX Exploration, Inc. (ORX), a regional oil and gas exploration and production company. These investments are reflected in Alleghany s financial statements in other invested assets. Alleghany also owns and manages properties in Sacramento, California 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. Alleghany also owned approximately 55 percent of Darwin Professional Underwriters, Inc. (Darwin) until its disposition on October 20, 2008. Accordingly, the operations of Darwin have been reclassified as discontinued operations for all periods presented. See Note 2.

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.

During the third quarter of 2008, Alleghany identified an error in the amount of $15.0 million with respect to additional deferred tax liability that relates to prior periods. The $15.0 million specifically relates to the capital gains taxes incurred by Alleghany at the date of Darwin s disposition. GAAP requires that capital gains taxes be accrued for over time as income is reported, from the date of Darwin s initial public offering in May 2006 until the date of Darwin s disposition. As a result, for the year ended December 31, 2007, earnings from discontinued operations (as well as net earnings) were reduced by $6.2 million related to the portion of the $15.0 million attributable to 2007. Similarly, for the year ended December 31, 2006, earnings from discontinued operations and net earnings were reduced by $3.3 million. Similar corrections to earnings from discontinued operations and net earnings will be made in future reports for the three-month period ended March 31, 2008 and for the six-month period ended June 30, 2008 in the amounts of $2.9 million and $5.5 million, respectively. These corrections are not material to Alleghany s consolidated financial statements.

b. Investments

Investments consist of equity securities, debt securities, short-term investments and other invested assets. Alleghany classifies its equity securities, debt securities and short-term investments as available for sale. Debt securities consist of securities with an initial fixed maturity of more than one year. Short-term investments include

Notes to Consolidated Financial Statements, continued

1. Summary of Significant Accounting Principles, continued

commercial paper, certificates of deposit, money market instruments and any fixed maturity with an initial maturity of one year or less.

At December 31, 2008 and 2007, available-for-sale securities are recorded at fair value.

Unrealized gains and losses during the year, net of the related tax effect applicable to available-for-sale securities, are excluded from earnings and reflected in comprehensive income and the cumulative effect is reported as a separate component of stockholders equity until realized. A decline in the fair value of an available-for-sale security below its cost that is deemed other-than-temporary is charged to earnings.

Realized gains and losses on investments are determined in accordance with the specific identification method.

Other invested assets include strategic equity investments in operating companies which are accounted for under the equity method, and partnership investments which are accounted for as either available-for-sale or equity-method investments.

Premiums and discounts arising from the purchase of certain debt securities are treated as a yield adjustment over the estimated useful life of the securities, adjusted for anticipated prepayments using the retrospective interest method. Under this method, the effective yield on a security is estimated. Such estimates are based on the prepayment terms of the security, past actual cash flows and assumptions as to future expected cash flow. The future cash flow assumptions consider various prepayment assumptions based on historical experience, as well as current market conditions. Periodically, the effective yield is re-estimated to reflect actual prepayments and updated future cash flow assumptions. Upon a re-estimation, the security s book value is restated at the most recently calculated effective yield, assuming that yield had been in effect since the security was purchased. This treatment results in an increase or decrease to net investment income (amortization of premium or discount) at the new measurement date.

c. Derivative Financial Instruments

Alleghany entered into an interest rate swap for purposes of matching interest expense with interest income. The interest rate swap was accounted for as a hedge of the obligation. Interest expense was recorded using the revised interest rate. The interest rate swap matured in January 2007, at no gain or loss to Alleghany.

d. Cash

For purposes of the consolidated statements of cash flows and consolidated balance sheets, cash includes all deposit balances with a bank that are available for immediate withdrawal, whether interest-bearing or non-interest bearing.

e. Premiums and Unearned Premiums

Premiums are recognized as revenue on a pro-rata basis over the term of an insurance policy. This recognition method is based on the short term (twelve months or less) nature of the lines of business written by AIHL s insurance operating units, which consist of property and casualty and surety lines. Unearned premiums represent the portion of premiums written which are applicable to the unexpired terms of insurance policies in force.

Premium balances receivable are reported net of an allowance for estimated uncollectible premium amounts. Ceded premiums are charged to income over the applicable terms of the various reinsurance contracts with third-party reinsurers.

Notes to Consolidated Financial Statements, continued

1. Summary of Significant Accounting Principles, continued

f. Reinsurance Recoverables

AIHL s insurance operating units reinsure a significant portion of the risks they underwrite in order to mitigate their exposure to losses, manage capacity and protect capital resources. Reinsuring loss exposures does not relieve AIHL s insurance operating units from their obligations to policyholders. AIHL s insurance operating units remain liable to their policyholders for the portion reinsured to the extent that any reinsurer does not meet the obligations assumed under the reinsurance agreements. To minimize their exposure to losses from a reinsurer s inability to pay, AIHL s insurance operating units evaluate the financial condition of their reinsurers upon placement of the reinsurance and periodically thereafter.

Reinsurance recoverables (including amounts related to IBNR and prepaid reinsurance premiums) are reported as assets. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured business. Ceded premiums are charged to income over the applicable terms of the various reinsurance contracts with third-party reinsurers.

Reinsurance contracts that do not result in a reasonable possibility that the reinsurer may realize a significant loss from the insurance risk assumed and that do not provide for the transfer of significant insurance risk generally do not meet the conditions for reinsurance accounting and are accounted for as deposits. Alleghany currently does not have any reinsurance contracts that qualify for deposit accounting.

g. Deferred Acquisition Costs

Acquisition costs related to unearned premiums that vary with, and are directly related to, the production of such premiums (principally commissions, premium taxes, compensation and certain other underwriting expenses) are deferred. Deferred acquisition costs are amortized to expense as the related premiums are earned. Deferred acquisition costs amortized to expense in 2008 and 2007 were $155.2 million and $146.1 million, respectively.

Deferred acquisition costs are periodically reviewed to determine their recoverability from future income, including investment income, and if any such costs are determined to be not recoverable they are charged to expense. In the second quarter of 2008, EDC wrote-off its deferred acquisition cost asset of $2.1 million, primarily reflecting a significant acceleration in claims emergence and higher than anticipated increases in industry-wide severity.

h. Property and Equipment

Property and equipment is recorded at cost, net of accumulated depreciation and amortization. Depreciation of buildings and equipment is principally calculated using the straight-line method over the estimated useful life of the respective assets. Estimated useful lives for such assets range from 3 to 20 years. Amortization of leasehold improvements is principally calculated using the straight-line method over the estimated useful life of the leasehold improvement or the life of the lease, whichever is less. Rental expense on operating leases is recorded on a straight-line basis over the term of the lease, regardless of the timing of actual lease payments.

i. Goodwill and Other Intangible Assets

Goodwill and other intangible assets, net of amortization, is recorded as a result of business acquisitions. Other intangible assets that are not deemed to have an indefinite useful life are amortized over their estimated useful lives. Goodwill and other intangible assets deemed to have an indefinite useful life are tested annually in the fourth quarter of every year for impairment. Goodwill and other intangible assets are also tested whenever events and changes in circumstances suggest that the carrying amount may not be recoverable. A significant amount of judgment is required in performing goodwill and other intangible assets impairment tests. These tests include estimating the fair value of Alleghany s operating units and other intangible assets. With respect to goodwill, as required by Financial Accounting Standards Board Statement No. 142 (SFAS 142) a comparison is made between the estimated fair values of Alleghany s operating units with their respective carrying amounts

Notes to Consolidated Financial Statements, continued

1. Summary of Significant Accounting Principles, continued

including goodwill. Under SFAS 142, fair value refers to the amount for which the entire operating unit may be bought or sold. The methods for estimating operating unit values include asset and liability fair values and other valuation techniques, such as discounted cash flows and multiples of earnings or revenues. All of these methods involve significant estimates and assumptions. If the carrying value exceeds estimated fair value, there is an indication of potential impairment, and a second step is performed to measure the amount of impairment. The second step involves calculating an implied fair value of goodwill by measuring the excess of the estimated fair value of Alleghany s operating units over the aggregate estimated fair values of the individual assets less liabilities. If the carrying value of goodwill exceeds the implied fair value of goodwill, an impairment charge is recorded for the excess. Subsequent reversal of any goodwill impairment charge is not permitted.

In connection with impairment testing of goodwill and other intangible assets during the fourth quarter of 2008, Alleghany determined that the $48.7 million of goodwill associated with Alleghany s acquisition of EDC was impaired. As a result, as of December 31, 2008, Alleghany recorded a non-cash charge of $48.7 million, which is classified as a net realized capital loss in Alleghany s consolidated statement of earnings and represents the entire EDC goodwill balance at such date. See Note 4 for further information on this impairment as well as information on goodwill and other intangible assets.

j. Income Taxes

Alleghany files a consolidated federal income tax return with its subsidiaries. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

k. Loss Reserves

The reserves for losses and loss adjustment expenses represent management s best estimate of the ultimate cost of all reported and unreported losses incurred through the balance sheet date and include, but are not limited to: (i) the accumulation of individual estimates for claims reported on direct business prior to the close of an accounting period; (ii) estimates received from reinsurers with respect to reported claims which have been reinsured; (iii) estimates for claims incurred but not reported (IBNR) based on past experience modified for current trends and industry data; and (iv) estimates of expenses for investigating and settling claims based on past experience. The reserves recorded are based on estimates resulting from the review process, and differences between estimates and ultimate payments are reflected as an expense in the statement of earnings in the period in which the estimates are revised.

l. Revenue Recognition for Land Sales

Revenue and profits from land sales are recognized using the full accrual method when title has passed to the buyer, the collectibility of the sales price is reasonably assured, the required minimum cash down payment has been received and Alleghany has no continuing involvement with the property. Alleghany records land sales under the full accrual method as all requirements have been met.

m. Earnings Per Share of Common Stock

Basic earnings per share of common stock are based on the average number of shares of common stock, par value $1.00 per share, of Alleghany (Common Stock) outstanding during the years ended December 31, 2008, 2007 and 2006, respectively, retroactively adjusted for stock dividends. Diluted earnings per share of Common Stock are based on those shares used to calculate basic earnings per common share. Diluted earnings per share of

Notes to Consolidated Financial Statements, continued

1. Summary of Significant Accounting Principles, continued

Common Stock also include the dilutive effect of stock-based compensation awards, retroactively adjusted for stock dividends.

n. Share-Based Compensation Plans

Alleghany follows Statement of Financial Accounting Standards No. 123 (revised), Share Based Payment (SFAS 123R). SFAS 123R requires that the cost resulting from all share-based compensation transactions be recognized in the financial statements, establishes fair value as the measurement objective in accounting for share-based compensation arrangements, and requires the application of the fair value based measurement method in accounting for share-based compensation transactions with employees. SFAS 123R was adopted by Alleghany for awards made or modified on or after January 1, 2006. Prior to SFAS 123R, Alleghany followed Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (SFAS 123). SFAS 123 established accounting and reporting standards for share-based employee compensation plans and allowed companies to choose between the fair value based method of accounting as defined in SFAS 123 and the intrinsic value based method of accounting as prescribed by Accounting Principles Board Opinion No. 25 Accounting for Stock Issued to Employees (APB25). Alleghany had elected to continue to follow the intrinsic value based method of accounting for awards granted prior to 2003, and accordingly, no expense was recognized with respect to stock option grants. Effective January 1, 2003, Alleghany adopted the fair value based method of accounting of SFAS 123, using the prospective transition method for awards granted after January 1, 2003. The fair value based method under SFAS 123 is similar to that employed under SFAS 123R. The impact of the adoption of SFAS 123R on Alleghany s consolidated financial results and financial condition was immaterial. Both SFAS 123 and SFAS 123R treat non-employee directors as employees for accounting purposes.

With respect to stock option grants, the fair value of each option award is estimated on the date of grant using the Black-Scholes option pricing model that uses the assumptions noted in the following table. Expected volatilities are based on historical volatility of the Common Stock. Alleghany uses historical data to estimate option exercise and employee termination within the valuation model. The expected term of options granted is derived from the output of the option valuation model and represents the period of time that options granted are expected to be outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant.

	2008	2007	2006
Expected volatility	19%	18%	18%-19%
Expected dividends			
Expected term (in years)	10	8-10	7-8
Risk-free rate	3.8%	5.2%	3.2%-5.2%

See Note 10 for further information on stock option grants as well as information on all other types of share-based compensation awards.

o. Reclassification

Certain prior year amounts have been reclassified to conform to the 2008 presentation.

p. Recent Accounting Standards

Recently Adopted

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

Notes to Consolidated Financial Statements, continued

1. Summary of Significant Accounting Principles, continued

provisions of SFAS 157 as of January 1, 2008, and the implementation did not have any material impact on Alleghany s results of operations and financial condition. See Note 14.

In October 2008, Financial Accounting Standards Board Staff Position No. 157-3 (FSP FAS 157-3) was issued. FSP FAS 157-3 clarifies the application of SFAS 157 in an inactive market. If a market becomes inactive, then the fair value determination for securities in that market may be based on inputs that are unobservable in the market, rather than being based on either unadjusted quoted prices or observable market inputs. FSP FAS 157-3 is effective upon issuance, including periods for which financial statements have not been issued. Alleghany has adopted the provisions of FSP FAS 157-3 as of September 30, 2008, and the implementation did not have a material impact on its results of operations and financial condition. See Note 14.

Future Application of Accounting Standards

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 141). 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.

q. Statutory Accounting Practices

Alleghany s insurance operating units, domiciled principally in the States of California, New Hampshire, Delaware, Wisconsin and Nebraska, prepare statutory financial statements in accordance with the accounting practices prescribed or permitted by the insurance departments of the states of domicile. Prescribed statutory accounting practices are those practices that are incorporated directly or by reference in state laws, regulations and general administrative rules applicable to all insurance enterprises domiciled in a particular state. Permitted statutory accounting practices include practices not prescribed by the domiciliary state, but allowed by the domiciliary state regulatory authority. The impact of any permitted accounting practices on statutory surplus of Alleghany is not material.

2. Discontinued Operations

On October 20, 2008, Darwin, of which AIHL owned approximately 55 percent, merged with Allied World Assurance Company Holdings, Ltd. (AWAC) whereby AWAC acquired all of the issued and outstanding shares of Darwin common stock for cash consideration of $32.00 per share (the Transaction). At that time, Alleghany received aggregate proceeds of approximately $300 million in cash for AIHL s 9,371,096 shares of Darwin common stock. Alleghany recorded an after-tax gain from the Transaction of approximately $92.1 million in the 2008 fourth quarter, including approximately $9.5 million of gain deferred at the time of Darwin s initial public offering in May 2006.

Alleghany has classified the operations of Darwin as "discontinued operations" in its consolidated financial statements for all periods presented.

Notes to Consolidated Financial Statements, continued

2. Discontinued Operations, continued

Historical balance sheet information related to the discontinued operations of Darwin, as included in Alleghany s consolidated financial statements, is set forth in the following table (in millions):

	December 31, 2007
Assets	
Available-for-sale securities at fair value	$ 449.4
Short-term investments	107.6
Cash	7.5
Reinsurance recoverables	136.4
Ceded unearned premium reserves	43.2
Other	68.0
	$ 812.1
Liabilities	
Losses and loss adjustment expenses	$ 387.9
Unearned premiums	141.1
Debt	5.0
Other	23.9
Minority interest (carried at the AIHL level)	105.4
	663.3
Alleghany Equity	
Alleghany s investment in Darwin	148.8
	$ 812.1

Alleghany s investment in Darwin excludes the portion of Darwin s stockholders equity that is attributable to common stockholders other than Alleghany.

Notes to Consolidated Financial Statements, continued

2. Discontinued Operations, continued

Historical information related to the results of operations of the discontinued operations of Darwin, as included in Alleghany s consolidated financial statements, is set forth in the following table (in millions):

	January 1, 2008 Through October 19, 2008	Years Ended December 31, 2007	2006
Revenues			
Net premiums earned	$ 170.9	$ 180.9	$ 132.4
Net investment income	19.4	22.6	16.4
Net realized capital (losses)	(3.4)		
Other income	4.7		
	191.6	203.5	148.8
Costs and expenses			
Losses and loss adjustment expenses	67.6	101.3	88.6
Commission, brokerage and other underwriting expenses	65.2	50.9	36.4
Other operating expenses	17.9	5.9	0.7
	150.7	158.1	125.7
Earnings before income taxes and minority interest	40.9	45.4	23.1
Income taxes	11.0	13.2	7.2
Earnings before minority interest	29.9	32.2	15.9
Minority interest*	14.6	20.7	8.9
Net earnings	$ 15.3	$ 11.5	$ 7.0

* Represents the portion of Darwin s earnings that is attributable to common stockholders other than Alleghany, as well as parent capital gains taxes incurred (see Note 1a). These expense accruals were made at the AIHL level.

Earnings before income taxes and minority interest during the 2008 period include a $32.5 million release of prior accident year loss reserves ($21.1 million after tax and before minority interest), reflecting favorable loss emergence. Net earnings during the 2008 period excludes the gain recorded associated with the Transaction of approximately $92.1 million in the 2008 fourth quarter, including approximately $9.5 million of gain deferred at the time of Darwin s initial public offering in May 2006.

Notes to Consolidated Financial Statements, continued

3. Investments

Available-for-sale securities at December 31, 2008 and 2007 are summarized as follows (in millions):

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2008				
Consolidated				
Equity securities:				
Common stock	$ 453.5	$ 215.0	$ (48.7)	$ 619.8
Preferred stock	9.7			9.7
Debt securities:				
U.S. Government obligations	274.7	11.9		286.6
Mortgage and asset-backed securities	707.7	10.1	(63.3)	654.5
States, municipalities, political subdivisions	1,421.8	23.4	(11.1)	1,434.1
Foreign	172.5	6.6	(1.8)	177.3
Corporate bonds and other	205.1	4.1	(1.7)	207.5
	2,781.8	56.1	(77.9)	2,760.0
Short-term investments	636.2			636.2
	$ 3,881.2	$ 271.1	$ (126.6)	$ 4,025.7
Industry Segment				
AIHL insurance group	$ 3,624.0	$ 79.2	$ (125.9)	$ 3,577.3
Corporate activities	257.2	191.9	(0.7)	448.4
	$ 3,881.2	$ 271.1	$ (126.6)	$ 4,025.7

Notes to Consolidated Financial Statements, continued

3. Investments, continued

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2007				
Consolidated				
Equity securities:				
Common stock	$ 656.6	$ 504.0	$ (27.6)	$ 1,133.0
Preferred stock	34.8	9.7	(1.1)	43.4
Debt securities:				
U.S. Government obligations	282.8	6.6	(0.1)	289.3
Mortgage and asset-backed securities	693.1	5.3	(5.4)	693.0
States, municipalities, political subdivisions	1,149.1	11.2	(2.2)	1,158.1
Foreign	176.0	6.2	(0.1)	182.1
Corporate bonds and other	240.5	2.6	(0.9)	242.2
	2,541.5	31.9	(8.7)	2,564.7
Short-term investments	316.9			316.9
	$ 3,549.8	$ 545.6	$ (37.4)	$ 4,058.0
Industry Segment				
AIHL insurance group	$ 3,345.6	$ 186.1	$ (36.8)	$ 3,494.9
Corporate activities	204.2	359.5	(0.6)	563.1
	$ 3,549.8	$ 545.6	$ (37.4)	$ 4,058.0

The amortized cost and estimated fair value of debt securities at December 31, 2008 by contractual maturity are shown below (in millions). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Short-term investments due in one year or less	$ 636.2	$ 636.2
Mortgage and asset-backed securities	707.7	654.5
Debt securities		
One year or less	165.0	166.7

Over one through five years	978.5	1,002.4
Over five through ten years	337.1	344.2
Over ten years	593.5	592.2
Equity securities	463.2	629.5
	$ 3,881.2	$ 4,025.7

The proceeds from sales of available-for-sale securities were $1,149.4 million, $824.3 million and $298.4 million, in 2008, 2007 and 2006, respectively. The amounts of gross realized gains and gross realized losses of available-for-sale securities were, respectively, $259.9 million and $303.3 million in 2008, $103.1 million and $10.3 million in 2007 and $38.6 million and $10.4 million in 2006. The gross loss amounts include impairment charges, as discussed below.

Notes to Consolidated Financial Statements, continued

3. Investments, continued

Alleghany continually monitors the difference between cost and the estimated fair value of its investments, which involves uncertainty as to whether declines in value are temporary in nature. If a decline in the value of a particular investment is deemed temporary, Alleghany records the decline as an unrealized loss in common stockholders equity. If a decline is deemed to be other than temporary, it is written down to the carrying value of the investment and a realized loss is recorded on Alleghany s statement of earnings. Management s assessment of a decline in value includes, among other things, (i) the duration of time and the relative magnitude to which fair value of the investment has been below cost; (ii) the financial condition and near-term prospects of the issuer of the investment; (iii) extraordinary events, including negative news releases and rating agency downgrades, with respect to the issuer of the investment; and (iv) Alleghany s ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery. If that judgment changes in the future, Alleghany may ultimately record a realized loss after having originally concluded that the decline in value was temporary. If the review indicates that the declines were other-than-temporary, Alleghany would record a realized capital loss. A debt security is impaired if it is probable that Alleghany will not be able to collect all amounts due under the security s contractual terms. An equity investment is deemed impaired if, among other things, its decline in estimated fair value has existed for more than twelve months or more or if its decline in estimated fair value from its cost is greater than 50 percent, absent compelling evidence to the contrary. Further, for securities expected to be sold, an other-than-temporary impairment charge is recognized if Alleghany does not expect the fair value of a security to recover its cost prior to the expected date of sale.

Net realized capital gains in 2008 include $244.0 million of impairment charges related to unrealized losses that were deemed to be other than temporary and, as such, are required to be charged against earnings. Of the $244.0 million of impairment charges, $144.8 million related to energy sector (including refinery) equity holdings, $34.4 million related to financial sector equity holdings, $30.4 million related to construction sector equity holdings, $13.6 million related to mining sector equity holdings, $17.6 million related to equity holdings in other sectors and $3.2 million related to fixed income security holdings. The determination that unrealized losses on such securities were other than temporary was primarily based on the severity of the declines in fair value of such securities relative to cost as of the balance sheet date. Such severe declines are primarily related to a significant deterioration of U.S. equity market conditions during 2008. Net realized capital gains in 2007 and 2006 include $7.7 million and $4.7 million, respectively, of impairment charges related to unrealized losses that were deemed to be other than temporary and, as such, are required to be charged against earnings.

Notes to Consolidated Financial Statements, continued

3. Investments, continued

After adjusting the cost basis of securities for the recognition of unrealized losses through impairment charges, the gross unrealized investment losses and related fair value for debt securities and equity securities at December 31, 2008 and December 31, 2007, were as follows (in millions):

	Fair Value	Gross Unrealized Losses
2008		
Debt securities		
U.S. Government obligations		
Less than 12 months	$	$
More than 12 months		
Mortgage & asset-backed securities		
Less than 12 months	311.9	46.1
More than 12 months	57.0	17.2
States, municipalities & political subdivisions		
Less than 12 months	380.1	8.6
More than 12 months	20.9	2.5
Foreign		
Less than 12 months	54.9	1.8
More than 12 months		
Corporate bonds and other		
Less than 12 months	39.8	1.1
More than 12 months	11.4	0.6
Total debt securities		
Less than 12 months	786.7	57.6
More than 12 months	89.3	20.3
Equity securities		
Less than 12 months	151.5	48.7
More than 12 months		
Total temporarily impaired securities		
Less than 12 months	938.2	106.3
More than 12 months	89.3	20.3
Total	$ 1,027.5	$ 126.6

Notes to Consolidated Financial Statements, continued

3. Investments, continued

	Fair Value	Gross Unrealized Losses
2007		
Debt securities		
U.S. Government obligations		
Less than 12 months	$	$
More than 12 months	10.5	0.1
Mortgage & asset-backed securities		
Less than 12 months	167.7	2.5
More than 12 months	109.1	2.9
States, municipalities & political subdivisions		
Less than 12 months	129.5	0.6
More than 12 months	180.8	1.6
Foreign		
Less than 12 months	8.5	0.1
More than 12 months	1.0	
Corporate bonds and other		
Less than 12 months	51.9	0.6
More than 12 months	54.4	0.3
Total debt securities		
Less than 12 months	357.6	3.8
More than 12 months	355.8	4.9
Equity securities		
Less than 12 months	269.0	28.7
More than 12 months		
Total temporarily impaired securities		
Less than 12 months	626.6	32.5
More than 12 months	355.8	4.9
Total	$ 982.4	$ 37.4

As of December 31, 2008, Alleghany held a total of 423 debt and equity investments that were in an unrealized loss position, of which 42 investments, all related to debt securities, were in an unrealized loss position continuously for 12 months or more. At December 31, 2008, the weighted average credit rating of Alleghany s debt portfolio was AA+, with virtually all of Alleghany s debt securities rated investment grade.

At December 31, 2008, non-income producing invested assets were insignificant.

At December 31, 2008 and 2007, investments carried at fair value totaling $294.4 million and $261.0 million, respectively, were on deposit with various states or governmental agencies to comply with state insurance regulations.

Notes to Consolidated Financial Statements, continued

3. Investments, continued

Net investment income was as follows (in millions):

	2008	2007	2006
Interest income	$ 122.2	$ 135.1	$ 121.1
Dividend income	20.1	17.5	10.6
Investment expenses	(4.7)	(6.3)	(4.2)
Equity in earnings of Homesite, net of purchase accounting adjustments	0.3	4.0	
Other investment (loss) income	(7.7)	(4.2)	0.4
	$ 130.2	$ 146.1	$ 127.9

4. Acquisitions

(a) EDC

On July 18, 2007 (the Acquisition Date), AIHL completed its acquisition of EDC for a purchase price of approximately $198.1 million, including approximately $5.6 million of incurred acquisition costs. After giving effect to the transaction, AIHL owned approximately 98.5 percent of the common stock of EDC with EDC senior management owning the remainder. EDC is included as an insurance operating unit within AIHL for segment reporting purposes.

The acquisition has been accounted for by the purchase method of accounting in accordance with SFAS 141, and therefore, the assets acquired and liabilities assumed have been recorded at their estimated fair values at the Acquisition Date. Any excess of the purchase price over the estimated fair values of the assets acquired, including identifiable intangible assets, and liabilities assumed is recorded as goodwill. Acquired identifiable intangible assets include trade names and licenses, which were determined to have indefinite useful lives. Acquired identifiable assets also include renewal rights, distribution rights and database development, which are being amortized over the estimated useful lives of ten years, ten years, and twenty years, respectively. The net impact of amortization expenses and purchase accounting on Alleghany s net income is not material. The estimated fair value of assets acquired, including identifiable intangible assets, and liabilities assumed at the Acquisition Date was as follows (in millions):

Available-for-sale securities	$ 257.5
Goodwill	48.7*
Other intangible assets	13.9
All other assets	81.1
Total assets assumed	$ 401.2
Liabilities assumed (primarily loss and loss adjustment expenses)	203.1
Net assets acquired	$ 198.1

* In connection with impairment testing of goodwill and other intangible assets during the fourth quarter of 2008, Alleghany determined that the $48.7 million of goodwill associated with Alleghany s acquisition of EDC was impaired. As a result, as of December 31, 2008, Alleghany recorded a non-cash charge of $48.7 million, which is classified as a net realized capital loss in the consolidated statement of earnings and represents the entire EDC goodwill balance at such date. The estimation of EDC s fair value was based primarily on observing the stock market-based valuations of other publicly-traded insurance carriers. The factors that contributed to Alleghany s determination that the EDC goodwill was impaired include the recent unfavorable conditions in the U.S. economy and California workers compensation insurance market, combined with EDC s poor results during 2008. There was no resulting impact to Alleghany s tax balances as a result of this charge.

Notes to Consolidated Financial Statements, continued

4. Acquisitions, continued

(b) Homesite

On December 29, 2006, Alleghany, through its subsidiary AIHL, invested $120.0 million in Homesite, a national, full-service, mono-line provider of homeowners insurance. As consideration for its $120.0 million investment, Alleghany received 85,714 shares of the common stock of Homesite, representing approximately 33 percent of the Homesite common stock after giving effect to the investment. As part of its investment, Alleghany incurred $0.7 million of transactions costs.

The $120.7 million cost is comprised of the following elements: $102.5 million representing Alleghany s share of the fair values of assets acquired (consisting primarily of available-for-sale investment securities), less liabilities assumed (consisting primarily of loss and loss adjustment expense reserves and unearned premium reserves); $7.1 million of purchased intangible assets; and $11.1 million of goodwill. The goodwill is not deductible for tax purposes.

Homesite is reported as a component of other invested assets. Alleghany s interest in Homesite is included in corporate activities for segment reporting purposes, and is accounted for under the equity-method of accounting.

(c) ORX

On July 18, 2008, Alleghany, through its subsidiary Alleghany Capital Corporation, acquired approximately 40 percent of the voting interests of ORX, a regional oil and gas exploration and production company, through a purchase of preferred stock for cash consideration of $50.0 million. The $50.0 million cost includes $16.1 million of goodwill. The goodwill is not deductible for tax purposes. This investment is reflected in Alleghany s financial statements in other invested assets. Alleghany s interest in ORX is included in corporate activities for segment reporting purposes and is accounted for under the equity-method of accounting.

(d) Goodwill and Intangible Assets

The amount of goodwill and intangible assets, net of amortization expense, that is reported separately on Alleghany s consolidated balance sheets, and that arose from prior acquisitions of majority- or wholly-owned subsidiaries that are included in Alleghany s consolidated balance sheets at December 31, 2008 and 2007 are as follows (in millions):

	2008	2007
AIHL insurance group Goodwill	$ 45.1	$ 93.9
AIHL insurance group Intangible assets		
Agency relationships	$ 11.5	$ 11.5
State insurance licenses	26.1	26.1
Trade name	39.2	39.1
Brokerage and reinsurance relationships	21.4	23.7
Renewal and distribution rights	3.3	8.0
Other	4.6	5.2

	$ 106.1	$ 113.6

The economic useful lives of intangible assets are as follows: agency relationships 15 years; state insurance licenses indefinite; trade name indefinite; broker and reinsurance relationships 15 years; and renewal and distribution rights between 5 and 10 years. Accumulated amortization expense as of December 31, 2008 and 2007 is $46.0 million and $37.8 million, respectively.

Notes to Consolidated Financial Statements, continued

5. Reinsurance

(a) AIHL Reinsurance Recoverable

In the ordinary course of business, AIHL s insurance operating units purchase reinsurance in order to mitigate their exposure to losses, manage capacity and protect capital resources. If the assuming reinsurers are unable or unwilling to meet the obligations assumed under the applicable reinsurance agreements, AIHL s insurance operating units would remain liable to their policyholders for such reinsurance portion not paid by their reinsurers.

Reinsurance recoverables at December 31, 2008 and 2007 consist of the following (in millions):

	2008	2007
Reinsurance recoverables on paid losses	$ 48.1	$ 51.9
Ceded outstanding losses and loss adjustment expenses	1,008.3	966.8
Reinsurance recoverables	$ 1,056.4	$ 1,018.7

Approximately 93.7 percent of AIHL s reinsurance recoverables balance at December 31, 2008 was due from reinsurers having an A.M. Best financial strength rating of A (Excellent) or higher. Information regarding concentration of AIHL s reinsurance recoverables at December 31, 2008 is as follows (in millions except for percentages):

Reinsurer(1)	Rating(2)	Dollar Amount	Percentage
Swiss Reinsurance Company	A+ (Superior)	$ 192.1	18.2%
The Chubb Corporation	A++ (Superior)	$ 121.5	11.5%
Platinum Underwriters Holdings, Ltd.	A (Excellent)	$ 92.8	8.8%
All other reinsurers		$ 650.0	61.5%
Total		$ 1,056.4	100.0%

(1) Reinsurance recoverable amounts reflect amounts due from one or more reinsurance subsidiaries of the listed reinsurer.

(2) Represents the A.M. Best rating for the applicable reinsurance subsidiary or subsidiaries from which the reinsurance recoverable is due.

At December 31, 2008, AIHL also had fully collateralized reinsurance recoverables of $161.1 million due from Darwin, now a subsidiary of AWAC. The A.M. Best financial strength rating of Darwin was A (Excellent) at

December 31, 2008. AIHL had no allowance for uncollectible reinsurance as of December 31, 2008.

(b) Prior Year Acquisitions

In connection with the acquisition by Alleghany of Platte River in 2002 and the acquisition by RSUI Indemnity Company (RIC), a wholly-owned subsidiary of RSUI, of Landmark American Insurance Company (Landmark) in 2003 (discussed in more detail below), the sellers contractually retained all of the loss and loss adjustment expense liabilities. These contractual provisions constituted loss reserve guarantees as contemplated under EITF D-54, Accounting by the Purchasers for a Seller s Guaranty of the Adequacy of Liabilities for Losses and Loss Adjustment Expenses of an Insurance Enterprise Acquired in a Purchase Business Combination.

On January 3, 2002, Alleghany acquired Platte River from Swiss Re pursuant to a Stock Purchase Agreement dated as of December 5, 2001, and transferred Platte River to AIHL pursuant to a Contribution Agreement dated January 3, 2002. The Stock Purchase Agreement provides that Swiss Re shall indemnify and hold harmless Alleghany, AIHL and Platte River and their respective directors, officers and employees from and against any and all liabilities arising out of binders, policies and contracts of insurance issued by Platte River to the date of closing under the Stock Purchase Agreement. AIHL recorded a reinsurance recoverable and a corresponding loss reserve liability in the amount of $181.3 million at the time it acquired Platte River. Such reinsurance recoverables and

Notes to Consolidated Financial Statements, continued

5. Reinsurance, continued

loss reserve liability may change as losses are reported. Such amounts were $19.6 million, $28.7 million and $32.7 million for Platte River at December 31, 2008, 2007 and 2006, respectively.

On September 2, 2003, RIC acquired Landmark from Guaranty National Insurance Company (Guaranty National) pursuant to a Stock Purchase Agreement dated as of June 6, 2003. In contemplation of the sale of Landmark to RIC, Landmark and Royal Indemnity Company, an affiliate of Guaranty National (Royal Indemnity), entered into a 100 percent Quota Share Reinsurance Agreement and an Assumption of Liabilities Agreement, each dated as of September 2, 2003. Pursuant to these two agreements, Royal Indemnity assumed all of Landmark s liabilities of any nature arising out of or relating to all policies, binders and contracts of insurance issued in Landmark s name prior to the closing under the Stock Purchase Agreement, and all other liabilities of Landmark. The reinsurance recoverable and loss reserve liability recorded was $10.8 million, $17.7 million and $19.9 million at December 31, 2008, 2007 and 2006, respectively.

(c) AIHL Premium Activity

The following table indicates property and casualty premiums written and earned for the years ended December 31, 2008, 2007 and 2006 (in millions):

	Written	Earned
2008		
Premiums direct	$ 1,324.2	$ 1,409.7
Premiums assumed	$ 16.5	$ 17.2
Premiums ceded	$ 442.5	$ 478.2
2007		
Premiums direct	$ 1,488.9	$ 1,580.1
Premiums assumed	$ 17.9	$ 19.3
Premiums ceded	$ 544.3	$ 625.1
2006		
Premiums direct	$ 1,618.0	$ 1,548.1
Premiums assumed	$ 3.6	$ 4.8
Premiums ceded	$ 705.4	$ 675.1

In general, AIHL s insurance operating units obtain reinsurance on a treaty and facultative basis.

Ceded loss recoveries for AIHL included in Alleghany s consolidated statements of earnings were approximately $236.9 million, $214.6 million and $241.6 million at December 31, 2008, 2007 and 2006, respectively.

(d) RSUI

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. Under its surplus share treaties, which generally provide coverage on a risk attaching basis (the treaties cover policies which become effective during the treaty coverage period) from January 1 to December 31, RSUI is indemnified on a pro rata basis against covered property losses. The amount indemnified is based on the proportionate share of risk ceded after consideration of a stipulated dollar amount of line for RSUI to retain in relation to the entire limit written. RSUI ceded approximately 29 percent of its property gross premiums written in 2008 under these surplus share treaties. Under RSUI s 2008-2009 per risk reinsurance program, which generally provides coverage on an annual basis for losses occurring from May 1 to the following April 30, RSUI is reinsured for $90.0 million in excess of a $10.0 million net retention per risk after the application of the surplus share treaties and facultative reinsurance.

Notes to Consolidated Financial Statements, continued

5. Reinsurance, continued

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. RSUI placed all of its catastrophe reinsurance program for the 2008-2009 period. RSUI s 2008-2009 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. In addition, RSUI s property per risk reinsurance program for the 2008-2009 period provides RSUI with coverage 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.

RSUI reinsures its other lines of business through quota share treaties, except for professional liability and binding authority lines where, with the exception of property coverages written by binding authority lines which are covered under RSUI s catastrophe reinsurance program, RSUI retains all of such business. RSUI s quota share reinsurance treaty for umbrella/excess renewed on June 1, 2008 and provides coverage for policies with limits up to $30.0 million, with RSUI ceding 35 percent of the premium and loss for policies with limits up to $15.0 million and ceding 67.5 percent of the premium and loss for policies with limits in excess of $15.0 million up to $30.0 million. RSUI s primary casualty lines treaty renewed on April 15, 2008 and provides coverage for policies with limits up to $2.0 million, with RSUI ceding 25 percent of the premium and loss. RSUI s directors and officers (D&O) liability line quota share reinsurance treaty renewed on July 1, 2008 and provides coverage for policies with limits up to $20.0 million, with RSUI ceding 35 percent of the premium and loss for all policies with limits up to $10.0 million and ceding 60 percent of the premium and loss for policies with limits in excess of $10.0 million up to $20.0 million.

(e) AIHL Re

AIHL Re was formed in June 2006 as a captive reinsurance subsidiary of AIHL to provide catastrophe reinsurance coverage for RSUI. AIHL Re and RSUI entered into a reinsurance agreement, effective July 1, 2006, whereby AIHL Re, in exchange for market-based premiums, took that portion of RSUI s catastrophe reinsurance program not covered by third-party reinsurers. Because AIHL Re is a wholly-owned subsidiary of AIHL, there was no net reduction in Alleghany s catastrophe exposure on a consolidated basis as a result of RSUI s arrangement with AIHL Re. RSUI s reinsurance coverage with AIHL Re expired on April 30, 2007, and AIHL Re has not participated in RSUI s catastrophe reinsurance program since that date.

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. AIHL Re s participation in this agreement expired in April of 2008 and AIHL Re did not participate in Homesite s catastrophe reinsurance program in the 2008-2009 period.

(f) CATA

CATA uses reinsurance to protect against severity losses. In 2008, CATA reinsured individual property and casualty and contract surety risks in excess of $1.5 million with various reinsurers. The commercial surety line was reinsured for individual losses above $1.25 million. In addition, CATA purchases facultative reinsurance coverage for risks in excess of $6.0 million on property and casualty and $15.0 million on commercial surety.

(g) EDC

EDC uses reinsurance to protect against catastrophe losses. Effective December 31, 2008, EDC retained the first $1.0 million of loss per occurrence and purchased reinsurance with various reinsurers for $74.0 million above that level. Any loss above $75.0 million would be the sole responsibility of EDC. EDC uses various catastrophe models to assist it in determining the amount of reinsurance to purchase. All of EDC s 2008 reinsurance includes

Notes to Consolidated Financial Statements, continued

5. Reinsurance, continued

foreign and domestic terrorism coverage, although nuclear, chemical, biological and radiological (NCBR) events are excluded. EDC has a separate NCBR treaty under which it retains the first $5.0 million of loss from an NCBR event and reinsurance provides $10.0 million of coverage in excess of such retention. Under the Terrorism Act, EDC cannot exclude any form of terrorism from its workers compensation policies.

6. Liability for Loss and Loss Adjustment Expenses

Activity in liability for losses and loss adjustment expenses (LAE) in 2008, 2007 and 2006 is summarized as follows (in millions):

	2008	2007	2006
Balance at January 1	$ 2,379.7	$ 2,228.9	$ 2,571.9
Reserves acquired		165.0	
Less reinsurance recoverables on unpaid losses	966.8	1,101.4	1,619.0
Net balance	1,412.9	1,292.5	952.9
Incurred related to:			
Current year	612.8	480.1	420.0
Prior years	(42.8)	(31.1)	(9.7)
Total incurred	570.0	449.0	410.3
Paid related to:			
Current year	116.4	71.7	63.0
Prior years	296.2	256.9	172.7
Total paid	412.6	328.6	235.7
Net balance at December 31	1,570.3	1,412.9	1,127.5
Plus reinsurance recoverables on unpaid losses	1,008.3	966.8	1,101.4
Balance at December 31	$ 2,578.6	$ 2,379.7	$ 2,228.9

Total gross loss and LAE reserves increased by $198.9 million during 2008, from $2,379.7 million in 2007 to $2,578.6 million in 2008. Of this increase, $153.4 million was due to the casualty lines of business, $40.0 million was due to workers compensation line of business and $33.8 million was due to property lines of business. These increases were partially offset by a modest decrease in other 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 accident years at RSUI. Such increases for RSUI were partially offset by net releases of prior accident year reserves. The increase in workers compensation gross loss and LAE reserves primarily relates to increases to both current and prior accident year reserves by EDC. The increase in property gross loss and LAE reserves primarily reflects three significant catastrophe gross losses incurred by RSUI during the third quarter of 2008 (Hurricanes Ike, Gustav and Dolly). The decrease in other reserves is due primarily to a reduction in loss and LAE reserves acquired in connection with prior acquisitions which are ceded 100 percent to the sellers.

Total gross loss and LAE reserves increased by $150.8 million during 2007, from $2,228.9 million in 2006 to $2,379.7 million in 2007. Of this increase, $255.4 million was due to the casualty lines of business, $175.9 million was due to the workers compensation line of business, partially offset by a decrease in the reserves of the property lines of business. The increase in casualty gross loss and LAE reserves primarily reflects increased earned premium in D&O liability and professional liability, combined with limited paid loss activity for the current and prior casualty accident years at RSUI. Such increases for RSUI were partially offset by net releases of prior accident year reserves. The increase in workers compensation gross loss and LAE reserves primarily related to the

Notes to Consolidated Financial Statements, continued

6. Liability for Loss and Loss Adjustment Expenses, continued

acquisition of EDC during 2007. The decrease in gross loss and LAE reserves in the property lines of business primarily reflects a decrease in RSUI s reserves relating to the 2005 hurricane activity, as payments were made by RSUI and reinsurance recoveries were received by RSUI during 2007.

The above reserve changes included adjustments to prior year reserves. RSUI s net prior year reserves were reduced by $43.7 million in 2008 and $34.7 million in 2007. These adjustments were primarily for the professional liability and D&O liability lines of business, and reflected favorable loss emergence, compared with loss emergence patterns assumed in earlier periods for such lines of business.

In addition, RSUI s net prior year property reserves were increased by $43.2 million in 2007 related primarily to its 2005 Hurricane Katrina reserve estimates. The increase reflects the results of a review of Katrina loss and loss adjustment expense reserves in light of the current uncertain legal environment. RSUI reviews its reserves quarterly. In 2007, settlements of pending claims were larger than expected, which contributed to RSUI s decision to increase reserves for its remaining pending Hurricane Katrina claims.

For CATA, net prior year reserves were reduced by $11.8 million in 2008 and $14.4 million in 2007. The releases primarily reflect favorable loss emergence principally in its casualty and commercial surety lines of business, compared with loss emergence patterns assumed in earlier periods.

For EDC, net prior year workers compensation reserves were increased in 2008 by $25.4 million for prior accident years. In addition, net current year workers compensation reserves were increased by $10.5 million. The increases for both the prior accident years and the current accident year primarily reflect a significant acceleration in claims emergence and higher than anticipated increases in industry-wide severity. In 2007, EDC net workers compensation reserves were reduced by $9.7 million, consisting of an $18.8 million decrease for prior accident years partially offset by a $9.1 million increase for the 2007 year through the date of the acquisition by AIHL. The reduction for prior years reflected favorable loss emergence, compared with loss emergence patterns assumed in earlier years. The increase for 2007 through the date of acquisition reflected unfavorable loss emergence patterns, compared with loss emergence patterns assumed in the period prior to the acquisition.

7. Credit Agreement

In October 2006, Alleghany entered into a three-year unsecured credit agreement (the Credit Agreement) with a bank syndicate, providing commitments for revolving credit loans in an aggregate principal amount of up to $200.0 million. Borrowings under the Credit Agreement will be available for working capital and general corporate purposes. At Alleghany s option, borrowings under the Credit Agreement will bear interest at either (x) the higher of (i) the administrative agent s prime commercial lending rate or (ii) the federal funds rate plus 0.50 percent, or (y) the London Interbank Overnight Rate plus a margin (currently 65 basis points) based on Alleghany s Standard & Poors and/or Moody s rating. The Credit Agreement requires that all loans shall be repaid in full no later than the October 23, 2009 (the Maturity Date), although Alleghany may request up to two one-year extensions of the Maturity Date subject to meeting certain conditions and upon agreement of the Lenders. The Credit Agreement requires Alleghany, among other things, to maintain tangible net worth of not less than approximately $1.9 billion, limit the amount of certain other indebtedness, and maintain certain levels of unrestricted liquid assets. Such agreement also contains restrictions with respect to mortgaging or pledging any of Alleghany s assets and the consolidation or merger with any other corporation. At December 31, 2008, Alleghany was in full compliance with these requirements and restrictions. The

Credit Agreement charges Alleghany a commitment fee of 15 basis points (0.15 percent) per annum of the unused commitment. There were no borrowings under the Credit Agreement in 2008.

Notes to Consolidated Financial Statements, continued

8. Income Taxes

Income tax expense (benefit) from continuing operations consists of the following (in millions):

	Federal	**State and Foreign**	**Total**
2008			
Current	$ 84.3	$ 1.7	$ 86.0
Deferred	(63.5)	(2.0)	(65.5)
	$ 20.8	$ (0.3)	$ 20.5
2007			
Current	$ 166.9	$ 3.6	$ 170.5
Deferred	(24.5)	(1.2)	(25.7)
	$ 142.4	$ 2.4	$ 144.8
2006			
Current	$ 142.4	$ 2.8	$ 145.2
Deferred	(47.0)	0.7	(46.3)
	$ 95.4	$ 3.5	$ 98.9

The difference between the federal income tax rate and the effective income tax rate on continuing operations is as follows:

	2008	2007	2006
Federal income tax rate	35.0%	35.0%	35.0%
Change in estimates and other true ups	(0.7)	1.2	(4.2)
Income subject to dividends-received deduction	(6.8)	(0.8)	(0.7)
Tax-exempt interest	(22.2)	(2.5)	(2.3)
State taxes, net of federal tax benefit		0.4	0.9
Goodwill impairment	27.9		
Other, net	0.4	0.2	0.4
	33.6%	33.5%	29.1%

The effective income tax rate on continuing operations in 2008 primarily reflects the impact of significant catastrophe losses incurred and unrealized losses on investments that were deemed to be other than temporary in the 2008 period, partially offset by the impact of non-deductible goodwill impairment charges. The tax effects of

Notes to Consolidated Financial Statements, continued

8. Income Taxes, continued

temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2008 and 2007 are as follows (in millions):

	2008	2007
Deferred tax assets		
Foreign tax credit carry forward	$ 1.1	$ 4.8
State net operating loss carry forward	15.0	14.8
Reserves for impaired assets	2.3	1.7
Expenses deducted for tax purposes when paid	1.8	1.6
Other-than-temporary impairment	69.5	4.0
Property and casualty loss reserves	66.5	59.7
Unearned premium reserves	31.5	35.6
Performance shares	1.9	3.6
Unrealized loss on investments	20.6	
Compensation accruals	43.7	46.9
Other	4.5	2.8
Deferred tax assets	258.4	175.5
Valuation allowance	(14.5)	(14.3)
Total net deferred tax asset	$ 243.9	$ 161.2
Deferred tax liabilities		
Unrealized gain on investments	$ 68.7	$ 178.2
Tax over book depreciation	1.4	1.2
Deferred gains	2.1	1.9
Burlington Northern redemption	4.2	7.1
Deferred acquisition costs	25.9	27.6
Purchase accounting adjustments	10.8	11.8
Other	0.5	5.0
Total deferred tax liabilities	113.6	232.8
Net deferred tax (assets) liabilities	$ (130.3)	$ 71.6

Alleghany sold World Minerals, Inc. (World Minerals) on July 14, 2005. As a result of the sale and Section 338(h)(10) election, Alleghany was able to retain certain tax benefits, including an estimated foreign tax credit carryover generated by World Minerals. In the first quarter of 2006, Alleghany adopted and implemented a formal plan which it believed would allow it to fully use such credits commencing in 2007, at which time a $10.8 million net benefit was recorded to earnings. Based on an analysis of its foreign tax credits and related information, completed in the fourth quarter of 2007, Alleghany adjusted its estimate of foreign tax credits and recorded a net tax adjustment of $5.2 million.

A valuation allowance is provided against deferred tax assets when, in the opinion of Alleghany management, it is more likely than not that some portion of the deferred tax asset will not be realized. Accordingly, a valuation allowance is maintained for certain state tax items. Specifically, in 2006, Alleghany recognized $13.9 million of additional deferred tax assets for state net operating loss carryovers. A valuation allowance of $13.9 million was established at that time since Alleghany does not currently anticipate generating sufficient income in the various states to absorb these loss carryovers.

Notes to Consolidated Financial Statements, continued

8. Income Taxes, continued

Alleghany s 2006 and 2007 income tax returns remain open to examination.

9. Stockholders Equity

(a) Mandatory Convertible Preferred Stock

On June 23, 2006, Alleghany completed an offering of 1,132,000 shares of its 5.75 percent mandatory convertible preferred stock (the Preferred Stock) at a public offering price of $264.60 per share, resulting in net proceeds of $290.4 million. The annual dividend on each share of Preferred Stock is $15.2144. Dividends on the Preferred Stock accrue and accumulate from the date of issuance, and, to the extent Alleghany is legally permitted to pay dividends and Alleghany s Board of Directors declares a dividend payable, Alleghany will pay dividends in cash on a quarterly basis. Each share of Preferred Stock has a liquidation preference of $264.60, plus any accrued, cumulated and unpaid dividends. Each share of Preferred Stock will automatically convert on June 15, 2009 into between 0.8475 and 1.0000 shares of Alleghany s Common Stock depending on the average market price per share of Common Stock over the 20 trading day period ending on the third trading day prior to such date. The conversion rate will also be subject to anti-dilution adjustments. At any time prior to June 15, 2009, holders of the Preferred Stock may elect to convert each share of Preferred Stock into 0.8475 shares of Common Stock, subject to anti-dilution adjustments. All of the above data has not been adjusted for subsequent stock dividends.

(b) Treasury Stock

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. In November 2008, the authorization to repurchase Alleghany common stock was expanded to include repurchases of Alleghany s 5.75% Mandatory Convertible Preferred Stock. During 2008, Alleghany purchased an aggregate of 78,817 shares of its common stock in the open market for approximately $25.1 million, at an average price per share of $318.05. As of December 31, 2008, Alleghany held 76,513 shares of treasury stock.

(c) Regulatory Matters

At December 31, 2008, approximately $785.8 million of the equity of all of Alleghany s subsidiaries was available for dividends or advances to Alleghany at the parent level. At that date, approximately $1.4 billion of the Alleghany s total equity of $2.7 billion was unavailable for dividends or advances to Alleghany from its subsidiaries. With respect to AIHL s insurance operating units, they are subject to various regulatory restrictions that limit the maximum amount of dividends available to be paid by them without prior approval of insurance regulatory authorities. Of the aggregate total equity of Alleghany s insurance operating units at December 31, 2008 of $1.6 billion, a maximum of $233.3 million was available for dividends without prior approval of the applicable insurance regulatory authorities. Additionally, payments of dividends (other than stock dividends) by Alleghany to its stockholders are permitted by the terms of its Credit Agreement provided that Alleghany maintains certain financial ratios as defined in the agreement. At December 31, 2008, approximately $455.8 million of stockholders equity was available for dividends by Alleghany to its stockholders.

Statutory net income of Alleghany s insurance operating units was $(42.4) million and $307.7 million for the years ended December 31, 2008 and 2007, respectively. Combined statutory capital and surplus of Alleghany s insurance operating units was $1,343.5 million and $1,539.5 million at December 31, 2008 and 2007, respectively.

10. Share-Based Compensation Plans

(a) General

As of December 31, 2008, Alleghany had share-based payment plans for parent-level employees and directors. As described in more detail below, parent-level share-based payments to current employees consist only

Notes to Consolidated Financial Statements, continued

10. Share-Based Compensation Plans, continued

of restricted stock awards, including units, and performance share awards, and no stock options. Parent-level share-based payments to non-employee directors consist of annual awards of stock options and restricted stock, including restricted stock units. In addition, as of December 31, 2008, RSUI and EDC had their own share-based payment plans, which are described below.

Amounts recognized as compensation expense in the consolidated statements of earnings and comprehensive income with respect to share-based awards under plans for parent-level employees and directors were $9.1 million, $11.7 million and $14.3 million in 2008, 2007 and 2006, respectively. The amount of related income tax benefit recognized as income in the consolidated statements of earnings and comprehensive income with respect to these plans was $3.2 million, $4.1 million and $5.0 million in 2008, 2007 and 2006, respectively. In 2008, 2007 and 2006, $6.8 million, $18.5 million and $6.0 million of Common Stock, at fair market value, respectively, and $3.9 million, $13.2 million and $3.5 million of cash, respectively, was paid by Alleghany under plans for parent-level employees and directors. As noted above, as of December 31, 2008 and December 31, 2007, all outstanding awards were accounted for under the fair value based method of accounting.

Alleghany does not have an established policy or practice of repurchasing shares of its Common Stock in the open market for the purpose of delivering Common Stock upon the exercise of stock options. Alleghany issues authorized but not outstanding shares of Common Stock to settle option exercises in those instances where the number of shares it has repurchased are not sufficient to settle an option exercise.

(b) Director Stock Option and Restricted Stock Plans

Alleghany provided, through its Amended and Restated Directors Stock Option Plan (under which options were granted through May 1999) and its 2000 Directors Stock Option Plan (which expired on December 31, 2004), for the automatic grant of non-qualified options to purchase 1,000 shares of Common Stock in each year after 1987 to each non-employee director. Currently, Alleghany s 2005 Directors Stock Plan (the 2005 Plan) provides for the automatic grant of nonqualified options to purchase 500 shares of Common Stock, as well as an automatic grant of 250 shares of restricted Common Stock or under certain circumstances, restricted stock units, to each non-employee director on an annual basis. In 2008 and 2007, Alleghany awarded a total of 2,250 restricted shares and units and 2,295 restricted shares and units, respectively, which vest over a one-year period.

A summary of option activity under the above plans as of December 31, 2008, and changes during the year then ended is presented below:

Options	Shares (000)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value ($ millions)
Outstanding at January 1, 2008	71	$ 194		
Granted	5	348		

Exercised	(14)		177			
Forfeited or expired						
Outstanding at December 31, 2008	62	$	209	4.0	$	5.2
Exercisable at December 31, 2008	53	$	187	3.2	$	5.2

The weighted-average grant-date fair value of options granted during the years 2008, 2007 and 2006, was $136.77, $136.32 and $89.73, respectively. The total intrinsic value of options exercised during the years ended December 31, 2008, 2007 and 2006, was $2.1 million, $2.2 million and $2.4 million, respectively.

Notes to Consolidated Financial Statements, continued

10. Share-Based Compensation Plans, continued

A summary of the status of Alleghany s nonvested shares as of December 31, 2008, and changes during the year ended December 31, 2008, is presented below:

Nonvested Shares	**Shares (000)**		**Weighted-Average Grant-Date Fair Value**
Nonvested at January 1, 2008	8	$	120.57
Granted	5		136.77
Vested	(4)		113.20
Forfeited			
Nonvested at December 31, 2008	9	$	132.00

As of December 31, 2008, there was $0.8 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the 2005 Plan. That cost is expected to be recognized over a weighted-average period of approximately one year. The total fair value of shares vested during the years ended December 31, 2008, 2007 and 2006, was $1.2 million, $1.5 million and $1.9 million, respectively.

(c) Alleghany 2002 and 2007 Long-Term Incentive Plans

Alleghany provided incentive compensation to management through its 2002 Long-Term Incentive Plan (the 2002 LTIP) until December 31, 2006 when the 2002 LTIP expired. In December 2006, Alleghany adopted the 2007 Long-Term Incentive Plan (the 2007 LTIP) which was approved by Alleghany stockholders in April 2007. The provisions of the 2002 LTIP and 2007 LTIP are substantially similar. Awards under the 2002 LTIP and 2007 LTIP may include, but are not limited to, cash and/or shares of Common Stock, rights to receive cash and/or shares of Common Stock, and options to purchase shares of Common Stock including options intended to qualify as incentive stock options under the Internal Revenue Code and options not intended to so qualify. Under the 2002 LTIP and 2007 LTIP, the following types of awards are outstanding:

(i) Performance Share Awards Participants are entitled, at the end of a four-year award period, to a maximum amount equal to the value of one and one-half shares of Common Stock for each performance share issued to them based on market value on the payment date. In general, performance share payouts will be made in cash to the extent of minimum statutory withholding requirements in respect of an award, with the balance in Common Stock. Payouts are made provided defined levels of performance are achieved. As of December 31, 2008, 73,139 performance shares were outstanding. Expense is recognized over the performance period on a pro rata basis.

(ii) *Restricted Share Awards* Alleghany has awarded to certain management employees restricted shares of Common Stock. These awards entitle the participants to a specified maximum amount equal to the value of one share of Common Stock for each restricted share issued to them based on the market value on the payment date. In most instances, payouts are made provided defined levels of performance are achieved. As of December 31, 2008, 57,911 restricted shares were outstanding, of which none were granted in 2008, 3,816 were granted in 2007, 32,013 were granted in 2004 and 22,082 were granted in 2003. The expense is recognized ratably over the performance period, which can be extended under certain circumstances. The 2004 awards are expected to vest over five years.

(d) RSUI Restricted Share Plan

RSUI has a Restricted Stock Unit Plan (the RSUI Plan) for the purpose of providing equity-like incentives to key employees. Under the RSUI Plan, restricted stock units (units) are issued. Additional units, defined as the Deferred Equity Pool, were issued in 2008, 2007 and 2006, and may be created in the future if certain financial performance measures are met. Units may only be settled in cash. The fair value of each unit is calculated pursuant to SFAS 123R, as stockholder s equity of RSUI, adjusted for certain capital transactions and accumulated

Notes to Consolidated Financial Statements, continued

10. Share-Based Compensation Plans, continued

compensation expense recognized under the RSUI Plan, divided by the sum of RSUI common stock outstanding and the original units available under the RSUI Plan. The units vest on the fourth anniversary of the date of grant and contain certain restrictions, relating to, among other things, forfeiture in the event of termination of employment and transferability. In 2008, 2007 and 2006, RSUI recorded \$21.7 million, \$43.9 million and \$34.8 million, respectively, in compensation expense related to the RSUI Plan. During the same periods, a deferred tax benefit of \$7.6 million, \$15.4 million and \$12.2 million, respectively, related to the compensation expense was recorded.

(e) EDC Share Plans

EDC has a share-based payment plan for each of its two senior executives. Under the plans, EDC reserved 4,000 of its authorized common shares (approximating 1.6 percent of all shares currently outstanding). These restricted stock awards generally vest depending on the compound annual growth rate of EDC s equity, with the earliest vesting date being December 31, 2011 through December 31, 2016. If a minimum of 7 percent growth rate is not achieved by December 31, 2016, all restricted stock will be forfeited. The plan resulted in a nominal accrual for compensation expense in 2007, which was subsequently reversed in 2008.

11. Employee Benefit Plans

(a) Alleghany Employee Defined Benefit Pension Plans

Alleghany has two unfunded noncontributory defined benefit pension plans for executives, and a smaller, funded noncontributory defined benefit pension plan for employees.

The primary executive plan currently provides for designated employees (including all of Alleghany s current executive officers) retirement benefits in the form of an annuity for the joint lives of the participant and his or her spouse or, alternatively, actuarially equivalent forms of benefits, including a lump sum. Under both executive plans, a participant must have completed five years of service with Alleghany before he or she is vested in, and thus has a right to receive, any retirement benefits following his or her termination of employment. The annual retirement benefit under the primary executive plan, if paid in the form of a joint and survivor life annuity to a participant who retires on reaching age 65 with 15 or more years of service, is equal to 67 percent of the participant s highest average annual base salary and related annual incentive award over a consecutive three-year period during the last ten years or, if shorter, the full calendar years of employment. Neither plan takes other payments or benefits, such as payouts of long-term incentives, into account in computing retirement benefits. During 2004, both plans were amended and changed from a funded to an unfunded plan resulting in the distribution of all accrued benefits to vested participants.

With respect to the funded employee plan, Alleghany s policy is to contribute annually the amount necessary to satisfy the Internal Revenue Service s funding requirements. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

Notes to Consolidated Financial Statements, continued

11. Employee Benefit Plans, continued

The following tables set forth the defined benefit plans funded status at December 31, 2008 and 2007 and total cost for each of the three years ended December 31, 2008 (in millions, except percentages):

	2008	2007
OBLIGATIONS AND FUNDING STATUS:		
Change benefit obligation		
Benefit obligation at beginning of year	$ 17.3	$ 13.9
Service cost	2.9	2.4
Interest cost	0.9	0.8
Amendments		
SFAS 88 curtailment loss		
Actuarial loss	0.5	0.3
Benefits paid	(1.3)	(0.1)
Projected benefit obligation at end of year	20.3	17.3
Change in plan assets		
Fair value of plan assets at beginning of year	2.3	2.1
Actual return on plan assets, net of expenses	0.4	0.2
Company contributions	1.2	0.1
Benefits paid	(1.3)	(0.1)
Fair value of plan assets at end of year	2.6	2.3
Funded status	$ (17.7)	$ (15.0)
Amounts recognized in statement of financial position consists of:		
Prepaid benefit cost	$ 0.8	$ 0.8
Accrued benefit liability	(14.4)	(11.6)
Accumulated other comprehensive income	(4.1)	(4.2)
Net amount recognized	$ (17.7)	$ (15.0)
Weighted average asset allocations		
Debt securities	100%	100%

Notes to Consolidated Financial Statements, continued

11. Employee Benefit Plans, continued

	2008	2007	2006
COST AND OTHER COMPREHENSIVE INCOME:			
Net pension cost included the following expense (income) components			
Service cost benefits earned during the year	$ 2.9	$ 2.3	$ 1.8
Interest cost on benefit obligation	0.9	0.8	0.5
Expected return on plan assets	(0.1)	(0.1)	(0.1)
Net amortization and deferral	0.2	0.2	0.1
Net periodic pension cost	3.9	3.2	2.3
SFAS 88 curtailment loss			1.0
SFAS 88 settlement charge	0.2		
Total cost	4.1	3.2	3.3
Change in other comprehensive income (pension-related)	(0.1)		0.1
Net periodic pension cost and other comprehensive income	$ 4.0	$ 3.2	$ 3.4

	2008	2007	2006
ASSUMPTIONS:			
Assumptions used in computing the net periodic pension cost of the plans is as follows			
Rates for increases in compensation levels	4.00%	4.00%	4.00%
Weighted average discount rates	6.00%	5.75%	5.50%
Expected long-term rates of return	5.00%	4.00%	4.00%
Assumptions used in computing the funded status of the plans is as follows			
Rates for increases in compensation levels	4.00%	4.00%	4.00%
Weighted average discount rates	6.00%	6.00%	5.75%

Discount rates were predicated primarily on Moody s Investor Service Aa long-term corporate bond index, rounded to the nearest 25 basis points. Alleghany s investment policy with respect to its defined benefit plans is to provide long-term growth combined with a steady income stream. The target allocation is 100 percent in debt securities. The overall long-term, rate-of-return-on-assets assumptions are based on historical investment returns.

Contributions of less than $0.1 million are expected to be made to Alleghany s funded employee plan during 2009.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be made (in millions):

2009	$ 2.3
2010	4.5
2011	0.1
2012	0.1
2013	0.1
2014-2018	0.5

The measurement date used to determine pension benefit plans is December 31, 2008.

Notes to Consolidated Financial Statements, continued

11. Employee Benefit Plans, continued

(b) Other Employee Retirement Plans

Alleghany has two unfunded retiree health plans, one for executives and one for employees. Participants eligible for benefits must be age 55 or older. In addition, non-executive employees must have completed at least 10 years of service. Under the plans, participants must pay a portion of the premiums charged by the medical insurance provider. All benefits cease upon retiree death. RSUI also has an unfunded retiree health plan for its employees. As of December 31, 2008 and December 31, 2007, the liability for all of these plans was $4.3 million and $4.1 million, respectively, representing the entire accumulated postretirement benefit obligation as of that date. Assumptions used on the accounting for these plans are comparable to those cited above for the Alleghany pension plans. Future benefit payments associated with these plans are not expected to be material to Alleghany.

Alleghany provides supplemental retirement benefits through deferred compensation programs and profit sharing plans for certain of its officers and employees. In addition, Alleghany s subsidiaries sponsor both qualified defined contribution retirement plans for substantially all employees, including executives, and non-qualified plans only for executives, both of which provide for voluntary salary reduction contributions by employees and matching contributions by each respective subsidiary, subject to specified limitations.

Alleghany has endorsement split-dollar life insurance policies for its officers that are effective during employment as well as retirement. Premiums are paid by Alleghany, and death benefits are split between Alleghany and the beneficiaries of the officers. Death benefits for current officers that inure to the beneficiaries are generally equal to four times the annual salary at the time of an officer s death. After retirement, death benefits that inure to the beneficiaries are generally equal to the annual ending salary of the officer at the date of retirement.

(c) Recently Adopted Accounting Standard

FASB Statement No. 158 (SFAS 158) was issued in September 2006 and adopted by Alleghany as of December 31, 2006. SFAS 158 requires an employer to: (a) recognize in its statement of financial position an asset for a plan s overfunded status or a liability for a plan s underfunded status; (b) measure a plan s assets and its obligations that determine its funded status as of the end of the employer s fiscal year (with limited exceptions); and (c) recognize changes in the funded status of a defined benefit postretirement plan in the year in which the changes occur. The changes are to be reported in comprehensive income as of December 31, 2006. Past standards only required an employer to disclose the complete funded status of its plans in the notes to the financial statements.

Notes to Consolidated Financial Statements, continued

12. 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 years ended December 31 (in millions, except share amounts):

	2008	2007	2006
Net earnings	$ 148.0	$ 299.1	$ 247.9
Preferred dividends	17.2	17.2	9.0
Income available to common stockholders for basic earnings per share	130.8	281.9	238.9
Preferred dividends		17.2	9.0
Effect of other dilutive securities		0.3	0.5
Income available to common stockholders for diluted earnings per share	$ 130.8	$ 299.4	$ 248.4
Weighted average shares outstanding applicable to basic earnings per share	8,313,591	8,309,953	8,299,847
Preferred stock		997,969	543,425
Effect of other dilutive securities		23,352	23,002
Adjusted weighted average shares outstanding applicable to diluted earnings per share	8,313,591	9,331,274	8,866,274

Contingently issuable shares of 1,147,351, 59,035 and 89,965 were potentially available during 2008, 2007 and 2006, 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.

13. Commitments and Contingencies

(a) Leases

Alleghany leases certain facilities, furniture and equipment under long-term lease agreements. In addition, certain land, office space and equipment are leased under noncancelable operating leases that expire at various dates through 2020. Rent expense was $10.3 million, $8.7 million and $7.1 million in 2008, 2007 and 2006, respectively.

The aggregate minimum payments under operating leases with initial or remaining terms of more than one year as of December 31, 2008 were as follows (in millions):

	Aggregate Minimum

Year	Lease Payments
2009	$ 9.7
2010	8.3
2011	8.1
2012	8.2
2013	8.4
2014 and thereafter	37.2

Notes to Consolidated Financial Statements, continued

13. Commitments and Contingencies, continued

(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 $20.4 million of gross reserves and $20.3 million of net reserves at December 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. Reserves for asbestos and environmental impairment claims cannot be estimated with traditional loss reserving techniques because of uncertainties that are greater than those associated with other types of claims. Factors contributing to those uncertainties include a lack of historical data, the significant periods of time that often elapse between the occurrence of an insured loss and the reporting of that loss to the ceding company and the reinsurer, uncertainty as to the number and identity of insureds with potential exposure to such risks, unresolved legal issues regarding policy coverage, and the extent and timing of any such contractual liability. Loss reserve estimates for such environmental and asbestos exposures include case reserves, which also reflect reserves for legal and other loss adjustment expenses and IBNR reserves. IBNR reserves are determined based upon historic general liability exposure base and policy language, previous environmental loss experience and the assessment of current trends of environmental law, environmental cleanup costs, asbestos liability law and judgmental settlements of asbestos liabilities.

For both asbestos and environmental reinsurance claims, CATA establishes case reserves by receiving case reserve amounts from its ceding companies, and verifies these amounts against reinsurance contract terms, analyzing from the first dollar of loss incurred by the primary insurer. In establishing the liability for claims for asbestos related liability and for environmental impairment claims, management considers facts currently known and the current state of the law and coverage litigation. Additionally, ceding companies often report potential losses on a precautionary basis to protect their rights under the reinsurance arrangement, which generally calls for prompt notice to the reinsurer. Ceding companies, at the time they report such potential losses, advise CATA of the ceding companies current estimate of the extent of such loss. CATA s claims department reviews each of the precautionary claims notices and, based upon current information, assesses the likelihood of loss to CATA. Such assessment is one of the factors used in determining the adequacy of the recorded asbestos and environmental reserves. 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 December 31, 2008.

(d) Indemnification Obligations

In connection with the sale of World Minerals, Alleghany undertook certain indemnification obligations pursuant to the Stock Purchase Agreement including a general indemnification provision for breaches of representations and warranties set forth in the Stock Purchase Agreement (the Contract Indemnification) and a special indemnification provision related to products liability claims arising from events occurring during pre-closing periods (the Products

Liability Indemnification). The representations and warranties to which the Contract Indemnification applies survive for a two-year period (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, applied only to aggregate losses in excess of $2.5 million, up to a maximum of approximately $123.0 million.

The Products Liability Indemnification is divided into two parts, the first relating to products liability claims arising in respect of events occurring during the period prior to Alleghany s acquisition of the World Minerals

Notes to Consolidated Financial Statements, continued

13. Commitments and Contingencies, continued

business from Johns Manville Corporation, Inc. (f/k/a Manville Sales Corporation) (Manville) in July 1991 (the Manville Period), and the second relating to products liability claims arising in respect of events occurring during the period of Alleghany ownership (the Alleghany Period). Under the terms of the Stock Purchase Agreement, Alleghany will provide indemnification at a rate of 100 percent for the first $100.0 million of losses arising from products liability claims relating to the Manville Period and at a rate of 50 percent for the next $100.0 million of such losses, so that Alleghany s maximum indemnification obligation in respect of products liability claims relating to the Manville Period is $150.0 million. This indemnification obligation in respect of Manville Period products liability claims will expire on July 31, 2016. The Stock Purchase Agreement states that it is the intention of the parties that, with regard to losses incurred in respect of products liability claims relating to the Manville Period, recovery should first be sought from Manville, and that Alleghany s indemnification obligation in respect of products liability claims relating to the Manville Period is intended to indemnify the Purchaser for such losses which are not recovered from Manville within a reasonable period of time after recovery is sought from Manville. In connection with World Minerals acquisition of the assets of the industrial minerals business of Manville in 1991, Manville agreed to indemnify World Minerals for certain product liability claims, in respect of products of the industrial minerals business manufactured during the Manville Period, asserted against World Minerals through July 31, 2006. In June 2006, Manville agreed to extend its indemnification for such claims asserted against World Minerals through July 31, 2009. World Minerals did not assume in the acquisition liability for product liability claims to the extent that such claims relate, in whole or in part, to the Manville Period, and Manville should continue to be responsible for such claims, notwithstanding the expiration of the Manville indemnity in 2009.

For products liability claims relating to the Alleghany Period, Alleghany will provide indemnification for up to $30.0 million in the aggregate. The $10.0 million holdback from the Adjusted Purchase Price paid at the closing secures performance of this indemnification obligation relating to the Alleghany Period, and, unless and until the holdback amount is exhausted, will be charged for any claim for payment in respect of this indemnification obligation that would otherwise be made to Alleghany. In addition to the indemnification obligation undertaken by Alleghany in respect of products liability claims relating to the Alleghany Period, the Stock Purchase Agreement provides that, after the closing, Alleghany will continue to make available to World Minerals $30.0 million per policy period of Alleghany s umbrella insurance coverage in effect on a Alleghany group-wide basis for policy periods beginning on April 1, 1996 (prior to April 1, 1996, World Minerals had its own umbrella insurance coverage). This portion of Alleghany s umbrella insurance coverage will be available to World Minerals for general liability claims as well as for products liability claims. The Stock Purchase Agreement states that it is the intention of the parties that, with regard to losses incurred in respect of products liability claims relating to the Alleghany Period, recovery should first be sought under any available World Minerals insurance policies and second under the portion of Alleghany s umbrella insurance coverage made available to World Minerals after the closing, and that Alleghany s indemnification obligation in respect of products liability claims relating to the Alleghany Period is intended to indemnify the Purchaser for such losses in respect of which coverage is not available under either the World Minerals insurance policies or under such portion of Alleghany s umbrella insurance coverage. Alleghany s indemnification obligation in respect of Alleghany Period products liability claims will expire on July 14, 2015, which is the tenth anniversary of the closing date.

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.

During the Alleghany Period, World Minerals was named in approximately 30 lawsuits that included product liability claims, many of which have been voluntarily dismissed by the plaintiffs. In most cases, plaintiffs claimed various medical problems allegedly stemming from their exposure to a wide variety of allegedly toxic products at their place of employment, and World Minerals was one among dozens of defendants that had allegedly supplied such products to plaintiffs employers. Through the date of sale, World Minerals did not incur any significant expense in respect of such cases. Based on Alleghany s experience to date and other analyses, Alleghany

Notes to Consolidated Financial Statements, continued

13. Commitments and Contingencies, continued

established a $600 thousand reserve in connection with the Products Liability Indemnification for the Alleghany Period. Such reserve was $365 thousand and $431 thousand at December 31, 2008 and 2007.

(e) Equity Holdings Concentration

At December 31, 2008 and 2007, Alleghany had a concentration of market risk in its available-for-sale equity securities portfolio of Burlington Northern Santa Fe Corporation (Burlington Northern), a railroad holding company, of $227.1 million and $416.2 million, respectively. In 2008, Alleghany sold approximately 2.0 million shares of its Burlington Northern stock holdings, resulting in a pre-tax gain of $152.3 million. In addition, subsequent to December 31, 2008, Alleghany sold approximately 1.0 million shares of Burlington Northern common stock, resulting in a pre-tax gain of $53.0 million, which will be recognized in the 2009 first quarter. During 2007, Alleghany sold approximately 0.8 million shares of its Burlington Northern stock holdings, resulting in a pre-tax gain of $55.9 million.

At December 31, 2008 and 2007, Alleghany also had a concentration of market risk in its available-for-sale equity securities with respect to certain energy sector businesses, of $290.8 million and $378.2 million, respectively.

14. Fair Value of Financial Instruments

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

	December 31, 2008		**December 31, 2007**	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Assets				
Investments (excluding equity-method investments)*	$ 4,057.7	$ 4,057.7	$ 4,069.3	$ 4,069.3

* 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, ORX 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.

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 management s determination of 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 management 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 Management s 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 management s valuations are based on quoted market prices.

Notes to Consolidated Financial Statements, continued

14. Fair Value of Financial Instruments, continued

Level 2 Management s 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 typically constitute a significant input in management s determination of the fair value of 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, 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 Management s 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 on the part of management. For Alleghany, assets utilizing Level 3 inputs are primarily limited to partnership investments. Quotes from the third-party general partner of the entity in which such investment was held, which will often be based on unobservable market inputs, constitute the primary input in management s determination of the fair value.

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

	Level 1	Level 2	Level 3	Total
Assets				
Equity securities	$ 619.9	$ 9.6	$	$ 629.5
Debt securities	266.3	2,493.0*	0.7	2,760.0
Short-term investments	175.9	460.3		636.2
Other invested assets**			32.0	32.0
Investments (excluding equity-method investments)	$ 1,062.1	$ 2,962.9	$ 32.7	$ 4,057.7

* Includes $8.9 million of debt securities that were previously classified as level 3 as of December 31, 2007.

** The carrying value of partnership investments of $32.0 million increased by $20.6 million from the December 31, 2007 carrying value of $11.4 million, due principally to $23.6 million of additional investments, partially offset by a $3.0 million decrease in estimated fair value during the period.

15. Segments 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 and EDC. In addition, AIHL Re, established in June 2006, is a wholly-owned subsidiary of AIHL that has, in the past, been available to provide reinsurance to Alleghany 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 the Significant Accounting Principles summarized in Note 1.

The primary components of corporate activities are Alleghany Properties, AIHL s investment in Homesite and ORX, 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.

Notes to Consolidated Financial Statements, continued

15. Segments of Business, continued

	2008	2007(1)	2006
		(in millions)	
Revenues:			
AIHL insurance group:			
Net premiums earned			
RSUI	$ 689.6	$ 707.5	$ 670.7
CATA	186.9	198.0	171.4
EDC	72.0	44.3	
AIHL Re	0.2	24.5	35.7
	948.7	974.3	877.8
Net investment income	112.6	126.5	107.1
Net realized capital (losses) gains	(248.4)(2)	36.5	13.9
Other income	0.7	0.5	1.8
Total insurance group	813.6	1,137.8	1,000.6
Corporate activities:			
Net investment income (3)	17.6	19.6	20.9
Net realized capital gains (4)	156.2	56.2	14.3
Other income (5)	1.7	15.0	24.5
Total	$ 989.1	$ 1,228.6	$ 1,060.3
Earnings from continuing operations before income taxes:			
AIHL insurance group:			
Underwriting profit (loss) (6)			
RSUI	$ 137.6(7)	$ 219.9	$ 197.4
CATA	15.2	19.4	19.1
EDC	(60.9)(8)	4.4	
AIHL Re	0.2	24.4	35.5
	92.1	268.1	252.0
Net investment income	112.6	126.5	107.1
Net realized capital (losses) gains	(248.4)(2)	36.5	13.9
Other income, less other expenses	(31.4)	(52.3)	(42.0)
Total insurance group	(75.1)	378.8	331.0
Corporate activities:			

Net investment income (3)	17.6	19.6	20.9
Net realized capital gains (4)	156.2	56.2	14.3
Other income (5)	1.7	15.0	24.6
Corporate administration and other expenses	38.7	35.9	45.4
Interest expense	0.7	1.4	5.6
Total	$ 61.0	$ 432.3	$ 339.8

(1) Includes the results of EDC, net of purchase accounting adjustments, commencing July 18, 2007. See Note 4.

Notes to Consolidated Financial Statements, continued

15. Segments of Business, continued

(2) Primarily reflects impairment charges for unrealized losses related to AIHL s investment portfolio that were deemed to be other than temporary. See Note 3. Also reflects an EDC goodwill impairment charge. See Note 4.

(3) Includes $0.3 million and $4.1 million of Alleghany s equity in earnings of Homesite, net of purchase accounting adjustments, for 2008 and 2007, respectively. See Note 4.

(4) Primarily reflects net realized capital gains from the sale of shares of Burlington Northern common stock. See Note 13e.

(5) Primarily reflects sales activity of Alleghany Properties.

(6) 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 attributable to underwriting activities, whereas the remainder constitutes other expenses.

(7) Loss and loss adjustment expenses in 2008 reflect $97.9 million of catastrophe losses, of which $80.9 million relate to the 2008 third quarter Hurricanes Gustav, Ike and Dolly.

(8) Reflects a significant increase in current year and prior year loss and loss adjustment expense reserves in 2008. See Note 6.

	2008	2007 (in millions)	2006
Identifiable assets at December 31			
AIHL insurance group	$ 5,554.2	$ 6,166.7	$ 5,386.4
Corporate activities	627.6	775.4	792.3
Total	$ 6,181.8	$ 6,942.1	$ 6,178.7
Capital expenditures			
AIHL insurance group	$ 9.8	$ 4.7	$ 4.2
Corporate activities		0.2	0.1
Total	$ 9.8	$ 4.9	$ 4.3
Depreciation and amortization			
AIHL insurance group	$ 25.0	$ 15.3	$ 9.9
Corporate activities	0.7	1.0	1.8

Total	$ 25.7	$ 16.3	$ 11.7

16. Other Information

a. Other Assets

Other assets shown in Alleghany s consolidated balance sheets include the following amounts at December 31, 2008 and 2007 (in millions):

	2008	2007
Real estate properties	$ 19.5	$ 20.6
Interest and dividends receivable	41.1	42.7
Other	40.2	40.8
	$ 100.8	$ 104.1

Notes to Consolidated Financial Statements, continued

16. Other Information, continued

b. Property and equipment

Property and equipment, net of accumulated depreciation and amortization, at December 31, 2008 and 2007, are as follows (in millions):

	2008	2007
Furniture and equipment	$ 41.2	$ 33.3
Leasehold improvements	5.7	4.4
Other	0.3	0.3
	47.2	38.0
Less: accumulated depreciation and amortization	(23.9)	(18.3)
	$ 23.3	$ 19.7

c. Other Liabilities

Other liabilities shown in Alleghany s consolidated balance sheets include the following amounts at December 31, 2008 and 2007 (in millions):

	2008	2007
Accounts payable	$ 7.3	$ 7.9
Incentive plans	129.2	152.1
Accrued salaries and wages	8.2	9.5
Deferred compensation	7.2	6.1
Accrued expenses	11.2	8.5
Taxes other than income	3.5	3.7
Deferred revenue	11.8	5.8
Payable to brokers	4.8	7.2
Pension and postretirement benefits	23.1	20.1
Funds held for surety bonds	56.7	41.9
Other funds held	8.6	6.3
Other	17.3	17.2
	$ 288.9	$ 286.3

Notes to Consolidated Financial Statements, continued

17. Quarterly Results of Operations (unaudited)

Selected quarterly financial data for 2008 and 2007 are presented below (in millions, except per share amounts):

	Quarters Ended			
	March 31	June 30	September 30	December 31
2008				
Revenues	$ 355.5	$ 253.4	$ 263.3	$ 116.9
Earnings from:				
Continuing operations	$ 90.6	$ 13.0	$ (8.8)	$ (54.1)
Discontinued operations	5.3	4.8	4.6	92.6
Net earnings	$ 95.9	$ 17.8	$ (4.2)	$ 38.5
Basic earnings per share of common stock: *				
Continuing operations	$ 10.35	$ 1.04	$ (1.58)	$ (7.00)
Discontinued operations	0.64	0.58	0.56	11.14
Total	$ 10.99	$ 1.62	$ (1.02)	$ 4.14
2007				
Revenues	$ 330.4	$ 282.0	$ 308.7	$ 307.6
Earnings from:				
Continuing operations	$ 103.5	$ 58.8	$ 67.4	$ 57.8
Discontinued operations	1.9	2.7	3.0	4.0
Net earnings	$ 105.4	$ 61.5	$ 70.4	$ 61.8
Basic earnings per share of common stock: *				
Continuing operations	$ 11.97	$ 6.55	$ 7.59	$ 6.43
Discontinued operations	0.22	0.33	0.35	0.48
Total	$ 12.19	$ 6.88	$ 7.94	$ 6.91

* Adjusted to reflect subsequent stock dividends.

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

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Alleghany Corporation:

We have audited the accompanying consolidated balance sheets of Alleghany Corporation and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of earnings and comprehensive income, changes in stockholders equity, and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Alleghany Corporation and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Alleghany Corporation s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 25, 2009 expressed an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

(-s- KPMG LLP)

New York, New York
February 25, 2009

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Alleghany Corporation:

We have audited Alleghany Corporation s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Alleghany Corporation s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

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

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

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

In our opinion, Alleghany Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Alleghany Corporation and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of earnings and comprehensive income, changes in stockholders equity, and cash flows for each of the years in the three-year period ended December 31, 2008, and our report dated February 25, 2009 expressed an unqualified opinion on those consolidated financial statements.

(-s- KPMG LLP)

New York, New York
February 25, 2009

Item 9A. Controls and Procedures.

Disclosure 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 the design and operation of our disclosure controls and procedures as of the end of the period covered by this Form 10-K Report pursuant to Rule 13a-15(e) or 15d-15(e) promulgated under the 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 Securities and Exchange Commission s rules and forms. We note that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and we cannot assure you that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

Management s Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control system was designed to provide reasonable assurance to our management and Board of Directors regarding the preparation and fair presentation of financial statements for external purposes.

We carried out an evaluation, under the supervision and with the participation of our management, including our CEO and CFO, of the effectiveness of our internal control over financial reporting based on the framework in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, our management, including our CEO and CFO, concluded that, as of December 31, 2008, our internal control over financial reporting was effective. Our independent registered public accounting firm that audited the consolidated financial statements included in this Form 10-K Report, KPMG LLP, has also audited and issued an opinion on the effectiveness of our internal control over financial reporting which appears in Item 8 of this Form 10-K Report. We note that all internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Changes in Internal Control Over Financial Reporting

There were no changes in internal control over financial reporting during the quarter ended December 31, 2008 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

New York Stock Exchange Certification

On May 15, 2008, we filed with the New York Stock Exchange the annual certification of our President and CEO, certifying that he was not aware of any violation by us of the New York Stock Exchange s corporate governance listing standards. Additionally, we filed the CEO and CFO certifications required by Section 302 of the Sarbanes-Oxley Act as Exhibits 31.1 and 31.2 to this Form 10-K Report.

SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ALLEGHANY CORPORATION
(Registrant)

Date: March 11, 2009

By: /s/ Weston M. Hicks
Weston M. Hicks
President and chief executive officer

INDEX TO EXHIBITS

Exhibit Number	Description
31.1	Certification of the Chief Executive Officer of Alleghany pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Chief Financial Officer of Alleghany pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer of Alleghany 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 Amendment.
32.2	Certification of the Chief Financial Officer of Alleghany 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 Amendment.