HANOVER INSURANCE GROUP, INC.
Form 10-K
February 27, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

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

For the fiscal year ended December 31, 2008

OR

¨ **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: 1-13754

THE HANOVER INSURANCE GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**04-3263626**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
440 Lincoln Street, Worcester, Massachusetts	**01653**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (508) 855-1000

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

Title of each class	**Name of each exchange on which registered**
Common Stock, $.01 par value	**New York Stock Exchange**
7 ^{5}/8% Senior Debentures due 2025	**New York Stock Exchange**

Securities registered pursuant to Section 12(g) of the Act: NONE

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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 definition of accelerated filer , large accelerated filer , and smaller reporting company in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller Reporting Company ¨

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

Based on the closing sales price of June 30, 2008 the aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant was $2,143,881,730.

The number of shares outstanding of the registrant s common stock, $.01 par value, was 51,139,602 shares as of February 20, 2009.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of The Hanover Insurance Group, Inc. s Proxy Statement relating to the 2009 Annual Meeting of Shareholders to be held May 12, 2009 to be filed pursuant to Regulation 14A are incorporated by reference in Part III.

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PART I

ITEM 1 BUSINESS

ORGANIZATION

The Hanover Insurance Group, Inc. (THG) is a holding company organized as a Delaware corporation in 1995. Our consolidated financial statements include the accounts of THG; The Hanover Insurance Company (Hanover Insurance) and Citizens Insurance Company of America (Citizens), which are our principal property and casualty subsidiaries, First Allmerica Financial Life Insurance Company (FAFLIC), our former run-off life insurance and annuity subsidiary, and certain other insurance and non-insurance subsidiaries. On January 2, 2009, we sold FAFLIC to Commonwealth Annuity and Life Insurance Company (Commonwealth Annuity), a subsidiary of The Goldman Sachs Group, Inc. (Goldman Sachs). The results of operations for FAFLIC are reported as discontinued operations.

FINANCIAL INFORMATION ABOUT OPERATING SEGMENTS

Our primary business operations include insurance products and services in three property and casualty operating segments. These segments are Personal Lines, Commercial Lines, and Other Property and Casualty. We report interest expense related to our corporate debt separately from the earnings of our operating segments. Corporate debt consists of our junior subordinated debentures and our senior debentures.

Information with respect to each of our segments is included in Segment Results on pages 28 to 45 in Management s Discussion and Analysis of Financial Condition and Results of Operations and in Note 16 on pages 105 and 106 of the Notes to the Consolidated Financial Statements included in Financial Statements and Supplementary Data of this Form 10-K.

DESCRIPTION OF BUSINESS BY SEGMENT

Following is a discussion of each of our operating segments.

PROPERTY AND CASUALTY

GENERAL

Our Property and Casualty group manages its operations principally through three segments: Personal Lines, Commercial Lines and Other Property and Casualty. We underwrite personal and commercial property and casualty insurance through Hanover Insurance, Citizens and other THG subsidiaries, primarily through an independent agent network concentrated in the Northeast, Southeast and Midwest United States. Additionally, our Other Property and Casualty segment consists of: Opus Investment Management, Inc. (OPUS), which markets investment management services to institutions, pension funds and other organizations; earnings on holding company assets; and a voluntary pools business in which we have not actively participated since 1999. Prior to its sale on June 2, 2008, Amgro, Inc. (AMGRO), our premium financing business, was also included in the Other Property and Casualty segment.

Our strategy in the Property and Casualty group focuses on strong agency relationships, active agency management, disciplined underwriting, pricing, quality claim handling, effective expense management and customer service. We have a strong regional focus. Our Property and Casualty group constituted the 32nd largest property and casualty insurance group in the United States based on 2007 direct premiums written, according to A.M. Best and Company.

RISKS

The industry s profitability and cash flow can be significantly affected by: price; competition; volatile and unpredictable developments such as extreme weather conditions and natural disasters, including catastrophes; legal developments affecting insurer and insureds liability; extra-contractual liability; size of jury awards; acts of terrorism; and fluctuations in interest rates and other general economic conditions and trends, such as inflationary pressures, that may affect the adequacy of reserves or the demand for insurance products. Our investment portfolio and its future returns may be further impacted by the current capital market turmoil that could affect our liquidity, the amount of realized losses and impairments that will be recognized, our ability to hold such investments until recovery and other factors that may affect investment returns and our capital. Additionally, the economic conditions in geographic locations where we conduct business, especially those locations where our business is concentrated, may affect the growth and profitability of our business. The regulatory environments in those locations where we conduct business, especially those locations where we have significant business, including any pricing, underwriting or product controls, shared market mechanisms or mandatory pooling arrangements, and other conditions, such as our agency relationships affect the growth and profitability of our business. In addition, our loss and loss adjustment expense (LAE) reserves are based on our estimates, principally involving actuarial projections, at a given time, of what we expect the ultimate settlement and administration of claims will cost based on facts and circumstances then known, predictions of future events, estimates of future trends in claims frequency and severity and judicial theories of liability, costs of repairs and replacement, legislative activity and other factors. Changes to the estimates may affect our profitability.

Reference is also made to Item 1A Risk Factors on pages 17 to 20 and Risks and Forward-Looking Statements on page 66 of Management s Discussion and Analysis of Financial Condition and Results of Operations contained in this Form 10-K.

LINES OF BUSINESS

We underwrite personal and commercial property and casualty insurance coverage.

Personal Lines

Our Personal Lines segment accounted for $1.6 billion, or 57.7%, of consolidated segment revenues; $1.5 billion, or 58.9%, of net written premiums and $123.5 million, or 40.9%, of segment income before federal income taxes for the year ended December 31, 2008. Personal automobile accounted for $1.0 billion, or 68.1%, and homeowners $432.5 million, or 29.1%, of Personal Lines net written premium in 2008.

Products

Personal Lines coverages include:

Personal automobile coverage insures individuals against losses incurred from personal bodily injury, bodily injury to third parties, property damage to an insured s vehicle, and property damage to other vehicles and other property. In 2008, the majority of our new personal automobile business was written through ***Connections® Auto*,** our multivariate auto product, which is available in eighteen states. ***Connections Auto*** utilizes a multivariate rating application which calculates rates based upon the magnitude and correlation of multiple risk factors and is intended to improve both our and our agents competitiveness in our target market segments by offering policies that are more appropriately priced to be commensurate with the underlying risks.

Homeowners coverage insures individuals for losses to their residences and personal property, such as those caused by fire, wind, hail, water damage (except for flooding), theft and vandalism, and against third party liability claims. Our homeowners product, ***Connections® Home***, is available in sixteen states. It is intended to improve our competitiveness for total account business by significantly improving ease of doing business for our agents and by providing better packaging of coverage for policyholders.

Other personal lines is comprised of personal inland marine, umbrella, fire, personal watercraft, earthquake and other miscellaneous coverages.

Having implemented a broader portfolio of products, we continue to refine these products and to work closely with high potential agents to increase the percentage of business they place with us and to ensure that it is consistent with our preferred mix of business. Additionally, we remain focused on diversifying our state mix beyond our four core states of Michigan, Massachusetts, New York and New Jersey. We expect these efforts to contribute to profitable growth and improved retention in our Personal Lines segment over time.

Commercial Lines

Our Commercial Lines segment accounted for $1.2 billion, or 41.5%, of consolidated segment revenues; $1.0 billion, or 41.1%, of net written premium and $169.7 million, or 56.2%, of segment income before federal income taxes for the year ended December 31, 2008. Commercial multiple peril net written premium accounted for $368.5 million, or 35.6%, commercial automobile $192.8 million, or 18.6%, workers compensation $127.2 million, or 12.3%, inland marine line of business $115.5 million, or 11.2%, and bonds $92.0 million, or 8.9%, of Commercial Lines net written premium in 2008.

We continue to develop our specialty businesses, including bond and inland marine, which on average are expected to offer higher margins over time and enable us to deliver a more complete product portfolio to our agents and policyholders. In the Commercial Lines business, the market continues to be competitive. Price competition requires us to continue to be highly disciplined in our underwriting process to ensure that we grow the business only at acceptable margins. Our specialty lines now account for approximately one third of our Commercial Lines business. Additional growth in our specialty lines continues to be a significant part of our strategy in the future. We continue to focus on expanding our product offerings in specialty businesses as evidenced by our recent acquisitions. In March 2008, we acquired Verlan Holdings, Inc. (Verlan), now referred to as Hanover Specialty Property, a specialty company providing property insurance to small and medium-sized manufacturing and distribution companies that are highly protected fire risks. Additionally, in November 2008, we acquired AIX Holdings, Inc. (AIX), a specialty property and casualty insurance carrier that focuses on underwriting and managing program business that utilizes alternative risk transfer techniques. In 2007, we acquired Professionals Direct, Inc. (PDI), now referred to as Hanover Professional, which provides professional liability coverage for small to medium sized legal practices. We believe these acquisitions provide us with better breadth and diversification of products and improve our competitive position with our agents.

Products

Avenues®, our Commercial Lines product suite, provides agents and customers with products designed for small, middle, and specialized markets. Commercial Lines coverages include:

Commercial multiple peril coverage insures businesses against third party liability from accidents occurring on their premises or arising out of their operations, such as injuries sustained from products sold. It also insures business property for damage, such as that caused by fire, wind, hail, water damage (except for flooding), theft and vandalism.

Commercial automobile coverage insures businesses against losses incurred from personal bodily injury, bodily injury to third parties, property damage to an insured s vehicle, and property damage to other vehicles and other property.

Workers compensation coverage insures employers against employee medical and indemnity claims resulting from injuries related to work. Workers compensation policies are often written in conjunction with other commercial policies.

Other commercial lines is comprised of inland marine, which insures businesses against physical losses to property, such as contractor s equipment, builders risk and goods in transit. It also includes bonds, which provides businesses with contract surety coverage in the event of performance or payment claims, and commercial surety coverage related to fiduciary or regulatory obligations. Other commercial lines coverages include umbrella, general liability, fire, specialty property and professional liability. We also offer, through AIX, underwriting and managing of program business that utilizes alternative risk transfer techniques, including to under-served markets where there are specialty coverage or risk management needs.

Other Property and Casualty

The Other Property and Casualty segment consists of: Opus, which provides investment advisory services to affiliates and also manages approximately $1.3 billion of assets for unaffiliated institutions, such as insurance companies, retirement plans and foundations; earnings on holding company assets; and voluntary pools business in which we have not actively participated since 1999. See also Reinsurance Facilities and Pools Voluntary Pools on page 9 of this Form 10-K. Prior to its sale on June 2, 2008, AMGRO, our premium financing business, was also included in the Other Property and Casualty segment.

MARKETING AND DISTRIBUTION

Our Property and Casualty group s structure allows us to maintain a strong focus on local markets and the flexibility to respond to specific market conditions while achieving operational effectiveness. During 2008, we wrote 29.2% of our business in Michigan and 11.8% in Massachusetts. Our structure is a key factor in the establishment and maintenance of productive long-term relationships with mid-sized, well-established independent agencies. We maintain twenty-five local branch sales and underwriting offices in twenty-one states, reflecting our strong regional focus. Processing support for these locations is provided from Worcester, Massachusetts; Howell, Michigan; and Atlanta, Georgia. Administrative functions are centralized in our headquarters in Worcester, Massachusetts.

Independent agents account for substantially all of the sales of our property and casualty products. Agencies are appointed based on profitability track record, financial stability, professionalism, and business strategy. Once appointed, we monitor each agency s performance and, in accordance with applicable legal and regulatory requirements, take actions as necessary to change these business relationships, such as discontinuing the authority of the agent to underwrite certain products or revising commissions or bonus opportunities. We compensate agents primarily through base commissions and bonus plans that are tied to an agency s written premium, growth and profitability.

We are licensed to sell property and casualty insurance in all fifty states in the United States, as well as in the District of Columbia. The following provides, our top personal and commercial geographical markets based on total net written premium in the state in 2008:

FOR THE YEAR ENDED DECEMBER 31, 2008 (In millions, except ratios)	Personal Lines GAAP Net Premiums Written	% of Total	Commercial Lines GAAP Net Premiums Written	% of Total	Total GAAP Net Premiums Written	% of Total
Michigan	$ 587.5	39.6%	$ 148.5	14.4%	$ 736.0	29.2%
Massachusetts	197.2	13.3	100.2	9.7	297.4	11.8
New York	123.8	8.3	125.9	12.2	249.7	9.9
New Jersey	86.8	5.8	74.4	7.2	161.2	6.4
Louisiana	68.6	4.6	28.6	2.8	97.2	3.9
Florida	40.6	2.7	51.1	4.9	91.7	3.6
Connecticut	59.2	4.0	28.1	2.7	87.3	3.5
Illinois	30.8	2.1	48.5	4.7	79.3	3.1
Georgia	50.1	3.4	28.4	2.7	78.5	3.1
Virginia	36.1	2.4	40.3	3.9	76.4	3.0
Indiana	43.7	2.9	31.0	3.0	74.7	3.0
Maine	33.1	2.2	39.1	3.8	72.2	2.9
Texas			60.1	5.8	60.1	2.4
Other	126.5	8.7	229.8	22.2	356.3	14.2
Total	$ 1,484.0	100.0%	$ 1,034.0	100.0%	$ 2,518.0	100.0%

More than 50% of our Personal Lines net written premium is generated in the combined states of Michigan and Massachusetts. In Michigan, according to A.M. Best, based upon direct written premium for 2007, we ranked 4th in the state for Personal Lines business, with approximately 8% of the state s total market. Approximately 65% of our Michigan Personal Lines business is in the personal automobile line and 33% is in the homeowners line. Michigan business represents approximately 38% of our total personal automobile net written premium and 45% of our total homeowners net written premium. In Michigan, we are a principal provider with many of our agencies averaging over $1.2 million of total direct written premium per agency in 2008.

Approximately 75% of our Massachusetts Personal Lines business is in the personal automobile line and 21% is in the homeowners line. Massachusetts business represents approximately 15% of our total personal automobile net written premium and 10% of our total homeowners net written premium.

We manage our Commercial Lines portfolio with a focus on growth from the most profitable industry segments within our underwriting expertise, which varies by line of business and geography. We continue to target, through mid-sized agents, small and first-tier middle markets, which encompass clients whose premiums are generally below $200,000. Approximately half of Commercial Lines direct written premium is comprised of small accounts having less than $25,000 in premium. First-tier middle market accounts, those with premium between $25,000 and $200,000, account for an additional 40% of the total. The Commercial Lines segment seeks to maintain strong agency relationships as a strategy to secure and retain our agents best business. The quality of business written is monitored through an ongoing quality review program, accountability for which is shared at the local, regional and corporate levels.

We sponsor local and national agent advisory councils to gain the benefit of our agents insight and enhance our relationships. These councils provide feedback, input on the development of products and services, guidance on marketing efforts, and support for our strategies, and assist us in enhancing our local market presence.

For our Other Property and Casualty segment business, investment advisory services are marketed directly through Opus.

PRICING AND COMPETITION

We seek to achieve targeted combined ratios in each of our product lines. Our targets vary by product and change with market conditions. The targeted combined ratios reflect competitive market conditions, current investment yield expectations, our loss payout patterns, and target returns on equity. This strategy is intended to better enable us to achieve measured growth and consistent profitability. In addition, we seek to utilize our knowledge of local markets to achieve superior underwriting results. We rely on market information provided by our local agents and on the knowledge of our staff in the local branch offices. Since we maintain a strong regional focus and a significant market share in a number of states, we can apply our knowledge and experience in making underwriting and rate setting decisions. Also, we

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seek to gather objective and verifiable information at a policy level during the underwriting process, such as past driving records and, where permitted, credit histories.

The property and casualty industry is a very competitive market. Our competitors include national, regional and local companies that sell insurance through various distribution channels, including independent agencies, captive agency forces and direct to consumers through the internet or otherwise. We market primarily through independent agents and compete for business on the basis of product, price, agency and customer service, local relationship and ratings, and effective claims handling, among other things. We believe that our emphasis on maintaining strong agency relationships and a local presence in our markets, coupled with investments in products, operating efficiency, technology and effective claims handling will enable us to compete effectively. Our total account strategy in Personal Lines and broad product offerings in Commercial Lines are instrumental to our strategy to capitalize on these relationships. Our Property and Casualty group is not dependent on a single customer or even a few customers, for which the loss of any one or more would have an adverse effect upon the group s insurance operation.

In our Michigan Personal Lines business, where we market our products under the Citizens Insurance brand name, we compete with a number of national direct writers and regional and local companies. Principal personal lines competitors in Michigan are AAA Auto Club of Michigan, State Farm Group and Auto Owners Insurance Group. We believe our agency relationships, Citizens Insurance brand recognition, and ***Connections Auto*** product enable us to distribute our products competitively in Michigan.

CLAIMS

We utilize experienced claims adjusters, appraisers, medical specialists, managers and attorneys to manage our claims. Our Property and Casualty group has field claims adjusters strategically located throughout our operating territories. Claims staff members work closely with the agents and seek to settle claims rapidly, fairly and efficiently.

Claims office adjusting staff is supported by general adjusters for large property and large casualty losses, by automobile and heavy equipment damage appraisers for automobile material damage losses, and by medical specialists whose principal concentration is on workers compensation and automobile injury cases. In addition, the claims offices are supported by staff attorneys who specialize in litigation defense and claim settlements. We also maintain a special investigative unit that investigates suspected insurance fraud and abuse.

We utilize claims processing technology which allows most of the smaller and more routine Personal Lines claims to be processed at centralized locations. In 2008, we continued enhancements to our claims related technology and processes, including the implementation of new technology in all states for personal and commercial automobile. We believe these enhancements and our centralization of processing will increase efficiency and reduce costs as we expand the new technology into additional product lines.

CATASTROPHES

We are subject to claims arising out of catastrophes, which may have a significant impact on our results of operations and financial condition. We may experience catastrophe losses in the future, which could have a material adverse impact on us. Catastrophes can be caused by various events, including snow, ice storm, hurricane, earthquake, tornado, wind, hail, terrorism, fire, explosion, or other extraordinary events. The incidence and severity of catastrophes are inherently unpredictable. We manage our catastrophe risks through underwriting procedures, including the use of deductibles and specific exclusions for floods and earthquakes, as allowed, and other factors, through geographic exposure management and through reinsurance programs. The catastrophe reinsurance program is structured to protect us on a per-occurrence basis. We monitor geographic location and coverage concentrations in order to manage corporate exposure to catastrophic events. Although catastrophes can cause losses in a variety of property and casualty lines, homeowners and commercial multiple peril insurance have, in the past, generated the majority of catastrophe-related claims.

TERRORISM

Private sector catastrophe reinsurance is limited and generally unavailable for losses attributed to acts of terrorism, particularly those involving nuclear, biological, chemical and/or radiological events. As a result, the Company s primary reinsurance protection against large-scale terrorist attacks is presently provided through a temporary Federal program that provides for a system of shared public and private compensation for insured losses resulting from acts of terrorism. Additionally, we are reinsured for certain terrorism related losses within existing Catastrophe, Property per Risk and Casualty Excess of Loss corporate treaties (see Reinsurance on pages 13 to 14 of this Form 10-K).

The Terrorism Risk Insurance Act of 2002 (TRIA) established the Terrorism Risk Insurance Program (the Program). Coverage under the Program applies to workers compensation, commercial multiple peril and certain other Commercial Lines policies. The Terrorism Risk

Insurance Program Reauthorization Act of 2007

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(TRIPRA) extended the Program through December 31, 2014, and extended coverage to include both domestic and foreign acts of terrorism.

In accordance with the Program, we offer policyholders in specific lines of insurance the option to elect terrorism coverage. In order for a loss to be covered under the Program, the loss must meet aggregate industry loss minimums and must be the result of an act of terrorism as certified by the Secretary of the Treasury. The Program requires us to retain 15% of any claims from a certified terrorist event in excess of our federally mandated deductible. Our deductible represents 20% of direct earned premium for the covered lines of business of the prior year. In 2008, the deductible was $150.1 million, which represents 9.0% of year-end 2007 statutory policyholder surplus, and is estimated to be $178 million in 2009, representing 11.2% of 2008 year-end statutory policyholder surplus. We may reinsure our retention and deductible under the Program, although at this time, we have not purchased additional specific terrorism-only reinsurance coverage.

Given the unpredictable nature of the frequency and severity of terrorism losses, future losses from acts of terrorism could be material to our operating results, financial position, and/or liquidity in the future. We manage our exposures on an individual line of business basis and in the aggregate by zip code.

STATE REGULATION

Our property and casualty insurance subsidiaries are subject to extensive regulation in the various states in which they transact business and are supervised by the individual state insurance departments. Numerous aspects of our business are subject to regulatory requirements, including premium rates, mandatory risks that must be covered, prohibited exclusions, licensing of agents, investments, restrictions on the size of risks that may be insured under a single policy, reserves and provisions for unearned premiums, losses and other obligations, deposits of securities for the benefit of policyholders, policy forms and coverages, advertising, and other conduct, including the use of credit information and other factors in underwriting, as well as other underwriting and claims practices. States also regulate various aspects of the contractual relationships between insurers and independent agents.

In addition, as a condition to writing business in certain states, insurers are required to participate in various pools or risk sharing mechanisms or to accept certain classes of risk, regardless of whether such risks meet its underwriting requirements for voluntary business. Some states also limit or impose restrictions on the ability of an insurer to withdraw from certain classes of business. For example, Massachusetts, New Jersey, New York, Louisiana and Florida each impose material restrictions on a company s ability to withdraw from certain lines of business in their respective states. The state insurance departments can impose significant charges on a carrier in connection with a market withdrawal or refuse to approve withdrawal plans on the grounds that they could lead to market disruption. Laws and regulations that limit cancellation and non-renewal and that subject withdrawal plans to prior approval requirements may significantly restrict an insurer s ability to exit unprofitable markets. For example, the state of Louisiana continues to restrict our ability to reduce exposure to areas affected by hurricanes Katrina and Rita and to increase or maintain rates on policies.

In February 2009, the Governor of Michigan called upon every automobile insurer operating in the state to freeze personal automobile insurance rates for 12 months to allow time for the legislature to enact comprehensive automobile insurance reform. In addition, she endorsed a number of proposals by her appointed Automobile and Home Insurance Consumer Advocate which would, among other things, change the current rate approval process from the current file and use system to prior approval , mandate affordable rates, reduce the threshold for lawsuits to be filed in at fault incidents, and prohibit the use of certain underwriting criteria such as credit scores. The Office of Financial and Insurance Regulation had previously issued regulations prohibiting the use of credit scores to rate personal lines insurance policies, which regulations are the subject of litigation which is expected to be reviewed by the Michigan Supreme Court. At this time, we are unable to predict the likelihood of adoption or impact on our business of any such proposals or regulations, but any such restrictions could have an adverse affect on our results of operations.

During 2007, the Massachusetts Commissioner of Insurance issued decisions pertaining to personal automobile insurance to end the fix-and-establish system of setting automobile rates, replaced it with a system of managed competition and began implementing an Assigned Risk Plan beginning with new business as of April 1, 2008. The implementation of this Assigned Risk Plan is expected to be completed over the next year and therefore, the effects of this new Assigned Risk Plan on our financial results are not yet completely known or determinable. The Assigned Risk Plan distributes the Massachusetts residual automobile market based on individual policyholder assignments rather than assigning carriers Exclusive Representative Producers as was done under the prior system. We believe the Assigned Risk Plan will provide for a more equitable distribution of residual market risks across all carriers in the market, and therefore, such plan is not likely to adversely affect our results of operations or financial position.

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Over the past three years, other state-sponsored insurers, reinsurers or involuntary pools have increased significantly, particularly those states which have Atlantic or Gulf Coast storm exposures. As a result, the potential assessment exposure of insurers doing business in such states and the attendant collection risks have increased, particularly, in our case, in the states of Massachusetts, Louisiana and Florida. Such actions and related regulatory restrictions may limit our ability to reduce our potential exposure to hurricane related losses. At this time we are unable to predict the likelihood or impact of any such potential assessments or other actions.

The insurance laws of many states generally provide that property and casualty insurers doing business in those states belong to statutory property and casualty guaranty funds. The purpose of these guaranty funds is to protect policyholders by requiring that solvent property and casualty insurers pay insurance claims of insolvent insurers. These guaranty associations generally pay these claims by assessing solvent insurers proportionately based on the insurer s share of voluntary written premium in the state. While most guaranty associations provide for recovery of assessments through subsequent rate increases, surcharges or premium tax credits, there is no assurance that insurers will ultimately recover these assessments, which could be material, particularly following a large catastrophe or in markets which become disrupted.

We are subject to periodic financial and market conduct examinations conducted by state insurance departments. We are also required to file annual and other reports relating to the financial condition of our insurance subsidiaries and other matters.

See also Contingencies and Regulatory Matters on pages 63 to 65 and Other Significant Transactions on page 58 to 59 in Management s Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K.

RESIDUAL MARKETS AND POOLING ARRANGEMENTS

As a condition of our license to do business in various states, we are required to participate in mandatory property and casualty shared market mechanisms or pooling arrangements which provide various insurance coverages where such coverage may not otherwise be available at rates which are deemed reasonable. Such mechanisms provide coverage primarily for personal and commercial property, personal and commercial automobile, and workers compensation and include assigned risk plans, reinsurance facilities and pools, joint underwriting associations, fair access to insurance requirements plans, and commercial automobile insurance plans. For example, since most states compel the purchase of a minimal level of automobile liability insurance, states have developed shared market mechanisms to provide the required coverages and in many cases, optional coverages, to those drivers who, because of their driving records or other factors, cannot find insurers who will insure them voluntarily. Our participation in such shared markets or pooling mechanisms is generally proportional to our direct writings for the type of coverage written by the specific pooling mechanism in the applicable state. We experienced an underwriting loss from participation in these mechanisms, mandatory pools and underwriting associations of $11.5 million and $12.3 million for 2008 and 2007, respectively, while an underwriting profit of $9.7 million resulted from our 2006 participation. In both years, the primary component of the underwriting loss was due to our mandatory participation in the Michigan Assigned Claims (MAC) facility, an assigned claims plan covering people injured in uninsured motor vehicle accidents. Our participation in the MAC facility is based on our share of personal and commercial automobile direct written premium in the state and resulted in an underwriting loss of $11.2 million, $10.4 million and $11.1 million in 2008, 2007 and 2006, respectively.

Reinsurance Facilities and Pools

Reinsurance facilities are currently in operation in various states that require an insurer to write all applications submitted by an agent, regardless of its pricing or underwriting characteristics. As a result, insurers in that state may be writing policies for applicants with a higher risk of loss, or at a lower premium, than they would normally accept. The reinsurance facility allows the insurer to cede this high risk business to the reinsurance facility, thus sharing the underwriting experience with all other insurers in the state. If a claim is paid on a policy issued in this market, the facility will reimburse the insurer. Typically, reinsurance facilities operate at a deficit, which is then recouped by levying assessments against the same insurers. These assessments are determined on the basis of each insurers share of net written premium in the state; therefore, our most significant liability to these facilities arise from the state of Michigan, which for 2008 represented 29.2% of our total net written premium. Other than the previously mentioned MAC facility, mandatory reinsurance facilities and pools, including those in Michigan and Massachusetts, were not significant to our 2008, 2007 or 2006 results of operations.

The Michigan Catastrophic Claims Association (MCCA) is a reinsurance mechanism that covers no-fault first party medical losses of retentions in excess of $440,000. All automobile insurers doing business in Michigan are required to participate in the MCCA. Insurers are reimbursed for their covered losses in excess of this threshold, which increased from $420,000 to $440,000 on July 1, 2008, and will continue to increase

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each July 1st in scheduled amounts until it reaches $500,000 in 2011. Funding for MCCA comes from assessments against automobile insurers based upon their proportionate market share of the state s automobile liability insurance market. Insurers are allowed to pass along this cost to Michigan automobile policyholders. We ceded to the MCCA premiums earned and losses and LAE of $60.9 million and $129.8 million in 2008, $70.1 million and $84.6 million in 2007, and $74.3 million and $118.8 million in 2006, respectively. At December 31, 2008, the MCCA represented at least 10% of our total reinsurance assets. At December 31, 2008 and 2007, we had reinsurance recoverables on paid and unpaid losses from the MCCA of $613.8 million and $557.7 million, respectively. We believe that we are unlikely to incur any material loss as a result of non-payment of amounts owed to us by MCCA, because (i) the payment obligations of the MCCA are extended over many years, resulting in relatively small current payment obligations in terms of MCCA s total assets, and (ii) the MCCA is supported by assessments permitted by statute. Reference is made to Note 18 Reinsurance , on pages 107 and 108 and Note 21 Commitments and Contingencies , on pages 110 to 112 of the Notes to Consolidated Financial Statements included in Financial Statements and Supplementary Data of this Form 10-K.

FAIR Plans and Other Involuntary Pools

The principal shared market mechanisms for property insurance are state mandated FAIR Plans, the formation of which were required by the federal government as a condition to an insurer s ability to obtain federal riot reinsurance coverage following the riots and civil disorder that occurred during the 1960s. These plans, created as mechanisms similar to automobile assigned risk plans, were designed to increase the availability of property insurance in urban areas, but over time have been extended to cover other circumstances where homeowners are unable to obtain insurance at rates deemed reasonable, such as in coastal or other areas prone to natural catastrophes. Thirty-three states have FAIR Plans, including Louisiana, Florida, Massachusetts, New York and North Carolina. During 2005, the Louisiana and Florida FAIR Plans experienced considerable losses as a result of hurricanes. Total FAIR Plan assessments were not significant to our 2008, 2007 or 2006 results of operations.

The maximum annual FAIR Plan assessment that can be levied against an insurer operating in Louisiana and Florida are approximately 30% and 20%, respectively, of the annual direct property premium written by the insurer in the prior year. Under the Louisiana FAIR Plan, we are allowed to recover such losses from policyholders, subject to annual limitations. The availability of private homeowners insurance in these states is declining as carriers seek to exit or significantly reduce their exposure in these states. This will increase the number of insureds seeking coverage from the FAIR Plans and could result in increased losses to us through the states FAIR Plans for future events. Also, the Massachusetts FAIR Plan has grown significantly because of coastal exposures. Although it is difficult to accurately estimate our ultimate exposure, a large coastal event, particularly affecting Florida, Louisiana, New York, New Jersey or Massachusetts, would likely be material to our financial position and/or results of operations.

Assigned Risk Plans

Assigned risk plans are the most common type of shared market mechanism. Most states, including New Jersey and New York, operate assigned risk plans, and Massachusetts implemented such a plan for new business beginning on April 1, 2008. Such plans assign applications from drivers who are unable to obtain insurance in the voluntary market to insurers licensed in the applicant s state. Each insurer is required to accept a specific percentage of applications based on its market share of voluntary business in the state. Once an application has been assigned to an insurer, the insurer issues a policy under its own name and retains premiums and pays losses as if the policy was voluntarily written. Total assigned risk plan costs were not significant to our 2008, 2007 or 2006 results of operations not only because of the direct business written by us in the state, but also because of various FAIR Plans and other assessments which can be imposed in such circumstances.

Voluntary Pools

We have terminated our participation in virtually all voluntary pool business; however, we continue to be subject to claims related to years in which we were a participant. The most significant of these pools is a voluntary excess and casualty reinsurance pool known as the Excess and Casualty Reinsurance Association (ECRA), in which we were a participant from 1950 to 1982. In 1982, the pool was dissolved and since that time the business has been in runoff. Our participation in this pool has resulted in average paid losses of approximately $2 million annually over the past ten years. Because of the inherent uncertainty regarding the types of claims in this pool, there can be no assurance that the reserves will be sufficient. Loss and LAE reserves for our voluntary pools were $67.0 million and $79.0 million at December 31, 2008 and 2007, respectively, including $52.0 million and $53.3 million at December 31, 2008 and 2007, respectively, related to ECRA. Excluding the ECRA pool, the average annual paid losses and reserve balances at December 31, 2008 for other voluntary pools were not individually significant.

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RESERVE FOR UNPAID LOSSES AND LOSS ADJUSTMENT EXPENSES

Reference is made to Property and Casualty Reserve for Losses and Loss Adjustment Expenses on pages 35 to 41 of Management s Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K.

Our property and casualty actuaries review the reserves each quarter and certify the reserves annually as required for statutory filings. Significant periods of time often elapse between the occurrence of an insured loss, the reporting of the loss to us and our settlement and payment of that loss. To recognize liabilities for unpaid losses on occurrences, we establish reserves as balance sheet liabilities representing estimates of amounts needed to pay reported and unreported losses and LAE.

We regularly review our reserving techniques, our overall reserving position and our reinsurance. We believe that adequate provision has been made for loss reserves. This belief is based on (i) our review of historical data, legislative enactments, judicial decisions, legal developments in impositions of damages, changes in political attitudes and trends in general economic conditions, (ii) our review of per claim information, (iii) our historical loss experience and that of the industry, (iv) the relatively short-term nature of most policies written by us, and (v) our internal estimates of required reserves. However, establishment of appropriate reserves is an inherently uncertain process and there can be no certainty that reserves will prove adequate in light of subsequent actual experience. A significant change to the estimated reserves could have a material effect on our results of operations or financial position. An increase or decrease in reserve estimates would result in a corresponding decrease or increase in financial results. For example, each one percentage point change in the aggregate loss and LAE ratio resulting from a change in reserve estimation is currently projected to have an approximate $25 million impact on the property and casualty group s segment income, based on 2008 full year premiums.

We do not use discounting techniques in establishing reserves for losses and LAE in our Property and Casualty, nor have we participated in any loss portfolio transfers or other similar transactions.

The following table reconciles reserves determined in accordance with accounting principles and practices prescribed or permitted by insurance statutory authorities (Statutory) to reserves determined in accordance with generally accepted accounting principles (GAAP). The primary difference between the following Statutory reserves and our GAAP reserves is the requirement, on a GAAP basis, to present reinsurance recoverables as an asset, whereas Statutory guidance provides that reserves are reflected net of the corresponding reinsurance recoverables.

DECEMBER 31 ***(In millions)***	**2008**	**2007**	**2006**
Statutory reserve for losses and LAE	**$ 2,211.0**	$ 2,225.3	$ 2,274.4
GAAP adjustments:			
Reinsurance recoverable on unpaid losses	**988.2**	940.5	889.5
Other	**2.1**		
GAAP reserve for losses and LAE	**$ 3,201.3**	$ 3,165.8	$ 3,163.9

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ANALYSIS OF LOSSES AND LOSS ADJUSTMENT EXPENSES RESERVE DEVELOPMENT

The following table sets forth the development of our GAAP reserves (net of reinsurance recoverables) for unpaid losses and LAE from 1998 through 2008:

DECEMBER 31 *(In millions)*	**2008**	**2007**	**2006**	**2005**	**2004**	**2003**	**2002**	**2001**	**2000**	**1999**	**1998**
Net reserve for losses and LAE[1]	$ 2,213.1	$ 2,225.3	$ 2,274.4	$ 2,351.1	$ 2,161.5	$ 2,078.9	$ 2,083.8	$ 2,056.9	$ 1,902.2	$ 1,924.5	$ 2,005.5
Cumulative amount paid as of[2]:											
One year later		711.1	689.9	729.5	622.0	658.3	784.5	763.6	780.3	703.8	638.0
Two years later			1,061.8	1,121.9	967.0	995.4	1,131.7	1,213.6	1,180.1	1,063.8	996.0
Three years later				1,368.3	1,175.4	1,217.1	1,339.5	1,423.9	1,458.3	1,298.2	1,203.0
Four years later					1,312.9	1,351.6	1,478.9	1,551.5	1,567.8	1,471.8	1,333.0
Five years later						1,436.5	1,566.8	1,636.9	1,636.9	1,524.4	1,446.0
Six years later							1,629.3	1,696.3	1,689.0	1,560.6	1,497.5
Seven years later								1,742.3	1,731.0	1,596.4	1,537.4
Eight years later									1,768.5	1,627.2	1,573.3
Nine years later										1,657.5	1,606.1
Ten years later											1,634.3
Net reserve re-estimated as of[3]:											
End of year	2,213.1	2,225.3	2,274.4	2,351.1	2,161.5	2,078.9	2,083.8	2,056.9	1,902.2	1,924.5	2,005.5
One year later		2,073.7	2,138.0	2,271.1	2,082.0	2,064.4	2,124.2	2,063.3	2,010.8	1,837.1	1,822.1
Two years later			2,008.9	2,155.8	1,989.6	2,017.4	2,115.3	2,122.5	2,028.2	1,863.3	1,781.4
Three years later				2,072.0	1,899.6	1,971.5	2,093.9	2,124.3	2,066.6	1,863.0	1,818.6
Four years later					1,853.2	1,917.3	2,074.0	2,121.6	2,071.1	1,893.6	1,823.5
Five years later						1,896.1	2,041.6	2,121.7	2,078.3	1,901.6	1,860.5
Six years later							2,034.9	2,103.2	2,084.1	1,913.4	1,871.0
Seven years later								2,100.6	2,074.8	1,925.4	1,883.1
Eight years later									2,076.8	1,920.9	1,897.6
Nine years later										1,925.6	1,896.0
Ten years later											1,900.2
Redundancy (deficiency), net[4]	$	$ 151.6	$ 265.5	$ 279.1	$ 308.3	$ 182.8	$ 48.9	$ (43.7)	$ (174.6)	$ (1.1)	$ 105.3

(1) Sets forth the estimated net liability for unpaid losses and LAE recorded at the balance sheet date for each of the indicated years; represents the estimated amount of net losses and LAE for claims arising in the current and all prior years that are unpaid at the balance sheet date, including incurred but not reported (IBNR) reserves.

(2) Cumulative loss and LAE payments made in succeeding years for losses incurred prior to the balance sheet date.

(3) Re-estimated amount of the previously recorded liability based on experience for each succeeding year; increased or decreased as payments are made and more information becomes known about the severity of remaining unpaid claims.

(4) Cumulative redundancy or deficiency at December 31, 2008 of the net reserve amounts shown on the top line of the corresponding column. A redundancy in reserves means the reserves established in prior years exceeded actual losses and LAE or were re-evaluated at less than the original reserved amount. A deficiency in reserves means the reserves established in prior years were less than actual losses and LAE or were re-evaluated at more than the original reserved amount.

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The following table sets forth the development of gross reserve for unpaid losses and LAE from 1999 through 2008:

DECEMBER 31 *(In millions)*	**2008**	**2007**	**2006**	**2005**	**2004**	**2003**	**2002**	**2001**	**2000**	**1999**
Reserve for losses and LAE:										
Gross liability	$ 3,201.3	$ 3,165.8	$ 3,163.9	$ 3,458.7	$ 3,068.6	$ 3,018.9	$ 2,961.7	$ 2,921.5	$ 2,719.1	$ 2,618.7
Reinsurance recoverable	988.2	940.5	889.5	1,107.6	907.1	940.0	877.9	864.6	816.9	694.2
Net liability	$ 2,213.1	$ 2,225.3	$ 2,274.4	$ 2,351.1	$ 2,161.5	$ 2,078.9	$ 2,083.8	$ 2,056.9	$ 1,902.2	$ 1,924.5
One year later:										
Gross re-estimated liability		$ 3,032.1	$ 3,047.0	$ 3,409.9	$ 3,005.9	$ 2,972.2	$ 3,118.6	$ 2,926.4	$ 2,882.0	$ 2,553.4
Re-estimated recoverable		963.4	909.0	1,138.8	923.9	907.8	994.4	863.1	871.2	716.3
Net re-estimated liability		$ 2,073.7	$ 2,138.0	$ 2,271.1	$ 2,082.0	$ 2,064.4	$ 2,124.2	$ 2,063.3	$ 2,010.8	$ 1,837.1
Two years later:										
Gross re-estimated liability			$ 2,960.5	$ 3,334.1	$ 2,941.5	$ 2,970.7	$ 3,113.5	$ 3,118.9	$ 2,913.0	$ 2,640.8
Re-estimated recoverable			951.6	1,178.3	951.9	953.3	998.2	996.4	884.8	777.5
Net re-estimated liability			$ 2,008.9	$ 2,155.8	$ 1,989.6	$ 2,017.4	$ 2,115.3	$ 2,122.5	$ 2,028.2	$ 1,863.3
Three years later:										
Gross re-estimated liability				$ 3,288.8	$ 2,897.7	$ 2,951.0	$ 3,129.4	$ 3,146.6	$ 3,063.9	$ 2,658.0
Re-estimated recoverable				1,216.8	998.1	979.5	1,035.5	1,022.3	997.3	795.0
Net re-estimated liability				$ 2,072.0	$ 1,899.6	$ 1,971.5	$ 2,093.9	$ 2,124.3	$ 2,066.6	$ 1,863.0
Four years later:										
Gross re-estimated liability					$ 2,886.8	$ 2,935.1	$ 3,128.6	$ 3,178.8	$ 3,088.5	$ 2,782.4
Re-estimated recoverable					1,033.6	1,017.8	1,054.6	1,057.2	1,017.4	888.8
Net re-estimated liability					$ 1,853.2	$ 1,917.3	$ 2,074.0	$ 2,121.6	$ 2,071.1	$ 1,893.6
Five years later:										
Gross re-estimated liability						$ 2,946.1	$ 3,134.4	$ 3,197.0	$ 3,126.1	$ 2,814.1
Re-estimated recoverable						1,050.0	1,092.8	1,075.3	1,047.8	912.5
Net re-estimated liability						$ 1,896.1	$ 2,041.6	$ 2,121.7	$ 2,078.3	$ 1,901.6
Six years later:										
Gross re-estimated liability							$ 3,163.9	$ 3,213.9	$ 3,148.7	$ 2,848.1
Re-estimated recoverable							1,129.0	1,110.7	1,064.6	934.7
Net re-estimated liability							$ 2,034.9	$ 2,103.2	$ 2,084.1	$ 1,913.4
Seven years later:										
Gross re-estimated liability								$ 3,259.3	$ 3,172.9	$ 2,871.6
Re-estimated recoverable								1,158.7	1,098.1	946.2
Net re-estimated liability								$ 2,100.6	$ 2,074.8	$ 1,925.4

Eight years later:		
Gross re-estimated liability	$ 3,221.1	$ 2,901.4
Re-estimated recoverable	1,145.3	980.5
Net re-estimated liability	$ 2,076.8	$ 1,920.9
Nine years later:		
Gross re-estimated liability		$ 2,954.0
Re-estimated recoverable		1,028.4
Net re-estimated liability		$ 1,925.6

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Reinsurance

We maintain a reinsurance program designed to protect against large or unusual loss and LAE activity. We utilize a variety of reinsurance agreements, which are intended to control our exposure to large property and casualty losses, stabilize earnings and protect capital resources, including facultative reinsurance, excess of loss reinsurance and catastrophe reinsurance. Catastrophe reinsurance serves to protect us, as the ceding insurer, from significant losses arising from a single event such as snow, ice storm, hurricane, earthquake, tornado, wind, hail, terrorism, fire, explosion, or other extraordinary events. We determine the appropriate amount of reinsurance based upon our evaluation of the risks insured, exposure analyses prepared by consultants and/or reinsurers and on market conditions, including the availability and pricing of reinsurance.

We cede to reinsurers a portion of our risk based upon insurance policies subject to such reinsurance. Reinsurance contracts do not relieve us from our obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to us. We believe that the terms of our reinsurance contracts are consistent with industry practice in that they contain standard terms with respect to lines of business covered, limit and retention, arbitration and occurrence. We believe our reinsurers are financially sound, based upon our ongoing review of their financial statements, financial strength ratings assigned to them by rating agencies, their reputations in the reinsurance marketplace, and the analysis and guidance of our reinsurance advisors.

As described under Terrorism above, although we exclude coverage of nuclear, chemical or biological events from the personal and commercial policies we write, we are required under TRIPRA to offer this coverage in our workers compensation policies. We have reinsurance coverage under our casualty reinsurance treaty for losses that result from nuclear, chemical or biological events of approximately $30 million. All other treaties exclude such coverage. Further, under TRIPRA, our retention of losses from such events, if deemed certified terrorist events, is limited to approximately $178 million deductible and 15% of losses in excess of this deductible in 2009. However, there can be no assurance that such events would not be material to our financial position or results of operations.

As described above under Residual Markets and Pooling Arrangements Reinsurance Facilities and Pools , we are subject to concentration of risk with respect to reinsurance ceded to various mandatory residual market mechanisms.

Reference is made to Note 18 Reinsurance on pages 107 and 108 of the Notes to Consolidated Financial Statements included in Financial Statements and Supplementary Data of this Form 10-K. Reference is also made to Reinsurance Facilities and Pools on pages 8 and 9 of this Form 10-K.

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Our 2009 reinsurance program is substantially consistent with our 2008 program. The following table summarizes both our 2008 and 2009 reinsurance programs (excluding coverage available under the federal terrorism reinsurance program):

(in millions)

Treaty	*Loss Amount*	*Loss Retention*	*Reinsurance Coverage, Including Non-Certified Terrorism*	*Certified Terrorism Coverage (as defined by TRIPRA)*
Property catastrophe occurrence treaty (1), (5)				
All perils, per occurrence	< $150.0	100%	NA	NA
	$150.0 to $250.0	47%	53%	53%; Personal Lines only
	$250.0 to $700.0	NA	100%	100%; Personal Lines only
	$700.0 to $900.0	45%	55%	55%; Personal Lines only
	> $900.0	100%	NA	NA
Property per risk treaty (1), (5)				
All perils including commercial marine, per risk	< $2.0	100%	NA	NA
	$2.0 to $5.0 (2)	NA	100%	100%
	$5.0 to $100.0	NA	100%	100%
	> $100.0	100%	N/A	NA
Casualty reinsurance (3), (5)				
Each loss, per occurrence for general liability, automobile liability, and workers compensation and umbrella	< $2.0	100%	NA	NA
	$2.0 to $5.0	25%	75%	subject to $10M annual aggregate limit
	$5.0 to $10.0	NA	100%	subject to $5M annual aggregate limit
	$10.0 to $30.0	NA	100%	subject to $20M annual aggregate limit
	> $30.0	100%	NA	NA
Surety/fidelity bond reinsurance (1)				
Excess of loss treaty on bond business	< $3.0	100%	NA	NA
	$3.0 to $35.0	10%	90%	NA
	> $35.0	100%	NA	NA
Professional liability reinsurance				
Lawyers and management liability (4)	< $1.0	100%	NA	NA
	$1.0 to $10.0	10%	90%	NA
	> $10.0	100%	NA	NA

NA Not applicable

(1) The property catastrophe occurrence treaty $200 million excess of $700 million layer was additionally purchased effective July 1, 2008 for a twelve month term ending on June 30, 2009 and provides coverage for perils in the Northeast. The property per risk and surety/fidelity bond treaties have an annual effective dates of July 1st. All other treaties have January 1st annual effective dates.

(2) The property per risk treaty $2 million to $5 million layer is subject to $6 million annual aggregate deductible.

(3) Coverage between $10 million and $20 million under this agreement is clash reinsurance. Clash reinsurance is a type of excess of loss reinsurance in which an insurance company is reinsured in the event there is a casualty loss affecting two or more insureds. Umbrella is covered under our casualty reinsurance treaty subject to separate limits as defined. Umbrella and casualty lines share coverage at the $2 million to $10 million layers with the maximum umbrella limit subject to the casualty treaty of $5 million. There is also a separate layer that provides umbrella coverage of $15 million excess of $5 million per occurrence.

(4) Professional liability reinsurance agreement provides coverage to $10 million for Lawyers Professional Liability and coverage to $5 million for Management Liability.

(5) As discussed in Other Significant Transactions in Managements Discussion and Analysis on pages 58 and 59 of this Form 10-K, we purchased AIX on November 28, 2008. In addition to certain layers of coverage from our reinsurance programs as described in this table, the AIX reinsurance program also includes surplus share, quota share, excess of loss, facultative and other forms of reinsurance that cover the writings from AIX specialty and proprietary programs.

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LIFE COMPANIES

OVERVIEW

During 2008, all of our Life Companies business was classified as discontinued operations. We segregated this business into two components: Discontinued Operations of our FAFLIC Business, and Discontinued Operations of our Variable Life Insurance and Annuity Business.

Our Discontinued Operations of our FAFLIC Business, which was sold to Commonwealth Annuity on January 2, 2009, included traditional life insurance products (principally the Closed Block), a block of retirement products and one guaranteed investment contract (GIC). Our Discontinued Operations of our Variable Life Insurance and Annuity business reflects the net costs and recoveries associated with the 2005 sale of this business, including indemnification costs and employee severance costs. Our discontinued operations, in total, generated a net loss of $63.9 million during 2008. Reference is made to Segment Results Discontinued Operations: Life Companies on pages 42 to 44 of Management s Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K.

Assets and liabilities related to our FAFLIC discontinued business and our reinsured variable life insurance and annuity business are reflected as assets and liabilities held-for-sale.

PRODUCTS

We did not issue any new business in 2008. The primary insurance products in FAFLIC were participating whole life insurance products and fixed individual annuities. Additionally, we managed group annuity accounts for participants of defined benefit plans whose retirement benefits were purchased for them by their defined benefit plan sponsor. Finally, we had one non-qualified GIC, often referred to as a funding agreement. This funding agreement was issued to a non-ERISA institutional buyer, denominated in British pounds and had a fixed interest rate.

The following table reflects total reserves held, both gross and net of reinsurance recoverables, for the Discontinued Operations major product lines, including the Closed Block (see Note 8 on page 92 of the Notes to the Consolidated Financial Statements included in Financial Statements and Supplementary Data of this Form 10-K), for the years ended December 31, 2008 and 2007.

DECEMBER 31	**2008**	**2007**	**2008**	**2007**
(in millions)	***Gross***		***Net of Reinsurance Recoverable***	
Individual life and health insurance	**$ 722.8**	$ 735.9	**$ 682.2**	$ 705.8
Accident and health business	**232.0**	262.4	**114.1**	62.8
Individual and group annuities	**393.3**	416.2	**309.6**	334.3
Trust instruments supported by funding obligations (GICs)	**15.0**	39.1	**15.0**	39.1
Separate account liabilities (1)	**263.4**	481.3	**263.4**	481.3

(1) Includes separate account liabilities subject to a modified coinsurance agreement with Commonwealth Annuity, of $189.8 million and $380.2 million as of December 31, 2008 and 2007, respectively.

Included in the table above are reserves related to our accident and health business, which was retained by THG through an assumption of such business by Hanover Insurance. The accident and health business assumed by Hanover Insurance includes interests in approximately 23 assumed accident and health reinsurance pools and arrangements. We ceased writing new premiums in this business in 1998. The reinsurance pool business consists primarily of direct and assumed medical stop loss, the medical and disability portions of workers compensation risks, small group managed care, long-term disability and long-term care pools, student accident and special risk business. Our total reserves for the assumed accident and health business were $232.0 million at December 31, 2008. The total amount recoverable from third party reinsurers was $117.9 million at December 31, 2008. Total net reserves were $114.1 million at December 31, 2008. We will continue to account for this business as Discontinued Operations.

Loss estimates associated with substantially all of this business are provided by managers of each pool. We adopt reserve estimates for this business that considers this information and other facts. We update these reserves as new information becomes available and further events occur that may affect the ultimate resolution of unsettled claims. We believe that the reserves recorded related to this business are adequate. However, since loss cost estimates related to our accident and health business are dependent on several assumptions, including, but not limited to, future health care costs, persistency of medical care inflation, claims, particularly in the long-term care business, morbidity and mortality assumptions, and

these assumptions can be impacted by technical developments and advancements in the medical field and other factors, there can be no assurance that the reserves established for this business will prove sufficient. Revisions to these reserves could have a material adverse effect on our results of operations for a particular quarterly or annual period or on our financial position.

INVESTMENT PORTFOLIO

We held $4.8 billion of investment assets at December 31, 2008, excluding $1.1 billion of assets sold on January 2, 2009 as part of our discontinued FAFLIC business. Approximately 89% of our investment assets relating to continuing operations are comprised of fixed maturities, which includes both investment grade and below investment grade public and private debt securities. An additional 9% of our investment assets are comprised of cash and cash equivalents, while the remaining 2% includes equity securities, commercial mortgage loans and other long-term investments. These investments are generally of high quality and our fixed maturities are broadly diversified across sectors of the fixed income market.

For our Property and Casualty business, we developed an investment strategy that is intended to maximize investment income with consideration towards driving long-term growth of shareholders equity and book value. The determination of the appropriate asset allocation is a process that focuses on the types of business written and the level of surplus required to support our different businesses and the risk return profiles of the underlying asset classes. We look to balance the goals of capital preservation, stability, liquidity and after-tax return.

The majority of our assets are invested in the fixed income markets. Through fundamental research and credit analysis, our investment professionals seek to identify a combination of stable income producing higher quality U.S. agency, corporate and mortgage-backed securities and undervalued securities in the credit markets. We have a general policy of diversifying investments both within and across all portfolios to mitigate credit and interest rate risk. We monitor the credit quality of our investments and our exposure to individual markets, borrowers, industries, sectors and, in the case of direct commercial mortgages and commercial mortgage-backed securities, property types and geographic locations.

All investments held by our insurance subsidiaries are subject to diversification requirements under state insurance laws. However, there is no regulatory requirement to match asset and liability durations. Our investment asset portfolio duration is approximately four years and is generally 2.0 2.5 times the duration of our insurance liabilities. We seek to maintain sufficient liquidity to support our cash flow requirements by monitoring the cash requirements associated with our insurance and corporate liabilities, closely monitoring our investment durations, holding highly liquid public securities and managing the purchases and sales of assets.

Reference is made to Investment Portfolio on pages 46 to 51 of Management s Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K.

RATING AGENCIES

Insurance companies are rated by rating agencies to provide both industry participants and insurance consumers information on specific insurance companies. Higher ratings generally indicate the rating agencies opinion regarding financial stability and a stronger ability to pay claims.

We believe that strong ratings are important factors in marketing our products to our agents and customers, since rating information is broadly disseminated and generally used throughout the industry. We believe that a rating of A- or higher from A.M. Best Co. is particularly important for our business. Insurance company financial strength ratings are assigned to an insurer based upon factors deemed by the rating agencies to be relevant to policyholders and are not directed toward protection of investors. Such ratings are neither a rating of securities nor a recommendation to buy, hold or sell any security.

See Rating Agency Actions on pages 65 and 66 in Management s Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K.

EMPLOYEES

We have approximately 4,000 employees located throughout the United States as of December 31, 2008. We believe our relations with employees are good.

EXECUTIVE OFFICERS OF THE REGISTRANT

Reference is made to Directors and Executive Officers of the Registrant in Part III, Item 10 on pages 117 to 118 of this Form 10-K.

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AVAILABLE INFORMATION

We file our annual report on Form 10-K, quarterly reports on Form 10-Q, periodic information on Form 8-K, our proxy statement, and other required information with the SEC. Shareholders may read and copy any materials on file with the SEC at the SEC s Public Reference Room at 100 F Street, NE, Washington, DC 20549. Shareholders may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet website, http://www.sec.gov, which contains reports, proxy and information statements and other information with respect to our filings.

Our website address is http://www.hanover.com. We make available free of charge on or through our website, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Additionally, our Code of Conduct is also available, free of charge, on our website. The Code of Conduct applies to our directors, officers and employees, including our Chief Executive Officer, Chief Financial Officer and Controller. While we do not expect to grant waivers to our Code of Conduct, any such waivers granted to our Chief Executive Officer, Chief Financial Officer or Controller, or any amendments to our Code will be posted on our website as required by law or rules of the New York Stock Exchange. Our Corporate Governance Guidelines and the charters of our Audit Committee, Compensation Committee, Committee of Independent Directors and Nominating and Corporate Governance Committee, are available on our website. All documents are also available in print to any shareholder who requests them.

ITEM 1A RISK FACTORS

We wish to caution readers that the current financial market turmoil and the following important factors, among others, in some cases have affected, and in the future could affect, our actual results and could cause our actual results for 2009 and beyond to differ materially from historical results and from those expressed in any of our forward-looking statements. When used in our Management s Discussion and Analysis, the words believes , anticipates , expects , projections , outlook , should , could , plan , guidance , likely and similar expressions are identify forward-looking statements. See Important Factors Regarding Forward-Looking Statements filed as Exhibit 99.2 to this Form 10-K. While any of these factors could affect our business as a whole, we have grouped certain factors by the business segment to which we believe they are most likely to apply.

RISKS RELATING TO OUR PROPERTY AND CASUALTY INSURANCE BUSINESS

We generate most of our total revenues and earnings through our property and casualty insurance subsidiaries. The results of companies in the property and casualty insurance industry historically have been subject to significant fluctuations and uncertainties. Our profitability could be affected significantly by (i) adverse loss development or loss adjustment expense for events we (including our recently acquired subsidiaries) have insured in either the current or in prior years, including risks indirectly insured through various mandatory market mechanisms or through discontinued pools which are included in the Other Property and Casualty segment (our discontinued Life Companies business also includes discontinued pools which present similar risks) or the expected decline in the amount of favorable development which has been realized in recent periods, which could be material, particularly in light of the significance of favorable development as a contributor to Property and Casualty Groups segment income; (ii) an inability to retain profitable policies in force and attract profitable policies in our Personal Lines and Commercial Lines segments, whether as the result of an increasingly competitive product pricing environment, the adoption by competitors of strategies to increase agency appointments and commissions, as well as marketing and advertising expenditures or otherwise; (iii) heightened competition, including the intensification of price competition and increased marketing efforts by our competitors, the entry of new competitors and the introduction of new products by new and existing competitors, or as the result of consolidation within the financial services industry and the entry of additional financial institutions into the insurance industry; (iv) failure to obtain new customers, retain existing customers or reductions of policies in force by existing customers, whether as a result of recent competition or otherwise; (v) increases in costs, particularly those occurring after the time our products are priced and including construction, automobile repair, and medical and rehabilitation costs, and including as the result of cost shifting from health insurers to casualty and liability insurers (whether as a result of an increasing number of injured parties without health insurance or coverage changes in health policies to make such coverage, in certain circumstances, secondary to other policies); (vi) restrictions on insurance underwriting, including as a result of proposals by the Governor of Michigan with respect to automobile insurance; (vii) adverse state and federal legislation or regulation, including mandated decreases in rates, the inability to obtain further rate increases, limitations on premium levels, increases in minimum capital and reserve requirements, benefit mandates, limitations on the ability to manage care and utilization, requirements to write certain classes of business, limitations on the use of credit scoring, such as proposals to ban the use of credit scores with respect to personal lines in Michigan and Florida or as proposed by Congress from time to time, restrictions on the use of certain compensation arrangements with agents and brokers, as well as continued compliance with state and federal regulations; (viii) adverse changes in the ratings obtained from independent rating agencies, such as Moody s, Standard and Poor s, Fitch and A.M. Best, whether due to investment impairments, additional capital requirements, our underwriting performance or other factors, including future rating agency requirements that may result from the current global economic crisis or otherwise; (ix) industry-wide change resulting from proposed regulations, investigations and inquiries relating to compensation arrangements with insurance brokers and agents; (x) disruptions caused by the introduction of new products, including new Commercial Lines specialty products, or in connection with the integration and expansion of newly acquired businesses; (xi) the impact of our acquisitions of Professionals Direct, Inc., Verlan Holdings, Inc., AIX Holdings, Inc., or other future acquisitions, including potential reserve deficiencies, distribution channel conflicts or disruptions in personnel or operating models.

Additionally, our profitability could be affected by adverse catastrophe experience (including terrorism), severe weather or other unanticipated significant losses. Further, certain new catastrophe models assume an increased frequency and severity of certain weather events, and financial strength rating agencies are placing increased emphasis on capital and reinsurance adequacy for insurers with certain geographic concentrations of risk, particularly in coastal areas. We have significant concentration of exposures in certain areas, including portions of the Northeast and Southeast and derive a material amount of profits from operations in the Midwest. There are also concerns that the higher level of weather-related catastrophes and other losses incurred by the industry in recent years is indicative of changing weather patterns, whether as a result of changing climate (global warming) or otherwise, which could cause such events to persist. This would lead to higher overall losses which we may not be able to recoup, particularly in the current economic and competitive environment.

Underwriting results and segment income could be adversely affected by further changes in our net loss and LAE estimates related to hurricanes Katrina, Ike, Gustav and other significant events. The risks and uncertainties in our business that may affect such estimates and future performance, including the difficulties in arriving at such estimates, should be considered. Estimating losses following any major catastrophe is an inherently uncertain process. Factors that add to the complexity in these events include the legal and regulatory uncertainty, the complexity of factors contributing to the losses, delays in claim reporting, the impact of demand surge and a slower pace of recovery resulting from the extent of damage sustained in the affected areas due in part to the availability and cost of resources to effect repairs. As a result, there can be no assurance that our ultimate costs associated with these events will not be substantially different from current estimates.

Additionally, future operating results as compared to prior years and forward-looking information regarding Personal Lines and Commercial Lines segment information on written and earned premiums, policies in force, underwriting results and segment income currently are expected to be adversely affected by competitive and regulatory pressures affecting rates, particularly in Michigan where the Governor has called for a freeze on automobile insurance rates. In addition, underwriting results and segment income could be adversely affected by changes in frequency and loss trends. Results in Personal Lines business may also be adversely affected by pricing decreases and market disruptions (including any caused by the current economic environment, particularly in Michigan, proposals in Michigan to reduce rates, expand coverage, limit territorial ratings, or expand circumstances in which parties can recover non-economic damages for bodily injury claims (i.e., efforts to modify or overturn the so-called Kreiner decision), the Michigan Commissioner of Insurance s proposed ban on the use of credit scores, or the Governor s executive order creating a position of the Automobile and Home Insurance Consumer Advocate, who is to act independent from the Michigan Commissioner of Insurance). The introduction of managed competition in Massachusetts has resulted in overall rate level reductions. Additionally, there is uncertainty regarding our ability to attract and retain customers in the market as new and larger carriers enter the state of Massachusetts as a result of managed competition .

Also, our Personal Lines business production and earnings may be unfavorably affected by the introduction of our multivariate auto product should we experience adverse selection because of our pricing, operational difficulties or implementation impediments with independent agents, or the inability to grow or sustain growth in new markets after the introduction of new products or the appointment of new agents. In addition, there are increased underwriting risks associated with premium growth and the introduction of new products or programs in both our Personal and Commercial Lines businesses, as well as the appointment of new agencies and the expansion into new geographical areas, and we have experienced increased loss ratios with respect to our new personal automobile business, which is written through our ***Connections Auto*** product, particularly in certain states where we have less experience and data.

Similarly, the introduction of new Commercial Lines products, including through our recently acquired subsidiaries and the development of new niche and specialty lines, presents new risks. Certain new specialty products may present longer tail risks and increased volatility in profitability.

Additionally, during the past few years we have made, and our current plans are to continue to make, significant investments in our Personal Lines and Commercial Lines businesses to, among other things, strengthen our product offerings and service capabilities, improve technology and our operating models, build expertise in our personnel, and expand our distribution capabilities, with the ultimate goal of achieving significant and sustained profitable growth and obtaining favorable returns on these investments. In order for these investment strategies to be profitable, we must achieve both profitable premium growth and the successful implementation of our operating models so that our expenses do not increase proportionately with growth. The ability to grow profitably throughout the property and casualty cycle is crucial to our current strategy. There can be no assurance that we will be successful in profitably growing our business, or that we will not alter our current strategy due to changes in our markets or an inability to successfully maintain acceptable margins on new business or for other reasons, in which case written and earned premium, segment income and net book value could be adversely affected.

Significant increases in recent years and expected further increases in the number of participants or insureds in state-sponsored reinsurance pools or FAIR Plans, particularly in the states of Massachusetts, Louisiana and Florida, combined with regulatory restrictions on the ability to adequately price, underwrite, or non-renew business, could expose us to significant exposures and assessment risks.

RISKS RELATING TO OUR DISCONTINUED LIFE COMPANIES BUSINESS

Our discontinued Life Companies businesses may be affected by (i) adverse actions related to legal and regulatory actions described under Contingencies and Regulatory Matters , including those which are subject to the FIN 45 reserve described under Life Companies Discontinued Operations ; (ii) adverse loss and expense development related to our discontinued assumed accident and health reinsurance pool business or failures of our reinsurers to timely pay their obligations (especially in light of the fact that historically these pools sometimes involved multiple layers of overlapping reinsurers, or so called spirals); (iii) possible indemnification claims relating to sales practices for insurance and investment products or our historical administration of such products or the Closed Block, including with respect to activities of our former agents; and (iv) the impact of contingent liabilities, including litigation and regulatory matters, assumed or retained by THG in connection with the transaction and the impact of other indemnification obligations owed from THG to Goldman Sachs and/or Commonwealth Annuity (including with respect to existing and potential litigation).

RISKS RELATING TO OUR BUSINESS GENERALLY

Other market fluctuations and general economic, market and political conditions also may negatively affect our business and profitability. These conditions include (i) the difficulties of estimating the impact of the current financial turmoil on the value of our investment portfolio and future investment income, including the amount of realized losses and impairments which will be recognized in future financial reports and our ability and intent to hold such investments until recovery; (ii) the impact on our capital and liquidity of the current financial turmoil, including as a result of defaults in our fixed income investment portfolio and the market decline in the value of non-government backed investments; (iii) changes in interest rates causing a reduction of investment income or in the market value of interest rate sensitive investments; (iv) higher service, administrative or general expense due to the need for additional advertising, marketing, administrative or management information systems expenditures; (v) the inability to attract, or the loss or retirement of key executives or other key employees, and increased costs associated with the replacement of key executives or employees; (vi) changes in our liquidity due to changes in asset and liability matching, including the effect of defaults of debt securities; (vii) failure of a reinsurer of our policies to pay its

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liabilities under reinsurance or coinsurance contracts or adverse effects on the cost and availability of reinsurance (including as a result of any such insurers losses in its investment portfolio as a result of the current economic conditions or the result of significant catastrophes such as the September 11, 2001 terrorist attacks or Hurricane Katrina); (viii) changes in the mix of assets comprising our investment portfolios and changes in general market conditions that may cause the market value of our investment portfolio to fluctuate, including the expansion of current concerns regarding sub-prime mortgages to prime mortgage and corresponding mortgage-backed or other debt securities and concerns relative to the ratings and capitalization of municipal bond and mortgage guarantees and the valuation of commercial mortgages and commercial mortgage-backed securities; (ix) losses resulting from our participation in certain reinsurance pools, including pools in which we no longer participate but may have unquantified potential liabilities relating to asbestos environmental and other latent exposure matters, or from fronting arrangements where the reinsurer does not meet all of its reinsurance obligations; (x) defaults or impairments of debt securities held by us; (xi) higher employee benefit costs due to the significant decline in market values of defined benefit retirement plan assets resulting from the current economic crisis, interest rate fluctuations, regulatory requirements or judicial interpretations of benefits (including with respect to our Cash Balance Plan which is the subject of the Durand litigation); (xii) the effects of our restructuring actions, including any resulting from our review of operational matters related to our business, including a review of our markets, products, organization, financial capabilities, agency management, regulatory environment, ancillary businesses and service processes; (xiii) errors or omissions in connection with the administration of any of our products; (xiv) breaches of our information technology security systems or other operational disruptions or breaches which result in the loss or compromise of confidential financial, personal, medical or other information about our policyholders, claimants, agents or others with whom we do business; and (xv) interruptions in our ability to conduct business as a result of terrorist actions, catastrophes or other significant events affecting infrastructure, and delays in recovery of our operating capabilities.

Recent developments in the global financial markets may adversely affect our investment portfolio and overall performance. Global financial markets have recently experienced unprecedented and challenging conditions, including a tightening in the availability of credit and the failure of several large financial institutions. As a result, certain government bodies and central banks worldwide, including the U.S. Treasury Department and the U.S. Federal Reserve, have undertaken unprecedented intervention programs, the effects of which remain uncertain. There can be no assurances that these intervention programs, including The Emergency Economic Stabilization Act of 2008 and The 2009 American Recovery and Reinvestment Act, will be successful in improving conditions in the global financial market. The U.S. economy has experienced and continues to experience significant declines in employment, household wealth, and lending. If conditions further deteriorate, our business could be affected in different ways. Continued turbulence in the U.S. economy and contraction in the credit markets could adversely affect our profitability, demand for our products or our ability to raise rates, and could also result in declines in market value and future impairments of our investment assets. There can be no assurances that conditions in the global financial markets will not worsen and/or further adversely affect our investment portfolio and overall performance. Recessionary economic periods and higher unemployment are historically accompanied by higher claims activity, particularly in the personal and workers compensation lines of business and higher defaults in contractors bonds.

ITEM 1B UNRESOLVED STAFF COMMENTS

None.

ITEM 2 PROPERTIES

We own our headquarters, located at 440 Lincoln Street, Worcester, Massachusetts, which consist primarily of approximately 758,000 square feet of office and conference space.

We also own office space, located at 645 W. Grand River, Howell, Michigan, which is approximately 104,000 square feet, and a three-building complex located at 808 North Highlander Way, Howell, Michigan, with approximately 157,000 square feet, where various business operations are conducted.

We lease offices throughout the country for branch sales, underwriting and claims processing functions, and the operations of our recently acquired subsidiaries.

We believe that our facilities are adequate for our present needs in all material respects. Certain of our properties may be made available for lease.

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ITEM 3 LEGAL PROCEEDINGS

DURAND LITIGATION

On March 12, 2007, a putative class action suit captioned Jennifer A. Durand v. The Hanover Insurance Group, Inc., The Allmerica Financial Cash Balance Pension Plan was filed in the United States District Court for the Western District of Kentucky. The named plaintiff, a former employee who received a lump sum distribution from our Cash Balance Plan at or about the time of her termination, claims that she and others similarly situated did not receive the appropriate lump sum distribution because in computing the lump sum, we understated the accrued benefit in the calculation. We filed a motion to dismiss on the basis that the plaintiff failed to exhaust administrative remedies, which motion was granted without prejudice in a decision dated November 7, 2007. Plaintiff filed a Notice of Appeal of this dismissal to the United States Court of Appeals for the Sixth Circuit; oral arguments on the plaintiff s appeal took place on October 28, 2008, and we are awaiting the court s decision. In our judgment, the outcome is not expected to be material to our financial position, although it could have a material effect on the results of operations for a particular quarter or annual period.

HURRICANE KATRINA LITIGATION

We have been named as a defendant in various litigations, including putative class actions, relating to disputes arising from damages which occurred as a result of Hurricane Katrina in 2005. As of December 31, 2008, there were approximately 145 such cases. These cases have been filed in both Louisiana state courts and federal district courts. These cases generally involve, among other claims, disputes as to the amount of reimbursable claims in particular cases (e.g. how much of the damage to an insured property is attributable to flood and therefore not covered, and how much is attributable to wind, which may be covered), as well as the scope of insurance coverage under homeowners and commercial property policies due to flooding, civil authority actions, loss of landscaping, business interruption and other matters. Certain of these cases claim a breach of duty of good faith or violations of Louisiana insurance claims handling laws or regulations and involve claims for punitive or exemplary damages.

On August 23, 2007, the State of Louisiana (individually and on behalf of the State of Louisiana, Division of Administration, Office of Community Development) filed a putative class action in the Civil District Court for the Parish of Orleans, State of Louisiana, entitled State of Louisiana, individually and on behalf of State of Louisiana, Division of Administration, Office of Community Development ex rel The Honorable Charles C. Foti, Jr., The Attorney General For the State of Louisiana, individually and as a class action on behalf of all recipients of funds as well as all eligible and/or future recipients of funds through The Road Home Program v. AAA Insurance, et al., No. 07-8970. The complaint named as defendants over 200 foreign and domestic insurance carriers, including us. Plaintiff seeks to represent a class of current and former Louisiana citizens who have applied for and received or will receive funds through Louisiana s Road Home program. On August 29, 2007, Plaintiff filed an Amended Petition in this case, asserting myriad claims, including claims for breach of contract, the implied covenant of good faith and fair dealing, fiduciary duty and Louisiana s bad faith statutes. Plaintiff seeks relief in the form of, among other things, declarations that (a) the efficient proximate cause of losses suffered by putative class members was windstorm, a covered peril under their policies; (b) the second efficient proximate cause of their losses was storm surge, which Plaintiff contends is not excluded under class members policies; (c) the damage caused by water entering affected parishes of Louisiana does not fall within the definition of flood ; (d) the damages caused by water entering Orleans Parish and the surrounding area was a result of a man-made occurrence and are properly covered under class members policies; (e) many class members suffered total losses to their residences; and (f) many class members are entitled to recover the full value for their residences stated on their policies pursuant to the Louisiana Valued Policy Law. In accordance with these requested declarations, Plaintiff seeks to recover amounts that it alleges should have been paid to policyholders under their insurance agreements, as well as penalties, attorneys fees, and costs. The case has been removed to the Federal District Court for the Eastern District of Louisiana.

We have established our loss and LAE reserves on the assumption that we will not have any liability under the Road Home or similar litigation, and that we will otherwise prevail in litigation as to the causes of certain large losses and not incur extra contractual or punitive damages.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders in the fourth quarter of the fiscal year covered by this Annual Report on Form 10-K.

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PART II

ITEM 5 MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

COMMON STOCK AND STOCKHOLDER OWNERSHIP

Our common stock is traded on the New York Stock Exchange under the symbol THG . On February 20, 2009, we had approximately 29,152 shareholders of record and 51,139,602 shares outstanding. On the same date, the trading price of our common stock was $34.92 per share.

COMMON STOCK PRICES AND DIVIDENDS

	High (1)	Low (1)	Dividends
2008			
First Quarter	**$ 47.17**	**$ 40.14**	
Second Quarter	**$ 46.83**	**$ 41.71**	
Third Quarter	**$ 51.00**	**$ 38.01**	
Fourth Quarter	**$ 45.00**	**$ 31.92**	**$ 0.45**
2007			
First Quarter	$ 49.11	$ 44.70	
Second Quarter	$ 49.73	$ 44.46	
Third Quarter	$ 49.76	$ 41.14	
Fourth Quarter	$ 46.21	$ 42.23	$ 0.40

(1) Common stock prices were obtained from a third party broker.

DIVIDENDS

On October 24, 2008, the Board of Directors declared a 45 cents per share cash dividend, which was paid on December 10, 2008 to shareholders of record as of November 26, 2008. The payment of future dividends on our common stock will be a business decision made by the Board of Directors from time to time based upon cash available at our holding company, our results of operations and financial condition and such other factors as the Board of Directors considers relevant.

Dividends to shareholders may be funded from dividends paid to us from our subsidiaries. Dividends from insurance subsidiaries are subject to restrictions imposed by state insurance laws and regulations. See Liquidity and Capital Resources on pages 60 to 62 of Management s Discussion and Analysis of Financial Condition and Results of Operations and Note 15 Dividend Restrictions on page 104 of the Notes to Consolidated Financial Statements included in Financial Statements and Supplementary Data of this Form 10-K.

ISSUER PURCHASES OF EQUITY SECURITIES

On October 16, 2007, the Board of Directors authorized the repurchase of up to $100 million of our common stock. Under this repurchase authorization, we may repurchase our common stock from time to time, in amounts and prices and at such times as we deem appropriate, subject to market conditions and other considerations. We are not required to purchase any specific number of shares or to make purchases by any certain date under this program.

Through June 2008, approximately $60 million of shares had been repurchased under this program. No shares were repurchased during the remainder of 2008.

Shares purchased in the quarter are unrelated to the repurchase program and are as follows:

Period	*Total Number of Shares Purchased*	*Average Price Paid per Share*	*Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs*	*Approximate Dollar Value of Shares That May Yet be Purchased Under the Plans or Programs*
October 1 31, 2008[1]	431	$ 34.84		$ 39,800,000
November 1 30, 2008[2]	465	40.32		39,800,000
December 1 31, 2008[1]	586	39.97		39,800,000
Total	1,482	$ 38.59		$ 39,800,000

(1) Shares were withheld to satisfy tax withholding amount due from employees upon their receipt of previously restricted shares.

(2) Shares were withheld to satisfy tax withholding amount due from employees related to the receipt of stock which resulted from the vesting of their performance based restricted stock units.

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ITEM 6 SELECTED FINANCIAL DATA

Five Year Summary Of Selected Financial Highlights

For The Years Ended December 31

(In millions, except per share data)	**2008**	**2007**	**2006**	**2005**	**2004**
Statements of Income					
Revenues					
Premiums	**$ 2,484.9**	$ 2,372.0	$ 2,219.2	$ 2,161.2	$ 2,249.1
Net investment income	**258.7**	247.0	228.5	209.7	197.4
Net realized investment (losses) gains	**(97.8)**	(0.9)	(0.2)	7.8	20.1
Fees and other income	**34.6**	56.0	57.9	42.6	42.4
Total revenues	**2,680.4**	2,674.1	2,505.4	2,421.3	2,509.0
Benefits, Losses and Expenses					
Policy benefits, claims, losses and loss adjustment expenses	**1,626.2**	1,457.4	1,387.1	1,601.6	1,558.1
Policy acquisition expenses	**556.2**	523.6	476.4	458.5	470.1
Other operating expenses	**333.6**	351.6	370.9	307.8	335.3
Total benefits, losses and expenses	**2,516.0**	2,332.6	2,234.4	2,367.9	2,363.5
Income from continuing operations before federal income taxes	**164.4**	341.5	271.0	53.4	145.5
Federal income tax expense (benefit)	**79.9**	113.2	87.2	(6.3)	26.2
Income from continuing operations	**84.5**	228.3	183.8	59.7	119.3
Discontinued operations:					
(Loss) income from operations of discontinued FAFLIC business, (including loss on assets held-for-sale of $77.3 in 2008), net of taxes	**(84.8)**	10.9	7.9	16.8	26.0
Income (loss) from operations of discontinued variable life insurance and annuity business, (including gain (loss) on disposal of variable life insurance and annuity business of $8.7, $7.9, $(29.8) and $(444.4) in 2008, 2007, 2006 and 2005), net of taxes	**11.3**	13.1	(29.8)	(401.7)	37.2
Income from operations of discontinued AMGRO Business (including gain on disposal of $11.1)	**10.1**				
Other discontinued operations	**(0.5)**	0.8	7.8		
Loss (income) from discontinued operations	**(63.9)**	24.8	(14.1)	(384.9)	63.2
Income (loss) before cumulative effect of change in accounting principle	**20.6**	253.1	169.7	(325.2)	182.5
Cumulative effect of change in accounting principle			0.6		(57.2)
Net income (loss)	**$ 20.6**	$ 253.1	$ 170.3	$ (325.2)	$ 125.3
Earnings (loss) per common share (diluted)	**$ 0.40**	$ 4.83	$ 3.27	$ (6.02)	$ 2.34
Dividends declared per common share (diluted)	**$ 0.45**	$ 0.40	$ 0.30	$ 0.25	$
Balance Sheets (at December 31)					
Total assets	**$ 9,230.2**	$ 9,815.6	$ 9,856.6	$ 10,634.0	$ 23,810.1
Long-term debt	**531.4**	511.9	508.8	508.8	508.8
Total liabilities	**7,343.0**	7,516.6	7,857.4	8,682.7	21,470.6
Shareholders equity	**1,887.2**	2,299.0	1,999.2	1,951.3	2,339.5

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ITEM 7

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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INTRODUCTION

The following Management s Discussion and Analysis of Financial Condition and Results of Operations is intended to assist readers in understanding the consolidated results of operations and financial condition of The Hanover Insurance Group, Inc. (the holding company) and its subsidiaries (collectively THG) and should be read in conjunction with the Consolidated Financial Statements and related footnotes included elsewhere herein.

Our results of operations include the accounts of The Hanover Insurance Company (Hanover Insurance) and Citizens Insurance Company of America (Citizens), our principal property and casualty companies First Allmerica Financial Life Insurance Company (FAFLIC), our former life insurance and annuity company, and certain other insurance and non-insurance subsidiaries. As of December 31, 2008 and for all prior periods presented, operations from FAFLIC have been classified as discontinued operations and the related assets and liabilities as held-for-sale due to the sale of FAFLIC on January 2, 2009 to Commonwealth Annuity and Life Insurance Company (Commonwealth Annuity), a subsidiary of The Goldman Sachs Group, Inc. (Goldman Sachs). (See Discontinued Operations: Life Companies on pages 42-44 of this Form 10-K for further information). Hanover Insurance and Citizens are domiciled in the states of New Hampshire and Michigan, respectively.

EXECUTIVE OVERVIEW

Our property and casualty business constitutes our primary ongoing operations and includes our Personal Lines segment, our Commercial Lines segment and our Other Property and Casualty segment. As noted above, on January 2, 2009, we sold FAFLIC to Commonwealth Annuity. Based on the December 31, 2008 asset and liability values, including a pre-close dividend from FAFLIC consisting of designated assets with a statutory book value of approximately $130 million, total net proceeds from the sale after estimated transaction expenses were approximately $230 million. Coincident with the sale transaction, Hanover Insurance and FAFLIC entered into a reinsurance contract whereby Hanover Insurance assumed FAFLIC s discontinued accident and health insurance business.

During 2008, unprecedented capital market events, including the failure of several large financial institutions, have resulted in a deterioration in the overall credit environment and caused the market value of both investment and below investment grade securities to depreciate. Concerns about asset quality expanded well beyond exposure to the residential mortgage market, causing one of the sharpest declines in financial asset values in recent history. Additionally, the uncertainty in the financial markets has resulted in the contraction of credit market liquidity. Our investment holdings consist primarily of fixed maturities, cash and cash equivalents, which totaled $4.8 billion at December 31, 2008, excluding those assets held-for-sale in connection with the FAFLIC transaction. Approximately 94% of our fixed maturity holdings are investment grade securities. In our investment grade bonds, credit spreads widened most significantly in the financial sector. In our below investment grade portfolio, corporate bonds with lower ratings experienced the most marked decline in value.

During 2008, we recognized impairment charges of $126.1 million, including $13.0 million related to our discontinued FAFLIC business, primarily related to credit-related losses on fixed maturities in the financial sector, including our holdings in securities issued by Lehman Brothers and Washington Mutual, and to a lesser extent, the industrial sector. As of December 31, 2008, we held securities with net unrealized loss positions of approximately $276 million. We expect that the markets will continue to be volatile in the near-term. There is uncertainty regarding what effect government programs will have on the financial markets and the time that is required for companies to successfully execute meaningful actions that will provide relief to the markets. We believe, however, that recent and ongoing government actions to support the banking and financial sectors, the quality of the assets we hold, and our relatively strong capital position will allow us, over time, to realize the anticipated long-term economic value related to securities we hold that are in an unrealized loss position. Additionally, we have a substantially liquid portfolio with a laddered duration structure which provides for periodic maturities and thus expect to have the ability to hold such securities for the period of time anticipated to allow for a recovery in fair value.

During 2008, we incurred $169.7 million of catastrophe losses on a pre-tax basis. This year was marked by several catastrophe events, with Hurricanes Ike and Gustav being the most significant. This catastrophe activity also generated significant losses for the industry. Hurricane Gustav s damage was concentrated in Louisiana, where our overall losses were lower than our respective market share due in part to specific catastrophe management initiatives undertaken over the past three years. Hurricane Ike was an unusually far reaching and long-lasting storm, affecting our Central and Midwest regions, and even impacting Michigan. We expect that our losses associated

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with Ike are consistent with our market share in the affected states. We believe that we have made significant progress with respect to effectively managing our catastrophe exposure by strengthening our underwriting guidelines and pro-actively utilizing catastrophe modeled data where appropriate.

Personal Lines

In our Personal Lines business, we are focused on making investments that are intended to help us maintain profitability, build a distinctive position in the market and provide us with profitable growth opportunities. We have continued to implement catastrophe management actions in coastal states, including Florida and Louisiana that, while reducing premium in our homeowners line, has improved our risk profile. Additionally, current market conditions continue to be challenging as pricing pressures and economic conditions remain difficult, especially in Michigan, impacting our ability to grow and retain business in this, our largest state and elsewhere. We are working closely with our partner agents in Michigan to remain a significant writer with strong margins. Also, in 2008 we continued our mix management initiatives relating to our ***Connections®* Auto** product to improve the overall profitability of the business. We are focused on reducing our growth in less profitable automobile segments and increasing our multi-car and account business consistent with our strategy. We believe that market conditions will remain challenging and competitive in Personal Lines. Despite these challenges and transitions, we experienced relatively flat growth levels in Personal Lines and expect that trend to continue in the near term as the industry continues to respond to the difficult economic environment.

Our ***Connections Auto*** product is available in eighteen states. We believe that this product will help us to profitably grow our market share over time. The ***Connections Auto*** product is designed to be competitive for a wide spectrum of drivers through its multivariate rating application, which calculates rates based upon the magnitude and correlation of multiple risk factors. At the same time, a core strategy is to broaden our portfolio offerings and write total accounts , which are accounts that include multiple personal line coverages for the same customer. Our homeowners product, ***Connections® Home***, is available in sixteen states. It is intended to improve our competitiveness for total account business by significantly improving ease of doing business for our agents and by providing better packaging of coverages for policyholders. Having implemented a broader portfolio of products, we continue to refine these products and to work closely with high potential agents to increase the percentage of business they place with us and to ensure that it is consistent with our preferred mix of business. Additionally, we remain focused on diversifying our state mix beyond our four core states of Michigan, Massachusetts, New York and New Jersey. We expect these efforts to contribute to profitable growth and improved retention in our Personal Lines segment over time.

Commercial Lines

In the Commercial Lines business, the market remains competitive. Price competition requires us to continue to be highly disciplined in our underwriting process to ensure that we grow the business only at acceptable margins. We continue to target, through mid-sized agents, small and first-tier middle markets, which encompass clients whose premiums are generally below $200,000. We also continue to develop our specialty businesses, which on average are expected to offer higher margins over time and enable us to deliver a more complete product portfolio to our agents and policyholders. Our specialty lines now account for approximately one third of our Commercial Lines business. Additional growth in our specialty lines continues to be a significant part of our strategy. Our ongoing focus on expanding our product offerings in specialty businesses during 2008 was evidenced by our acquisitions of Verlan Holdings, Inc. (Verlan), which we market as Hanover Specialty Property, a specialty company providing property insurance to small and medium-sized manufacturing and distribution companies that are highly protected fire risks, and AIX Holdings, Inc. (AIX), a specialty property and casualty insurance carrier that focuses on underwriting and managing program business that utilizes alternative risk transfer techniques. In the fourth quarter of 2007, we acquired Professionals Direct, Inc. (PDI), which we market as Hanover Professionals, providing professional liability coverage for small to medium-sized legal practices. Additionally, over the two prior years, we developed our niche insurance programs, such as for schools, religious institutions and moving and storage companies. We believe these acquisitions and the development of our niche businesses provide us with better breadth and diversification of products and improve our competitive position with our agents.

In 2008, we internally developed another specialty niche for Human Services organizations, which was introduced in January 2009 in 13 states. As a complimentary initiative, we have established a business focused on management liability, specifically non-profit Directors and Officers liability, employment practices liability and eventually private company Directors and Officers liability. In addition, we have made a number of enhancements to our core products and technology platforms that are intended to drive more total account placements in our Small Commercial business, which we believe will enhance margins. Our focus continues to be on improving and expanding our partnerships with agents. We believe our specialty capabilities and small commercial platform, coupled with distinctiveness in the middle market, enables us to deliver significant value to our agents and policyholders in our target markets.

DESCRIPTION OF OPERATING SEGMENTS

Our primary business operations include insurance products and services in three property and casualty operating segments. These segments are Personal Lines, Commercial Lines and Other Property and Casualty. As of December 31, 2008, due to the sale of FAFLIC on January 2, 2009, the operations of our Life Companies have been classified as Discontinued Operations. Certain ongoing expenses have been reclassified from our Life Companies segment to our Property and Casualty business. We present the separate financial information of each segment consistent with the manner in which our chief operating decision maker evaluates results in deciding how to allocate resources and in assessing performance.

The Property and Casualty group manages its operations principally through three segments: Personal Lines, Commercial Lines and Other Property and Casualty. Personal Lines includes personal automobile, homeowners and other personal coverages, while Commercial Lines includes commercial multiple peril, commercial automobile, workers compensation and other commercial coverages, such as bonds and inland marine business. In addition, the Other Property and Casualty segment consists of: Opus Investment Management, Inc. (OPUS), which markets investment management services to institutions, pension funds and other organizations; earnings on holding company assets; and voluntary pools business in which we have not actively participated since 1995. Prior to its sale on June 2, 2008, Amgro, Inc. (AMGRO), our premium financing business, was also included in the Other Property and Casualty segment.

We report interest expense related to our corporate debt separately from the earnings of our operating segments. Corporate debt consists of our junior subordinated debentures and our senior debentures.

RESULTS OF OPERATIONS

Our consolidated net income includes the results of our three operating segments (segment income), which we evaluate on a pre-tax basis, and our interest expense on corporate debt. In addition, segment income excludes certain items which we believe are not indicative of our core operations. The income of our segments excludes items such as federal income taxes and net realized investment gains and losses, including net gains or losses on certain derivative instruments, because fluctuations in these gains and losses are determined by interest rates, financial markets and the timing of sales. Also, segment income excludes net gains and losses on disposals of businesses, discontinued operations, restructuring costs, extraordinary items, the cumulative effect of accounting changes and certain other items. Although the items excluded from segment income may be significant components in understanding and assessing our financial performance, we believe segment income enhances an investor s understanding of our results of operations by highlighting net income attributable to the core operations of the business. However, segment income should not be construed as a substitute for net income determined in accordance with generally accepted accounting principles (GAAP).

Catastrophe losses are a significant component in understanding and assessing the financial performance of our business. However, catastrophic events, such as Hurricanes Katrina, Ike and Gustav make it difficult to assess the underlying trends in this business. Management believes that providing certain financial metrics and trends, excluding the effects of catastrophes, help investors to understand the variability in periodic earnings and to evaluate the underlying performance of our operations.

Our consolidated net income was $20.6 million in 2008, compared to $253.1 million in 2007. The $232.5 million decrease in earnings is primarily due to net realized investment losses of $97.8 million, and loss from operations of our discontinued FAFLIC business, including the $77.3 million estimated loss on the sale of FAFLIC, and $14.4 million of additional net realized investment losses from FAFLIC. Additionally, there were increased after-tax catastrophe losses of $67.9 million in 2008. Partially offsetting these decreases was a $24.4 million increase in non-catastrophe related pre-tax segment income and a $10.1 million net gain on the sale of AMGRO.

Our consolidated net income was $253.1 million in 2007, compared to a net income of $170.3 million in 2006.

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The $82.8 million increase in earnings primarily reflects increased after-tax segment results of $44.3 million, and the absence of $29.8 million of losses incurred in 2006 related to the disposal, in 2005, of our variable life insurance and annuity business. The increase in segment results primarily reflects a decrease in catastrophe related activity, as well as higher net investment income.

The following table reflects segment income (loss) as determined in accordance with Statement of Financial Accounting Standards No. 131, *Disclosures about Segments of an Enterprise and Related Information*, and a reconciliation of total segment income to consolidated net income.

For The Years Ended December 31 *(In millions)*	**2008**	**2007**	**2006**
Segment income before federal income taxes:			
Property and Casualty			
Personal Lines	**$ 123.5**	$ 208.2	$ 181.3
Commercial Lines	**169.7**	169.3	117.7
Other Property and Casualty	**9.0**	4.8	11.9
Total Property and Casualty	**302.2**	382.3	310.9
Interest expense on corporate debt	**(39.9)**	(39.9)	(39.9)
Total segment income before federal income taxes	**262.3**	342.4	271.0
Federal income tax expense on segment income	**(86.3)**	(113.7)	(86.6)
Change in prior years tax reserves			1.4
Federal income tax settlement	**6.4**		
Net realized investment losses	**(97.8)**	(0.9)	(0.2)
Other non-segment items	**(0.1)**		0.2
Federal income tax benefit (expense) on non-segment items		0.5	(2.0)
Income from continuing operations, net of taxes	**84.5**	228.3	183.8
Discontinued operations:			
(Loss) income from continued FAFLIC business, net of taxes (including loss on assets held-for-sale of $77.3 in 2008)	**(84.8)**	10.9	7.9
Income (loss) from discontinued variable life insurance and annuity business, net of taxes (including gain (loss) on disposal of $11.3, $7.9 and ($29.8) in 2008, 2007 and 2006)	**11.3**	13.1	(29.8)
Income from operations of AMGRO (including gain on disposal of $11.1), net of taxes	**10.1**		
Other discontinued operations	**(0.5)**	0.8	7.8
Income before cumulative effect of change in accounting principle	**20.6**	253.1	169.7
Cumulative effect of change in accounting principle, net of taxes			0.6