WHITE MOUNTAINS INSURANCE GROUP LTD
Form 10-Q
November 05, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the period ended September 30, 2007

OR

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

For the transition period from to

Commission file number 1-8993

WHITE MOUNTAINS INSURANCE GROUP, LTD.

(Exact name of registrant as specified in its charter)

Bermuda	**94-2708455**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

80 South Main Street,

Hanover, New Hampshire	**03755-2053**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(603) 640-2200**

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 o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

As of November 2, 2007, 10,560,272 common shares with a par value of $1.00 per share were outstanding (which includes 54,000 restricted common shares that were not vested at such date).

WHITE MOUNTAINS INSURANCE GROUP, LTD.

Table of Contents

PART I. FINANCIAL INFORMATION.

Item 1. Financial Statements

WHITE MOUNTAINS INSURANCE GROUP, LTD.

CONSOLIDATED BALANCE SHEETS

(Millions, except share and per share amounts)		September 30, 2007 Unaudited		December 31, 2006
Assets				
Fixed maturity investments, at fair value (amortized cost: $7,291.7 and $7,377.0)	$	**7,436.7**	$	7,475.3
Common equity securities, at fair value (cost: $1,232.8 and $972.0)		**1,471.3**		1,212.6
Short-term investments, at amortized cost (which approximates fair value)		**1,614.8**		1,344.9
Other investments (cost: $484.5 and $467.1)		**549.3**		524.8
Convertible fixed maturity investments, at fair value (amortized cost: $529.5 and $435.9)		**529.5**		436.2
Trust account investments, at amortized cost (fair value $309.5 and $337.9)		**308.7**		338.9
Total investments		**11,910.3**		11,332.7
Cash		**185.6**		159.0
Reinsurance recoverable on unpaid losses		**1,789.3**		2,134.5
Reinsurance recoverable on unpaid losses - Berkshire Hathaway Inc.		**1,792.6**		1,881.2
Reinsurance recoverable on paid losses		**58.1**		159.4
Insurance and reinsurance premiums receivable		**971.1**		913.6
Securities lending collateral		**824.6**		649.8
Funds held by ceding companies		**352.3**		452.8
Investments in unconsolidated affiliates		**404.4**		335.5
Deferred acquisition costs		**358.6**		320.3
Deferred tax asset		**238.7**		276.0
Ceded unearned premiums		**129.2**		87.9
Accrued investment income		**89.1**		87.4
Accounts receivable on unsettled investment sales		**21.7**		8.5
Other assets		**593.1**		645.1
Total assets	$	**19,718.7**	$	19,443.7
Liabilities				
Loss and loss adjustment expense reserves	$	**8,249.3**	$	8,777.2
Unearned insurance and reinsurance premiums		**1,743.2**		1,584.9
Debt		**1,192.8**		1,106.7
Securities lending payable		**824.6**		649.8
Deferred tax liability		**327.2**		311.5
Long-term incentive compensation payable		**202.5**		285.2
Reserves for structured contracts		**78.8**		147.1
Funds held under reinsurance treaties		**99.5**		141.6
Ceded reinsurance payable		**124.0**		138.4
Accounts payable on unsettled investment purchases		**85.4**		66.8
Other liabilities		**901.5**		913.7
Preferred stock subject to mandatory redemption:				
Held by Berkshire Hathaway Inc. (redemption value $300.0)		**268.5**		242.3
Held by others (redemption value $20.0)				20.0
Total liabilities		**14,097.3**		14,385.2
Minority interest - OneBeacon, Ltd.		**536.3**		490.7
Minority interest - WMRe Group Preference Shares		**250.0**		
Minority interest - consolidated limited partnerships		**102.5**		112.5
Total minority interest		**888.8**		603.2
Common shareholders equity				
		10.8		10.8

Common shares at $1 par value per share - authorized 50,000,000 shares; issued and outstanding 10,842,613 and 10,782,753 shares				
Paid-in surplus		**1,723.9**		1,716.7
Retained earnings		**2,737.3**		2,496.0
Accumulated other comprehensive income, after-tax:				
Net unrealized gains on investments		**184.3**		194.0
Net unrealized foreign currency translation gains		**79.1**		37.2
Other		**(2.8)**		.6
Total common shareholders equity		**4,732.6**		4,455.3
Total liabilities, minority interest and common shareholders equity	**$**	**19,718.7**	$	19,443.7

See Notes to Consolidated Financial Statements

WHITE MOUNTAINS INSURANCE GROUP, LTD.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

Unaudited

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Millions, except per share amounts)	**2007**	**2006**	**2007**	**2006**
Revenues:				
Earned insurance and reinsurance premiums	**$ 936.3**	$ 918.9	**$ 2,835.0**	$ 2,773.4
Net investment income	**128.9**	108.7	**373.6**	311.6
Net realized investment gains	**29.9**	67.8	**192.9**	202.8
Other revenue	**60.3**	90.8	**130.6**	157.1
Total revenues	**1,155.4**	1,186.2	**3,532.1**	3,444.9
Expenses:				
Loss and loss adjustment expenses	**591.9**	558.1	**1,797.3**	1,885.9
Insurance and reinsurance acquisition expenses	**183.9**	189.3	**580.1**	562.6
Other underwriting expenses	**103.6**	122.8	**377.5**	361.5
General and administrative expenses	**43.0**	53.1	**158.3**	120.0
Accretion of fair value adjustment to loss and loss adjustment expense reserves	**5.4**	6.6	**16.0**	18.2
Interest expense on debt	**19.8**	12.9	**54.9**	36.5
Interest expense - dividends on preferred stock subject to mandatory redemption	**7.1**	7.6	**22.2**	22.7
Interest expense - accretion on preferred stock subject to mandatory redemption	**9.2**	7.3	**26.2**	20.6
Total expenses	**963.9**	957.7	**3,032.5**	3,028.0
Pre-tax income	**191.5**	228.5	**499.6**	416.9
Income tax provision	**(64.3)**	(69.3)	**(151.3)**	(66.9)
Income before minority interest and equity in earnings of unconsolidated affiliates	**127.2**	159.2	**348.3**	350.0
Minority interest	**(24.0)**	(2.7)	**(69.4)**	(5.5)
Equity in earnings of unconsolidated affiliates	**8.2**	5.6	**27.3**	29.4
Net income	**111.4**	162.1	**306.2**	373.9
Change in net unrealized gains and losses for investments held	**43.1**	151.8	**83.3**	55.6
Change in foreign currency translation and other	**24.4**	1.0	**38.5**	33.9
Recognition of net unrealized gains and losses for investments sold	**(2.8)**	(39.2)	**(93.0)**	(114.6)
Comprehensive net income	**$ 176.1**	$ 275.7	**$ 335.0**	$ 348.8
Basic earnings per share	**$ 10.33**	$ 15.05	**$ 28.40**	$ 34.72
Diluted earnings per share	**10.32**	15.01	**28.35**	34.61
Dividends declared and paid per common share	**$ 2.00**	$ 2.00	**$ 6.00**	$ 6.00

See Notes to Consolidated Financial Statements

WHITE MOUNTAINS INSURANCE GROUP, LTD.

CONSOLIDATED STATEMENTS OF COMMON SHAREHOLDERS EQUITY

Unaudited

(Millions)	Common shareholders equity	Common shares and paid-in surplus	Retained earnings	Accum. other comprehensive income, after-tax	Unearned compensation
Balances at January 1, 2007	$ 4,455.3	$ 1,727.5	$ 2,496.0	$ 231.8	$
Cumulative effect adjustment - taxes (FIN 48)	.2		.2		
Net income	306.2		306.2		
Other comprehensive income, after-tax	28.8			28.8	
Dividends declared on common shares	(65.1)		(65.1)		
Issuances of common shares	1.8	1.8			
Repurchases and retirements of common shares	(2.5)	(2.5)			
Amortization of restricted share and option awards	7.9	7.9			
Balances at September 30, 2007	**$ 4,732.6**	**$ 1,734.7**	**$ 2,737.3**	**$ 260.6**	**$**

(Millions)	Common shareholders equity	Common shares and paid-in surplus	Retained earnings	Accum. other comprehensive income, after-tax	Unearned compensation
Balances at January 1, 2006	$ 3,833.2	$ 1,727.2	$ 1,899.8	$ 208.1	$ (1.9)
Net income	373.9		373.9		
Other comprehensive income, after-tax	(25.1)			(25.1)	
Cumulative effect adjustment - hybrid instruments (FAS 155)			9.2	(9.2)	
Cumulative effect adjustment - share-based compensation (FAS 123R)		(1.9)			1.9
Dividends declared on common shares	(64.7)		(64.7)		
Issuances of common shares	.1	.1			
Amortization of restricted share and option awards	1.3	1.3			
Balances at September 30, 2006	**$ 4,118.7**	**$ 1,726.7**	**$ 2,218.2**	**$ 173.8**	**$**

See Notes to Consolidated Financial Statements

WHITE MOUNTAINS INSURANCE GROUP, LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited

(Millions)	Nine Months Ended September 30, 2007	2006
Cash flows from operations:		
Net income	$ **306.2**	$ 373.9
Charges (credits) to reconcile net income to net cash used for operations:		
Net realized investment gains	**(192.9)**	(202.8)
Minority interest	**69.4**	5.5
Other operating items:		
Net change in loss and loss adjustment expense reserves	**(572.1)**	(833.7)
Net change in reinsurance recoverable on paid and unpaid losses	**544.5**	519.5
Net change in unearned insurance and reinsurance premiums	**136.6**	168.2
Net change in funds held by ceding companies	**110.1**	157.5
Net change in deferred acquisition costs	**(34.0)**	(50.0)
Net change in ceded unearned premiums	**(38.7)**	65.1
Net change in funds held under reinsurance treaties	**(42.4)**	(49.9)
Net change in insurance and reinsurance premiums receivable	**(45.1)**	16.0
Net change in other assets and liabilities, net	**(78.9)**	(108.2)
Net cash provided from operations	**162.7**	61.1
Cash flows from investing activities:		
Net change in short-term investments	**(267.7)**	(472.4)
Sales of fixed maturity investments	**3,940.6**	3,398.4
Maturities, calls and paydowns of fixed maturity investments	**980.2**	613.4
Maturities of trust account investments	**33.8**	
Sales of common equity securities	**365.9**	557.7
Sales of other investments	**120.6**	49.9
Purchases of other investments	**(47.1)**	(80.6)
Sales of consolidated affiliates, net of cash sold	**47.2**	121.1
Sale of Agri renewal rights		32.0
Purchases of common equity securities	**(622.4)**	(435.8)
Purchases of fixed maturity investments	**(4,823.1)**	(3,671.6)
Purchases of unconsolidated affiliates	**(51.6)**	
Sale of shares of OneBeacon Ltd.	**16.7**	
Net change in unsettled investment purchases and sales	**5.5**	(72.2)
Net acquisitions of property and equipment	**(19.9)**	(11.9)
Net cash (used for) provided from investing activities	**(321.3)**	28.0
Cash flows from financing activities:		
Issuance of WMRe Group Preference Shares, net of issuance costs	**246.6**	
Issuance of debt	**394.4**	65.0
Repayment of debt	**(322.0)**	(50.0)
Redemption of mandatorily redeemable preferred stock	**(20.0)**	
Interest rate swap agreements	**(2.4)**	
Cash dividends paid to the Company s common shareholders	**(65.1)**	(64.7)
Cash dividends paid to OneBeacon Ltd. s minority common shareholders	**(17.8)**	
Cash dividends paid to preferred shareholders	**(22.2)**	(22.7)
Cash dividends paid on WMRe Group Preference Shares	**(1.9)**	
OneBeacon Ltd. common shares repurchased and retired	**(5.8)**	
Common shares repurchased	**(2.5)**	
Proceeds from option exercises	**1.8**	.1
Net cash provided from (used for) financing activities	**183.1**	(72.3)

Effect of exchange rate changes on cash		**2.1**		5.8
Net increase in cash during the period		**26.6**		22.6
Cash balances at beginning of period		**159.0**		187.7
Cash balances at end of period	**$**	**185.6**	$	210.3
Supplemental cash flows information:				
Interest paid	**$**	**(30.0)**	$	(23.9)
Net Federal income taxes (paid) received		**(81.7)**		17.5

See Notes to Consolidated Financial Statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. Summary of Significant Accounting Policies

Basis of presentation

These interim consolidated financial statements include the accounts of White Mountains Insurance Group, Ltd. (the Company or the Registrant) and its subsidiaries (collectively with the Company, White Mountains) and have been prepared in accordance with generally accepted accounting principles in the United States (GAAP). The Company is an exempted Bermuda limited liability company whose principal businesses are conducted through its property and casualty insurance and reinsurance subsidiaries and affiliates. The Company s headquarters are located at Bank of Butterfield Building, 42 Reid Street, Hamilton, Bermuda HM 12, its principal executive office is located at 80 South Main Street, Hanover, New Hampshire 03755-2053 and its registered office is located at Clarendon House, 2 Church Street, Hamilton, Bermuda HM 11. White Mountains reportable segments are OneBeacon, White Mountains Re, Esurance and Other Operations. Significant transactions among White Mountains segments have been eliminated in this report.

The OneBeacon segment consists of OneBeacon Insurance Group, Ltd. (OneBeacon Ltd.), an exempted Bermuda limited liability company that owns a family of U.S.-based property and casualty insurance companies (collectively OneBeacon), substantially all of which operate in a multi-company pool. OneBeacon offers a wide range of specialty, personal and commercial products and services sold primarily through select independent agents and brokers. OneBeacon was acquired by White Mountains in 2001 (the OneBeacon Acquisition). During the fourth quarter of 2006, White Mountains sold 27.6 million, or 27.6%, of OneBeacon Ltd. s common shares in an initial public offering (the OneBeacon Offering). In connection with the OneBeacon Offering, White Mountains undertook an internal reorganization (the Reorganization) and formed OneBeacon Ltd. for the purpose of holding certain of its property and casualty insurance businesses. As a result of the Reorganization, certain of White Mountains businesses that had been historically reported as part of its Other Operations segment are now owned by OneBeacon Ltd., and accordingly have been included in the OneBeacon segment for all periods presented in this report. In addition, certain other businesses of White Mountains that had been historically reported as part of its OneBeacon segment and which were not held by OneBeacon Ltd. following the OneBeacon Offering are included in the Other Operations segment for all periods presented in this report.

The White Mountains Re segment consists of White Mountains Re Ltd., an exempted Bermuda limited liability company, and its subsidiaries (collectively, White Mountains Re). White Mountains Re offers reinsurance capacity for property, liability, accident & health, aviation and certain other exposures on a worldwide basis through its subsidiaries, Folksamerica Reinsurance Company (Folksamerica Re , together with its immediate parent, Folksamerica Holding Company (Folksamerica Holdings), Folksamerica), Sirius International Insurance Corporation (Sirius International) and Fund American Reinsurance Company, Ltd. (FARe). White Mountains Re also provides reinsurance advisory services, specializing primarily in property and other short-tailed lines of reinsurance, through White Mountains Re Underwriting Services Ltd. (WMRUS). On August 3, 2006, White Mountains Re sold one of its subsidiaries, Sirius America Insurance Company (Sirius America), to an investor group. As part of the transaction, White Mountains acquired an equity interest of approximately 18% in the acquiring entity, Lightyear Delos Acquisition Corp. (Delos), and accounts for Delos on the equity method within its Other Operations segment.

The Esurance segment consists of Esurance Holdings, Inc., and its subsidiaries (collectively, Esurance). Esurance sells personal auto insurance directly to customers online and through select online agents.

White Mountains Other Operations segment consists of the Company and its intermediate holding companies, its wholly-owned investment management subsidiary, White Mountains Advisors LLC (WM Advisors), its weather risk management business (Galileo), its variable annuity reinsurance business, White Mountains Life Reinsurance (Bermuda) Ltd. (WM Life Re), as well as the International American Group, Inc. (the International American Group) and various other entities not included in other segments. The International American Group, which was acquired by White Mountains in 1999, includes American Centennial Insurance Company (American Centennial) and British Insurance Company of Cayman (British Insurance Company), both of which are in run-off. The Other Operations segment also includes White Mountains investments in common shares and warrants to purchase common shares of Symetra Financial Corporation (Symetra), the consolidated results of the Tuckerman Capital, LP and Tuckerman Capital II, LP funds (Tuckerman Funds), common and preferred shares of Delos and warrants to purchase common shares of Montpelier Re Holdings, Ltd. (Montpelier Re), which White Mountains sold back to Montpelier Re on May 1, 2007.

All significant intercompany transactions have been eliminated in consolidation. These interim financial statements include all adjustments considered necessary by management to fairly present the financial position, results of operations and cash flows of White Mountains and are of a normal recurring nature. These interim financial statements may not be indicative of financial results for the full year and should be read in conjunction with the Company s 2006 Annual Report on Form 10-K. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Refer to the Company s 2006 Annual Report on Form 10-K for a complete discussion regarding White Mountains significant accounting policies.

Minority Interest

Minority interests consist of the ownership interests of noncontrolling shareholders in consolidated subsidiaries, and are presented separately on the balance sheet. The portion of income attributable to minority interests is presented net of related income taxes in the statement of income and comprehensive income. The change in unrealized investment gains, foreign currency translation and the change in the fair value of the interest rate swap to hedge OneBeacon s exposure to variability in the interest rate on its mortgage note are presented in accumulated other comprehensive income net of the minority interest portion. The percentage of the noncontrolling shareholders ownership interest in OneBeacon Ltd. at September 30, 2007 and December 31, 2006 was 28.1% and 27.6%.

White Mountains began to present minority interest subsequent to the OneBeacon Offering. The portion of income attributable to minority interest in certain limited partnership investments has been reclassified to conform with the presentation of the minority interest in OneBeacon Ltd.

On May 24, 2007, White Mountains Re Group, Ltd. (WMRe Group), an intermediate holding company of White Mountains Re, issued $250 million non-cumulative perpetual preference shares (the Preference Shares) (See Note 2). The Preference Shares and dividends thereon are included in minority interest on the balance sheet and as minority interest expense on the statement of income and comprehensive income, respectively.

Recently Adopted Changes in Accounting Principles

Federal, State and Foreign Income Taxes

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

On January 1, 2007 White Mountains adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 prescribes when the impact of a given tax position should be recognized and how it should be measured. Under the new guidance, recognition is based upon whether or not a company determines that it is more likely than not that a tax position will be sustained upon examination based upon the technical merits of the position. In evaluating the more-likely-than-not recognition threshold, White Mountains must presume that the tax position will be subject to examination by a taxing authority with full knowledge of all relevant information. If the recognition threshold is met, then the tax position is measured at the largest amount of benefit that is more than 50% likely of being realized upon ultimate settlement.

FIN 48 also addresses how interest and penalties should be accrued for uncertain tax positions, requiring that interest expense should be recognized in the first period interest would be accrued under the tax law. White Mountains classifies all interest and penalties on unrecognized tax benefits as part of income tax expense. At January 1, 2007, White Mountains had accrued interest and penalties of $3.8 million, net of federal benefit. In connection with the adoption of FIN 48, White Mountains recognized a $.2 million decrease in the liability for unrecognized tax benefits, primarily as a result of reductions in its estimates of accrued interest. The effect of adoption has been recorded as an adjustment to opening retained earnings.

At January 1, 2007, White Mountains had $70.6 million of unrecognized tax benefits. If recognized, $60.3 million would increase net income and reduce the effective tax rate. The remaining $10.3 million of unrecognized tax benefits relate to tax positions for which ultimate deductibility is highly certain but the timing of deductibility is uncertain. Recognition of these tax benefits, other than any applicable interest and penalties, would not affect the effective tax rate. There have been no material changes to these balances since adoption.

With few exceptions, White Mountains is no longer subject to U.S. federal, state or non-U.S. income tax examinations by tax authorities for years before 2003. The Internal Revenue Service (IRS) commenced an examination of White Mountains U.S. income tax returns for 2003 and 2004 in the second quarter of 2006 that is anticipated to be completed by the end of 2008. As of September 30, 2007, the IRS has not proposed any significant adjustments to taxable income. White Mountains does not expect the IRS to propose any adjustments that would result in a material change to its financial position.

As of September 30, 2007, White Mountains does not anticipate any significant changes to its total unrecognized tax benefits within the next twelve months.

Recent Accounting Pronouncements

Fair Value Measurements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (FAS 157). The Statement provides a revised definition of fair value and guidance on the methods used to measure fair value. The Statement also expands financial statement disclosure requirements for fair value information. The Statement establishes a fair value hierarchy that distinguishes between assumptions based on market data from independent sources (observable inputs) and a reporting entity s internal assumptions based upon the best information available when external market data is limited or unavailable (unobservable inputs). The fair value hierarchy in FAS 157 prioritizes inputs within three levels. Quoted prices in active markets have the highest priority (Level 1) followed by observable inputs other than quoted prices (Level 2) with unobservable inputs having the lowest priority (Level 3). The guidance in FAS 157 is applicable to derivatives as well as other financial instruments measured at fair value and nullifies the guidance that provided for the deferral of gains at the date of initial measurement. The Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. White Mountains has not yet determined the effect of adoption on its financial condition, results of operations or cash flows.

Fair Value Option

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (FAS 159). The Statement allows companies to make an election, on an individual instrument basis, to report financial assets and liabilities at fair value. The election must be made at the inception of a transaction and may not be reversed. The election may also be made for existing financial assets and liabilities at the time of adoption. Unrealized gains and losses on assets or liabilities for which the fair value option has been elected are to be reported in earnings. The Statement requires additional disclosures for instruments for which the election has been made, including a description of management s reasons for making the election. The Statement is effective as of fiscal years beginning after November 15, 2007 and is to be adopted prospectively and concurrently with the adoption of FAS 157. White Mountains has not yet determined the effect of adoption on its financial condition, results of operations or cash flows.

Note 2. Significant Transactions

Preference Shares

On May 24, 2007, WMRe Group issued 250,000 non-cumulative perpetual preference shares with a $1,000 per share liquidation preference. Proceeds of $245.7 million, net of $4.3 million of issuance costs and commissions, were received from the issuance. Holders of the Preference Shares receive dividends on a non-cumulative basis when and if declared by WMRe Group. The holders of the Preference Shares have the right to elect two directors to WMRe Group s board in the event of non-payment of dividends for six quarterly dividend periods. The right ceases upon the payment of dividends for four quarterly periods or the redemption of the Preference Shares. In addition, WMRe Group may not declare or pay dividends on its common shares unless it is current on its most recent dividend period. The dividend rate is fixed at an annual rate of 7.506% until June 30, 2017. After June 30, 2017, the dividend rate will be paid at a floating annual rate, equal to the greater of 3 month LIBOR plus 3.20% or 7.506%. The Preference Shares are redeemable solely at the discretion of WMRe Group on or after June 30, 2017 at their liquidation preference, plus any declared but unpaid dividends. Prior to June 30, 2017, WMRe Group may elect to redeem the Preference Shares at an amount equal to the greater of 1) the aggregate liquidation preference of the shares to be redeemed and 2) the sum of the present values of the aggregate liquidation preference of the shares to be redeemed and the remaining scheduled dividend payments on the shares to be redeemed (excluding June 30, 2017), discounted to the redemption date on a semi-annual basis at a rate equal to the rate on a comparable treasury issue, plus 45 basis points. In the event of liquidation of WMRe Group, the holders of the Preference Shares would have preference over the common shareholders and would receive a distribution equal to the liquidation preference per share, subject to availability of funds.

Note 3. Loss and Loss Adjustment Expense Reserves

The following table summarizes the loss and loss adjustment expense (LAE) reserve activities of White Mountains insurance subsidiaries for the three and nine months ended September 30, 2007 and 2006:

Millions	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Gross beginning balance	**$ 8,364.7**	$ 9,775.3	**$ 8,777.2**	$ 10,231.2
Less beginning reinsurance recoverable on unpaid losses	**(3,693.2)**	(4,664.2)	**(4,015.7)**	(5,025.7)
Net loss and LAE reserves	**4,671.5**	5,111.1	**4,761.5**	5,205.5
Loss and LAE reserves sold - Sirius America		(124.1)		(124.1)
Loss and LAE incurred relating to:				
Current year losses	**592.8**	529.2	**1,850.7**	1,652.1
Prior year losses	**(.9)**	28.9	**(53.4)**	233.8
Total incurred losses and LAE	**591.9**	558.1	**1,797.3**	1,885.9
Net change in loss reserves - Sierra Insurance Group (1)	**(9.0)**		**(9.0)**	
Accretion of fair value adjustment to loss and LAE reserves	**5.4**	6.6	**16.0**	18.2
Foreign currency translation adjustment to loss and LAE reserves	**24.1**	3.1	**31.3**	23.0
Loss and LAE paid relating to:				
Current year losses	**(304.2)**	(229.2)	**(685.5)**	(600.2)
Prior year losses	**(312.3)**	(461.7)	**(1,244.2)**	(1,544.4)
Total loss and LAE payments	**(616.5)**	(690.9)	**(1,929.7)**	(2,144.6)
Net ending balance	**4,667.4**	4,863.9	**4,667.4**	4,863.9
Plus ending reinsurance recoverable on unpaid losses	**3,581.9**	4,250.3	**3,581.9**	4,250.3
Gross ending balance	**$ 8,249.3**	$ 9,114.2	**$ 8,249.3**	$ 9,114.2

(1) During the three months ended September 30, 2007, White Mountains Re recorded a $9.0 million decrease on its workers compensation loss reserves relating to its Sierra Insurance Group acquisition, which was offset dollar-for-dollar by an increase in the principal amount of the Sierra Note that White Mountains Re issued as part of that acquisition (See Note 6).

White Mountains experienced $.9 million and $53.4 million of net favorable development on prior accident year loss reserves during the three and nine months ended September 30, 2007. For the three months ended September 30, 2007, OneBeacon had net favorable development of $16.5 million that was offset primarily by $15.0 million of net unfavorable development at Esurance. For the nine months ended September 30, 2007, OneBeacon, White Mountains Re, and Other Operations had net favorable development of $41.2 million, $25.1 million and $10.5 million, respectively, offset by $23.4 million of net unfavorable development at Esurance. OneBeacon s net favorable development in 2007 that primarily related to professional liability and tuition reimbursement in specialty lines, property and general liability in commercial lines and automobile liability in traditional personal lines and at AutoOne. Esurance experienced net unfavorable development in 2007 that primarily related to bodily injury claims from prior accident years. Net favorable development at White Mountains Re in 2007 primarily related to property lines. The Other Operations segment experienced $10.5 million of favorable development during 2007 primarily due to the settlement of a large claim at British Insurance Company.

White Mountains experienced $28.9 million of net unfavorable development on prior accident year loss reserves during the three months ended September 30, 2006, primarily due to $9.4 million of adverse development at OneBeacon, which mostly related to prior year catastrophe losses, and $12.0 million of adverse development at Folksamerica Re on business assumed through a prior acquisition. White Mountains experienced $233.8 million of net unfavorable development on prior accident year loss reserves during the nine months ended September 30, 2006, which in addition to the items listed above, primarily related to hurricanes Katrina, Rita and Wilma.

In connection with purchase accounting for the acquisitions of OneBeacon, Sirius International and Stockbridge Insurance Company, White Mountains was required to adjust loss and LAE reserves and the related reinsurance recoverables to fair value on their respective acquired balance sheets. The net reduction to loss and LAE reserves is being recognized through an income statement charge ratably with and over the period the claims are settled. Accordingly, White Mountains recognized $5.4 million and $16.0 million of such charges for the three and nine months ended September 30, 2007, respectively, and $6.6 million and $18.2 million of such charges for the three and nine months ended September 30, 2006, respectively.

Note 4. Third Party Reinsurance

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

OneBeacon

At September 30, 2007, OneBeacon had $20.6 million of reinsurance recoverables on paid losses and $2,924.7 million (gross of $225.1 million in purchase accounting adjustments) that will become recoverable if claims are paid in accordance with current reserve estimates. The collectibility of balances due from OneBeacon s reinsurers is critical to OneBeacon s financial strength because reinsurance contracts do not relieve OneBeacon of its primary obligation to its policyholders. OneBeacon is selective with its reinsurers, placing reinsurance with only those reinsurers having a strong financial condition. OneBeacon monitors the financial strength of its reinsurers on an ongoing basis. As a result, uncollectible amounts have historically not been significant. The following table provides a listing of OneBeacon s top reinsurers, excluding industry pools and associations, based upon recoverable amounts, the percentage of total reinsurance recoverables and the reinsurer s A.M. Best rating.

Top Reinsurers (Millions)		**Balance at September 30, 2007**	**% of Total**	**A.M. Best Rating (1)**
Subsidiaries of Berkshire (NICO and GRC) (2)	$	2,107.3	78%	A++
Nichido (formerly Tokio Fire and Marine Insurance Company)				