OneBeacon Insurance Group, Ltd.
Form 10-Q
July 31, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the period ended June 30, 2009

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 1-33128

ONEBEACON INSURANCE GROUP, LTD.

(Exact name of Registrant as specified in its charter)

Bermuda (State or other jurisdiction of incorporation or organization)	**98-0503315** (I.R.S. Employer Identification No.)
601 Carlson Parkway **Minnetonka, Minnesota** (Address of principal executive offices)	**55305** (Zip Code)

Registrant s telephone number, including area code: **(952) 852-2431**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No 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.

Large accelerated filer o	Accelerated Filer x
Non-accelerated filer o	Smaller reporting company o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

As of July 29, 2009, 23,366,312 Class A common shares, par value of $0.01 per share, and 71,754,738 Class B common shares, par value of $0.01 per share, were outstanding.

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ONEBEACON INSURANCE GROUP, LTD.

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PART 1. FINANCIAL INFORMATION

ITEM 1. Financial Statements

ONEBEACON INSURANCE GROUP, LTD.

CONSOLIDATED BALANCE SHEETS

	June 30, 2009 (Unaudited)	December 31, 2008
	($ in millions, except share and per share amounts)	
Assets		
Investment Securities:		
Fixed maturity investments, at fair value (amortized cost $2,710.1 and $2,246.4)	$ 2,745.2	$ 2,134.8
Common equity securities, at fair value (cost $55.1 and $284.6)	58.0	276.7
Convertible bonds, at fair value (amortized cost $231.8 and $255.0)	225.5	241.2
Short-term investments, at amortized cost (which approximates fair value)	553.0	962.2
Other investments, at fair value (cost $158.1 and $178.6)	189.4	196.6
Total investments	3,771.1	3,811.5
Cash	50.0	53.0
Reinsurance recoverable on unpaid losses	723.9	859.4
Reinsurance recoverable on unpaid losses Berkshire Hathaway, Inc.	1,577.3	1,643.9
Reinsurance recoverable on paid losses	22.0	21.7
Premiums receivable	552.2	527.6
Securities lending collateral		100.7
Deferred acquisition costs	222.8	225.5
Net deferred tax asset	136.2	252.7
Investment income accrued	30.7	25.7
Ceded unearned premiums	65.2	66.5
Accounts receivable on unsettled investment sales	4.0	49.0
Other assets	339.0	303.6
Total assets	$ 7,494.4	$ 7,940.8
Liabilities		
Loss and LAE reserves	$ 4,060.5	$ 4,294.0
Unearned premiums	1,076.1	1,088.2
Debt	641.3	731.9
Securities lending payable	1.7	107.7
Ceded reinsurance payable	52.6	70.5
Accounts payable on unsettled investment purchases	1.1	6.8
Other liabilities	355.7	469.4
Total liabilities	6,189.0	6,768.5
Shareholders equity and noncontrolling interests		
OneBeacon s shareholders equity		
Common shares and paid-in surplus (par value $0.01; authorized, 200,000,000 shares; issued and outstanding, 95,121,050 and 95,094,199 shares)	1,017.6	1,016.7
Retained earnings	284.5	163.4
Accumulated other comprehensive loss, after-tax:		
Net unrealized foreign currency translation losses	(0.6)	(0.6)
Other comprehensive loss items	(17.1)	(24.4)
Total OneBeacon s shareholders equity	1,284.4	1,155.1
Total noncontrolling interests	21.0	17.2
Total OneBeacon s shareholders equity and noncontrolling interests	1,305.4	1,172.3
Total liabilities, OneBeacon s shareholders equity and noncontrolling interests	$ 7,494.4	$ 7,940.8

See Notes to Consolidated Financial Statements

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ONEBEACON INSURANCE GROUP, LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions, except per share amounts)			
Revenues				
Earned premiums	$ 490.2	$ 463.8	$ 978.0	$ 919.1
Net investment income	36.1	44.6	58.0	94.7
Net realized and unrealized investment gains (losses)	127.4	(2.6)	121.5	(58.0)
Net other revenues	1.1	2.6	10.5	6.2
Total revenues	654.8	508.4	1,168.0	962.0
Expenses				
Loss and LAE	275.7	274.4	563.7	575.3
Policy acquisition expenses	97.0	84.3	192.9	169.0
Other underwriting expenses	84.3	79.2	157.0	149.3
General and administrative expenses	6.5	4.5	12.0	7.4
Accretion of fair value adjustment to loss and LAE reserves	1.3	3.0	2.7	6.0
Interest expense on debt	10.1	11.4	21.0	22.9
Interest expense dividends on preferred stock subject to mandatory redemption		4.7		11.8
Interest expense accretion on preferred stock subject to mandatory redemption		11.1		21.6
Total expenses	474.9	472.6	949.3	963.3
Pre-tax income (loss)	179.9	35.8	218.7	(1.3)
Income tax (expense) benefit	(51.0)	(11.0)	(56.5)	2.9
Net income including noncontrolling interests	128.9	24.8	162.2	1.6
Less: Net income attributable to noncontrolling interests	(0.7)	(1.0)	(1.2)	(2.1)
Net income (loss) attributable to OneBeacon s shareholders	128.2	23.8	161.0	(0.5)
Change in other comprehensive income and loss items	6.2	1.2	7.3	
Comprehensive net income (loss) attributable to OneBeacon s shareholders	$ 134.4	$ 25.0	$ 168.3	$ (0.5)
Basic and diluted earnings (loss) per share attributable to OneBeacon s shareholders				
Basic:				
Net income (loss) attributable to OneBeacon s shareholders	$ 1.35	$ 0.25	$ 1.69	$ (0.01)
Diluted:				
Net income (loss) attributable to OneBeacon s shareholders	$ 1.35	$ 0.25	$ 1.69	$ (0.01)
Dividends declared and paid per share	$ 0.21	$ 0.21	$ 0.42	$ 2.45

See Notes to Consolidated Financial Statements

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ONEBEACON INSURANCE GROUP, LTD.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

(Unaudited)

	OneBeacon s Shareholders Equity				
	Common shareholders equity	**Common shares and paid-in surplus**	**Retained earnings ($ in millions)**	**Accum. other comprehensive (loss) income, after tax**	**Noncontrolling interests, after tax**
Balances at January 1, 2009	$ 1,155.1	$ 1,016.7	$ 163.4	$ (25.0)	$ 17.2
Net income	161.0		161.0		1.2
Accrued option expense	0.6	0.6			
Issuance of common shares	0.3	0.3			
Repurchases and retirements of common shares					0.3
Dividends	(39.9)		(39.9)		(0.6)
Contributions					2.9
Other comprehensive income, after tax	7.3			7.3	
Balances at June 30, 2009	$ 1,284.4	$ 1,017.6	$ 284.5	$ (17.7)	$ 21.0

	OneBeacon s Shareholders Equity				
	Common shareholders equity	**Common shares and paid-in surplus**	**Retained earnings ($ in millions)**	**Accum. other comprehensive income (loss), after tax**	**Noncontrolling interests, after tax**
Balances at January 1, 2008	$ 1,906.5	$ 1,084.4	$ 641.0	$ 181.1	$ 21.3
Adjustment to adopt SFAS No. 159, after tax			180.6	(180.6)	
Net (loss) income	(0.5)		(0.5)		2.1
Accrued option expense	0.8	0.8			
Repurchases and retirements of common shares	(62.2)	(62.2)			0.3
Dividends	(235.5)		(235.5)		(0.6)
Contributions					0.8
Other comprehensive income, after tax					
Balances at June 30, 2008	$ 1,609.1	$ 1,023.0	$ 585.6	$ 0.5	$ 23.9

See Notes to Consolidated Financial Statements

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ONEBEACON INSURANCE GROUP, LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions)	
Cash flows from operations:		
Net income including noncontrolling interests	$ 162.2	$ 1.6
Charges (credits) to reconcile net income to cash flows used for operations:		
Net realized and unrealized investment (gains) losses	(121.5)	58.0
Net realized gains from sale of common stock of subsidiary		(1.0)
Net realized loss on settlement of interest rate swap	7.4	
Net other realized gains	(4.4)	
Dividends paid on mandatorily redeemable preferred stock of subsidiary		11.8
Deferred income tax expense (benefit)	112.6	(31.5)
Other operating items:		
Net change in loss and LAE reserves	(233.5)	(54.8)
Net change in unearned premiums	(12.1)	44.4
Net change in ceded reinsurance payable	(17.9)	(4.5)
Net change in premiums receivable	(24.6)	(62.3)
Net change in reinsurance recoverable on paid and unpaid losses	201.8	57.4
Net change in other assets and liabilities	(129.3)	(118.6)
Net cash used for operations	(59.3)	(99.5)
Cash flows from investing activities:		
Net maturities, purchases and sales of short-term investments	410.6	(88.7)
Purchases of short-term held-to-maturity investments		(7.1)
Maturities of fixed maturity investments	189.9	481.9
Maturities of fixed maturity investments held-to-maturity		312.6
Sales of fixed maturity investments	389.2	586.3
Sales of common equity securities	212.8	135.5
Sales of convertible bonds	96.8	126.2
Distributions and redemptions of other investments	14.2	18.9
Purchases of fixed maturity investments	(1,073.2)	(611.1)
Purchases of common equity securities	(16.2)	(74.3)
Purchases of convertible bonds	(71.6)	(215.7)
Contributions for other investments	(3.8)	(20.6)
Sale of common stock of subsidiary, net of sales costs		4.2
Net change in unsettled investment purchases and sales	39.3	63.1
Net acquisitions of property and equipment	1.7	(0.1)
Net cash provided from investing activities	189.7	711.1
Cash flows from financing activities:		
Repayment of debt	(42.8)	(2.0)
Settlement of interest rate swap	(7.4)	
Repurchases of debt	(43.3)	
Cash dividends paid to common shareholders	(39.9)	(235.5)
Repurchases and retirements of Class A common shares		(62.2)
Redemption of mandatorily redeemable preferred stock of subsidiary		(300.0)
Dividends paid on mandatorily redeemable preferred stock of subsidiary		(11.8)
Net cash used for financing activities	(133.4)	(611.5)
Net (decrease) increase in cash during period	(3.0)	0.1
Cash balance at beginning of period	53.0	49.4
Cash balance at end of period	$ 50.0	$ 49.5
Supplemental cash flows information:		
Interest paid	$ 28.6	$ 22.2
Net tax payments to national governments	13.5	45.9

See Notes to Consolidated Financial Statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. Nature of Operations and Summary of Significant Accounting Policies

Basis of presentation

These interim consolidated financial statements include the accounts of OneBeacon Insurance Group, Ltd. (the Company or the Registrant) and its subsidiaries (collectively, OneBeacon) and have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The OneBeacon operating companies are U.S.-based property and casualty insurance writers, most of which operate in a multi-company pool. OneBeacon offers a wide range of specialty, commercial and personal products and services sold primarily through select independent agencies, brokers and managing general agencies.

OneBeacon was acquired by White Mountains Insurance Group, Ltd. (White Mountains) from Aviva plc (Aviva , formerly CGNU) in 2001 (the OneBeacon Acquisition). White Mountains is a holding company whose businesses provide property and casualty insurance, reinsurance and certain other products. During the fourth quarter of 2006, White Mountains sold 27.6 million or 27.6% of the Company s common shares in an initial public offering. Prior to the initial public offering, OneBeacon was a wholly-owned subsidiary of White Mountains. As of June 30, 2009 and December 31, 2008, White Mountains owned 75.4% and 75.5%, respectively, of the Company s common shares. Within this report, the term OneBeacon is used to refer to one or more entities within the consolidated organization, as the context requires. The Company is a Bermuda exempted limited company with its headquarters located at 14 Wesley Street, 5th Floor, Hamilton HM 11, Bermuda. The Company s principal executive office is located at 601 Carlson Parkway, Minnetonka, Minnesota 55305, its U.S. headquarters are located at 1 Beacon Lane, Canton, Massachusetts 02021 and its registered office is located at Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda. OneBeacon s reportable segments are Insurance Operations and Other Operations, as defined below.

OneBeacon s Insurance Operations segment, formerly known as Primary Insurance Operations, includes the results of its insurance operations. OneBeacon s Other Operations segment consists of the Company and its intermediate holding companies which include OneBeacon U.S. Enterprises Holdings, Inc. and OneBeacon U.S. Holdings, Inc. (OBH), both U.S.-domiciled companies, as well as various intermediate holding companies domiciled in the United States, Gibraltar, Luxembourg and Bermuda.

All significant intercompany transactions have been eliminated in consolidation. These interim financial statements include all adjustments, consisting of a normal recurring nature, considered necessary by management to fairly present the financial position, results of operations and cash flows of OneBeacon. These interim financial statements may not be indicative of financial results for the full year and should be read in conjunction with the Company s 2008 Annual Report on Form 10-K. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Refer to the Company s 2008 Annual Report on Form 10-K for a complete discussion regarding OneBeacon s significant accounting policies. Certain amounts in the prior period financial statements have been reclassified to conform to the current presentation.

Recently Adopted Changes in Accounting Principles

Business Combinations and Noncontrolling Interests

On January 1, 2009, OneBeacon adopted Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 141 (Revised 2007), Business Combinations A Replacement of FASB Statement No. 141 (SFAS 141R) and SFAS No. 160, Noncontrolling Interests an amendment to ARB 51 (SFAS 160).

SFAS 141R requires the acquiring company to recognize the fair value of all assets acquired and liabilities assumed at their fair values at the acquisition date, with certain exceptions including income taxes which will continue to be accounted for under SFAS No. 109, Accounting for Income Taxes (SFAS 109). This represents a basic change in approach from the old cost allocation method originally described in SFAS No. 141, Business Combinations (SFAS 141). In addition, SFAS 141R changes the accounting for step acquisitions since it requires recognition of all assets acquired and liabilities assumed, regardless of the acquirer s percentage of ownership in the acquiree. This means that the acquirer will measure and recognize all of the assets, liabilities and goodwill, not just the acquirer s share. Assets and liabilities arising from contractual contingencies are to be recognized at the acquisition date, at fair value. Non-contractual contingencies are to be recognized when it is more likely than not that they meet the Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements (A Replacement of FASB Concepts Statement No. 3 Incorporating an Amendment of FASB Concepts Statement No. 2) criteria for an asset or liability. Previously under SFAS 141, recognition of preacquisition contingencies was deferred until the criteria in SFAS No. 5, Accounting for Contingencies had been met. Changes in the amount of deferred taxes arising from a business combination are to be recognized in either income or

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through a change in contributed capital, depending on the circumstances. Previously under SFAS 109, such changes were recognized through goodwill. Acquisition related costs, such as legal fees and due diligence costs would be expensed and would not be recognized as part of goodwill. The classification of insurance and reinsurance contracts is re-evaluated at the acquisition date only if their terms were changed in connection with the acquisition. SFAS 141R applies prospectively to business combinations effective January 1, 2009. SFAS 141R did not impact OneBeacon s previous transactions involving purchase accounting.

SFAS 160 requires all companies to account for noncontrolling interests (formerly referred to as minority interests) in subsidiaries as equity, clearly identified and presented separately from parent company equity. Once a controlling interest has been acquired, any subsequent acquisitions or dispositions of noncontrolling interests that do not result in a change of control are to be accounted for as equity transactions. Assets and liabilities acquired are measured at fair value only once; at the original acquisition date, i.e., the date at which the acquirer gained control. When a subsidiary is deconsolidated, any retained noncontrolling equity investment is to be measured at fair value with the gain or loss on the deconsolidation being measured using fair value rather than the carrying amount of the retained ownership interest. The recognition and measurement requirements of SFAS 160 apply prospectively upon adoption; the presentation and disclosure requirements must be retrospectively applied. Accordingly, upon adoption of SFAS 160, OneBeacon has changed the presentation of its financial statements for prior periods to conform to the required presentation as follows: noncontrolling interests are presented on the balance sheets within equity, separate from OneBeacon s shareholders equity; the portion of net income and comprehensive income attributable to OneBeacon s common shareholders and the noncontrolling interests are presented separately on the consolidated statements of operations and comprehensive income (loss); and the consolidated statements of shareholders equity include a reconciliation of the noncontrolling interests from the beginning to the end of each reporting period.

Derivatives and Hedging Activities

On January 1, 2009, OneBeacon adopted SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities an Amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 requires companies that use derivatives to disclose the following: objectives and strategies for using derivative instruments in terms of underlying risk and accounting designation; the fair values of derivative instruments and their gains and losses in a tabular format; and information about credit-risk-related contingent features. The adoption of SFAS 161 had no impact on OneBeacon s financial position or results of operations. See Note 6 for disclosures related to OneBeacon s interest rate swap.

Participating Securities Granted in Share-Based Payment Transactions

On January 1, 2009, OneBeacon adopted FASB Staff Position (FSP) EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Transactions are Participating Securities. The FSP addresses whether instruments granted in share-based payment transactions should be considered participating securities prior to vesting. The FSP requires that such instruments that hold unforfeitable rights to dividends or dividend equivalents, regardless of whether paid or unpaid, should be considered participating securities and accordingly should be included in the calculation of earnings per share under the two-class method instead of the treasury stock method. Unvested restricted stock issued under employee incentive compensation plans containing such dividend participation features would be considered participating securities. None of OneBeacon s share-based payment transactions include participating securities. This FSP did not impact OneBeacon s earnings per share calculation. See Note 12 for the calculation of earnings per share.

Fair Value Measurements

On January 1, 2009, OneBeacon adopted FSP FAS 157-2, Effective Date of FASB Statement No. 157 (FSP FAS 157-2). FSP FAS 157-2 delayed the effective date of SFAS No. 157, Fair Value Measurements (SFAS 157) for nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008. OneBeacon adopted SFAS 157 for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) as of January 1, 2008 with respect to its investments securities. Refer to Note 5 for the required disclosures related to investment securities. The adoption of FSP FAS 157-2 had no impact on OneBeacon s financial position or results of operations.

Other-Than-Temporary Impairments

On June 30, 2009, OneBeacon adopted FSP FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments (FSP FAS 115-2 and FAS 124-2) which amends the guidance for other-than temporary impairments for debt securities classified as held-to-maturity or available-for-sale. FSP FAS 115-2 and FAS 124-2 requires that in evaluating if an impairment of a debt security is other-than-temporary, the entity is to assess whether it has the intent to sell the security or if it is more likely than not that it will be required to sell the security before the recovery of its amortized cost basis. If the present value of cash flows expected to be collected is less than the amortized cost of the security, a credit loss is deemed to exist and the security is

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considered to be impaired. The portion of the impairment loss related to a credit loss is to be recognized in earnings. The portion of the impairment loss related to factors other than credit loss is recognized in other comprehensive income. Upon adoption of FSP FAS 115-2 and FAS 124-2, a cumulative effect adjustment to the opening balance of retained earnings shall be recorded with a corresponding adjustment to accumulated other comprehensive income.

OneBeacon accounts for its investments in debt securities under SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159) and accordingly, all changes in the fair value of its debt securities are recognized in revenues regardless of whether or not such changes in fair value represent a temporary or other-than-temporary decline in value. Accordingly, the adoption of FSP FAS 115-2 and FAS 124-2 had no effect on OneBeacon s method of accounting for its portfolio of investment securities.

Determining Fair Values in an Inactive Market and Distressed Transactions

On June 30, 2009, OneBeacon adopted FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly (FSP FAS 157-4). This FSP provides guidance for estimating fair value in accordance with SFAS 157 when the volume and level of activity for the asset or liability have significantly decreased and on identifying circumstances that indicate a transaction is not orderly. Factors to consider include few recent transactions, price quotations that are not based on current information or which vary substantially over time or among market makers, a significant increase in implied liquidity risk premiums, yields, or performance indicators, a wide bid-ask spread, a significant decline or absence of a market for new issuances or limited information released publicly. A reporting entity should evaluate whether there has been a significant decrease in the volume and level of activity for the asset or liability when compared with normal activity for the asset or liability or similar assets or liabilities. If the reporting entity concludes that there has been a significant decrease in the volume and level of activity, transactions or quoted prices may not be determinative of fair value. Further analysis of the transactions or quoted prices is needed, and a significant adjustment to the transactions or quoted prices may be necessary to estimate fair value in accordance with SFAS 157, which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction. In addition, FSP FAS 157-4 expands interim disclosures to require a description of the inputs and valuation techniques used to estimate fair value and a discussion of changes during the period. The adoption of FSP FAS 157-4 had no material impact on OneBeacon s financial position or results of operations.

Interim Fair Value Disclosures

On June 30, 2009, OneBeacon adopted FSP FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments (FSP FAS 107-1 and APB 28-1) which amends SFAS No. 107, Disclosures about Fair Value of Financial Instruments and Accounting Principles Board Opinion (APB) No. 28, Interim Financial Reporting . Under FSP FAS 107-1 and APB 28-1, a publicly traded company shall disclose in the body or the accompanying notes of its summarized financial information for interim reporting periods and in its financial statements for its annual reporting periods the fair value of all financial instruments for which it is practicable to estimate that value. An entity shall also disclose the method(s) and significant assumptions used to estimate the fair value of the financial instruments and any changes in the method(s) and significant assumptions, if any, during the period. OneBeacon carries its financial instruments on its balance sheet at fair value with the exception of its fixed-rated, long-term indebtedness. See Note 11 for required disclosures.

Subsequent Events

On June 30, 2009, OneBeacon adopted SFAS No. 165, Subsequent Events (SFAS 165) which establishes principles and requirements for subsequent events. SFAS 165 establishes the period after the balance sheet date during which management shall evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; the circumstances under which an entity shall recognize events or transactions occurring after the balance sheet date in its financial statements; and the disclosures that an entity shall make about events or transactions that occurred after the balance sheet date. Subsequent events that provide additional evidence about conditions that existed at the balance sheet date are to be recognized in the financial statements. Subsequent events that are conditions that arose after the balance sheet date but prior to the issuance of the financial statements are not recognized in the financial statements, but should be disclosed if failure to do so would render the financial statements misleading. SFAS 165 requires disclosure of the date through which subsequent events have been evaluated. For subsequent events not recognized, disclosures should include a description of the nature of the event and either an estimate of its financial effect or a statement that such an estimate cannot be made. The adoption of SFAS 165 had no impact on the recognition or disclosure of subsequent events. OneBeacon evaluates subsequent events through the date it files its Quarterly Report on Form 10-Q with the Securities and Exchange Commission (SEC). For the period ended June 30, 2009, this date was July 31, 2009.

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Recent Accounting Pronouncements

Disclosures about Postretirement Benefit Plan Assets

In December 2008, the FASB issued FSP FAS 132(R)-1, Employers Disclosures about Postretirement Benefit Plan Assets. The FSP requires additional disclosures regarding plan assets of a defined benefit pension or other postretirement plan. The disclosures are to provide users of financial statements with an understanding of how investment allocation decisions are made, the major categories of plan assets, the inputs and valuation techniques used to measure the fair value of plan assets, the effect of fair value measurements using significant unobservable inputs on changes in plan assets for the period and significant concentrations of risk within plan assets. This FSP is effective for fiscal years ending after December 15, 2009 with earlier adoption permitted. OneBeacon is currently evaluating the potential impact of adopting this FSP.

Transfers of Financial Assets and Amendments to FIN 46R

In June 2009, the FASB issued SFAS No. 166, Accounting for Transfers of Financial Assets (SFAS 166) and SFAS No. 167, Amendments to FIN46(R) (SFAS 167). SFAS 166 eliminates the concept of a qualifying special-purpose entity (QSPE) and accordingly, any existing QSPE must be evaluated for consolidation upon adoption of SFAS 166. Under SFAS 166, the appropriateness of derecognition is evaluated based on whether or not the transferor has surrendered control of the transferred assets. The evaluation must consider any continuing involvement by the transferor. SFAS 167 amends FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities (FIN 46R) to require a reporting entity to perform an analysis to determine if its variable interests or interests give it a controlling financial interest in a variable interest entity (VIE). The analysis required under SFAS 167 identifies the primary beneficiary of a VIE as the entity having both of the following:

- The power to direct the activities of a variable interest entity that most significantly impact the entity s economic performance; and

- The obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE.

In addition, a reporting entity must assess whether it has an implicit financial responsibility to ensure that a VIE operates as designed when determining if it has the power to direct the activities of the VIE that most significantly affect the entity s economic performance. The concept of a reconsideration event is retained in SFAS 167, however it amends FIN 46R to require ongoing reassessments of whether a reporting entity is the primary beneficiary of a VIE. Specifically, the list of reconsideration events includes a change in facts and circumstances where the holders of an equity investment at risk as a group lose the power from voting or similar rights to direct the activities of the entity that most significantly affect the entity s economic performance. In addition, a troubled debt-restructuring is now defined as reconsideration event. Both statements expand required disclosures and are effective as of the beginning of the first annual reporting period that begins after November 15, 2009. OneBeacon is currently evaluating the potential impact of adopting SFAS 166 and SFAS 167.

Accounting Standards Codification

In June 2009, the FASB issued SFAS No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles (SFAS 168) which establishes the FASB Accounting Standards Codification (Codification) as the source of authoritative accounting principles to be applied in the preparation of financial statements in conformity with GAAP. SFAS 168 is effective for interim and annual periods ending after September 15, 2009. At that date, all then-existing non-SEC accounting and reporting standards will be superseded by the Codification. OneBeacon will adopt SFAS 168 for the interim period ending September 30, 2009. Adoption is not expected to have any effect on OneBeacon s accounting policies or financial statement presentation. However, since the Codification will change the basis for reference to authoritative GAAP guidance, OneBeacon s note disclosures that reference such guidance will change to reflect the references under Codification upon adoption.

NOTE 2. Acquisitions and Dispositions

During the first six months of 2009, there were no acquisitions or dispositions. During the first quarter of 2008, OneBeacon sold one of its inactive licensed subsidiaries, Midwestern Insurance Company, to National Guaranty Insurance Company for $4.2 million in cash and recorded a pre-tax gain of $1.0 million through net other revenues.

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NOTE 3. Reserves for Unpaid Loss and LAE

The following table summarizes the loss and LAE reserve activities of OneBeacon s insurance subsidiaries for the three and six months ended June 30, 2009 and 2008:

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
	($ in millions)			
Gross beginning balance	$ 4,211.2	$ 4,460.4	$ 4,294.0	$ 4,480.3
Less beginning reinsurance recoverable on unpaid losses	(2,440.9)	(2,601.3)	(2,503.3)	(2,629.5)
Net loss and LAE reserves	1,770.3	1,859.1	1,790.7	1,850.8
Loss and LAE incurred relating to:				
Current year losses	293.5	274.0	596.3	587.5
Prior year losses	(17.8)	0.4	(32.6)	(12.2)
Total incurred loss and LAE	275.7	274.4	563.7	575.3
Accretion of fair value adjustment to net loss and LAE reserves	1.3	3.0	2.7	6.0
Loss and LAE paid relating to:				
Current year losses	(113.0)	(117.9)	(189.3)	(186.0)
Prior year losses	(175.0)	(165.0)	(408.5)	(392.5)
Total loss and LAE payments	(288.0)	(282.9)	(597.8)	(578.5)
Net ending balance	1,759.3	1,853.6	1,759.3	1,853.6
Plus ending reinsurance recoverable on unpaid losses	2,301.2	2,571.9	2,301.2	2,571.9
Gross ending balance	$ 4,060.5	$ 4,425.5	$ 4,060.5	$ 4,425.5

During the three months ended June 30, 2009, OneBeacon experienced $17.8 million of favorable loss and LAE reserve development primarily due to lower than expected severity on non-catastrophe losses related to professional liability in specialty lines and commercial multi-peril in commercial lines. During the three months ended June 30, 2008, OneBeacon experienced $0.4 million of adverse loss and LAE reserve development primarily related to adverse loss reserve development at AutoOne Insurance (AutoOne) and in run-off, offset by favorable loss reserve development due to lower than expected severity on non-catastrophe losses primarily related to professional liability in specialty lines and package business in commercial lines.

During the six months ended June 30, 2009, OneBeacon experienced $32.6 million of favorable loss and LAE reserve development primarily due to lower than expected severity on non-catastrophe losses related to professional liability in specialty lines and commercial multi-peril in commercial lines, partially offset by adverse loss reserve development primarily related to New York personal injury protection litigation at AutoOne. During the six months ended June 30, 2008, OneBeacon experienced $12.2 million of favorable loss and LAE reserve development due to lower than expected severity on non-catastrophe losses and favorable loss reserve development on a prior accident year catastrophe. The favorable non-catastrophe loss reserve development was primarily related to professional liability in specialty lines and package business in commercial lines partially offset by adverse loss reserve development at AutoOne and in run-off.

In connection with purchase accounting for the OneBeacon Acquisition, loss and LAE reserves and the related reinsurance recoverables were adjusted to fair value on the balance sheets. The net reduction to loss and LAE reserves is being accreted through an income statement charge ratably with and over the period the claims are settled. Accordingly, OneBeacon recognized $1.3 million and $2.7 million of such charges for the three and six months ended June 30, 2009, respectively, and $3.0 million and $6.0 million of such charges for the three and six months ended June 30, 2008, respectively. As of June 30, 2009, the outstanding pre-tax unaccreted adjustment was $2.7 million.

NOTE 4. Reinsurance

In the normal course of business, OneBeacon s insurance subsidiaries seek to limit losses that may arise from catastrophes or other events by reinsuring with third party reinsurers. OneBeacon remains liable for risks reinsured even if the reinsurer does not honor its obligations under reinsurance contracts.

Effective July 1, 2009, OneBeacon renewed its property catastrophe reinsurance program through June 30, 2010. The program provides coverage for OneBeacon s personal and commercial property business as well as certain acts of terrorism. Under the program, the first $100 million of losses resulting from any single catastrophe are retained and the next $750 million of losses resulting from the catastrophe are reinsured. Any loss above $850 million would be retained. In the event of a catastrophe, OneBeacon s property catastrophe reinsurance program is reinstated for the remainder of the original contract term by paying a reinstatement premium that is based on the percentage of coverage reinstated and the original property catastrophe coverage premium.

OneBeacon entered into a 30% quota share agreement with a group of reinsurers effective from January 1, 2009 through December 31, 2009. During the three and six months ended June 30, 2009, OneBeacon ceded $16.4 million and $30.0 million, respectively, of written premiums from its Northeast homeowners business written through OneBeacon Insurance Company (OBIC) and its subsidiary companies, along with Adirondack Insurance Exchange and New Jersey Skylands Insurance Association in New York and New Jersey, respectively.

At June 30, 2009, OneBeacon had $22.0 million of reinsurance recoverables on paid losses and $2,499.0 million (gross of $197.8 million in purchase accounting adjustments, as described in Note 3) that will become recoverable if claims are paid in accordance with current reserve estimates. Reinsurance contracts do not relieve OneBeacon of its primary obligation to its insureds. Therefore, collectibility of balances due from its reinsurers is critical to OneBeacon s financial strength. OneBeacon is selective in regard to its reinsurers, principally placing reinsurance with those reinsurers with strong financial condition, industry ratings and underwriting ability. Management monitors the financial condition and ratings of its reinsurers on an ongoing basis. As a result, uncollectible amounts have historically not been significant. The following table provides a listing of OneBeacon s top reinsurers for its insurance operations, excluding industry pools and associations and affiliates of OneBeacon, based upon recoverable amounts, the percentage of total reinsurance recoverables and the reinsurers A.M. Best Company, Inc. (A.M. Best) ratings.

($ in millions)		Balance at June 30, 2009	% of total	A.M. Best Rating (1)
National Indemnity Company and General Reinsurance Corporation (2)	$	1,897.5	75%	A++
QBE Insurance Corporation		42.1	2%	A
Munich Reinsurance America		40.6	2%	A+
Tokio Marine and Nichido Fire (3)		35.0	1%	A++
Swiss Re		20.8	1%	A

(1) A.M. Best ratings as detailed above are: A++ (Superior, which is the highest of fifteen ratings), A+ (Superior, which is the second highest of fifteen ratings), and A (Excellent, which is the third highest of fifteen ratings).

(2) Includes $320.2 million of Third Party Recoverables, which NICO would pay under the terms of the NICO Cover if they are unable to collect from third party reinsurers. OneBeacon also has an additional $183.3 million of Third Party Recoverables from various reinsurers, the majority of which are rated A or better by A.M. Best.

(3) Excludes $40.6 million of reinsurance recoverables from various reinsurers that are guaranteed by Tokio Marine and Nichido Fire under the terms of a 100% quota share reinsurance agreement between Houston General Insurance Company and Tokio Marine and Nichido Fire.

In connection with the OneBeacon Acquisition, Aviva caused OneBeacon to purchase two reinsurance contracts: a reinsurance contract with National Indemnity Company (NICO) for up to $2.5 billion in old asbestos and environmental (A&E) claims and certain other exposures (the NICO Cover) and an adverse loss reserve development cover from General Reinsurance Corporation (GRC) for up to $570.0 million, comprised of $400.0 million of adverse loss reserve development occurring in years 2000 and prior (the GRC Cover) in addition to $170.0 million of reserves ceded as of the date of the OneBeacon Acquisition. The NICO Cover and GRC Cover, which were contingent on and occurred contemporaneously with the OneBeacon Acquisition, were put in place in lieu of a seller guarantee of loss and LAE reserves and are therefore accounted for as a seller guarantee under GAAP in accordance with Emerging Issues Task Force Technical Matter Document No. D-54. NICO and GRC are wholly-owned subsidiaries of Berkshire Hathaway, Inc.

Under the terms of the NICO Cover, NICO receives the economic benefit of reinsurance recoverables from certain of OneBeacon s third party reinsurers (Third Party Reinsurers) in existence at the time the NICO Cover was executed (Third Party Recoverables). As a result, the Third Party Recoverables serve to protect the $2.5 billion limit of NICO coverage for the benefit of OneBeacon. OneBeacon estimates that on an incurred basis it has used approximately $2.2 billion of the coverage provided by NICO at June 30, 2009. Since entering into the NICO Cover, $53.1 million of the $2.2 billion of utilized coverage relates to uncollectible Third Party Recoverables. Net losses paid totaled approximately $1.2 billion as of June 30, 2009. To the extent that actual experience differs from OneBeacon s estimate of ultimate A&E losses and Third Party Recoverables, future losses could exceed the $320.2 million of protection remaining under the NICO Cover.

Pursuant to the GRC Cover, OneBeacon is not entitled to recover losses to the full contract limit if such losses are reimbursed by GRC more quickly than anticipated at the time the contract was signed. OneBeacon intends to seek reimbursement from GRC only for claims which result in payment patterns similar to those supporting its recoverables recorded pursuant to the GRC Cover. The

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economic cost of not submitting certain other eligible claims to GRC is primarily the investment spread between the rate credited by GRC and the rate achieved by OneBeacon on its own investments. This cost, if any, is expected to be nominal.

NOTE 5. Investment Securities

OneBeacon s invested assets are comprised of securities and other investments held for general investment purposes. Refer to the Company s 2008 Annual Report on Form 10-K for a complete discussion.

On January 1, 2008, OneBeacon adopted SFAS 159, which allows companies to make an election, on an individual instrument basis, to report financial assets and liabilities at fair value. The election must be made at the inception of a transaction and may not be reversed. The election may also be made for existing financial assets and liabilities at the time of adoption. Unrealized gains and losses on assets or liabilities for which the fair value option has been elected are reported in revenues. In connection with the adoption of SFAS 159, OneBeacon recorded an adjustment of $180.6 million to reclassify net unrealized gains, after tax, and net unrealized foreign currency translation gains, after tax, related to investments from accumulated other comprehensive income to opening retained earnings.

In accordance with its adoption of SFAS 159, OneBeacon classifies its portfolio of fixed maturity investments and common equity securities, including convertible bonds, held for general investment purposes as trading. Trading securities are reported at fair value as of the balance sheet date as determined by quoted market prices when available. Realized and unrealized investment gains and losses on trading securities are reported pre-tax in revenues.

Short-term investments consist of money market funds, certificates of deposit and other securities which, at the time of purchase, mature or become available for use within one year. Short-term investments are carried at amortized cost, which approximated fair value as of June 30, 2009 and December 31, 2008.

Other investments include hedge funds and private equity funds. Upon adoption of SFAS 159, OneBeacon measures its investments in hedge funds and private equity funds at fair value with changes therein reported in revenues on a pre-tax basis.

OneBeacon participates in a securities lending program as a mechanism for generating additional investment income on its fixed maturity and common equity portfolios. Under the securities lending arrangements, certain of its fixed maturity and common equity investments are loaned to other institutions for short periods of time through a lending agent. OneBeacon maintains control over the securities it lends, retains the earnings and cash flows associated with the loaned securities and receives a fee from the borrower for the temporary use of the asset. Collateral, in the form of cash and United States government securities, is required at a rate of 102% of the fair value of the loaned securities. An indemnification agreement with the lending agent protects OneBeacon in the event a borrower becomes insolvent or fails to return any of the securities on loan. In the event of a shortfall in the collateral amount required to be returned to the securities lending counterparty (e.g., as a result of investment losses), OneBeacon is obligated to make up any deficiency.

In February 2009, OneBeacon amended the terms of the securities lending program to give it more control over the investment of borrowers collateral and to separate the assets supporting that collateral into a segregated account. Pursuant to the amendment, (i) the guidelines for the investment of any new cash collateral as well as the reinvestment of cash were narrowed to permit investment in only cash equivalent securities, (ii) OneBeacon has the authority to direct the lending agent to both sell specific collateral securities in the segregated account and to not sell certain collateral securities which the lending agent proposes to sell, and (iii) OneBeacon and the lending agent agreed to manage the securities lending program toward an orderly wind-down. In May 2009, OneBeacon instructed the lending agent not to make any additional loans of securities and to recall all of the securities on loan and fund the return of collateral to the borrower. As of June 30, 2009, $1.7 million in collateral had not been returned to the borrower.

Prior to February 2009, the collateral was controlled by the lending agent. The lending agent managed the investment of the cash collateral, however, other than in the event of default by the borrower, this collateral was not available to OneBeacon and was remitted to the borrower by the lending agent upon the return of the loaned securities. Because of these restrictions, OneBeacon considered its securities lending activities to be non-cash transactions. The fair value of the securities lending collateral was recorded as both an asset and liability on the balance sheet. At December 31, 2008, prior to the amendment of the terms of the securities lending program, the total market value of OneBeacon s securities on loan was $107.7 million with corresponding collateral of $100.7 million. As a result of the actions described above, the securities lending assets are no longer segregated and are included within the investment securities of OneBeacon.

OneBeacon s net investment income is comprised primarily of interest income associated with OneBeacon s fixed maturity investments, dividend income from its equity investments and interest income from its short-term investments. Net investment income for the three and six months ended June 30, 2009 and 2008 consisted of the following:

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	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions)			
Investment income:				
Fixed maturity investments	$ 35.7	$ 39.5	$ 56.7	$ 82.4
Common equity securities	0.6	4.3	1.0	9.1
Convertible bonds	1.6	1.6	3.1	3.2
Short-term investments	0.4	2.4	2.0	6.0
Other investments	0.7	0.7	1.0	1.2
Gross investment income	39.0	48.5	63.8	101.9
Less investment expenses	(2.9)	(3.9)	(5.8)	(7.2)
Net investment income, pre-tax	$ 36.1	$ 44.6	$ 58.0	$ 94.7

The composition of net realized investment gains (losses), a component of net realized and unrealized investment gains (losses), consisted of the following:

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions)			
Fixed maturity investments	$ (5.5)	$ (6.8)	$ (23.7)	$ (13.5)
Common equity securities	6.6	10.2	(33.0)	14.3
Convertible bonds	1.1	(5.5)	1.8	(1.8)
Short-term investments			0.1	
Other investments	(10.8)	0.4	(10.1)	3.0
Net realized investment (losses) gains, pre-tax	$ (8.6)	$ (1.7)	$ (64.9)	$ 2.0

The net changes in fair value for the three months ended June 30, 2009 and 2008 are as follows:

	Three months ended June 30, 2009		
	Changes in net unrealized gains and losses (1)	Changes in net foreign currency translation gains and losses (1)	Total net changes in fair value reflected in revenues (1)
		($ in millions)	
Fixed maturity investments	$ 97.8	$ 9.1	$ 106.9
Common equity securities	1.6		1.6
Convertible bonds	9.1		9.1
Short-term investments	(0.1)	0.8	0.7
Other investments	17.7		17.7
Total	$ 126.1	$ 9.9	$ 136.0

	Three months ended June 30, 2008		
	Changes in net unrealized gains and losses (1)	Changes in net foreign currency translation gains and losses (1)	Total net changes in fair value reflected in revenues (1)
		($ in millions)	
Fixed maturity investments	$ (44.2)	$ 2.5	$ (41.7)
Common equity securities	23.0	0.3	23.3
Convertible bonds	(0.2)		(0.2)

Short-term investments				0.4		0.4
Other investments		17.3				17.3
Total	$	(4.1)	$	3.2	$	(0.9)

(1) Includes changes in net deferred gains and losses on sales of investments between OneBeacon and entities under White Mountains common control of $0.1 million and $(0.7) million, pre-tax, for the three months ended June 30, 2009 and 2008, respectively.

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The net changes in fair value for the six months ended June 30, 2009 and 2008 are as follows:

	Six months ended June 30, 2009		
	Changes in net unrealized gains and losses (1)	Changes in net foreign currency translation gains and losses (1) ($ in millions)	Total net changes in fair value reflected in revenues (1)
Fixed maturity investments	$ 131.5	$ 15.5	$ 147.0
Common equity securities	10.7	0.1	10.8
Convertible bonds	7.4		7.4
Short-term investments	(0.2)	1.0	0.8
Other investments (2)	20.4		20.4
Total	$ 169.8	$ 16.6	$ 186.4

	Six months ended June 30, 2008		
	Changes in net unrealized gains and losses (1)	Changes in net foreign currency translation gains and losses (1) ($ in millions)	Total net changes in fair value reflected in revenues (1)
Fixed maturity investments	$ (41.2)	$ 3.2	$ (38.0)
Common equity securities	(12.4)	(0.5)	(12.9)
Convertible bonds	(15.2)		(15.2)
Short-term investments		1.4	1.4
Other investments	4.7		4.7
Total	$ (64.1)	$ 4.1	$ (60.0)

(1) Includes changes in net deferred gains and losses on sales of investments between OneBeacon and entities under White Mountains common control of $0.3 million and $(1.0) million, pre-tax, for the six months ended June 30, 2009 and 2008, respectively.

(2) Includes net unrealized gains related to OneBeacon s securities lending program of $7.0 million, pre-tax, for the six months ended June 30, 2009

The components of OneBeacon s ending net unrealized investment gains and losses, excluding the impact of net unrealized foreign currency translation gains and losses, on its trading investment portfolio as of June 30, 2009 and December 31, 2008 were as follows:

	June 30, 2009	December 31, 2008
	($ in millions)	
Investment securities:		
Gross unrealized investment gains	$ 128.5	$ 74.1
Gross unrealized investment losses	(62.3)	(170.6)
Net unrealized gains (losses) from investment securities	66.2	(96.5)
Income taxes attributable to such (gains) losses	(23.2)	33.7
Total net unrealized investment gains (losses), after tax	$ 43.0	$ (62.8)

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The cost or amortized cost, gross unrealized investment gains and losses, and carrying values of OneBeacon s fixed maturity investments as of June 30, 2009 and December 31, 2008, were as follows:

	June 30, 2009				
	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses ($ in millions)	Net foreign currency losses	Carrying value
U.S. Government and agency obligations	$ 442.5	$ 11.0	$ (0.3)	$	$ 453.2
Debt securities issued by industrial corporations	1,294.5	54.0	(15.2)	(3.2)	1,330.1
Municipal obligations	4.9	0.3			5.2
Asset-backed securities	876.8	12.9	(19.7)		870.0
Foreign government obligations	20.6	0.5	(0.6)		20.5
Preferred stocks	70.8	0.5	(5.1)		66.2
Total fixed maturity investments	$ 2,710.1	$ 79.2	$ (40.9)	$ (3.2)	$ 2,745.2

	December 31, 2008				
	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses ($ in millions)	Net foreign currency losses	Carrying value
U.S. Government and agency obligations	$ 417.3	$ 5.3	$ (13.0)	$	$ 409.6
Debt securities issued by industrial corporations	914.9	13.2	(39.2)	(18.7)	870.2
Municipal obligations	4.8	0.2			5.0
Asset-backed securities	791.9	9.3	(42.3)		758.9
Foreign government obligations	46.0	0.4	(7.8)		38.6
Preferred stocks	71.5	0.2	(19.2)		52.5
Total fixed maturity investments	$ 2,246.4	$ 28.6	$ (121.5)	$ (18.7)	$ 2,134.8

The cost or amortized cost, gross unrealized investment gains and losses, and carrying values of OneBeacon s common equity securities, convertible bonds and other investments as of June 30, 2009 and December 31, 2008, were as follows:

	June 30, 2009				
	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses ($ in millions)	Net foreign currency gains	Carrying value
Common equity securities	$ 55.1	$ 2.9	$	$	$ 58.0
Convertible bonds	231.8	4.0	(10.3)		225.5
Other investments	158.1	42.4	(11.1)		189.4

	December 31, 2008				
	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses ($ in millions)	Net foreign currency losses	Carrying value
Common equity securities	$ 284.6	$ 6.4	$ (14.2)	$ (0.1)	$ 276.7
Convertible bonds	255.0	2.4	(16.2)		241.2

Other investments	178.6	36.7	(18.7)	196.6

Fair value measurements at June 30, 2009

On January 1, 2008, OneBeacon adopted SFAS 157 which provides a revised definition of fair value, establishes a framework for measuring fair value and expands financial statement disclosure requirements for fair value information. Under SFAS 157, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants (an exit price). SFAS 157 establishes a fair value hierarchy that distinguishes between inputs based on market data from independent sources (observable inputs) and a reporting entity s internal assumptions based upon the best information available when external market data is limited or unavailable (unobservable inputs). The fair value hierarchy in SFAS 157 prioritizes fair value measurements into three levels based on the nature of the inputs as follows:

Level 1 Valuations based on quoted prices in active markets for identical assets;

Level 2 Valuations based on observable inputs that do not meet the criteria for Level 1, including quoted prices in inactive markets and quoted prices in active markets for similar, but not identical instruments; and

Level 3 Valuations based on unobservable inputs.

As of both June 30, 2009 and December 31, 2008, approximately 92% of the investment portfolio recorded at fair value was priced based upon observable inputs.

Fair values for securities for which quoted prices are unavailable are estimated based upon reference to observable inputs other than quoted prices, such as benchmark interest rates, market comparables, broker quotes and other relevant observable inputs. In circumstances where observable inputs are adjusted to reflect management s best estimate of fair value, such fair value measurements are considered a lower level measurement in the SFAS 157 fair value hierarchy.

Other investments, which are comprised of hedge funds and private equity funds for which the SFAS 159 fair value option has been elected, are carried at fair value based upon OneBeacon s proportionate interest in the underlying fund s net asset value, which is deemed to approximate fair value. The fair value of OneBeacon s investments in hedge funds and private equity funds has been estimated using net asset value because it reflects the fair value of the funds underlying investments in accordance with SFAS 157. OneBeacon employs a number of procedures to assess the reasonableness of the fair value measurements, including obtaining and reviewing each fund s audited financial statements and discussing each fund s pricing with the fund s manager. However, since the fund managers do not provide sufficient information to independently evaluate the pricing inputs and methods for each underlying investment, the inputs are considered to be unobservable. Accordingly, the fair values of OneBeacon s investment in hedge funds and private equity funds have been classified as Level 3 under SFAS 157.

In circumstances where the underlying investments are publicly traded, such as the investments made by hedge funds, the fair value of the underlying investments is determined using current market prices. In circumstances where the underlying investments are not publicly traded, such as the investments made by private equity funds, the private equity fund managers have considered the need for a liquidity discount on each of the underlying investments when determining the fund s net asset value in accordance with SFAS 157. In circumstances where OneBeacon s portion of a fund s net asset value is deemed to differ from fair value due to illiquidity or other factors associated with OneBeacon s investment in the fund, including counterparty credit risk, the net asset value is adjusted accordingly. At June 30, 2009 and December 31, 2008, OneBeacon did not record an adjustment to the net asset value related to its investments in hedge funds or private equity funds.

As of both June 30, 2009 and December 31, 2008, other investments represented approximately 5% of the investment portfolio recorded at fair value. Other investments accounted for at fair value as of June 30, 2009 and December 31, 2008 were comprised of $117.2 million and $117.3 million, respectively, in hedge funds, $58.1 million and $65.2 million, respectively, in private equity funds and $14.1 million for both periods of an investment in a community reinvestment vehicle. At June 30, 2009 and December 31, 2008, OneBeacon held investments in 19 and 20 hedge funds, respectively, and 17 and 16 private equity funds, respectively. The largest investment in a single fund was $28.6 million and $26.1 million at June 30, 2009 and December 31, 2008, respectively.

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The fair value measurements at June 30, 2009 and December 31, 2008 and their related inputs are as follows:

	Fair value at June 30, 2009	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
		($ in millions)		
Fixed maturity investments:				
U.S. Government and agency obligations	$ 453.2	$ 453.2	$	$
Debt securities issued by industrial corporations	1,330.1		1,329.4	0.7
Municipal obligations	5.2		5.2	
Asset-backed securities	870.0		837.9	32.1
Foreign government obligations	20.5	20.5		
Preferred stocks	66.2		0.9	65.3
Fixed maturity investments	2,745.2	473.7	2,173.4	98.1
Common equity securities	58.0	28.5		29.5
Convertible bonds	225.5		222.7	2.8
Short-term investments	553.0	553.0		
Other investments	189.4			189.4
Total	$ 3,771.1	$ 1,055.2	$ 2,396.1	$ 319.8

	Fair value at December 31, 2008	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
		($ in millions)		
Fixed maturity investments:				
U.S. Government and agency obligations	$ 409.6	$ 409.6	$	$
Debt securities issued by industrial corporations	870.2		870.2	
Municipal obligations	5.0		5.0	
Asset-backed securities	758.9		730.9	28.0
Foreign government obligations	38.6	20.2	18.4	
Preferred stocks	52.5		1.2	51.3
Fixed maturity investments	2,134.8	429.8	1,625.7	79.3
Common equity securities	276.7	249.2	1.3	26.2
Convertible bonds	241.2		241.2	
Short-term investments	962.2	962.2		
Other investments	196.6			196.6
Total	$ 3,811.5	$ 1,641.2	$ 1,868.2	$ 302.1

At June 30, 2009 and December 31, 2008, OneBeacon held one private preferred stock that represented approximately 98% and 97%, respectively, of its preferred stock portfolio. OneBeacon used quoted market prices for similar securities that were adjusted to reflect management s best estimate of fair value; this security is classified as a Level 3 measurement.

In addition to the investment portfolio described above, OneBeacon had $21.9 million and $20.2 million, respectively, of liabilities recorded at fair value in accordance with SFAS 157 and included in other liabilities as of June 30, 2009 and December 31, 2008. These liabilities relate to securities that have been sold short by a limited partnership that OneBeacon invests in and is required to consolidate in accordance with GAAP. All of the liabilities included in the $21.9 million and $20.2 million, respectively, have been deemed to have a Level 1 designation as of June 30, 2009 and December 31, 2008. As of December 31, 2008, other liabilities also included $10.4 million related to the fair value of the interest rate swap on the mortgage note. The interest rate swap was deemed to have a Level 2 designation at December 31, 2008. During the second quarter of 2009, OneBeacon repaid the outstanding balance on the mortgage note and settled the interest rate swap. See Note 6.

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The changes in Level 3 fair value measurements for the three and six months ended June 30, 2009 are as follows:

	Fixed maturity investments	Common equity securities	Convertible bonds ($ in millions)	Other investments	Total
Balance at January 1, 2009	$ 79.3	$ 26.2	$	$ 196.6	$ 302.1
Total net realized and unrealized gains (losses)	(1.0)	0.2		(4.6)	(5.4)
Purchases	12.0		0.5	3.5	16.0
Sales	(4.2)			(6.2)	(10.4)
Transfers in	11.2				11.2
Transfers out	(5.3)				(5.3)
Balance at March 31, 2009	$ 92.0	$ 26.4	$ 0.5	$ 189.3	$ 308.2
Total net realized and unrealized gains (losses)	15.9	3.1	0.1	7.9	27.0
Purchases			2.4	0.3	2.7
Sales	(8.5)		(0.2)	(8.1)	(16.8)
Transfers in	16.1				16.1
Transfers out	(17.4)				(17.4)
Balance at June 30, 2009	$ 98.1	$ 29.5	$ 2.8	$ 189.4	$ 319.8

Level 3 measurements for fixed maturities at March 31, 2009 and June 30, 2009 comprise securities for which the estimated fair value has not been determined based upon quoted market prices for identical or similar securities.

During the three months ended March 31, 2009 two securities for which the quoted market prices provided by a third party source were deemed to be unreliable based upon industry standard pricing models are reflected in Transfers in of $11.2 million. The fair value of these securities were estimated using industry standard pricing models in which management selected inputs using its best judgment. Inputs included matrix pricing, benchmark interest rates, market comparables and other relevant inputs. The industry standard pricing models used by OneBeacon apply the same valuation methodology for all Level 3 measurements for fixed maturities. Because these measurements are not directly observable, they are considered to be Level 3. The fair value for these securities determined using the industry standard pricing models was $0.8 million less than the estimated fair value based upon the third party source. Observable inputs in the form of quoted market prices for these securities had been used at December 31, 2008 to estimate fair value and these securities had been categorized as Level 2 measurements. In addition, during the first quarter one security which had been classified as a Level 3 measurement at December 31, 2008 was recategorized as a Level 2 measurement when quoted market prices became available and were deemed to be reliable at March 31, 2009. This measurement comprises Transfers out of $5.3 million for the three months ended March 31, 2009.

During the second quarter, OneBeacon identified three securities for which the quoted market prices provided by a third party source were deemed to be unreliable based upon industry standard pricing models described above and are reflected in Transfers in of $16.1 million. Because these measurements are not directly observable, they are considered to be Level 3. The fair value for these securities determined using the industry standard pricing models was $1.5 million less than the estimated fair value based upon the third party source. Observable inputs in the form of quoted market prices for these securities had been used at March 31, 2009 to estimate fair value and these securities had been categorized as Level 2 measurements. In addition, during the second quarter, three securities which had been classified as Level 3 measurements at March 31, 2009 were recategorized as Level 2 measurements when quoted market prices became available and were deemed to be reliable at June 30, 2009. These measurements comprise Transfers out of $13.0 million for the three months ended June 30, 2009.

In addition, during the three months ended March 31, 2009, OneBeacon took control of certain securities that were previously included in securities lending collateral and under the control of the lending agent. Because the pricing methodology and inputs used by the lending agent to estimate fair value for a number of these securities did not provide sufficient transparency to permit validation of the measurements, these measurements were categorized as Level 3 and are included in Purchases for the first quarter. During the second quarter, OneBeacon was able to obtain quoted market prices for similar or identical securities. The fair value measurements for these securities were estimated using those observable price inputs and the measurements were reclassified to Level 2 measurements and are included in Transfers out of $4.4 million.

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The following table summarizes the change in net unrealized gains or losses for assets designated as Level 3 at June 30, 2009 and 2008:

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions)			
Fixed maturity investments	$ 14.3	$ (18.2)	$ 13.9	$ (23.9)
Common equity securities	3.1	1.5	3.4	2.2
Convertible bonds	0.1		0.1	
Short-term investments				
Other investments	17.7	17.3	20.4	4.7
Total	$ 35.2	$ 0.6	$ 37.8	$ (17.0)

NOTE 6. Debt

OneBeacon s debt outstanding as of June 30, 2009 and December 31, 2008 consisted of the following:

	June 30, 2009	December 31, 2008
	($ in millions)	
Senior unsecured notes, at face value	$ 628.1	$ 676.0
Unamortized original issue discount	(0.8)	(0.9)
Senior unsecured notes, carrying value	627.3	675.1
Mortgage note on real estate owned		40.8
Atlantic Specialty Note	14.0	16.0
Total debt	$ 641.3	$ 731.9

Senior Notes

In May 2003, OBH, a wholly-owned subsidiary of the Company, issued $700.0 million face value of senior unsecured debt through a public offering, at an issue price of 99.7% (the Senior Notes). The Senior Notes bear an annual interest rate of 5.875%, payable semi-annually in arrears on May 15 and November 15, until maturity on May 15, 2013, and are fully and unconditionally guaranteed as to the payment of principal and interest by White Mountains. OBH incurred $7.3 million in expenses related to the issuance of the Senior Notes (including the $4.5 million underwriting discount), which have been deferred and are being recognized into interest expense over the life of the Senior Notes. Taking into effect the amortization of the original issue discount and all underwriting and issuance expenses, the Senior Notes have an effective yield to maturity of approximately 6.0% per annum. During the third quarter of 2008, OBH repurchased $24.0 million of the outstanding Senior Notes for $22.3 million, which resulted in a $1.6 million gain. During the first quarter of 2009, OBH repurchased $10.6 million of outstanding Senior Notes for $8.1 million, which resulted in a $2.5 million gain. During the second quarter of 2009, OBIC purchased $37.3 million of outstanding Senior Notes for $35.2 million, which resulted in a $1.9 million gain. At June 30, 2009, OBH was in compliance with all of the covenants under the Senior Notes.

White Mountains has provided and, pursuant to a separation agreement, continues to provide an irrevocable and unconditional guarantee as to the payment of principal and interest on the Senior Notes. Refer to Note 18. Related Party Disclosures of the Company s 2008 Annual Report on

Form 10-K.

Mortgage Note on Real Estate Owned

In connection with its December 2005 purchase of land and an office building that is now its U.S. headquarters, OneBeacon entered into a $40.8 million, 18-year mortgage note which had a variable interest rate based upon the lender s 30-day LIBOR rate. As of December 31, 2008, OneBeacon had drawn the full amount of $40.8 million on the mortgage note. Repayment on the mortgage note commenced in January 2009. During the three months ended March 31, 2009, OneBeacon repaid $0.2 million of principal in accordance with the terms of the mortgage note. On May 7, 2009, OneBeacon repaid $40.6 million, representing the outstanding principal on the mortgage note.

Concurrent with entering into the mortgage note, OneBeacon also entered into an interest rate swap to hedge its exposure to the variability in the interest rate on the mortgage note. The notional amount of the swap was equal to the debt outstanding on the mortgage note and was adjusted to match the drawdowns and repayments on the mortgage note so that the principal amount of the mortgage note and the notional amount of the swap were equal at all times. Under the terms of the swap, OneBeacon paid a fixed

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interest rate of approximately 6% and received a variable interest rate based on the same LIBOR index used for the mortgage note. Interest paid or received on the swap was reported in interest expense. In accordance with SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities , OneBeacon accounted for the swap as a cash flow hedge and recorded the interest rate swap at fair value on the balance sheet in other assets or liabilities depending on the value as of the balance sheet date. Changes in the fair value of the interest rate swap were reported as a component of other comprehensive income or loss. Any gains and losses on the derivatives representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness were recorded in revenues. At the time of repayment of the outstanding balance on the mortgage note, OneBeacon paid $7.4 million to settle the interest rate swap. The $7.4 million settlement amount is recorded as an expense in net other revenues on a pre-tax basis and in other comprehensive income and loss items as an increase of $4.8 million on an after tax basis ($7.4 million pre-tax). The three and six months ended June 30, 2009 also included $1.1 million and $2.0 million after tax, respectively, in other comprehensive income and loss items related to changes in fair value on the interest rate swap.

Other Debt of Operating Subsidiaries

In connection with the acquisition of Atlantic Specialty Insurance Company on March 31, 2004, OneBeacon issued a $20.0 million ten-year note to the seller (the Atlantic Specialty Note). OneBeacon is required to repay $2.0 million of principal on the Atlantic Specialty Note each year, commencing in January 2007. The Atlantic Specialty Note accrues interest at a rate of 5.2% except that the outstanding principal amount in excess of $15.0 million accrues interest at a rate of 3.6%. During each of the three months ended March 31, 2009 and 2008, OneBeacon repaid $2.0 million on the Atlantic Specialty Note.

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NOTE 7. Segment Information

OneBeacon s segments consist of the following: (1) Insurance Operations, formerly known as Primary Insurance Operations; and (2) Other Operations. OneBeacon has made its segment determination based on consideration of the following criteria: (i) the nature of the business activities of each of the Company s subsidiaries and affiliates; (ii) the manner in which the Company s subsidiaries and affiliates are organized; (iii) the existence of primary managers responsible for specific subsidiaries and affiliates; and (iv) the organization of information provided to the Board of Directors (the Board). Significant intercompany transactions among OneBeacon s segments have been eliminated herein. Financial information for OneBeacon s segments follows:

	Insurance Operations	Other Operations ($ in millions)	Total
Three months ended June 30, 2009			
Earned premiums	$ 490.2	$	$ 490.2
Net investment income (expense)	36.3	(0.2)	36.1
Net realized and unrealized investment gains	127.3	0.1	127.4
Net other (expenses) revenues	(0.3)	1.4	1.1
Total revenues	653.5	1.3	654.8
Loss and LAE	275.7		275.7
Policy acquisition expenses	97.0		97.0
Other underwriting expenses	84.3		84.3
General and administrative expenses	4.6	1.9	6.5
Accretion of fair value adjustment to loss and LAE reserves		1.3	1.3
Interest expense on debt	0.4	9.7	10.1
Interest expense on preferred stock subject to mandatory redemption			
Total expenses	462.0	12.9	474.9
Pre-tax income (loss) (1)	$ 191.5	$ (11.6)	$ 179.9
Three months ended June 30, 2008			
Earned premiums	$ 463.8	$	$ 463.8
Net investment income	41.2	3.4	44.6
Net realized and unrealized investment losses	(2.4)	(0.2)	(2.6)
Net other revenues (expenses)	3.0	(0.4)	2.6
Total revenues	505.6	2.8	508.4
Loss and LAE	274.4		274.4
Policy acquisition expenses	84.3		84.3
Other underwriting expenses	79.2		79.2
General and administrative expenses	2.2	2.3	4.5
Accretion of fair value adjustment to loss and LAE reserves		3.0	3.0
Interest expense on debt	0.8	10.6	11.4
Interest expense on preferred stock subject to mandatory redemption		15.8	15.8
Total expenses	440.9	31.7	472.6
Pre-tax income (loss) (1)	$ 64.7	$ (28.9)	$ 35.8

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	Insurance Operations	Other Operations ($ in millions)	Total
Six months ended June 30, 2009			
Earned premiums	$ 978.0	$	$ 978.0
Net investment income	57.9	0.1	58.0
Net realized and unrealized investment gains	121.4	0.1	121.5
Net other revenues	7.0	3.5	10.5
Total revenues	1,164.3	3.7	1,168.0
Loss and LAE	563.7		563.7
Policy acquisition expenses	192.9		192.9
Other underwriting expenses	157.0		157.0
General and administrative expenses	8.6	3.4	12.0
Accretion of fair value adjustment to loss and LAE reserves		2.7	2.7
Interest expense on debt	1.2	19.8	21.0
Interest expense on preferred stock subject to mandatory redemption			
Total expenses	923.4	25.9	949.3
Pre-tax income (loss) (1)	$ 240.9	$ (22.2)	$ 218.7
Six months ended June 30, 2008			
Earned premiums	$ 919.1	$	$ 919.1
Net investment income	84.3	10.4	94.7
Net realized and unrealized investment losses	(55.1)	(2.9)	(58.0)
Net other revenues (expenses)	7.0	(0.8)	6.2
Total revenues	955.3	6.7	962.0
Loss and LAE	575.3		575.3
Policy acquisition expenses	169.0		169.0
Other underwriting expenses	149.3		149.3
General and administrative expenses	2.8	4.6	7.4
Accretion of fair value adjustment to loss and LAE reserves		6.0	6.0
Interest expense on debt	1.8	21.1	22.9
Interest expense on preferred stock subject to mandatory redemption		33.4	33.4
Total expenses	898.2	65.1	963.3
Pre-tax income (loss) (1)	$ 57.1	$ (58.4)	$ (1.3)
June 30, 2009			
Total investments	$ 3,725.0	$ 46.1	$ 3,771.1
Reinsurance recoverable on paid and unpaid losses	2,521.0	(197.8)	2,323.2
Total assets	7,622.8	(128.4)	7,494.4
Loss and LAE reserves	4,261.0	(200.5)	4,060.5
Total liabilities	5,731.6	457.4	6,189.0
Total OneBeacon s shareholders equity	1,870.2	(585.8)	1,284.4
Total OneBeacon s shareholders equity and noncontrolling interests	1,891.2	(585.8)	1,305.4
December 31, 2008			
Total investments	$ 3,653.3	$ 158.2	$ 3,811.5
Reinsurance recoverable on paid and unpaid losses	2,730.1	(205.1)	2,525.0
Total assets	7,962.7	(21.9)	7,940.8
Loss and LAE reserves	4,504.5	(210.5)	4,294.0
Total liabilities	6,241.8	526.7	6,768.5
Total OneBeacon s shareholders equity	1,703.7	(548.6)	1,155.1
Total OneBeacon s shareholders equity and noncontrolling interests	1,720.9	(548.6)	1,172.3

(1) Includes income from noncontrolling interests.

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The following tables provide ratios, net written premiums and earned premiums for OneBeacon s Insurance Operations by major underwriting unit and in total for the three and six months ended June 30, 2009 and 2008:

	Specialty	Commercial	Personal	Total(1)
		($ in millions)		
Three months ended June 30, 2009				
Ratios:				
Loss and LAE	48.2%	54.3%	66.6%	56.2%
Expense	39.4	38.3	32.5	37.0
Total GAAP combined	87.6%	92.6%	99.1%	93.2%
Net written premiums	$ 176.7	$ 183.2	$ 137.9	$ 497.9
Earned premiums	171.5	172.5	146.1	490.2
Three months ended June 30, 2008				
Ratios:				
Loss and LAE	49.3%	53.6%	64.6%	59.2%
Expense	36.5	36.4	32.9	35.2
Total GAAP combined	85.8%	90.0%	97.5%	94.4%
Net written premiums	$ 158.6	$ 202.2	$ 168.9	$ 529.6
Earned premiums	119.4	182.7	161.7	463.8
Six months ended June 30, 2009				
Ratios:				
Loss and LAE	39.9%	56.2%	78.0%	57.6%
Expense	39.3	37.7	30.2	35.8
Total GAAP combined	79.2%	93.9%	108.2%	93.4%
Net written premiums	$ 355.4	$ 342.1	$ 269.6	$ 967.3
Earned premiums	334.2	347.3	296.3	978.0
Six months ended June 30, 2008				
Ratios:				
Loss and LAE	52.3%	62.8%	64.7%	62.6%
Expense	34.3	37.2	31.8	34.6
Total GAAP combined	86.6%	100.0%	96.5%	97.2%
Net written premiums	$ 269.5	$ 371.9	$ 313.6	$ 955.3
Earned premiums	229.8	363.7	325.3	919.1

(1) Includes results from run-off.

NOTE 8. Retirement Plans

OneBeacon sponsors qualified and non-qualified, non-contributory, defined benefit pension plans covering substantially all employees who were employed as of December 31, 2001 and remain actively employed with OneBeacon. Current plans include a OneBeacon qualified pension plan (the Qualified Plan) and a OneBeacon non-qualified pension plan (the Non-qualified Plan) (collectively the Plans). OneBeacon s Plans were frozen and curtailed in the fourth quarter of 2002.

The components of net periodic benefit cost (income) for the three and six months ended June 30, 2009 and 2008 were as follows:

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions)			
Service cost	$ 0.2	$ 0.2	$ 0.3	$ 0.4
Interest cost	1.6	1.7	3.2	3.4
Expected return on plan assets	(1.6)	(2.1)	(3.2)	(4.2)
Amortization of unrecognized loss	0.4	0.1	0.8	0.2
Net periodic benefit cost (income)	$ 0.6	$ (0.1)	$ 1.1	$ (0.2)

OneBeacon does not expect to make a contribution to its Qualified Plan in 2009. OneBeacon anticipates contributing $2.9 million to the Non-qualified Plan, for which OneBeacon has assets held in rabbi trusts. As of June 30, 2009, $1.5 million in contributions have been made to the Non-qualified Plan.

NOTE 9. Employee Share-Based Incentive Compensation Plans

OneBeacon s share-based compensation plans consist of performance shares, stock options granted in connection with the initial public offering and restricted stock units. OneBeacon s share-based compensation plans are designed to maximize shareholder value over long periods of time by aligning the financial interests of its management with those of its owners. Performance shares are payable only upon achievement of pre-defined business goals and are valued based on the market value of OneBeacon s common shares at the time awards are earned. See Performance Shares below. Performance shares are typically paid in cash, though, in some instances, they may be paid in common shares or may be deferred in accordance with the terms of one of the deferred compensation plans of the Company s subsidiaries. OneBeacon expenses the full cost of all its share-based compensation.

OneBeacon records its share-based compensation in accordance with SFAS No. 123(R), Share-Based Payment (SFAS 123R), which is a revision to SFAS No. 123, Accounting for Stock Based Compensation and supersedes APB No. 25, Accounting for Stock Issued to Employees . SFAS 123R applies to new grants of share-based awards, award modifications and the remaining portion of the fair value of unvested awards. The unvested portion of OneBeacon performance share awards, as well as new awards, such as the stock options granted in connection with the initial public offering, are subject to the fair value measurement and recognition requirements of SFAS 123R.

Performance Shares

The following summarizes performance share activity for performance shares whose value is based upon the market price of an underlying OneBeacon common share (OB Performance Shares) for the three and six months ended June 30, 2009 and 2008:

	Three months ended June 30,					
	2009			2008		
	Target OB Performance Shares outstanding		Accrued expense	Target OB Performance Shares outstanding		Accrued expense
			($ in millions)			
Beginning of period	2,318,849	$	5.7	2,131,894	$	6.9
Payments and deferrals						
New awards	29,178			69,958		
Forfeitures and net change in assumed forfeitures	(70,899)			(15,644)		(0.2)
Expense recognized			2.3			3.0
End of period	2,277,128	$	8.0	2,186,208	$	9.7

	Six months ended June 30,					
	2009			2008		
	Target OB Performance Shares outstanding		Accrued expense	Target OB Performance Shares outstanding		Accrued expense
			($ in millions)			
Beginning of period	2,212,313	$	4.6	1,058,194	$	9.2
Payments and deferrals (1)	(137,400)			(117,363)		(1.6)
New awards	377,205			1,397,100		
Forfeitures and net change in assumed forfeitures	(174,990)		(0.3)	(151,723)		(0.6)

Expense recognized			3.7			2.7
End of period	2,277,128	$	8.0	2,186,208	$	9.7

(1) Performance share payments in March 2009 for the 2007-2008 performance cycle were based upon a performance factor of 1.4%.

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The following summarizes performance shares outstanding and accrued performance share expense at June 30, 2009 for each performance cycle:

	Target OB Performance Shares outstanding		Accrued expense
		($ in millions)	
Performance cycle:			
2007 2009	684,339	$	
2008 2010	1,273,972		7.4
2009 2011	377,205		0.8
Sub-total	2,335,516		8.2
Assumed forfeitures	(58,388)		(0.2)
Total at June 30, 2009	2,277,128	$	8.0

If 100% of the outstanding performance shares had been vested on June 30, 2009, the total additional compensation cost to be recognized would have been $11.0 million, based on current accrual factors (common share price and payout assumptions).

All performance shares earned for the 2007-2008 performance cycle were settled in cash or by deferral into certain non-qualified deferred compensation plans of the Company s subsidiaries.

Stock Options

As described in the Company s 2008 Annual Report on Form 10-K, in connection with the initial public offering, OneBeacon issued options to acquire 1,420,000 common shares of the Company to certain members of management. The following summarizes option activity for the three and six months ended June 30, 2009 and 2008:

	Three Months Ended June 30,					
	2009			2008		
	Target options outstanding		Accrued expense	Target options outstanding		Accrued expense
			($ in millions)			
Beginning of period	1,148,350	$	2.8	1,258,091	$	1.7
Forfeitures	(40,130)			(20,219)		
Expense recognized			0.3			0.5
End of period	1,108,220	$	3.1	1,237,872	$	2.2

Six Months Ended June 30,

2009 2008

	Target options outstanding	Accrued expense	Target options outstanding	Accrued expense
		($ in millions)		
Beginning of period	1,237,872	$ 2.5	1,324,306	$ 1.4
Forfeitures	(129,652)		(86,434)	
Expense recognized		0.6		0.8
End of period	1,108,220	$ 3.1	1,237,872	$ 2.2

The options vest in equal installments on each of the third, fourth and fifth anniversaries of their issuance. These options expire five and a half years from the anniversary of issuance. The fair value of each option award at grant date was estimated using a Black-Scholes option pricing model using an expected volatility assumption of 30%, a risk-free interest rate assumption of 4.6%, a forfeiture assumption of 5%, an expected dividend rate assumption of 3.4% and an expected term assumption of 5.5 years. The options originally had a per share exercise price of $30.00. On May 27, 2008, the Compensation Committee of the Board (the Compensation Committee) amended the exercise price to $27.97 as a result of the $2.03 per share special dividend paid in the first quarter of 2008. The compensation expense associated with the options and the incremental fair value of the award modification is being recognized ratably over the remaining period.

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Restricted Stock Units

The options granted in connection with OneBeacon s initial public offering did not include a mechanism in the options to reflect the contribution to total return from the regular quarterly dividend. As a result, on February 26, 2008, OneBeacon granted 116,270 Restricted Stock Units (RSUs) to actively employed option holders. The RSUs vest one-third on each of November 9, 2009, 2010 and 2011 subject to, for each vesting tranche of units, the attainment of growth of 4% per cycle in adjusted book value per share. Upon vesting, the RSUs will be mandatorily deferred into one of the non-qualified deferred compensation plans of the Company s subsidiaries and will be paid out in 2012 in cash or shares at the discretion of the Compensation Committee. The expense associated with the RSUs is being recognized over the vesting period. For the three and six months ended June 30, 2009, OneBeacon recognized $0.3 million and $0.4 million, respectively, in expense. For the three and six months ended June 30, 2008, OneBeacon recognized $0.2 million and $0.4 million, respectively, in expense. As of June 30, 2009, 102,140 RSUs were outstanding.

NOTE 10. Income Taxes

While OneBeacon is subject to taxation in several jurisdictions, the majority of OneBeacon s subsidiaries file a consolidated tax return in the United States. Income earned or losses generated by companies outside the United States are generally subject to an overall effective rate lower than that imposed by the United States.

OneBeacon s income tax expense (benefit) related to pre-tax income or loss for the three months ended June 30, 2009 and 2008 represented effective tax rates of 28.3% and 30.7%, respectively. The effective tax rates for the six months ended June 30, 2009 and 2008 were 25.8% and (223.1%), respectively. For the three and six months ended June 30, 2009 the effective tax rate was lower than the U.S. statutory rate of 35% primarily due to income generated in jurisdictions other than the United States. The effective tax rate for the three months ended June 30, 2008 was lower than the U.S. statutory rate of 35% due to income generated in jurisdictions other than the United States, partially offset by non-deductible dividends and accretion on the Berkshire Hathaway, Inc. Preferred Stock (Berkshire Preferred Stock) which was redeemed in May 2008. The effective tax rate for the six months ended June 30, 2008 was higher than the U.S. statutory rate of 35% due to a pre-tax loss resulting from the reporting of the change in net unrealized investment gains and losses, a component of net realized and unrealized investment losses, in revenues pursuant to SFAS 159 and income generated in jurisdictions other than the United States, partially offset by non-deductible dividends and accretion on the Berkshire Preferred Stock.

In arriving at the effective tax rate for the three and six months ended June 30, 2009, OneBeacon is treating the net realized and unrealized investment gains as a discrete item separate from the other components of pre-tax income or loss. Therefore, the expense of these net gains is calculated at the statutory rate applicable to the jurisdiction in which the gains are recorded. The majority of the investment assets incurring current period net realized and unrealized gains for the three and six months ended June 30, 2009 are recorded in the U.S. and are taxed at the statutory rate of 35%. Net realized and unrealized investment gains were treated as a discrete item due to the inability to reliably estimate this amount for the full year.

Under FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN48), OneBeacon classifies all interest and penalties on unrecognized tax benefits as part of income tax expense. With few exceptions, OneBeacon is no longer subject to U.S. federal, state or non-U.S. income tax examinations for years before 2003. The Internal Revenue Service (IRS) commenced an examination of OneBeacon s U.S. income tax returns for 2003 through 2004 in the second quarter of 2006. On January 22, 2009, OneBeacon received Form 4549-A (Income Tax Examination Changes) from the IRS relating to the audit of tax years 2003 and 2004 assessing an additional $65.7 million of tax. The estimated total assessment, including interest, withholding tax and utilization of alternative minimum and foreign tax credit carryovers, is $132.0 million. OneBeacon disagrees with the adjustments proposed by the IRS and intends to vigorously defend its position. The timing of the resolution of these items is uncertain, however, it is reasonably possible that the resolution could occur within the next 12 months. OneBeacon s overall liability for tax assessments for 2003 and 2004 is limited due to the Tax Make Whole Agreement with White Mountains, which fixes the liability for these items at the amount recorded on OneBeacon s books. Refer to Note 18. Related Party Disclosures of the Company s 2008 Annual Report on Form 10-K. OneBeacon does not expect the resolution of this examination to result in a material change to its financial position. In October 2008, the IRS commenced examination of OneBeacon s U.S. income tax returns for 2005 through 2006. As of June 30, 2009, the IRS has not proposed any significant adjustments to taxable income as a result of the 2005 through 2006 audit. OneBeacon does not expect to receive any adjustments that would result in a material change to its financial position.

NOTE 11. Fair Value of Financial Instruments

SFAS No. 107, Disclosure about Fair Value of Financial Instruments (SFAS 107), and FSP FAS 107-1 and APB 28-1 require disclosure of fair value information of financial instruments. For certain financial instruments where quoted market prices are not available, other independent valuation techniques and assumptions are used. Because considerable judgment is used, these

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estimates are not necessarily indicative of amounts that could be realized in a current market exchange. SFAS 107 excludes certain financial instruments from disclosure, including insurance contracts, other than financial guarantees and investment contracts. OneBeacon carries its financial instruments on its balance sheet at fair value with the exception of its fixed-rate, long-term indebtedness.

The fair values of the fixed-rate, long-term indebtedness were estimated by discounting future cash flows using current market rates for similar obligations or using quoted market prices. Considerable judgment is required to develop such estimates of fair value. Therefore, the estimate provided herein is not necessarily indicative of the amounts that could be realized in a current market exchange.

At June 30, 2009 and December 31, 2008, the fair value of OneBeacon s Senior Notes (its fixed-rate, long-term indebtedness) was $593.5 million and $483.3 million, respectively, which compared to a carrying value of $627.3 million and $675.1 million, respectively.

In December 2005, OneBeacon entered into a mortgage note with a variable interest rate based on 30-day LIBOR. At December 31, 2008, the carrying value of the note of $40.8 million was considered to approximate its fair value. OneBeacon repaid the mortgage note in its entirety in May 2009. Refer to Note 6.

In March 2004, OneBeacon issued the Atlantic Specialty Note. At June 30, 2009 and December 31, 2008, the carrying value of the note of $14.0 million and $16.0 million, respectively, were considered to approximate its fair value.

NOTE 12. Earnings per Share

Basic and diluted earnings (loss) per share amounts have been determined in accordance with SFAS No. 128, Earnings per Share. During the second quarter of 2009 and 2008, 26,851 shares and 4,103 shares, respectively, of the Company s Class A common shares were awarded to certain non-employee directors in lieu of their 2009 and 2008 annual cash retainers. During the third quarter of 2007, the Company began a share repurchase program. Since the inception of this program, the Company has repurchased and retired 5.0 million of its Class A common shares. During the three and six months ended June 30, 2009, no shares were repurchased. During the three and six months ended June 30, 2008, the Company repurchased and retired 0.5 million and 3.0 million, respectively, of its Class A common shares for $9.4 million and $62.2 million, respectively.

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Basic earnings (loss) attributable to OneBeacon s shareholders (in millions):				
Net income (loss) attributable to OneBeacon s shareholders	$ 128.2	$ 23.8	$ 161.0	$ (0.5)
Weighted average shares outstanding	95.1	95.8	95.1	96.7
Diluted earnings (loss) attributable to OneBeacon s shareholders (in millions):				
Net income (loss) attributable to OneBeacon s shareholders	$ 128.2	$ 23.8	$ 161.0	$ (0.5)
Weighted average shares outstanding (1)	95.1	95.8	95.1	96.7

Basic earnings (loss) per share attributable to OneBeacon s shareholders (in dollars):								
Net income (loss) attributable to OneBeacon s shareholders	$	1.35	$	0.25	$	1.69	$	(0.01)
Diluted earnings (loss) per share attributable to OneBeacon s shareholders (in dollars):								
Net income (loss) attributable to OneBeacon s shareholders	$	1.35	$	0.25	$	1.69	$	(0.01)

(1) Common shares issuable upon exercise of the options (see Note 9) were not included as their inclusion would be anti-dilutive for the periods presented.

NOTE 13. Subsequent Events

During July 2009, OBIC purchased $15.7 million of outstanding Senior Notes for $14.9 million, which resulted in a $0.8 million gain.

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

The following discussion contains forward-looking statements. Statements that are not historical in nature are forward-looking statements. OneBeacon cannot promise that its expectations in such forward-looking statements will turn out to be correct. OneBeacon s actual results could be materially different from and worse than its expectations. See Forward-Looking Statements on page 48 for specific important factors that could cause actual results to differ materially from those contained in forward-looking statements.

Book Value Per Share for the Three and Six Months Ended June 30, 2009

We ended the second quarter of 2009 with a book value per share of $13.51, reflecting an 11.5% increase for the second quarter of 2009 and 14.7% growth through June 30, 2009, including dividends. The increase includes a 4.4% and 4.9% total return on invested assets for the three and six months ended June 30, 2009, respectively. We reported comprehensive net income attributable to OneBeacon s shareholders of $134.4 million and $168.3 million in the three and six months ended June 30, 2009, respectively, compared to a comprehensive net income (loss) attributable to OneBeacon s shareholders of $25.0 million and $(0.5) million in the same periods of 2008. Our GAAP combined ratios were 93.2% and 93.4% for the three and six months ended June 30, 2009, respectively, compared to 94.4% and 97.2% for the three and six months ended June 30, 2008, respectively. The decrease in the combined ratio was primarily due to lower current accident year catastrophe losses as well as higher favorable loss reserve development. The six months ended June 30, 2009 also included the impact of lower current accident year non-catastrophe losses. Total net written premiums decreased 6.0% in the three months ended June 30, 2009 to $497.9 million, compared to $529.6 million in the three months ended June 30, 2008. The decrease in net written premiums is due primarily to increased market competition in commercial lines and decreases in personal lines in both traditional personal lines, mainly due to the 30% homeowners quota share as described below, and lower premiums at AutoOne Insurance (AutoOne). Total net written premiums increased 1.3% in the six months ended June 30, 2009 to $967.3 million, compared to $955.3 million for the six months ended June 30, 2008. The increase in net written premiums was driven primarily by premiums from our collector car and boat business that we began writing in the second quarter of 2008 and Entertainment Brokers International Insurance Services (EBI) which we acquired in the third quarter of 2008.

The following table presents our book value per share.

	June 30, 2009	March 31, 2009	December 31, 2008
		(in millions, except per share amounts)	
Numerator			
OneBeacon s shareholders equity	**$ 1,284.4**	$ 1,169.3	$ 1,155.1
Denominator			
Common shares outstanding	**95.1**	95.1	95.1
Book value per share	**$ 13.51**	$ 12.30	$ 12.15

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Results of Operations

Review of Consolidated Results

A summary of our consolidated financial results for the three and six months ended June 30, 2009 and 2008 is as follows:

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
	($ in millions)			
Net written premiums	$ 497.9	$ 529.6	$ 967.3	$ 955.3
Revenues				
Earned premiums	$ 490.2	$ 463.8	$ 978.0	$ 919.1
Net investment income	36.1	44.6	58.0	94.7
Net realized and unrealized investment gains (losses)	127.4	(2.6)	121.5	(58.0)
Net other revenues	1.1			