

ALLEGHANY CORP /DE
Form 10-Q
November 03, 2015
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2015

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER 1-9371

ALLEGHANY CORPORATION
EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER

DELAWARE

STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION

51-0283071

I.R.S. EMPLOYER IDENTIFICATION NO.

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

ADDRESS OF PRINCIPAL EXECUTIVE OFFICES, INCLUDING ZIP CODE

212-752-1356

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE

NOT APPLICABLE

FORMER NAME, FORMER ADDRESS, AND FORMER FISCAL YEAR, IF CHANGED SINCE LAST REPORT

INDICATE BY CHECK MARK WHETHER THE REGISTRANT: (1) HAS FILED ALL REPORTS REQUIRED TO BE FILED BY SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 DURING THE PRECEDING 12 MONTHS (OR FOR SUCH SHORTER PERIOD THAT THE REGISTRANT WAS REQUIRED TO FILE SUCH REPORTS), AND (2) HAS BEEN SUBJECT TO SUCH FILING REQUIREMENTS FOR THE PAST 90 DAYS. YES NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT HAS SUBMITTED ELECTRONICALLY AND POSTED ON ITS CORPORATE WEB SITE, IF ANY, EVERY INTERACTIVE DATA FILE REQUIRED TO BE SUBMITTED AND POSTED PURSUANT TO RULE 405 OF REGULATION S-T (SECTION 232.405 OF THIS CHAPTER) DURING THE PRECEDING 12 MONTHS (OR SUCH SHORTER PERIOD THAT THE REGISTRANT WAS REQUIRED TO SUBMIT AND POST SUCH FILES). YES NO

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

LARGE ACCELERATED FILER ACCELERATED FILER
NON-ACCELERATED FILER (DO NOT CHECK IF A SMALLER REPORTING COMPANY)

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A SHELL COMPANY (AS DEFINED IN RULE 12B-2 OF THE EXCHANGE ACT). YES NO

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

15,572,593 SHARES, PAR VALUE \$1.00 PER SHARE, AS OF OCTOBER 28, 2015

Table of Contents

ALLEGHANY CORPORATION

TABLE OF CONTENTS

	Page
<u>PART I</u>	
ITEM 1. <u>Financial Statements</u>	1
ITEM 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	22
ITEM 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	58
ITEM 4. <u>Controls and Procedures</u>	60
<u>PART II</u>	
ITEM 1. <u>Legal Proceedings</u>	60
ITEM 1A. <u>Risk Factors</u>	60
ITEM 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	61
ITEM 4. <u>Mine Safety Disclosures</u>	61
ITEM 6. <u>Exhibits</u>	61
<u>SIGNATURES</u>	
<u>EXHIBIT INDEX</u>	

Table of Contents**Part I. FINANCIAL INFORMATION****Item 1. Financial Statements.**

ALLEGHANY CORPORATION AND SUBSIDIARIES

Consolidated Balance Sheets

	September 30, 2015	December 31, 2014
	(unaudited)	
	(in thousands, except share amounts)	
Assets		
Investments:		
Available-for-sale securities at fair value:		
Equity securities (cost: 2015 \$2,826,902; 2014 \$2,366,035)	\$ 3,012,070	\$ 2,815,484
Debt securities (amortized cost: 2015 \$14,382,992; 2014 \$14,364,430)	14,530,255	14,598,641
Short-term investments	362,034	715,553
	17,904,359	18,129,678
Other invested assets	737,350	705,665
	18,641,709	18,835,343
Cash	563,187	605,259
Accrued investment income	119,698	136,511
Premium balances receivable	722,614	683,848
Reinsurance recoverables	1,419,683	1,361,083
Ceded unearned premiums	198,788	184,435
Deferred acquisition costs	377,268	353,169
Property and equipment at cost, net of accumulated depreciation and amortization	95,740	88,910
Goodwill	111,904	111,904
Intangible assets, net of amortization	137,193	133,378
Current taxes receivable	6,260	91,202
Net deferred tax assets	489,636	389,597
Other assets	550,455	514,797
	\$ 23,434,135	\$ 23,489,436
Liabilities and Stockholders Equity		
Loss and loss adjustment expenses	\$ 11,422,492	\$ 11,597,216
Unearned premiums	1,936,803	1,834,184
Senior Notes	1,759,488	1,767,125
Reinsurance payable	75,694	79,100
Other liabilities	778,871	729,767

Edgar Filing: ALLEGHANY CORP /DE - Form 10-Q

Total liabilities	15,973,348	16,007,392
Common stock (shares authorized: 2015 and 2014 22,000,000; shares issued: 2015 and 2014 17,459,961)	17,460	17,460
Contributed capital	3,611,286	3,610,717
Accumulated other comprehensive income	116,333	353,584
Treasury stock, at cost (2015 1,808,262 shares; 2014 1,405,638 shares)	(696,491)	(507,699)
Retained earnings	4,403,583	3,999,366
Total stockholders' equity attributable to Alleghany stockholders	7,452,171	7,473,428
Noncontrolling interest	8,616	8,616
Total stockholders' equity	7,460,787	7,482,044
Total liabilities and stockholders' equity	\$ 23,434,135	\$ 23,489,436

See accompanying Notes to Unaudited Consolidated Financial Statements.

Table of Contents

ALLEGHANY CORPORATION AND SUBSIDIARIES

Consolidated Statements of Earnings and Comprehensive Income (Loss)

(unaudited)

	Three Months Ended September 30,	
	2015	2014
	(in thousands, except per share amounts)	
Revenues		
Net premiums earned	\$ 1,049,071	\$ 1,136,215
Net investment income	118,159	118,284
Net realized capital gains	29,202	59,368
Other than temporary impairment losses	(52,680)	(720)
Other income	45,285	38,769
Total revenues	1,189,037	1,351,916
Costs and Expenses		
Net loss and loss adjustment expenses	594,729	623,132
Commissions, brokerage and other underwriting expenses	360,203	372,291
Other operating expenses	68,453	59,622
Corporate administration	10,922	9,455
Amortization of intangible assets	(1,104)	(1,142)
Interest expense	22,691	22,671
Total costs and expenses	1,055,894	1,086,029
Earnings before income taxes	133,143	265,887
Income taxes	36,045	79,547
Net earnings	97,098	186,340
Net earnings attributable to noncontrolling interest	568	25
Net earnings attributable to Alleghany stockholders	\$ 96,530	\$ 186,315
Net earnings	\$ 97,098	\$ 186,340
Other comprehensive income (loss):		
Change in unrealized gains, net of deferred taxes of (\$81,256) and (\$29,255) for 2015 and 2014, respectively	(150,904)	(54,330)
Less: reclassification for net realized capital gains and other than temporary impairment losses, net of taxes of \$8,217 and (\$20,527) for 2015 and 2014, respectively	15,261	(38,121)
Change in unrealized currency translation adjustment, net of deferred taxes of (\$208) and (\$14,039) for 2015 and 2014, respectively	(386)	(26,073)
Retirement plans	129	(6)

Comprehensive (loss) income	(38,802)	67,810
Comprehensive income attributable to noncontrolling interest	568	25
Comprehensive (loss) income attributable to Alleghany stockholders	\$ (39,370)	\$ 67,785
Basic earnings per share attributable to Alleghany stockholders	\$ 6.07	\$ 11.40
Diluted earnings per share attributable to Alleghany stockholders	6.07	11.40

See accompanying Notes to Unaudited Consolidated Financial Statements.

Table of Contents

ALLEGHANY CORPORATION AND SUBSIDIARIES

Consolidated Statements of Earnings and Comprehensive Income

(unaudited)

	Nine Months Ended September 30,	
	2015	2014
	(in thousands, except per share amounts)	
Revenues		
Net premiums earned	\$ 3,140,965	\$ 3,289,156
Net investment income	334,628	342,961
Net realized capital gains	158,513	197,728
Other than temporary impairment losses	(112,278)	(6,872)
Other income	125,270	106,801
Total revenues	3,647,098	3,929,774
Costs and Expenses		
Net loss and loss adjustment expenses	1,737,100	1,863,504
Commissions, brokerage and other underwriting expenses	1,067,766	1,056,131
Other operating expenses	199,670	179,200
Corporate administration	33,441	31,774
Amortization of intangible assets	(3,815)	(3,879)
Interest expense	69,158	66,414
Total costs and expenses	3,103,320	3,193,144
Earnings before income taxes	543,778	736,630
Income taxes	138,113	196,415
Net earnings	405,665	540,215
Net earnings attributable to noncontrolling interest	1,448	40
Net earnings attributable to Alleghany stockholders	\$ 404,217	\$ 540,175
Net earnings	\$ 405,665	\$ 540,215
Other comprehensive income:		
Change in unrealized gains, net of deferred taxes of (\$106,986) and \$163,086 for 2015 and 2014, respectively	(198,689)	302,873
Less: reclassification for net realized capital gains and other than temporary impairment losses, net of taxes of (\$16,182) and (\$66,800) for 2015 and 2014, respectively	(30,053)	(124,056)
Change in unrealized currency translation adjustment, net of deferred taxes of (\$4,444) and (\$10,681) for 2015 and 2014, respectively	(8,253)	(19,836)
Retirement plans	(256)	120

Comprehensive income	168,414	699,316
Comprehensive income attributable to noncontrolling interest	1,448	40
Comprehensive income attributable to Alleghany stockholders	\$ 166,966	\$ 699,276
Basic earnings per share attributable to Alleghany stockholders	\$ 25.31	\$ 32.74
Diluted earnings per share attributable to Alleghany stockholders	25.30	32.74

See accompanying Notes to Unaudited Consolidated Financial Statements.

Table of Contents

ALLEGHANY CORPORATION AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(unaudited)

	Nine Months Ended September 30,	
	2015	2014
	(in thousands)	
Cash flows from operating activities		
Net earnings	\$ 405,665	\$ 540,215
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:		
Depreciation and amortization	124,533	132,280
Net realized capital (gains) losses	(158,513)	(197,728)
Other than temporary impairment losses	112,278	6,872
(Increase) decrease in reinsurance recoverables, net of reinsurance payable	(62,006)	(2,736)
(Increase) decrease in premium balances receivable	(38,766)	(56,287)
(Increase) decrease in ceded unearned premiums	(14,353)	(34,588)
(Increase) decrease in deferred acquisition costs	(24,099)	(43,922)
Increase (decrease) in unearned premiums	102,619	209,374
Increase (decrease) in loss and loss adjustment expenses	(174,724)	(245,448)
Change in unrealized foreign exchange losses (gains)	132,006	83,397
Other, net	157,018	(185,652)
Net adjustments	155,993	(334,438)
Net cash provided by (used in) operating activities	561,658	205,777
Cash flows from investing activities		
Purchases of debt securities	(5,866,914)	(5,120,358)
Purchases of equity securities	(2,793,006)	(1,235,381)
Sales of debt securities	4,295,126	4,141,811
Maturities and redemptions of debt securities	1,318,270	1,115,943
Sales of equity securities	2,320,298	655,862
Net (purchase) sale in short-term investments	391,904	522,274
Purchases of property and equipment	(45,285)	(37,333)
Purchase of subsidiary, net of cash acquired	(47,469)	
Other, net	17,177	(232,058)
Net cash (used in) provided by investing activities	(409,899)	(189,240)
Cash flows from financing activities		
Proceeds from issuance of Senior Notes		297,942
Debt issue costs paid		(3,625)
Treasury stock acquisitions	(192,522)	(222,445)

Other, net	14,926	24,849
Net cash (used in) provided by financing activities	(177,596)	96,721
Effect of exchange rate changes on cash	(16,235)	(3,968)
Net (decrease) increase in cash	(42,072)	109,290
Cash at beginning of period	605,259	498,315
Cash at end of period	\$ 563,187	\$ 607,605

Supplemental disclosures of cash flow information

Cash paid during the period for:

Interest paid	\$ 67,345	\$ 60,423
Income taxes paid (refunds received)	22,613	251,434

See accompanying Notes to Unaudited Consolidated Financial Statements.

Table of Contents

ALLEGHANY CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Financial Statements**1. Summary of Significant Accounting Principles*****(a) Principles of Financial Statement Presentation***

This Quarterly Report on Form 10-Q (this Form 10-Q) should be read in conjunction with the Annual Report on Form 10-K for the year ended December 31, 2014 (the 2014 10-K) and the Quarterly Reports on Form 10-Q for the quarters ended March 31, 2015 and June 30, 2015 of Alleghany Corporation (Alleghany).

Alleghany, a Delaware corporation, owns and manages certain operating subsidiaries and investments, anchored by a core position in property and casualty reinsurance and insurance. Through its wholly-owned subsidiary Alleghany Insurance Holdings LLC (AIHL) and its subsidiaries, Alleghany is engaged in the property and casualty insurance business. AIHL's insurance operations are principally conducted by its subsidiaries RSUI Group, Inc. (RSUI), CapSpecialty, Inc. (CapSpecialty) and Pacific Compensation Corporation (PacificComp). CapSpecialty has been a subsidiary of AIHL since January 2002, RSUI has been a subsidiary of AIHL since July 2003 and PacificComp has been a subsidiary of AIHL since July 2007. AIHL Re LLC (AIHL Re), a captive reinsurance company which provides reinsurance to Alleghany's insurance operating subsidiaries and affiliates, has been a wholly-owned subsidiary of Alleghany since its formation in May 2006. Alleghany's reinsurance operations commenced on March 6, 2012, when Alleghany consummated a merger with Transatlantic Holdings, Inc. (TransRe), and TransRe became one of Alleghany's wholly-owned subsidiaries. Alleghany's public equity investments, including those held by TransRe and AIHL's operating subsidiaries, are managed primarily through Alleghany's wholly-owned subsidiary Roundwood Asset Management LLC (Roundwood).

Although Alleghany's primary sources of revenues and earnings are its reinsurance and insurance operations and investments, Alleghany also manages, sources, executes and monitors certain private capital investments primarily through its wholly-owned subsidiary Alleghany Capital Corporation (Alleghany Capital). Alleghany Capital's private capital investments are included in corporate activities for segment reporting purposes and include: (i) Stranded Oil Resources Corporation (SORC), an exploration and production company focused on enhanced oil recovery, headquartered in Golden, Colorado; (ii) Bourn & Koch, Inc. (Bourn & Koch), a manufacturer and remanufacturer/retrofitter of precision machine tools and supplier of replacement parts, headquartered in Rockford, Illinois; (iii) R.C. Tway Company, LLC (Kentucky Trailer), a manufacturer of custom trailers and truck bodies for the moving and storage industry and other markets, headquartered in Louisville, Kentucky; (iv) an approximately 40 percent equity interest in ORX Exploration, Inc. (ORX), a regional oil and gas exploration and production company, headquartered in New Orleans, Louisiana; and (v) a 30 percent equity interest in Jazwares, LLC (Jazwares), a toy and consumer electronics company, headquartered in Sunrise, Florida, which interest was acquired on July 31, 2014 for \$60.3 million. ORX and Jazwares are accounted for under the equity method of accounting. In addition, Alleghany owns and manages properties in the Sacramento, California region through its wholly-owned subsidiary Alleghany Properties Holdings LLC (Alleghany Properties).

Unless the context otherwise requires, references to Alleghany include Alleghany together with its subsidiaries.

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

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

The portion of stockholders' equity, net earnings and accumulated other comprehensive income that is not attributable to Alleghany stockholders is presented on the Consolidated Balance Sheets and the Consolidated Statements of Earnings and Comprehensive Income as noncontrolling interest. Bourn & Koch and Kentucky Trailer each had approximately 20 percent noncontrolling interests outstanding during the first nine months of 2015 and 2014.

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 as of the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Alleghany relies on historical experience and on various other assumptions that it believes to be reasonable under the circumstances to make judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ materially from those reported results to the extent that those estimates and assumptions prove to be inaccurate. Changes in estimates are reflected in the consolidated statement of earnings and comprehensive income in the period in which the change is made. The results of operations for any interim period are not necessarily indicative of results for the full year.

Table of Contents

(b) Other Significant Accounting Principles

Alleghany's significant accounting principles can be found in Note 1 to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

(c) Recent Accounting Standards

Recently Adopted

In April 2014, the Financial Accounting Standards Board (the FASB) issued guidance that changed the criteria for reporting discontinued operations. Under the new guidance, only disposals that represent a strategic shift in operations qualify as discontinued operations. In addition, the new guidance requires expanded disclosure about discontinued operations. This guidance was effective in the first quarter of 2015. Alleghany adopted this guidance in the first quarter of 2015 and the implementation did not have an impact on its results of operations and financial condition.

Future Application of Accounting Standards

In May 2014, the FASB, together with the International Accounting Standards Board, issued guidance on the recognition of revenue from contracts with customers. Under the new guidance, revenue is recognized as the transfer of goods and services to customers takes place, and in amounts that reflect the payment or payments that are expected to be received from the customers for those goods and services. The new guidance also requires new disclosures about revenue. Insurance- and reinsurance-related revenues are not impacted by this guidance. In July 2015, the FASB decided to delay the effective date of the new revenue standard by a year. This guidance is now effective in the first quarter of 2018 for public entities, with early adoption permitted in 2017. Alleghany will adopt this guidance in the first quarter of 2018 and does not currently believe that the implementation will have a material impact on its results of operations and financial condition.

In February 2015, the FASB issued guidance that amended the analysis that must be performed to determine whether an entity should consolidate certain types of legal entities. Under the new guidance, the evaluation of whether limited partnerships and similar entities are variable interest entities or voting interest entities is modified, the presumption that general partners should consolidate limited partnerships is eliminated and the process to determine the primary beneficiary of a variable interest entity is modified. This guidance is effective in the first quarter of 2016 for public entities, with early adoption permitted. Alleghany will adopt this guidance in the first quarter of 2016 and does not currently believe that the implementation will have a material impact on its results of operations and financial condition.

In April 2015, the FASB issued guidance that requires debt issuance costs related to debt liabilities be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, which is consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected. This guidance is effective in the first quarter of 2016 for public entities, with early adoption permitted. Alleghany will adopt this guidance in the first quarter of 2016 and does not currently believe that the implementation will have an impact on its results of operations and financial condition.

In May 2015, the FASB issued guidance that requires disclosures related to short-duration insurance contracts. The guidance applies to property and casualty insurance and reinsurance entities, among others, and requires the following annual disclosure related to the liability for loss and loss adjustment expenses (LAE): (i) net incurred and paid claims development information by accident year for up to ten years; (ii) a reconciliation of incurred and paid claims development information to the aggregate carrying amount of the liability for loss and LAE;

(iii) incurred-but-not-reported liabilities by accident year and in total; (iv) a description of reserving methodologies (as well as any changes to those methodologies); (v) quantitative information about claim frequency by accident year; and (vi) the average annual percentage payout of incurred claims by age by accident year. In addition, the guidance requires insurance entities to disclose for annual and interim reporting periods a roll-forward of the liability for loss and LAE. This guidance is effective for annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016, with early adoption permitted. Alleghany will adopt this guidance as of December 31, 2016 and does not currently believe that the implementation will have an impact on its results of operations and financial condition.

Table of Contents**2. Fair Value of Financial Instruments**

The carrying values and estimated fair values of Alleghany's consolidated financial instruments as of September 30, 2015 and December 31, 2014 were as follows:

	September 30, 2015		December 31, 2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in millions)			
Assets				
Investments (excluding equity method investments) ⁽¹⁾	\$ 17,935.9	\$ 17,935.9	\$ 18,153.8	\$ 18,153.8
Liabilities				
Senior Notes ⁽²⁾	\$ 1,759.5	\$ 1,888.5	\$ 1,767.1	\$ 1,948.6

(1) This table includes available-for-sale (AFS) investments (debt and equity securities as well as partnership and non-marketable equity investments carried at fair value that are included in other invested assets). This table excludes investments accounted for using the equity method and certain loans receivable that are carried at cost, all of which are included in other invested assets. The fair value of short-term investments approximates amortized cost. Fair value for all other categories of investments is discussed in Note 1(c) to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

(2) See Note 8 to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

Alleghany's financial instruments measured at fair value and the level of the fair value hierarchy of inputs used as of September 30, 2015 and December 31, 2014 were as follows:

	Level 1	Level 2	Level 3	Total
	(in millions)			
As of September 30, 2015				
Equity securities:				
Common stock	\$ 3,006.0	\$ 6.1	\$	\$ 3,012.1
Preferred stock				
Total equity securities	3,006.0	6.1		3,012.1
Debt securities:				
U.S. Government obligations		1,071.5		1,071.5
Municipal bonds		4,766.3		4,766.3
Foreign government obligations		919.3		919.3
U.S. corporate bonds		2,123.8	51.6	2,175.4
Foreign corporate bonds		1,316.0		1,316.0
Mortgage and asset-backed securities:				
Residential mortgage-backed securities (RMBS ⁽¹⁾)		1,475.3	15.9	1,491.2

Edgar Filing: ALLEGHANY CORP /DE - Form 10-Q

Commercial mortgage-backed securities (CMBS)	1,117.0	20.9	1,137.9
Other asset-backed securities ⁽²⁾	678.7	974.0	1,652.7
Total debt securities	13,467.9	1,062.4	14,530.3
Short-term investments	362.0		362.0
Other invested assets ⁽³⁾		31.5	31.5
Total investments (excluding equity method investments)	\$ 3,006.0	\$ 13,836.0	\$ 17,935.9
Senior Notes	\$	\$ 1,888.5	\$ 1,888.5

Table of Contents

	Level 1	Level 2	Level 3	Total
	(in millions)			
As of December 31, 2014				
Equity securities:				
Common stock	\$ 2,805.3	\$ 10.2	\$	\$ 2,815.5
Preferred stock				
Total equity securities	2,805.3	10.2		2,815.5
Debt securities:				
U.S. Government obligations		541.1		541.1
Municipal bonds		5,197.5		5,197.5
Foreign government obligations		900.4		900.4
U.S. corporate bonds		2,118.1	36.7	2,154.8
Foreign corporate bonds		1,497.7	6.0	1,503.7
Mortgage and asset-backed securities:				
RMBS ⁽¹⁾		1,637.7	18.2	1,655.9
CMBS		1,102.0	23.3	1,125.3
Other asset-backed securities ⁽²⁾		586.8	933.1	1,519.9
Total debt securities		13,581.3	1,017.3	14,598.6
Short-term investments		715.6		715.6
Other invested assets ⁽³⁾			24.1	24.1
Total investments (excluding equity method investments)	\$ 2,805.3	\$ 14,307.1	\$ 1,041.4	\$ 18,153.8
Senior Notes	\$	\$ 1,948.6	\$	\$ 1,948.6

(1) Primarily includes government agency pass-through securities guaranteed by a government agency or government sponsored enterprise, among other types of RMBS.

(2) Includes \$952.4 million and \$900.7 million of collateralized loan obligations as of September 30, 2015 and December 31, 2014, respectively.

(3) Includes partnership and non-marketable equity investments accounted for on an AFS basis, and excludes investments accounted for using the equity method and certain loans receivable that are carried at cost.

In the three and nine months ended September 30, 2015, there were transfers of \$3.0 million and \$19.3 million, respectively, of debt securities out of Level 3 that were principally due to an increase in observable inputs related to the valuation of such assets. Of the \$19.3 million of transfers, \$13.8 million related to U.S. corporate bonds and \$5.5 million related to foreign corporate bonds.

In the three and nine months ended September 30, 2015, there were transfers of \$5.9 million and \$15.5 million, respectively, of securities into Level 3 that were principally due to a decrease in observable inputs related to the valuation of such assets. Of the \$15.5 million of transfers, \$9.8 million related to U.S. corporate bonds, \$5.0 million related to other invested assets and \$0.7 million related to foreign corporate bonds. There were no other transfers between Levels 1, 2 or 3 in the three and nine months ended September 30, 2015.

In the nine months ended September 30, 2014, there were transfers of \$238.1 million of other invested assets out of Level 3. Of the \$238.1 million of transfers, \$232.9 million related to the conversion of an equity interest held by AIHL in the second quarter of 2014. As further described in Note 3(g), AIHL's investment in Ares Management L.P. (Ares) converted to limited partner interests in certain Ares subsidiaries during the second quarter of 2014, at which time the investment ceased to qualify as a financial instrument measured at fair value. No gain or loss was recognized upon the conversion.

In the three and nine months ended September 30, 2014, there were transfers of \$6.3 million and \$44.4 million, respectively, of debt securities into Level 3 that were principally due to a decrease in observable inputs related to the valuation of such securities. Of the \$44.4 million of transfers, \$29.1 million related to other asset-backed securities (specifically, collateralized loan obligations), \$15.0 million related to U.S. corporate bonds and \$0.3 million related to foreign corporate bonds. There were no other transfers between Levels 1, 2 or 3 in the three and nine months ended September 30, 2014.

Table of Contents

The following tables present reconciliations of the changes in Level 3 assets measured at fair value during the nine months ended September 30, 2015 and 2014:

Nine Months Ended September 30, 2015	Debt Securities						Total
	U.S. Corporate Bonds	Foreign Corporate Bonds	RMBS	Mortgage and asset-backed CMBS	Other Asset-backed Securities	Other Invested Assets ⁽¹⁾	
Balance as of January 1, 2015	\$ 36.7	\$ 6.0	\$ 18.2	\$ 23.3	\$ 933.1	\$ 24.1	\$ 1,041.4
Net realized/unrealized gains (losses) included in:							
Net earnings ⁽²⁾	0.5		0.5	(0.3)	2.0	0.2	2.9
Other comprehensive income	(0.8)	0.8	(0.6)	(1.5)	(4.8)	0.8	(6.1)
Purchases	33.9				219.5	1.6	255.0
Sales	(1.8)	(2.0)			(167.9)	(0.2)	(171.9)
Issuances							
Settlements	(12.9)		(2.2)	(0.6)	(7.9)		(23.6)
Transfers into Level 3	9.8	0.7				5.0	15.5
Transfers out of Level 3	(13.8)	(5.5)					(19.3)
Balance as of September 30, 2015	\$ 51.6	\$ 15.9	\$ 20.9	\$ 974.0	\$ 31.5	\$ 1,093.9	

Nine Months Ended September 30, 2014	Debt Securities						Total	
	Common stock	U.S. Corporate Bonds	Foreign Corporate Bonds	RMBS	Mortgage and asset-backed CMBS	Other Asset-backed Securities		Other Invested Assets ⁽¹⁾
Balance as of January 1, 2014	\$	\$ 27.5	\$ 1.0	\$ 78.8	\$ 60.8	\$ 258.4	\$ 282.0	\$ 708.5
Net realized/unrealized gains (losses) included in:								
Net earnings ⁽²⁾		(0.9)		4.1	(0.3)	0.5	0.2	3.6
Other comprehensive income		(0.3)		2.5	(1.3)	(6.9)	1.4	(4.6)
Purchases	4.5	21.6	2.5		22.0	730.5		781.1
Sales		(9.0)	(1.2)	(12.2)	(3.0)	(78.7)	(0.2)	(104.3)
Issuances								
Settlements		(7.6)	(1.5)	(8.3)	(41.4)	(11.2)	(21.0)	(91.0)
Transfers into Level 3		15.0	0.3			29.1		44.4
Transfers out of Level 3							(238.1)	(238.1)
Balance as of September 30, 2014	\$ 4.5	\$ 46.3	\$ 1.1	\$ 64.9	\$ 36.8	\$ 921.7	\$ 24.3	\$ 1,099.6

(1) Includes partnership and non-marketable equity investments accounted for on an AFS basis.

(2) There were no other than temporary impairment (OTTI) losses recorded in net earnings related to Level 3 investments still held as of September 30, 2015 and 2014.

Net unrealized losses related to Level 3 investments as of September 30, 2015 and December 31, 2014 were not material.

See Note 1(c) to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K for Alleghany s accounting policy on fair value.

Table of Contents**3. Investments****(a) Unrealized Gains and Losses**

The amortized cost or cost and the fair value of AFS securities as of September 30, 2015 and December 31, 2014 are summarized as follows:

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(in millions)				
As of September 30, 2015				
Equity securities:				
Common stock	\$ 2,826.9	\$ 329.3	\$ (144.1)	\$ 3,012.1
Preferred stock				
Total equity securities	2,826.9	329.3	(144.1)	3,012.1
Debt securities:				
U.S. Government obligations	1,067.7	8.2	(4.4)	1,071.5
Municipal bonds	4,660.0	120.1	(13.8)	4,766.3
Foreign government obligations	898.7	21.1	(0.5)	919.3
U.S. corporate bonds	2,183.2	30.9	(38.7)	2,175.4
Foreign corporate bonds	1,300.7	28.5	(13.2)	1,316.0
Mortgage and asset-backed securities:				
RMBS	1,483.4	16.1	(8.3)	1,491.2
CMBS	1,124.5	17.1	(3.7)	1,137.9
Other asset-backed securities ⁽¹⁾	1,664.8	5.3	(17.4)	1,652.7
Total debt securities	14,383.0	247.3	(100.0)	14,530.3
Short-term investments	362.0			362.0
Total	\$ 17,571.9	\$ 576.6	\$ (244.1)	\$ 17,904.4

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(in millions)				
As of December 31, 2014				
Equity securities:				
Common stock	\$ 2,366.0	\$ 530.3	\$ (80.8)	\$ 2,815.5
Preferred stock				
Total equity securities	2,366.0	530.3	(80.8)	2,815.5
Debt securities:				

Edgar Filing: ALLEGHANY CORP /DE - Form 10-Q

U.S. Government obligations	541.2	3.4	(3.5)	541.1
Municipal bonds	5,067.3	139.3	(9.1)	5,197.5
Foreign government obligations	876.7	23.7		900.4
U.S. corporate bonds	2,136.5	39.5	(21.2)	2,154.8
Foreign corporate bonds	1,460.5	47.7	(4.5)	1,503.7
Mortgage and asset-backed securities:				
RMBS	1,646.9	20.7	(11.7)	1,655.9
CMBS	1,104.2	22.5	(1.4)	1,125.3
Other asset-backed securities ⁽¹⁾	1,531.2	2.2	(13.5)	1,519.9
Total debt securities	14,364.5	299.0	(64.9)	14,598.6
Short-term investments	715.6			715.6
Total	\$ 17,446.1	\$ 829.3	\$ (145.7)	\$ 18,129.7

(1) Includes \$952.4 million and \$900.7 million of collateralized loan obligations as of September 30, 2015 and December 31, 2014, respectively.

Table of Contents**(b) Contractual Maturity**

The amortized cost and estimated fair value of debt securities as of September 30, 2015 by contractual maturity are shown below. 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 or Cost	Fair Value
	(in millions)	
Short-term investments due in one year or less	\$ 362.0	\$ 362.0
Mortgage and asset-backed securities ⁽¹⁾	4,272.7	4,281.8
Debt securities with maturity dates:		
One year or less	573.7	576.5
Over one through five years	3,102.1	3,137.1
Over five through ten years	3,013.8	3,048.6
Over ten years	3,420.7	3,486.3
Total debt securities	14,383.0	14,530.3
Equity securities	2,826.9	3,012.1
Total	\$ 17,571.9	\$ 17,904.4

(1) Mortgage and asset-backed securities by their nature do not generally have single maturity dates.

(c) Net Investment Income

Net investment income for the three and nine months ended September 30, 2015 and 2014 were as follows:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
	(in millions)			
Interest income	\$ 96.1	\$ 96.2	\$ 283.2	\$ 288.9
Dividend income	13.8	15.8	40.1	46.0
Investment expenses	(7.1)	(7.2)	(20.4)	(21.6)
Equity in results of Pillar Investments ⁽¹⁾	7.3	5.0	14.9	12.5
Equity in results of Ares ⁽¹⁾	2.5	2.7	8.2	5.8
Equity in results of ORX	(1.6)	0.1	(6.3)	(0.6)
Other investment results	7.2	5.7	14.9	12.0

Total	\$ 118.2	\$ 118.3	\$ 334.6	\$ 343.0
-------	----------	----------	----------	----------

(1) See Note 3(g) for discussion of the Pillar Investments as defined therein and the investment in Ares. As of September 30, 2015, non-income producing invested assets were insignificant.

(d) Realized Gains and Losses

The proceeds from sales of AFS securities were \$1.4 billion and \$1.1 billion for the three months ended September 30, 2015 and 2014, respectively, and \$6.6 billion and \$4.8 billion for the nine months ended September 30, 2015 and 2014, respectively.

Table of Contents

Realized capital gains and losses for the three and nine months ended September 30, 2015 and 2014 primarily reflect sales of equity securities. Realized capital gains from equity securities for the nine months ended September 30, 2015 include the sales of certain equity securities resulting from a modification of Alleghany's equity investment strategy, as well as the sales of certain equity securities which had their cost basis reduced in earlier periods for the recognition of OTTI losses. Realized capital gains in the nine months ended September 30, 2014 include a realized capital gain of \$34.0 million from the sales of long-dated U.S. Treasury Strip debt securities in April 2014, and some additional realized capital gains taken on debt securities in the three and nine months ended September 30, 2014. The amounts of gross realized capital gains and gross realized capital losses for the three and nine months ended September 30, 2015 and 2014 were as follows:

	Three Months Ended		Nine Months	
	September 30,		Ended	
	2015	2014	2015	2014
	(in millions)			
Gross realized capital gains	\$ 42.4	\$ 61.6	\$ 258.6	\$ 215.4
Gross realized capital losses	(13.2)	(2.2)	(100.1)	(17.7)
Net realized capital gains	\$ 29.2	\$ 59.4	\$ 158.5	\$ 197.7

Gross realized loss amounts exclude OTTI losses, as discussed below.

(e) OTTI Losses

Alleghany holds its equity and debt securities as AFS and, as such, these securities are recorded at fair value. 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. The analysis of any individual security's decline in value is performed in its functional currency. If the decline of a particular investment is deemed temporary, Alleghany records the decline as an unrealized loss in stockholders' equity. If the decline is deemed to be other than temporary, Alleghany writes its cost-basis or amortized cost-basis down to the fair value of the investment and records an OTTI loss on its statement of earnings. In addition, any portion of such decline related to debt securities that is believed to arise from factors other than credit is recorded as a component of other comprehensive income rather than charged against earnings.

Management's assessment of equity securities initially involves an evaluation of all securities that are in an unrealized loss position, regardless of the duration or severity of the loss, as of the applicable balance sheet date. Such initial review consists primarily of assessing whether: (i) there has been a negative credit or news event with respect to the issuer that could indicate the existence of an OTTI; and (ii) Alleghany has the ability and intent to hold an equity security for a period of time sufficient to allow for an anticipated recovery (generally considered to be one year from the balance sheet date).

To the extent that an equity security in an unrealized loss position is not impaired based on the initial review described above, Alleghany then further evaluates such equity security and deems it to be other than temporarily impaired if it has been in an unrealized loss position for 12 months or more or if its unrealized loss position is greater than 50 percent of its cost, absent compelling evidence to the contrary.

Alleghany then evaluates those equity securities where the unrealized loss is at least 20 percent of cost as of the balance sheet date or which have been in an unrealized loss position continuously for six months or more preceding the balance sheet date. This evaluation takes into account quantitative and qualitative factors in determining whether such securities are other than temporarily impaired, including: (i) market valuation metrics associated with the equity security (such as dividend yield and price-to-earnings ratio); (ii) current views on the equity security, as expressed by either Alleghany's internal stock analysts and/or by third party stock analysts or rating agencies; and (iii) credit or news events associated with a specific issuer, such as negative news releases and rating agency downgrades with respect to the issuer of the investment.

Debt securities in an unrealized loss position are evaluated for OTTI if they meet any of the following criteria: (i) they are trading at a discount of at least 20 percent to amortized cost for an extended period of time (nine consecutive months or longer); (ii) there has been a negative credit or news event with respect to the issuer that could indicate the existence of an OTTI; or (iii) Alleghany intends to sell, or it is more likely than not that Alleghany will sell, the debt security before recovery of its amortized cost basis.

If Alleghany intends to sell, or it is more likely than not that Alleghany will sell, a debt security before recovery of its amortized cost basis, the total amount of the unrealized loss position is recognized as an OTTI loss in earnings. To the extent that a debt security that is in an unrealized loss position is not impaired based on the preceding, Alleghany will consider a debt security to be impaired when it believes it to be probable that Alleghany will not be able to collect the entire amortized cost basis. For debt securities in an unrealized loss position as of the end of each quarter, Alleghany develops a best estimate of the present value of expected cash flows. If the results of the cash flow analysis indicate Alleghany will not recover the full amount of its amortized cost basis in the debt security, Alleghany records an OTTI loss in earnings equal to the difference between the present value of expected cash flows and the

Table of Contents

amortized cost basis of the debt security. If applicable, the difference between the total unrealized loss position on the debt security and the OTTI loss recognized in earnings is the non-credit related portion and is recorded as a component of other comprehensive income.

In developing the cash flow analyses for debt securities, Alleghany considers various factors for the different categories of debt securities. For municipal bonds, Alleghany takes into account the taxing power of the issuer, source of revenue, credit risk and credit enhancements and pre-refunding. For mortgage and asset-backed securities, Alleghany discounts its best estimate of future cash flows at an effective rate equal to the original effective yield of the security or, in the case of floating rate securities, at the current coupon. Alleghany's models include assumptions about prepayment speeds, default and delinquency rates and underlying collateral (if any), as well as credit ratings, credit enhancements and other observable market data. For corporate bonds, Alleghany reviews business prospects, credit ratings and available information from asset managers and rating agencies for individual securities.

OTTI losses in the first nine months of 2015 reflect \$112.3 million of unrealized losses that were deemed to be other than temporary and, as such, were required to be charged against earnings. Upon the ultimate disposition of the securities for which OTTI losses have been recorded, a portion of the loss may be recoverable depending on market conditions at the time of disposition. Of the \$112.3 million of OTTI losses, \$107.3 million related to equity securities, primarily in the airline, energy, gaming, pharmaceutical and mining sectors, and \$5.0 million related to debt securities, primarily in the energy and finance sectors. The determination that unrealized losses on equity and debt securities were other than temporary was primarily due to the fact that Alleghany lacked the intent to hold the securities for a period of time sufficient to allow for an anticipated recovery and, to a lesser extent, based on the duration of the decline in the fair value of equity securities relative to their costs. Of the \$112.3 million of OTTI losses, \$52.7 million was incurred in the third quarter of 2015.

OTTI losses for the first nine months of 2014 reflect \$6.9 million of unrealized losses that were deemed to be other than temporary and, as such, were required to be charged against earnings. Of the \$6.9 million of OTTI losses, \$5.3 million related to equity securities and \$1.6 million related to debt securities. The determination that unrealized losses on equity and debt securities were other than temporary was primarily based on the fact that Alleghany lacked the intent to hold the securities for a period of time sufficient to allow for an anticipated recovery. Of the \$6.9 million of OTTI losses, \$0.7 million was incurred in the third quarter of 2014.

After adjusting the cost basis of securities for the recognition of OTTI losses, the remaining gross unrealized investment losses for debt and equity securities as of September 30, 2015 were deemed to be temporary, based on, among other factors: (i) the duration of time and the relative magnitude to which the fair value of these investments had been below cost were not indicative of an OTTI loss (for example, no equity security was in a continuous unrealized loss position for 12 months or more as of September 30, 2015); (ii) the absence of compelling evidence that would cause Alleghany to call into question the financial condition or near-term business prospects of the issuer of the investment; and (iii) Alleghany's ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery.

Alleghany may ultimately record a realized loss after having originally concluded that the decline in value was temporary. Risks and uncertainties are inherent in the methodology. Alleghany's methodology for assessing other than temporary declines in value contains inherent risks and uncertainties which could include, but are not limited to, incorrect assumptions about financial condition, liquidity or future prospects, inadequacy of any underlying collateral and unfavorable changes in economic conditions or social trends, interest rates or credit ratings.

Table of Contents**(f) Aging of Gross Unrealized Losses**

As of September 30, 2015 and December 31, 2014, gross unrealized losses and related fair values for equity securities and debt securities, grouped by duration of time in a continuous unrealized loss position, were as follows:

	Less Than 12 Months Fair Value	12 Months Gross Unrealized Losses	12 Months or More Fair Value	12 Months or More Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
	(in millions)					
As of September 30, 2015						
Equity securities:						
Common stock	\$ 1,745.8	\$ 144.1	\$	\$	\$ 1,745.8	\$ 144.1
Preferred stock						
Total equity securities	1,745.8	144.1			1,745.8	144.1
Debt securities:						
U.S. Government obligations	380.0	4.4	8.1		388.1	4.4
Municipal bonds	588.3	7.2	109.7	6.6	698.0	13.8
Foreign government obligations	180.3	0.5			180.3	0.5
U.S. corporate bonds	835.6	24.7	82.5	14.0	918.1	38.7
Foreign corporate bonds	357.5	12.5	11.5	0.7	369.0	13.2
Mortgage and asset-backed securities:						
RMBS	373.3	2.2	374.1	6.1	747.4	8.3
CMBS	249.9	3.4	28.7	0.3	278.6	3.7
Other asset-backed securities	816.4	11.2	279.9	6.2	1,096.3	17.4
Total debt securities	3,781.3	66.1	894.5	33.9	4,675.8	100.0
Total temporarily impaired securities	\$ 5,527.1	\$ 210.2	\$ 894.5	\$ 33.9	\$ 6,421.6	\$ 244.1

	Less Than 12 Months Fair Value	12 Months Gross Unrealized Losses	12 Months or More Fair Value	12 Months or More Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
	(in millions)					
As of December 31, 2014						
Equity securities:						
Common stock	\$ 514.4	\$ 80.8	\$	\$	\$ 514.4	\$ 80.8
Preferred stock						
Total equity securities	514.4	80.8			514.4	80.8
Debt securities:						

Edgar Filing: ALLEGHANY CORP /DE - Form 10-Q

U.S. Government obligations	270.5	3.1	16.3	0.4	286.8	3.5
Municipal bonds	105.2	0.8	372.0	8.3	477.2	9.1
Foreign government obligations	6.1		5.7		11.8	
U.S. corporate bonds	574.7	17.2	150.7	4.0	725.4	21.2
Foreign corporate bonds	133.4	4.1	26.2	0.4	159.6	4.5
Mortgage and asset-backed securities:						
RMBS	187.9	0.5	586.4	11.2	774.3	11.7
CMBS	176.5	0.7	60.9	0.7	237.4	1.4
Other asset-backed securities	1,041.1	12.7	175.3	0.8	1,216.4	13.5
Total debt securities	2,495.4	39.1	1,393.5	25.8	3,888.9	64.9
Total temporarily impaired securities	\$ 3,009.8	\$ 119.9	\$ 1,393.5	\$ 25.8	\$ 4,403.3	\$ 145.7

As of September 30, 2015, Alleghany held a total of 885 debt securities and equity securities that were in an unrealized loss position, of which 106 securities, all debt securities, were in an unrealized loss position continuously for 12 months or more. The unrealized losses associated with the 106 debt securities consisted primarily of losses related to U.S. corporate bonds, municipal bonds, other asset-backed securities and RMBS.

Table of Contents

As of September 30, 2015, the vast majority of Alleghany's debt securities were rated investment grade, with approximately 3.5 percent of debt securities having issuer credit ratings that were below investment grade or not rated.

(g) Investments in Certain Other Invested Assets

In December 2012, TransRe obtained an ownership interest in Pillar Capital Holdings Limited (Pillar Holdings), a Bermuda-based insurance asset manager focused on collateralized reinsurance and catastrophe insurance-linked securities. Additionally, TransRe invested \$175.0 million and AIHL invested \$25.0 million in limited partnership funds managed by Pillar Holdings (the Funds). The objective of the Funds is to create portfolios with attractive risk-reward characteristics and low correlation with other asset classes, using the extensive reinsurance and capital market experience of the principals of Pillar Holdings. Alleghany has concluded that both Pillar Holdings and the Funds (collectively, the Pillar Investments) represent variable interest entities and that Alleghany is not the primary beneficiary, as it does not have the ability to direct the activities that most significantly impact each entity's economic performance. Therefore, the Pillar Investments are not consolidated and are accounted for under the equity method of accounting. Alleghany's potential maximum loss in the Pillar Investments is limited to its cumulative net investment. As of September 30, 2015, Alleghany's carrying value in the Pillar Investments, as determined under the equity method of accounting, was \$230.4 million, which is net of returns of capital received from the Pillar Investments.

In July 2013, AIHL invested \$250.0 million in Ares, an asset manager, in exchange for a 6.25 percent equity stake in Ares, with an agreement to engage Ares to manage up to \$1.0 billion in certain investment strategies. In May 2014, Ares completed an initial public offering of its common units. Upon completion of the initial public offering, Alleghany's equity investment in Ares converted to limited partner interests in certain Ares subsidiaries that are convertible into an aggregate 5.9 percent interest in Ares common units. As of September 30, 2015, at Alleghany's discretion, half of these interests may be converted at any time, and the remaining half may be converted in May 2016. Until Alleghany determines to convert its limited partner interests into Ares common units, Alleghany classifies its investment in Ares as a component of other invested assets, and accounts for its investment using the equity method of accounting. As of September 30, 2015, AIHL's carrying value in Ares was \$228.4 million, which is net of returns of capital received from Ares.

4. Reinsurance Ceded***(a) Overview***

Alleghany's reinsurance and insurance subsidiaries reinsure portions of the risks they underwrite in order to reduce the effect of individual or aggregate exposure to losses, manage capacity, protect capital resources, reduce volatility in specific lines of business, improve risk-adjusted portfolio returns and enable them to increase gross premium writings and risk capacity without requiring additional capital. Alleghany's reinsurance and insurance subsidiaries purchase reinsurance and retrocessional coverages from highly-rated third party reinsurers. If the assuming reinsurers are unable or unwilling to meet the obligations assumed under the applicable reinsurance agreements, Alleghany's reinsurance and insurance subsidiaries would remain liable for such reinsurance portion not paid by these reinsurers. As such, funds, trust agreements and letters of credit are held to collateralize a portion of Alleghany's reinsurance and insurance subsidiaries' reinsurance recoverables, and Alleghany's reinsurance and insurance subsidiaries reinsure portions of the risks they underwrite or assume with multiple reinsurance programs.

(b) Significant Reinsurance Contracts

As discussed in Note 5(d) to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K, RSUI reinsures its property lines of business through a program consisting of surplus share treaties, facultative placements, per risk and catastrophe excess of loss treaties. RSUI's catastrophe reinsurance program (which covers catastrophe risks including, among others, windstorms and earthquakes) and property per risk reinsurance program run on an annual basis from May 1 to the following April 30 and portions expired on April 30, 2015.

RSUI's catastrophe reinsurance program covers catastrophe risks including, among others, windstorms and earthquakes. As of May 1, 2015, the catastrophe reinsurance program consists of three layers with the first two layers placed on May 1, 2015 and the third layer placed on May 1, 2014. Portions of the catastrophe reinsurance program include multi-year terms, some of which were entered into in 2014. The catastrophe reinsurance program provides coverage for \$600.0 million of losses in excess of a \$200.0 million net retention after application of surplus share treaties and facultative reinsurance. The first layer provides coverage for \$300.0 million of losses, subject to a 5.0 percent co-participation by RSUI in excess of \$200.0 million, the second layer provides coverage for \$100.0 million of losses in excess of \$500.0 million, with no co-participation by RSUI, and the third layer provides coverage for \$200.0 million of losses in excess of \$600.0 million, with no co-participation by RSUI. The first and second layers of coverage include expiration terms as follows: 34.0 percent of coverage limits will expire on April 30, 2016; 33.0 percent of coverage limits will expire on April 30, 2017; and 33.0 percent of coverage limits will expire on April 30, 2018. The third layer of coverage will expire on April 30, 2017.

Table of Contents

In addition, RSUI's property per risk reinsurance program runs on an annual basis from May 1 to the following April 30 and thus expired on April 30, 2015. On May 1, 2015, the property per risk program was renewed and will expire on April 30, 2016. For the 2015 to 2016 period, RSUI's property per risk reinsurance program provides coverage for \$90.0 million of losses, subject to a 10.0 percent co-participation by RSUI, in excess of a \$10.0 million net retention per risk after application of surplus share treaties and facultative reinsurance.

(c) Intercompany Reinsurance Contracts

In the third quarter of 2015, AIHL Re and CapSpecialty (specifically, the insurance subsidiaries of CapSpecialty) entered into an intercompany reinsurance contract, effective July 1, 2015, pursuant to which AIHL Re will provide CapSpecialty with coverage for adverse development on net loss and allocated LAE for accident years 2014 and prior in excess of its carried reserves at June 30, 2015. AIHL Re's commitments are intended to cover the statutory collateral requirements at CapSpecialty, if and when necessary, and AIHL Re's obligations are subject to an aggregate limit of \$50.0 million. In connection with such intercompany reinsurance agreement, Alleghany and AIHL Re entered into a contract whereby Alleghany will guarantee the recoverable balances owed to CapSpecialty from AIHL Re up to \$50.0 million. The above agreements had no impact on Alleghany's consolidated results of operations and financial condition.

5. Income Taxes

The effective tax rate on earnings before income taxes for the first nine months of 2015 was 25.4 percent, compared with 26.7 percent for the first nine months of 2014. The slight decrease in the effective tax rate in the first nine months of 2015 compared with the first nine months of 2014 primarily reflects lower taxable income in the first nine months of 2015, partially offset by lower interest income arising from municipal bond securities.

Alleghany believes that, as of September 30, 2015, it had no material uncertain tax positions. Interest and penalties relating to unrecognized tax expenses (benefits) are recognized in income tax expense, when applicable. There were no material liabilities for interest or penalties accrued as of September 30, 2015.

6. Stockholders Equity***(a) Common Stock Repurchases***

In October 2012, the Alleghany Board of Directors authorized a program to repurchase shares of common stock of Alleghany, at such times and at prices as management determined advisable, up to an aggregate of \$300.0 million (the 2012 Repurchase Program). In July 2014, the Alleghany Board of Directors authorized, upon the completion of the 2012 Repurchase Program, the repurchase of additional shares of common stock, at such times and at prices as management determines advisable, up to an aggregate of \$350.0 million (the 2014 Repurchase Program). In the fourth quarter of 2014, Alleghany completed the 2012 Repurchase Program and subsequent repurchases have been made pursuant to the 2014 Repurchase Program.

Table of Contents

Under the 2012 Repurchase Program and the 2014 Repurchase Program, as applicable, Alleghany repurchased shares of its common stock in the three and nine months ended September 30, 2015 and 2014 as follows:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Shares repurchased	324,661	148,231	412,844	549,853
Cost of shares repurchased (in millions)	\$ 152.0	\$ 62.5	\$ 192.5	\$ 222.4
Average price per share repurchased	\$ 468.11	\$ 421.89	\$ 466.33	\$ 404.55

(b) Accumulated Other Comprehensive Income

The following table presents a reconciliation of the changes during the nine months ended September 30, 2015 and 2014 in accumulated other comprehensive income attributable to Alleghany stockholders:

	Unrealized Appreciation of Investments	Unrealized Currency Adjustment	Retirement Plans	Total
Balance as of January 1, 2015	\$ 455.4	\$ (89.2)	\$ (12.6)	\$ 353.6
Other comprehensive income, net of tax:				
Other comprehensive (loss) before reclassifications	(198.7)	(8.3)	(0.3)	(207.3)
Reclassifications from accumulated other comprehensive income	(30.0)			(30.0)
Total	(228.7)	(8.3)	(0.3)	(237.3)
Balance as of September 30, 2015	\$ 226.7	\$ (97.5)	\$ (12.9)	\$ 116.3

	Unrealized Appreciation of Investments	Unrealized Currency Adjustment	Retirement Plans	Total
Balance as of January 1, 2014	\$ 238.4	\$ (49.3)	\$ (2.2)	\$ 186.9
Other comprehensive income, net of tax:				
Other comprehensive income (loss) before reclassifications	302.9	(19.8)	0.1	283.2
Reclassifications from accumulated other comprehensive income	(124.1)			(124.1)
Total	178.8	(19.8)	0.1	159.1

Table of Contents

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
	(in millions, except share amounts)			
Net earnings available to Alleghany stockholders	\$ 96.5	\$ 186.3	\$ 404.2	\$ 540.2
Effect of dilutive securities			0.1	
Income available to common stockholders for diluted earnings per share	\$ 96.5	\$ 186.3	\$ 404.3	\$ 540.2
Weighted average common shares outstanding applicable to basic earnings per share	15,900,759	16,343,904	15,969,984	16,496,537
Effect of dilutive securities			8,155	
Adjusted weighted average common shares outstanding applicable to diluted earnings per share	15,900,759	16,343,904	15,978,139	16,496,537

72,865 and 71,411 contingently issuable shares were potentially available during the first nine months of 2015 and 2014, 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.

8. Commitments and Contingencies***(a) Legal Proceedings***

Certain of 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.

(b) Indemnification Obligations

On July 14, 2005, Alleghany completed the sale of its worldwide industrial minerals business. Pursuant to the terms of the sale, Alleghany undertook certain indemnification obligations, including a general indemnification for breaches of representations and warranties, and a special indemnification related to products liability claims arising from events that occurred during pre-closing periods, including the period of Alleghany ownership, that will expire on July 31, 2016. Additional information about these indemnification obligations can be found in Note 12(b) to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

(c) Leases

Alleghany and its subsidiaries lease certain facilities, furniture and equipment under long-term lease agreements. Additional information about leases can be found in Note 12(c) to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

(d) Asbestos-Related Illness and Environmental Impairment Exposure

Loss and LAE include amounts for risks relating to asbestos-related illness and environmental impairment. As of September 30, 2015 and December 31, 2014, such gross and net reserves were as follows:

	September 30, 2015		December 31, 2014	
	Gross	Net	Gross	Net
	(in millions)			
TransRe	\$ 597.9	\$ 438.8	\$ 593.5	\$ 438.3
CapSpecialty	8.9	8.8	9.2	9.1
Total	\$ 606.8	\$ 447.6	\$ 602.7	\$ 447.4

The reserves carried for such claims, including the incurred but not reported portion, are based upon known facts and current law at the respective balance sheet dates. However, significant uncertainty exists in determining the amount of ultimate liability for asbestos-related illness and environmental impairment losses, particularly for those occurring in 1985 and prior, which represents the majority of TransRe's asbestos-related illness and environmental impairment reserves. This uncertainty is due to inconsistent and changing court resolutions and judicial interpretations with respect to underlying policy intent and coverage and uncertainties as to the allocation of responsibility for resultant damages, among other reasons. Further, possible future changes in statutes, laws, regulations, theories of liability and other factors could have a material effect on these liabilities and, accordingly, future earnings.

Table of Contents**9. Segments of Business****(a) Overview**

Alleghany's segments are reported in a manner consistent with the way management evaluates the businesses. As such, Alleghany classifies its business into two reportable segments—reinsurance and insurance. In addition, reinsurance and insurance underwriting activities are evaluated separately from investment and corporate activities. Net realized capital gains and OTTI losses are not considered relevant in evaluating investment performance on an annual basis. Segment accounting policies are described in Note 1 to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

The reinsurance segment consists of property and casualty reinsurance operations conducted by TransRe's reinsurance operating subsidiaries and is further reported by major product lines—property and casualty & other. TransRe provides property and casualty reinsurance to insurers and reinsurers through brokers and on a direct basis to ceding companies. TransRe also writes a modest amount of insurance business, which is included in the reinsurance segment.

Approximately half of the premiums earned by TransRe's operations are generated by offices located in Canada, Europe, Asia, Australia, Africa and those serving Latin America and the Caribbean. Although the majority of the premiums earned by these offices typically relate to the regions where they are located, a significant portion may be derived from other regions of the world, including the U.S. In addition, although a significant portion of the assets and liabilities of these foreign offices generally relate to the countries where ceding companies and reinsurers are located, most investments are located in the country of domicile of these offices.

The insurance segment consists of property and casualty insurance operations conducted in the U.S. by AIHL through its insurance operating subsidiaries RSUI, CapSpecialty and PacificComp. RSUI also writes a modest amount of assumed reinsurance business, which is included in the insurance segment.

The primary components of corporate activities are Alleghany Properties, SORC, Bourn & Koch, Kentucky Trailer and Alleghany's investment in ORX and other activities at the parent level. Beginning July 31, 2014, corporate activities also include Alleghany's investment in Jazwares.

In addition, corporate activities include interest expense associated with senior notes issued by Alleghany, whereas interest expense associated with senior notes issued by TransRe is included in Total Segments. Information related to Alleghany's and TransRe's senior notes can be found in Note 8 to Notes to Consolidated Financial Statements set forth in Part II, Item 8, Financial Statements and Supplementary Data of the 2014 10-K.

(b) Results

Segment results for Alleghany's two reportable segments and for corporate activities for the three and nine months ended September 30, 2015 and 2014 are shown in the tables below:

Three Months Ended September 30, 2015	Reinsurance Segment			Insurance Segment			Total Segments	Corporate Activities	Consolidated	
	Property & Casualty	Casualty & other ⁽¹⁾	Total	RSUI	Cap Specialty	Pacific Comp				Total
	(in millions)									
Net premiums written	\$ 258.0	\$ 572.0	\$ 830.0	\$ 255.5	\$ 60.5	\$ 28.3	\$ 344.3	\$ 1,174.3	\$ (6.3)	\$ 1,168.0
Net premiums written	200.6	552.5	753.1	176.8	55.2	28.1	260.1	1,013.2		1,013.3
Net premiums earned	207.1	559.8	766.9	202.4	52.4	27.4	282.2	1,049.1		1,049.3

Edgar Filing: ALLEGHANY CORP /DE - Form 10-Q

Net loss and LAE	85.2	353.4	438.6	105.7	29.7	20.7	156.1	594.7	594.7	
Commissions, brokerage and other underwriting expenses	70.4	201.1	271.5	55.4	24.0	9.3	88.7	360.2	360.2	
Underwriting profit (loss) ⁽³⁾	\$ 51.5	\$ 5.3	\$ 56.8	\$ 41.3	\$ (1.3)	\$ (2.6)	\$ 37.4	94.2	94.2	
Net investment income								113.4	4.8	118.2
Net realized capital gains								28.2	1.0	29.2
Other than temporary impairment losses								(44.3)	(8.4)	(52.7)
Other income								0.3	45.0	45.3
Other operating expenses								16.7	51.8	68.5
Corporate administration								0.2	10.7	10.9
Amortization of intangible assets								(1.2)	0.1	(1.1)
Interest expense								9.7	13.1	22.8
Earnings (losses) before income taxes								\$ 166.4	\$ (33.3)	\$ 133.1

Table of Contents

Three Months Ended September 30, 2014	Reinsurance Segment			Insurance Segment			Total Segments	Corporate Activities	Consolidated	
	Property & other ⁽¹⁾	Casualty	Total	RSUI	Cap Specialty	Pacific Comp				Total
	(in millions)									
Gross premiums written	\$ 324.8	\$ 597.9	\$ 922.7	\$ 282.0	\$ 52.8	\$ 19.4	\$ 354.2	\$ 1,276.9	\$ (7.6)	\$ 1,269.3
Net premiums written	286.1	580.6	866.7	193.4	48.2	19.2	260.8	1,127.5		1,127.5
Net premiums earned	278.2	581.0	859.2	210.9	48.0	18.1	277.0	1,136.2		1,136.2
Net loss and LAE	113.4	361.0	474.4	106.9	25.8	16.0	148.7	623.1		623.1
Commissions, brokerage and other underwriting expenses	87.5	197.1	284.6	56.5	23.0	8.2	87.7	372.3		372.3
Underwriting profit (loss) ⁽³⁾	\$ 77.3	\$ 22.9	\$ 100.2	\$ 47.5	\$ (0.8)	\$ (6.1)	\$ 40.6	140.8		140.8
Investment income								113.0	5.3	118.3
Realized capital gains								56.3	3.1	59.4
Other than temporary impairment losses								(0.7)		(0.7)
Other income								0.9	37.9	38.8
Other operating expenses								18.4	41.2	59.6
Corporate administration								0.1	9.4	9.5
Amortization of intangible assets								(1.2)	0.1	(1.1)
Interest expense								12.2	10.5	22.7
Earnings (losses) before income taxes								\$ 280.8	\$ (14.9)	\$ 265.9

Reinsurance
SegmentInsurance
Segment

&nbs