MARKEL CORP
Form 10-K
February 28, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
Annual report pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934 for the fiscal year ended December 31, 2012
Commission File Number 001-15811
MARKEL CORPORATION
(Exact name of registrant as specified in its charter)
A Virginia Corporation
IRS Employer Identification No. 54-1959284
4521 Highwoods Parkway, Glen Allen, Virginia 23060-6148
(Address of principal executive offices) (Zip code)
Registrant's telephone number, including area code: (804) 747-0136
Securities registered pursuant to Section 12(b) of the Act:
Common Stock, no par value
New York Stock Exchange, Inc.
(title of each class and name of the exchange on which registered)
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 whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ 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
The aggregate market value of the shares of the registrant's Common Stock held by non-affiliates as of June 30, 2012 was approximately $4,003,000,000.
The number of shares of the registrant's Common Stock outstanding at February 11, 2013: 9,630,012.
Documents Incorporated By Reference
The portions of the registrant's Proxy Statement for the Annual Meeting of Shareholders scheduled to be held on May 13, 2013, referred to in Part III.

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BUSINESS OVERVIEW

We are a diverse financial holding company serving a variety of niche markets. Our principal business markets and underwrites specialty insurance products. We believe that our specialty product focus and niche market strategy enable us to develop expertise and specialized market knowledge. We seek to differentiate ourselves from competitors by our expertise, service, continuity and other value-based considerations. We compete in three segments of the specialty insurance marketplace: the Excess and Surplus Lines, the Specialty Admitted and the London Insurance Market segments. We also own interests in various industrial and service businesses that operate outside of the specialty insurance marketplace. Our financial goals are to earn consistent underwriting and operating profits and superior investment returns to build shareholder value.

Specialty Insurance

The specialty insurance market differs significantly from the standard market. In the standard market, insurance rates and forms are highly regulated, products and coverages are largely uniform with relatively predictable exposures and companies tend to compete for customers on the basis of price. In contrast, the specialty market provides coverage for hard-to-place risks that generally do not fit the underwriting criteria of standard carriers. For example, United States insurance regulations generally require an excess and surplus lines (E&S) account to be declined by admitted carriers before an E&S company may write the business. Hard-to-place risks written in the specialty admitted market cover insureds engaged in similar, but highly specialized activities who require a total insurance program not otherwise available from standard insurers or insurance products that are overlooked by large admitted carriers. Hard-to-place risks in the London market are generally distinguishable from standard risks due to the complexity or significant size of the risk.

Competition in the specialty insurance market tends to focus less on price than in the standard insurance market and more on other value-based considerations, such as availability, service and expertise. While specialty market exposures may have higher perceived insurance risks than their standard market counterparts, we seek to manage these risks to achieve higher financial returns. To reach our financial and operational goals, we must have extensive knowledge and expertise in our chosen markets. Many of our accounts are considered on an individual basis where customized forms and tailored solutions are employed.

By focusing on the distinctive risk characteristics of our insureds, we have been able to identify a variety of niche markets where we can add value with our specialty product offerings. Examples of niche markets that we have targeted include wind and earthquake-exposed commercial properties, liability coverage for highly specialized professionals, equine-related risks, workers' compensation insurance for small businesses, yachts and other watercraft, motorcycles and marine, energy and environmental-related activities. Our market strategy in each of these areas of specialization is tailored to the unique nature of the loss exposure, coverage and services required by insureds. In each of our niche markets, we assign teams of experienced underwriters and claims specialists who provide a full range of insurance services.

Markets

The E&S market focuses on hard-to-place risks and loss exposures that generally cannot be written in the standard market. E&S eligibility allows our insurance subsidiaries to underwrite unique loss exposures with more flexible policy forms and unregulated premium rates. This typically results in coverages that are more restrictive and more expensive than coverages in the standard market.

In 2011, the E&S market represented approximately $31 billion, or 6%, of the approximately $502 billion United States property and casualty (P&C) industry.[(1)] We are the seventh largest E&S writer in the United States as measured by direct premium writings.[(1)] In 2012, we wrote $956 million of business in our Excess and Surplus Lines segment.

(1) U.S. Surplus Lines Market Review Special Report, A.M. Best (October 1, 2012).

We also write business in the United States specialty admitted market. Most of these risks, although unique and hard-to-place in the standard market, must remain with an admitted insurance company for marketing and regulatory reasons. The specialty admitted market is subject to more state regulation than the E&S market, particularly with regard to rate and form filing requirements, restrictions on the ability to exit lines of business, premium tax payments and membership in various state associations, such as state guaranty funds and assigned risk plans. In 2012, we wrote $670 million of business in our Specialty Admitted segment.

The London market, which produced approximately $67 billion of gross written premium in 2011, is the largest insurance market in Europe and third largest in the world.[(2)] The London market is known for its ability to provide innovative, tailored coverage and capacity for unique and hard-to-place risks. It is primarily a broker market, which means that insurance brokers bring most of the business to the market. The London market is also largely a subscription market, which means that loss exposures brought into the market are typically insured by more than one insurance company or Lloyd's syndicate, often due to the high limits of insurance coverage required. We write business on both a direct and subscription basis in the London market. When we write business in the subscription market, we prefer to participate as lead underwriter in order to control underwriting terms, policy conditions and claims handling.

In 2011, gross premium written through Lloyd's syndicates generated approximately half of the London market's international insurance business,[(2)] making Lloyd's the world's largest commercial surplus lines insurer[(1)]and fifth largest reinsurer.[(4)] Corporate capital providers often provide a majority of a syndicate's capacity and also generally own or control the syndicate's managing agent. This structure permits the capital provider to exert greater influence on, and demand greater accountability for, underwriting results. In 2011, corporate capital providers accounted for approximately 88% of total underwriting capacity in Lloyd's.[(3)]

We participate in the London market through Markel International, which includes Markel Capital Limited (Markel Capital) and Markel International Insurance Company Limited (MIICL). Markel Capital is the corporate capital provider for our syndicate at Lloyd's, Markel Syndicate 3000, which is managed by Markel Syndicate Management Limited. In 2012, we wrote $888 million of business in our London Insurance Market segment.

In 2012, 30% of consolidated premium writings related to foreign risks (i.e., coverage for risks located outside of the United States), of which 20% were from the United Kingdom and 16% were from Canada. In 2011, 31% of our premium writings related to foreign risks, of which 20% were from the United Kingdom and 18% were from Canada. In 2010, 28% of our premium writings related to foreign risks, of which 25% were from the United Kingdom and 17% were from Canada. In each of these years, there were no other individual foreign countries from which premium writings were material. Premium writings are attributed to individual countries based upon location of risk.

Competition

We compete with numerous domestic and international insurance companies and reinsurers, Lloyd's syndicates, risk retention groups, insurance buying groups, risk securitization programs and alternative self-insurance mechanisms. Competition may take the form of lower prices, broader coverages, greater product flexibility, higher quality services or higher ratings by independent rating agencies. In all of our markets, we compete by developing specialty products to satisfy well-defined market needs and by maintaining relationships with agents, brokers and insureds who rely on our expertise. This expertise is our principal means of competing. We offer over 100 product lines. Each of these products has its own distinct competitive environment. With each of our products, we seek to compete with innovative ideas, appropriate pricing, expense control and quality service to policyholders, agents and brokers.

(1) U.S. Surplus Lines Market Review Special Report, A.M. Best (October 1, 2012).

(2) Insurance 2013, TheCityUK (January 2013).
(3) Lloyd's Annual Report 2011.
(4) Reinsurance/Capital Markets, Best's Review (September 2012).

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Few barriers exist to prevent insurers from entering our segments of the P&C industry. Market conditions and capital capacity influence the degree of competition at any point in time. Periods of intense competition, which typically include broader coverage terms, lower prices and excess underwriting capacity, are referred to as a "soft market." A favorable insurance market is commonly referred to as a "hard market" and is characterized by stricter coverage terms, higher prices and lower underwriting capacity. During soft markets, unfavorable conditions exist due in part to what many perceive as excessive amounts of capital in the industry. In an attempt to use their capital, many insurance companies seek to write additional premiums without appropriate regard for ultimate profitability, and standard insurance companies are more willing to write specialty coverages. The opposite is typically true during hard markets.

The Insurance Market Cycle

Since 2005, we have generally been in a soft insurance market and have experienced intense competition, resulting in price deterioration in virtually all of our product areas due in part to an increased presence of standard insurance companies in our markets. During 2008, given the rapid deterioration in underwriting capacity as a result of the disruptions in the financial markets and losses from catastrophes, the rate of decline in prices began to slow. However, the effects of the economic environment contributed to further declines in gross premium volume in 2009 and 2010. Premiums for many of our product lines are based upon our insureds' revenues, gross receipts or payroll, which were negatively impacted by the depressed levels of business activity in recent years. In 2010, we continued to experience pricing pressure due in part to intense competition, which resulted in further price deterioration across many of our product lines, most notably our professional and products liability programs within the Excess and Surplus Lines segment. However, we experienced moderate price increases in several product lines during 2010, most notably those offered within the London Insurance Market segment. During 2011, the unfavorable pricing trends noted in 2010 continued for some of our product lines, most notably our professional and products liability programs within the Excess and Surplus Lines segment. However, price declines stabilized for most of our product lines during 2011, and we achieved moderate price increases in several lines, most notably the marine and energy products within the London Insurance Market segment. During 2012, market conditions have improved and we have generally seen mid-single digit favorable rate changes across our portfolio. Gross premium volume has further improved as revenues, gross receipts and payrolls of our insureds have been favorably impacted by improved economic conditions.

We routinely review the pricing of our major product lines and will continue to pursue price increases for most product lines in 2013; however, when we believe the prevailing market price will not support our underwriting profit targets, the business is not written. As a result of our underwriting discipline, gross premium volume may vary when we alter our product offerings to maintain or improve underwriting profitability.

Underwriting Philosophy

By focusing on market niches where we have underwriting expertise, we seek to earn consistent underwriting profits. Underwriting profits are a key component of our strategy. We believe that the ability to achieve consistent underwriting profits demonstrates knowledge and expertise, commitment to superior customer service and the ability to manage insurance risk. We use underwriting profit or loss as a basis for evaluating our underwriting performance.

The combined ratio is a measure of underwriting performance and represents the relationship of incurred losses, loss adjustment expenses and underwriting, acquisition and insurance expenses to earned premiums. A combined ratio less than 100% indicates an underwriting profit, while a combined ratio greater than 100% reflects an underwriting loss. In 2012, our combined ratio was 97%. See Management's Discussion & Analysis of Financial Condition and Results of

Operations for further discussion of our underwriting results.

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The following graph compares our combined ratio to the P&C industry's combined ratio for the past five years.

Underwriting Segments

We define our underwriting segments based on the areas of the specialty insurance market in which we compete, the excess and surplus lines, specialty admitted and London markets. See note 17 of the notes to consolidated financial statements for additional segment reporting disclosures.

For purposes of segment reporting, our Other Insurance (Discontinued Lines) segment includes lines of business that have been discontinued in conjunction with acquisitions. The lines were discontinued because we believed some aspect of the product, such as risk profile or competitive environment, would not allow us to earn consistent underwriting profits.

Markel Corporation
2012 Consolidated Gross Premium Volume ($2.5 billion)

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Excess and Surplus Lines Segment

Our Excess and Surplus Lines segment reported gross premium volume of $956.3 million, earned premiums of $793.2 million and an underwriting profit of $50.1 million in 2012.

Business in the Excess and Surplus Lines segment is written through two distribution channels, professional surplus lines general agents who have limited quoting and binding authority and wholesale brokers. The majority of the business produced by this segment is written on a surplus lines basis through either Essex Insurance Company, which is domiciled in Delaware, or Evanston Insurance Company, which is domiciled in Illinois.

The Excess and Surplus Lines segment is comprised of five regions, and each regional underwriting office is responsible for serving the wholesale producers located in its region. Our regional teams focus on customer service and marketing, underwriting and distributing our insurance solutions and provide customers easy access to our products.

In the Excess and Surplus Lines segment, we wrote business through the following regional underwriting offices during 2012:

- Markel Northeast (Red Bank, NJ)
- Markel Southeast (Glen Allen, VA)
- Markel Midwest (Deerfield, IL)
- Markel Mid South (Plano, TX)
- Markel West (Woodland Hills, CA and Scottsdale, AZ)

We also have a product line leadership group that has primary responsibility for both developing and maintaining underwriting and pricing guidelines on our existing products and new product development. The product line leadership group also delegates underwriting authority to the regional underwriters to ensure that the products needed by our customers are available through the regional offices and provides underwriting training and development so that our regional underwriting teams have the expertise to underwrite the risk or to refer risks to our product line experts as needed. The product line leadership group is under the direction of our Chief Underwriting Officer, who also is ultimately responsible for the underwriting activities of our Specialty Admitted and London Insurance Market segments.

Excess and Surplus Lines Segment
2012 Gross Premium Volume ($956 million)

Product offerings within the Excess and Surplus Lines segment fall within the following major product groupings:

- Property and Casualty
- Professional Liability
- Other Product Lines

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Property coverages consist principally of fire, allied lines (including windstorm, hail and water damage) and other specialized property coverages, including catastrophe-exposed property risks such as earthquake and wind on both a primary and excess basis. Catastrophe-exposed property risks are typically larger and are lower frequency and higher severity in nature than more standard property risks. Our property risks range from small, single-location accounts to large, multi-state, multi-location accounts. Casualty product offerings include a variety of liability coverages targeting apartments and office buildings, retail stores, contractors and recreational and hospitality businesses. We also offer products liability coverages on either an occurrence or claims-made basis to manufacturers, distributors, importers and re-packagers of manufactured products.

Professional liability coverages include unique solutions for highly specialized professions, including architects and engineers, lawyers, agents and brokers, service technicians and computer consultants. We offer claims-made medical malpractice coverage for doctors, dentists and podiatrists; claims-made professional liability coverage to individual healthcare providers such as therapists, pharmacists, physician assistants and nurse anesthetists; and coverages for medical facilities and other allied healthcare risks such as clinics, laboratories, medical spas, home health agencies, small hospitals, pharmacies and nursing homes. This product line also includes for-profit and not-for profit management liability coverage which can be bundled or written mono-line and include employment practices liability, directors' and officers' liability and fiduciary liability coverages. Additionally, we offer a data privacy and security product, which provides coverage for data breach and privacy liability, data breach loss to insureds and electronic media coverage.

Other product lines within the Excess and Surplus Lines segment include:

- excess and umbrella products, which provide coverage over approved underlying insurance carriers on either an occurrence or claims-made basis;
- environmental products, which include environmental consultants' professional liability, contractors' pollution liability and site-specific environmental impairment liability coverages;
- transportation-related products, which provide auto physical damage coverage for high-value automobiles as well as all types of specialty commercial vehicles, dealers’ open lot and garagekeeper legal liability coverages, vehicular liability and physical damage coverages for local and intermediate haul commercial trucks and liability coverage to operators of non-emergency ambulances and multi-line specialty products designed for the unique characteristics of the garage industry;
- inland marine products, which provide a number of specialty coverages for risks such as motor truck cargo coverage for damage to third party cargo while in transit, warehouseman's legal liability coverage for damage to third party goods in storage, contractor's equipment coverage for first party property damage and builder's risk coverage;
- ocean marine products, which provide general liability, professional liability, property and cargo coverages for marine artisan contractors, boat dealers and marina owners including hull physical damage, protection and indemnity and third party property coverages for ocean cargo;
- casualty facultative reinsurance written for individual casualty risks focusing on general liability, products liability, automobile liability and certain classes of miscellaneous professional liability and targeting classes which include low frequency, high severity, short-tail general liability risks;
- railroad-related products, which provide first party coverages for short-line and regional railroads, scenic and tourist railroads, commuter and light rail trains and railroad equipment; and
- public entity insurance and reinsurance programs, which provide coverage for government entities including counties, municipalities, schools and community colleges.

In late 2012, we ceased writing coverage for taxicab fleets and third party railroad-related products.

Specialty Admitted Segment

Our Specialty Admitted segment reported gross premium volume of $669.7 million, earned premiums of $588.8 million and an underwriting loss of $46.8 million in 2012.

The majority of the business in the Specialty Admitted segment is written by retail insurance agents who have very limited underwriting authority. Agents are carefully selected and agency business is controlled through regular audits and pre-approvals. Certain products and programs are marketed directly to consumers or distributed through wholesale producers. Personal lines coverages included in this segment are marketed directly to the consumer using direct mail, internet and telephone promotions, as well as relationships with various motorcycle and boat manufacturers, dealers and associations.

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The majority of the business produced by this segment is written on an admitted basis either through Markel Insurance Company (MIC), which is domiciled in Illinois, Markel American Insurance Company (MAIC), which is domiciled in Virginia, or FirstComp Insurance Company (FCIC), which is domiciled in Nebraska. MIC and MAIC are licensed to write P&C insurance in all 50 states and the District of Columbia, while FCIC is currently licensed in 28 states and specializes in workers' compensation coverage.

In the Specialty Admitted market, we wrote business through the following underwriting units during 2012:

- Markel Specialty (Glen Allen, VA)
- Markel American Specialty Personal and Commercial Lines (Pewaukee, WI)
- Markel FirstComp (Omaha, NE)

The Markel Specialty unit focuses on providing total insurance programs for businesses engaged in highly specialized activities. These activities typically do not fit the risk profiles of standard insurers and make complete coverage difficult to obtain from a single insurer. The Markel Specialty unit is organized into product areas that concentrate on particular markets and customer groups including youth and recreation oriented organizations, social service organizations, amateur sports organizations and horse and farm operations. In January 2012, we acquired Thompson Insurance Enterprises, LLC, a privately held program administrator that underwrites multi-line, industry-focused insurance programs that complement the Markel Specialty product offerings. Examples include social service organizations, senior living, childcare and fitness centers.

The Markel American Specialty Personal and Commercial Lines unit offers its insurance products in niche markets and focuses its underwriting on marine, recreational vehicle, property and other personal and commercial line coverages. The products offered by this unit are characterized by high numbers of transactions, low average premiums and creative solutions for under-served and emerging markets.

The Markel FirstComp unit provides workers' compensation insurance and related services, principally to small businesses and distributes its products through independent insurance agencies, generally located in small towns, which have been underserved by other market participants because of their size. Using its proprietary technology platform, Markel FirstComp is able to service these small agencies in a cost-efficient manner. Through June 30, 2011, Markel FirstComp also acted as a managing general agent producing business for unaffiliated insurance companies.

Specialty Admitted Segment
2012 Gross Premium Volume ($670 million)

Product offerings within the Specialty Admitted segment fall within the following major product groupings:

- Workers' Compensation
- Property and Casualty
- Personal Lines
- Accident and Health
- Other Product Lines

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Workers' compensation products provide wage replacement and medical benefits to employees injured in the course of employment and target main-street, service and artisan contractor businesses, retail stores and restaurants.

Property and casualty products included in this segment are offered on a monoline or package basis and generally target specialized commercial markets and customer groups. Targeted groups include youth and recreation oriented organizations, social service organizations, museums and historic homes, performing arts organizations, bed and breakfast inns, outfitters and guides, hunting and fishing lodges, dude ranches and rod and gun clubs.

Personal lines products provide first and third party coverages for a variety of personal watercrafts including older boats, high performance boats and yachts, as well as for recreational vehicles including motorcycles, snowmobiles and ATVs. Additionally, property coverages are offered for mobile homes, dwellings and homeowners that do not qualify for standard homeowner's coverage. Other products offered include special event protection, supplemental natural disaster coverage, renters' protection coverage, excess flood coverage and collector vehicle coverage.

Accident and health products offer liability and accident insurance for amateur sports organizations, monoline accident and medical coverage for various niche markets, short-term medical insurance and pet health insurance. During 2012, we ceased writing coverage for certain accident and health products, including accident and medical insurance for academic institutions, stop-loss insurance for self-insured medical plans and medical excess reinsurance coverage.

Other product lines within the Specialty Admitted segment include:

- coverages for equine-related risks, such as horse mortality, theft, infertility, transit and specified perils, as well as property and liability coverages for farms and boarding, breeding and training facilities;
- first and third party coverages for auto repair garages, gas stations and convenience stores and used car dealers;
- general agent programs that use managing general agents to offer single source admitted and non-admitted programs for a specific class or line of business;
- first and third party coverages for small fishing ventures, charters, utility boats and boat rentals; and
- professional liability coverages that we design and administer on behalf of other insurance carriers and ultimately assume on a reinsurance basis.

London Insurance Market Segment

Our London Insurance Market segment reported gross premium volume of $887.7 million, earned premiums of $765.2 million and an underwriting profit of $81.6 million in 2012.

This segment is comprised of Markel International, which is headquartered in London, England. In addition to seven branch offices in the United Kingdom, Markel International has offices in Canada, Spain, Singapore, Sweden, Hong Kong, China, Germany and the Netherlands. Markel International writes specialty property, casualty, professional liability, equine, marine, energy and trade credit insurance on a direct and reinsurance basis. Business is written worldwide through either MIICL or Markel Syndicate 3000 with approximately 16% of writings coming from the United States.

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London Insurance Market Segment
2012 Gross Premium Volume ($888 million)

Product offerings within the London Insurance Market segment fall within the following major product groupings:

- Marine and Energy
- Professional and General Liability
- Reinsurance
- Property
- Other Product Lines

Marine and energy products include a portfolio of coverages for cargo, energy, hull, liability, war, terrorism and specie risks. The cargo account is an international transit-based book covering many types of cargo. Energy coverage includes all aspects of oil and gas activities. The hull account covers physical damage to ocean-going tonnage, yachts and mortgagee's interest. Liability coverage provides for a broad range of energy liabilities, as well as traditional marine exposures including charterers, terminal operators and ship repairers. The war account covers the hulls of ships and aircraft, and other related interests, against war and associated perils. Terrorism coverage provides for property damage and business interruption related to political violence including war and civil war. The specie account includes coverage for fine art on exhibition and in private collections, securities, bullion, precious metals, cash in transit and jewelry.

Professional and general liability products include professional indemnity, directors' and officers' liability, intellectual property, some miscellaneous defense costs, incidental commercial crime, general and products liability coverages targeting consultants, construction professionals, financial service professionals, professional practices, social welfare organizations and medical products. Professional and general liability products are written on a worldwide basis, limiting exposure in the United States.

Reinsurance products include property and casualty treaty reinsurance. Property treaty products are offered on an excess of loss and proportional basis for per risk and catastrophe exposures. A significant portion of the excess of loss catastrophe and per risk property treaty business comes from the United States with the remainder coming from international property treaties. Casualty treaty reinsurance is offered on an excess of loss basis and primarily targets specialist writers of motor products in the United Kingdom and Europe. Excess of loss casualty treaty reinsurance also is offered for select writers of employers' and products liability coverages.

Property products target a wide range of insureds, providing coverage ranging from fire to catastrophe perils such as earthquake and windstorm. Business is written primarily on an open market basis for direct and facultative risks targeting Fortune 1000 companies on a worldwide basis by our underwriters to London brokers, with each risk being considered on its own merits. We also provide property coverage for small to medium-sized commercial risks on both a stand-alone and package basis through our branch offices. During 2012, we ceased writing delegated property business, which was primarily written through coverholders in the United States.

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Other product lines within the London Insurance Market segment include:

- crime coverage primarily targeting financial institutions and providing protection for bankers' blanket bond, computer crime and commercial fidelity;
- contingency coverage including event cancellation, non-appearance and prize indemnity;
- accident and health coverage targeting affinity groups and schemes, high value and high risks accounts and sports groups;
- coverage for equine-related risks such as horse mortality, theft, infertility, transit and specified perils;
- specialty coverages include mortality risks for farms, zoos, animal theme parks and safari parks;
- short-term trade credit coverage for commercial risks, including insolvency and protracted default as well as political risks coverage in conjunction with commercial risks for currency inconvertibility, government action, import/export license cancellation, public buyer default and war; and
- products liability, excess and umbrella and environmental liability coverages targeted at Canadian domiciled insureds.

Recent Developments

In October 2012, we announced that we had entered into a definitive agreement to acquire Essentia Insurance Company from OneBeacon Insurance Group LLC. The transaction was completed effective January 1, 2013. Essentia Insurance Company will continue to underwrite insurance exclusively for Hagerty Insurance Agency and Hagerty Classic Marine Insurance Agency (collectively, Hagerty) throughout the United States. Hagerty offers insurance for classic cars, vintage boats, motorcycles and related automotive collectibles. Hagerty remains a privately-owned, family business. Premiums associated with this business for 2011 were in excess of $170 million. Results attributable to this acquisition will be included in the Specialty Admitted segment.

In December 2012, we, together with Alterra Capital Holdings Limited (Alterra), announced that our boards of directors had approved an agreement providing for the merger of Alterra with one of our subsidiaries. As a result of the transaction, Alterra would become our wholly-owned subsidiary and each issued and outstanding share of Alterra common stock (other than shares as to which appraisal rights are exercised and restricted shares that do not vest in connection with the transaction) would be converted into the right to receive (1) 0.04315 shares of our common stock and (2) $10.00 in cash. Based on our closing stock price on December 18, 2012, the day the agreement was entered into, the aggregate consideration payable to Alterra shareholders would be approximately $3.1 billion. Following the transaction, we estimate that our current shareholders would own approximately 69% of the combined company and Alterra shareholders would own approximately 31%. The transaction has been approved by shareholders of both companies, but remains subject to receipt of regulatory approvals. Closing is expected to occur in the first half of 2013.

Alterra is a Bermuda-headquartered, global enterprise dedicated to providing diversified specialty insurance and reinsurance products to corporations, public entities and property and casualty insurers. As of December 31, 2012, Alterra reported $10.7 billion in total assets and $2.8 billion in shareholders' equity. Its reported net income for 2012 was $143.8 million on $1.7 billion in total revenues.

We believe that our acquisition of Alterra will create a strong company in global specialty insurance and investments, with a demonstrated track record of underwriting discipline in niche market segments and proven asset management strengths that should benefit shareholders. Two individuals designated by Alterra and approved by the Nominating/Corporate Governance Committee of our Board of Directors will be added to our Board of Directors upon completion of the transaction. Our current executive officers will hold the same, or substantially similar, positions after the transaction, although individual responsibilities may change to reflect the nature of the combined operations. Roles for Alterra officers and management personnel (other than its chief executive officer who is expected to leave the company after the transaction) are being identified as part of a transition planning process.

Reinsurance

Reinsurance is used to manage our net retention on individual risks and overall exposure to losses while providing us with the ability to offer policies with sufficient limits to meet policyholder needs. As part of our underwriting philosophy, we seek to offer products with limits that do not require significant reinsurance. We purchase catastrophe reinsurance coverage for our catastrophe-exposed policies, and we seek to manage our exposures under this coverage so that no exposure to any one reinsurer is material to our ongoing business. Net retention of gross premium volume was 88% in 2012 and 89% in 2011. We do not purchase or sell finite reinsurance products or use other structures that would have the effect of discounting loss reserves.

The ceding of insurance does not legally discharge us from our primary liability for the full amount of the policies, and we will be required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance agreement. We attempt to minimize credit exposure to reinsurers through adherence to internal reinsurance guidelines. To become our reinsurance partner, prospective companies generally must: (i) maintain an A.M. Best Company (Best) or Standard & Poor's (S&P) rating of "A" (excellent) or better; (ii) maintain minimum capital and surplus of $500 million and (iii) provide collateral for recoverables in excess of an individually established amount. In addition, certain foreign reinsurers for our United States insurance operations must provide collateral equal to 100% of recoverables, with the exception of reinsurers who have been granted authorized status by an insurance company's state of domicile. Lloyd's syndicates generally must have a minimum of a "B" rating from Moody's Investors Service (Moody's) to be our reinsurers.

When appropriate, we pursue reinsurance commutations that involve the termination of ceded reinsurance contracts. Our commutation strategy related to ceded reinsurance contracts is to reduce credit exposure and eliminate administrative expenses associated with the run-off of reinsurance placed with certain reinsurers.

The following table displays balances recoverable from our ten largest reinsurers by group at December 31, 2012. The contractual obligations under reinsurance agreements are typically with individual subsidiaries of the group or syndicates at Lloyd's and are not typically guaranteed by other group members or syndicates at Lloyd's. These ten reinsurance groups represent approximately 74% of our $901.1 million reinsurance recoverable balance before considering allowances for bad debts.

Reinsurers	A.M. Best Rating	Reinsurance Recoverable (dollars in thousands)
Munich Re Group	A+	$159,033
Lloyd's of London	A	99,521
XL Capital Group	A	75,807
Fairfax Financial Group	A	69,431
Swiss Re Group	A+	61,399
HDI Group	A	46,970
Aspen (Bermuda) Group	A	46,354
W.R. Berkley Group	A+	39,984
ACE Group	A+	34,628
White Mountains Insurance Group	A	29,274
Reinsurance recoverable on paid and unpaid losses for ten largest reinsurers		662,401
Total reinsurance recoverable on paid and unpaid losses		$901,067

Reinsurance recoverable balances in the preceding table are shown before consideration of balances owed to reinsurers and any potential rights of offset, any collateral held by us and allowances for bad debts.

Reinsurance treaties are generally purchased on an annual basis and are subject to yearly renegotiations. In most circumstances, the reinsurer remains responsible for all business produced before termination. Treaties typically contain provisions concerning ceding commissions, required reports to reinsurers, responsibility for taxes, arbitration in the event of a dispute and provisions that allow us to demand that a reinsurer post letters of credit or assets as security if a reinsurer becomes an unauthorized reinsurer under applicable regulations or if its rating falls below an acceptable level.

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See note 13 of the notes to consolidated financial statements and Management's Discussion & Analysis of Financial Condition and Results of Operations for additional information about our reinsurance programs and exposures.

Investments

Our business strategy recognizes the importance of both consistent underwriting and operating profits and superior investment returns to build shareholder value. We rely on sound underwriting practices to produce investable funds while minimizing underwriting risk. The majority of our investable assets come from premiums paid by policyholders. Policyholder funds are invested predominantly in high-quality corporate, government and municipal bonds with relatively short durations. The balance, comprised of shareholder funds, is available to be invested in equity securities, which over the long run, have produced higher returns relative to fixed maturity investments. When purchasing equity securities, we seek to invest in profitable companies, with honest and talented management, that exhibit reinvestment opportunities and capital discipline, at reasonable prices. We intend to hold these investments over the long term. The investment portfolio is managed by company employees.

Total investment return includes items that impact net income, such as net investment income and net realized investment gains or losses, as well as changes in net unrealized gains on investments, which do not impact net income. In 2012, net investment income was $282.1 million and net realized investment gains were $31.6 million. During the year ended December 31, 2012, net unrealized gains on investments increased by $353.8 million. We do not lower the quality of our investment portfolio in order to enhance or maintain yields. We focus on long-term total investment return, understanding that the level of realized and unrealized investment gains or losses may vary from one period to the next.

We believe our investment performance is best analyzed from the review of total investment return over several years. The following table presents taxable equivalent total investment return before and after the effects of foreign currency movements.

Annual Taxable Equivalent Total Investment Returns

	Years Ended December 31,					Weighted Average Five-Year Annual Return	Weighted Average Ten-Year Annual Return
	2008	2009	2010	2011	2012		
Equities	(34.0)%	25.7%	20.8%	3.8%	19.6%	7.2%	9.2%
Fixed maturities [1]	0.2%	9.8%	5.4%	7.6%	5.1%	5.7%	5.3%
Total portfolio, before foreign currency effect	(6.9)%	11.7%	8.1%	6.7%	8.6%	5.8%	6.0%
Total portfolio	(9.6)%	13.2%	7.9%	6.5%	9.0%	5.6%	6.2%
Invested assets, end of year (in millions)	$6,893	$7,849	$8,224	$8,728	$9,333		

(1) Includes short-term investments and cash and cash equivalents.

Taxable equivalent total investment return provides a measure of investment performance that considers the yield of both taxable and tax-exempt investments on an equivalent basis.

We monitor our portfolio to ensure that credit risk does not exceed prudent levels. S&P and Moody's provide corporate and municipal debt ratings based on their assessments of the credit quality of an obligor with respect to a specific obligation. S&P's ratings range from "AAA" (capacity to pay interest and repay principal is extremely strong) to "D" (debt is in payment default). Securities with ratings of "BBB" or higher are referred to as investment grade securities. Debt rated "BB" and below is regarded by S&P as having predominantly speculative characteristics with respect to capacity to pay interest and repay principal. Moody's ratings range from "Aaa" to "C" with ratings of "Baa" or higher considered investment grade.

Our fixed maturity portfolio has an average rating of "AA," with approximately 94% rated "A" or better by at least one nationally recognized rating organization. Our policy is to invest in investment grade securities and to minimize investments in fixed maturities that are unrated or rated below investment grade. At December 31, 2012, less than 1% of our fixed maturity portfolio was unrated or rated below investment grade. Our fixed maturity portfolio includes securities issued with financial guaranty insurance. We purchase fixed maturities based on our assessment of the credit quality of the underlying assets without regard to insurance.

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At December 31, 2012, we held fixed maturities of $38.9 million, or less than 1% of invested assets, from sovereign and non-sovereign issuers domiciled in Portugal, Ireland, Italy, Greece or Spain and $630.3 million, or 7% of invested assets, from sovereign and non-sovereign issuers domiciled in other European countries including supranationals. At December 31, 2011, we held fixed maturities of $53.9 million, or less than 1% of invested assets, from sovereign and non-sovereign issuers domiciled in Portugal, Ireland, Italy, Greece or Spain and $730.4 million, or 8% of invested assets, from sovereign and non-sovereign issuers domiciled in other European countries including supranationals.

The following chart presents our fixed maturity portfolio, at estimated fair value, by rating category at December 31, 2012.

2012 Credit Quality of Fixed Maturity Portfolio ($5.0 billion)

See "Market Risk Disclosures" in Management's Discussion & Analysis of Financial Condition and Results of Operations for additional information about investments.

Non-Insurance Operations (Markel Ventures)

Through our wholly-owned subsidiary Markel Ventures, Inc., we own interests in various industrial and service businesses that operate outside of the specialty insurance marketplace. These businesses are viewed by management as separate and distinct from our insurance operations. Local management teams oversee the day-to-day operations of these companies, while strategic decisions are made in conjunction with members of our executive management team, principally our President and Chief Investment Officer. The financial results of those companies in which we own controlling interests have been consolidated in our financial statements. The financial results of those companies in which we hold a noncontrolling interest are accounted for under the equity method of accounting.

Our strategy in making these private equity investments is similar to our strategy for purchasing equity securities. We seek to invest in profitable companies, with honest and talented management, that exhibit reinvestment opportunities and capital discipline, at reasonable prices. We intend to own the businesses acquired for a long period of time.

Our non-insurance operations, which we refer to collectively as Markel Ventures, are comprised of a diverse portfolio of industrial and service companies from various industries, including manufacturers of dredging equipment, high-speed bakery equipment, laminated furniture products and food processing equipment, an owner and operator of manufactured housing communities, a real estate investment fund manager, a retail intelligence services company, a manager of behavioral health programs, a provider of concierge medical and executive health services, a manufacturer and lessor of trailer tubes used by industrial, chemical and distribution companies to transport gas and liquids and a manufacturer of laminated oak and composite wood flooring used in the assembly of truck trailers, intermodal containers and truck bodies. In 2012, our non-insurance operations reported revenues of $489.4 million and net income to shareholders of $13.5 million.

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Shareholder Value

Our financial goals are to earn consistent underwriting and operating profits and superior investment returns to build shareholder value. More specifically, we measure financial success by our ability to compound growth in book value per share at a high rate of return over a long period of time. To mitigate the effects of short-term volatility, we generally use five-year time periods to measure ourselves. We believe that growth in book value per share is the most comprehensive measure of our success because it includes all underwriting, operating and investing results. For the year ended December 31, 2012, book value per share increased 15% primarily due to net income to shareholders of $253.4 million and a $242.2 million increase in net unrealized gains on investments, net of taxes. For the year ended December 31, 2011, book value per share increased 8% primarily due to net income to shareholders of $142.0 million and a $123.4 million increase in net unrealized gains on investments, net of taxes. Over the past five years, we have grown book value per share at a compound annual rate of 9% to $403.85 per share.

The following graph presents book value per share for the past five years as of December 31.

Book Value Per Share

Regulatory Environment

Our insurance subsidiaries are subject to regulation and supervision by the insurance regulatory authorities of the various jurisdictions in which they conduct business. This regulation is intended for the benefit of policyholders rather than shareholders or holders of debt securities.

United States Insurance Regulation. In the United States, state regulatory authorities have broad regulatory, supervisory and administrative powers relating to solvency standards, the licensing of insurers and their agents, the approval of forms and policies used, the nature of, and limitations on, insurers' investments, the form and content of annual statements and other reports on the financial condition of such insurers and the establishment of loss reserves. Additionally, the business written in the Specialty Admitted segment typically is subject to regulatory rate and form review.

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As an insurance holding company, we are also subject to certain state laws. Under these laws, insurance departments may, at any time, examine us, require disclosure of material transactions, require approval of certain extraordinary transactions, such as extraordinary dividends from our insurance subsidiaries to us, or require approval of changes in control of an insurer or an insurance holding company. Generally, control for these purposes is defined as ownership or voting power of 10% or more of a company's shares.

The laws of the domicile states of our insurance subsidiaries govern the amount of dividends that may be paid to our holding company, Markel Corporation. Generally, statutes in the domicile states of our insurance subsidiaries require prior approval for payment of extraordinary as opposed to ordinary dividends. At December 31, 2012, our United States insurance subsidiaries could pay up to $186.5 million during the following 12 months under the ordinary dividend regulations.

Our United States insurance subsidiaries are also subject to risk-based capital requirements that provide a method to measure the capital of each subsidiary taking into account that subsidiary's investments and products. These requirements provide a formula which, for P&C insurance companies, establishes capital thresholds for four categories of risk: asset risk, insurance risk, interest rate risk and business risk. At December 31, 2012, the capital and surplus of each of our United States insurance subsidiaries was above the minimum regulatory thresholds.

United Kingdom Insurance Regulation. With the enactment of the Financial Services and Markets Act, the United Kingdom government authorized the Financial Services Authority (FSA) to supervise all securities, banking and insurance businesses, including Lloyd's. The FSA oversees compliance with established periodic auditing and reporting requirements, risk assessment reviews, minimum solvency margins and individual capital assessment requirements, dividend restrictions, restrictions governing the appointment of key officers, restrictions governing controlling ownership interests and various other requirements. Both MIICL and Markel Syndicate Management Limited are authorized and regulated by the FSA. We are required to provide 14 days advance notice to the FSA for any dividends from MIICL. In addition, our United Kingdom insurance subsidiaries must comply with the United Kingdom Companies Act of 2006, which provides that dividends may only be paid out of profits available for that purpose.

Ratings

Financial stability and strength are important purchase considerations of policyholders and insurance agents and brokers. Because an insurance premium paid today purchases coverage for losses that might not be paid for many years, the financial viability of the insurer is of critical concern. Various independent rating agencies provide information and assign ratings to assist buyers in their search for financially sound insurers. Rating agencies periodically re-evaluate assigned ratings based upon changes in the insurer's operating results, financial condition or other significant factors influencing the insurer's business. Changes in assigned ratings could have an adverse impact on an insurer's ability to write new business.

Best assigns financial strength ratings (FSRs) to P&C insurance companies based on quantitative criteria such as profitability, leverage and liquidity, as well as qualitative assessments such as the spread of risk, the adequacy and soundness of reinsurance, the quality and estimated market value of assets, the adequacy of loss reserves and surplus and the competence, experience and integrity of management. Best's FSRs range from "A++" (superior) to "F" (in liquidation).

Six of our insurance subsidiaries rated by Best have been assigned an FSR of "A" (excellent), one is rated "A-" (excellent) and one is rated "B++" (good). Markel Syndicate 3000 has been assigned an FSR of "A" (excellent) by Best.

In addition to Best, seven of our eight insurance subsidiaries are rated by Fitch Ratings (Fitch), an independent rating agency. All seven of our insurance subsidiaries rated by Fitch have been assigned an FSR of "A" (strong).

The various rating agencies typically charge companies fees for the rating and other services they provide. During 2012, we paid rating agencies, including Best and Fitch, $0.9 million for their services.

Risk Factors

A wide range of factors could materially affect our future prospects and performance. The matters addressed under "Safe Harbor and Cautionary Statements," "Critical Accounting Estimates" and "Market Risk Disclosures" in Management's Discussion and Analysis of Financial Condition and Results of Operations and other information included or incorporated in this report describe most of the significant risks that could affect our operations and financial results. We are also subject to the following risks.

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We may experience losses from catastrophes. As a property and casualty insurance company, we may experience losses from man-made or natural catastrophes. Catastrophes may have a material adverse effect on operations. Catastrophes include, but are not limited to, windstorms, hurricanes, earthquakes, tornadoes, hail, severe winter weather and fires and may include terrorist events. We cannot predict how severe a particular catastrophe will be before it occurs. The extent of losses from catastrophes is a function of the total amount of losses incurred, the number of insureds affected, the frequency and severity of the events, the effectiveness of our catastrophe risk management program and the adequacy of our reinsurance coverage. Most catastrophes occur over a small geographic area; however, some catastrophes may produce significant damage in large, heavily populated areas. If, as many forecast, climate change results in an increase in the frequency and severity of weather-related catastrophes, we may experience additional catastrophe-related losses, which may be material.

Our results may be affected because actual insured losses differ from our loss reserves. Significant periods of time often elapse between the occurrence of an insured loss, the reporting of the loss to us and our payment of that loss. To recognize liabilities for unpaid losses, we establish reserves as balance sheet liabilities representing estimates of amounts needed to pay reported and unreported losses and the related loss adjustment expenses. The process of estimating loss reserves is a difficult and complex exercise involving many variables and subjective judgments. This process may become more difficult if we experience a period of rising inflation. As part of the reserving process, we review historical data and consider the impact of such factors as:

- trends in claim frequency and severity,
- changes in operations,
- emerging economic and social trends,
- uncertainties relating to asbestos and environmental exposures,
- inflation or deflation, and
- changes in the regulatory and litigation environments.

This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for predicting future events. There is no precise method, however, for evaluating the impact of any specific factor on the adequacy of reserves, and actual results will differ from original estimates. As part of the reserving process, we regularly review our loss reserves and make adjustments as necessary. Future increases in loss reserves will result in additional charges to earnings, which may be material.

We are subject to regulation by insurance regulatory authorities that may affect our ability to implement and achieve our business objectives. Our insurance subsidiaries are subject to supervision and regulation by the insurance regulatory authorities in the various jurisdictions in which they conduct business. This regulation is intended for the benefit of policyholders rather than shareholders or holders of debt securities. Insurance regulatory authorities have broad regulatory, supervisory and administrative powers relating to solvency standards, licensing, coverage requirements, policy rates and forms and the form and content of financial reports. In light of recent economic conditions, regulatory and legislative authorities are implementing enhanced or new regulatory requirements intended to prevent future financial crises or otherwise assure the stability of financial institutions. Regulatory authorities also may seek to exercise their supervisory or enforcement authority in new or more aggressive ways, such as imposing increased capital requirements. Any such actions, if they occurred, could affect the competitive market and the way we conduct our business and manage our capital. As a result, such actions could materially affect our results of operations, financial condition and liquidity.

Our ability to make payments on debt or other obligations depends on the receipt of funds from our subsidiaries. We are a holding company, and substantially all of our insurance operations are conducted through our regulated insurance subsidiaries. As a result, our cash flow and our ability to service our debt are dependent upon the earnings of our subsidiaries and on the distribution of earnings, loans or other payments by our subsidiaries to us. In addition, payment of dividends by our insurance subsidiaries may require prior regulatory notice or approval.

Our investment results may be impacted by changes in interest rates, U.S. and international monetary and fiscal policies as well as broader economic conditions. We receive premiums from customers for insuring their risks. We invest these funds until they are needed to pay policyholder claims or until they are recognized as profits. Fluctuations in the value of our investment portfolio can occur as a result of changes in interest rates, U.S. and international monetary and fiscal policies as well as broader economic conditions (including, for example, equity market conditions and significant inflation or deflation). Our investment results may be materially impacted by one or more of these factors.

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Competition in the property and casualty insurance industry could adversely affect our ability to improve or maintain underwriting margins or to grow or maintain premium volume. Among our competitive strengths have been our specialty product focus and our niche market strategy. These strengths also make us vulnerable in periods of intense competition to actions by other insurance companies who seek to write additional premiums without appropriate regard for underwriting profitability. During soft markets, it is very difficult for us to grow or maintain premium volume levels without sacrificing underwriting profits. If we are not successful in maintaining rates or achieving rate increases, it may be difficult for us to improve or maintain underwriting margins or to grow or maintain premium volume levels.

We invest a significant portion of our invested assets in equity securities, which may result in significant variability in our investment results and may adversely impact shareholders' equity. Additionally, our equity investment portfolio is concentrated and declines in the value of these significant investments could adversely affect our financial results. Equity securities were 62% and 55% of our shareholders' equity at both December 31, 2012 and 2011. Equity securities have historically produced higher returns than fixed maturities; however, investing in equity securities may result in significant variability in investment returns from one period to the next. In volatile financial markets, we could experience significant declines in the fair value of our equity investment portfolio, which would result in a material decrease in shareholders' equity. Our equity portfolio is concentrated in particular issuers and industries and, as a result, a decline in the fair value of these concentrated investments also could result in a material decrease in shareholders' equity. A material decrease in shareholders' equity may adversely impact our ability to carry out our business plans.

Deterioration in financial markets could lead to investment losses and adverse effects on our business. The severe downturn in the public debt and equity markets beginning in 2008, reflecting uncertainties associated with the mortgage and credit crises, worsening economic conditions, widening of credit spreads, bankruptcies and government intervention in large financial institutions, resulted in significant realized and unrealized losses in our investment portfolio. In the event of another major financial crisis (for example, a crisis precipitated by the failure to adequately address U.S. government deficit spending and tax revenue generation, downgrades or defaults in U.S. and/or foreign sovereign debt obligations, or the collapse of the Eurozone), we could incur substantial realized and unrealized investment losses in future periods, which would have an adverse impact on our results of operations, financial condition, debt and financial strength ratings, insurance subsidiaries' capital and ability to access capital markets.

We rely on reinsurance and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance agreement. We purchase reinsurance in order to reduce our retention on individual risks and to have the ability to underwrite policies with sufficient limits to meet policyholder needs. The ceding of insurance does not legally discharge us from our primary liability for the full amount of the policies. Such reliance on reinsurance may create credit risk as a result of the reinsurer's inability or unwillingness to pay reinsurance claims when due. Deterioration in the credit quality of existing reinsurers or disputes over the terms of reinsurance could result in additional charges to earnings, which may have a materially adverse impact our results of operations and financial condition.

Our information technology systems could fail or suffer a security breach, which could adversely affect our business or reputation. Our business is dependent upon the successful functioning and security of our computer systems. Among other things, we rely on these systems to interact with producers and insureds, to perform actuarial and other modeling functions, to underwrite business, to prepare policies and process premiums, to process claims and make claims payments, and to prepare internal and external financial statements and information. A significant failure of these systems, whether because of a breakdown, natural disaster or an attack on our systems, could have a material adverse affect on our business. In addition, a security breach of our computer systems could damage our reputation or result in material liabilities.

The integration of acquired companies may not be as successful as we anticipate. We have recently engaged in a number of acquisitions in an effort to achieve profitable growth in our insurance operations and to create additional value on a diversified basis in our non-insurance operations. Acquisitions present operational, strategic and financial risks, as well as risks associated with liabilities arising from the previous operations of the acquired companies. Assimilation of the operations and personnel of acquired companies (especially those that are outside of our core insurance operations) may prove more difficult than anticipated, which may result in failure to achieve financial objectives associated with the acquisition or diversion of management attention. In addition, integration of formerly privately-held companies into the management and internal control and financial reporting systems of a publicly-held company presents additional risks.

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On December 19, 2012 we announced the acquisition of Alterra for an aggregate consideration of approximately $3.1 billion in stock and cash (the Alterra Acquisition). We expect the Alterra Acquisition to close in the first half of 2013. Failure to complete the Alterra Acquisition on a timely basis or the fact that the Alterra Acquisition is pending could negatively impact the share price of Markel and the future business and financial results of Markel. The acquisition agreement with Alterra contains a number of conditions precedent that must be satisfied or waived before the closing of the Alterra Acquisition. Also, the Alterra Acquisition agreement may be terminated by one or both of the parties under certain circumstances. Further, the ongoing business of Markel may be adversely affected by the fact that the Alterra Acquisition is pending or if the Alterra Acquisition is not completed as follows:

- the manner in which brokers, insureds, cedants and other third parties perceive Markel may be negatively impacted, which in turn could affect the ability of Markel to compete for or write new business or obtain renewals in the marketplace;
- current and prospective employees of Markel may experience uncertainty about their future roles with the combined company, which may adversely affect the ability of Markel to attract and retain key personnel;
- the attention of management of Markel will be diverted to the Alterra Acquisition or to the integration of the two companies after the Alterra Acquisition instead of being directed solely to our own operations and pursuit of other opportunities that may be beneficial to Markel;
- Markel will have to pay costs relating to the Alterra Acquisition, including legal, accounting and financial advisory fees;
- Markel may be required, in certain circumstances, to pay a termination fee to Alterra; and
- the ratings of either Markel or its respective insurance subsidiaries may be adversely affected, which would likely result in a material adverse effect on their respective business, financial condition and operating results.

Markel will be exposed to underwriting and other business risks during the period that Alterra's business continues to be operated independently from Markel. Until completion of the Alterra Acquisition, each of Markel and Alterra will operate independently from the other in accordance with such party's distinct underwriting guidelines, investment policies, referral processes, authority levels and risk management policies and practices. As a result, during this period, Alterra may assume risks that Markel would not have assumed for itself or for the combined company, accept premiums that, in Markel's judgment, do not adequately compensate it for the risks assumed, make investment decisions that would not adhere to Markel's investment policies or otherwise make business decisions or take on exposure that, while consistent with Alterra's general business approach and practices, are not the same as those of Markel. Significant delays in consummating the Alterra Acquisition will materially increase the risk that Alterra will operate its business in a manner that differs from how the business would have been conducted under the combined company.

The integration of Markel and Alterra following the Alterra Acquisition may present significant challenges and costs. Markel and Alterra may face significant challenges, including technological, accounting and other challenges, in combining Markel's and Alterra's operations. Markel and Alterra entered into the Alterra Acquisition agreement because each company believes that the Alterra Acquisition will be beneficial to it and its respective shareholders. Achieving the anticipated benefits of the Alterra Acquisition will depend in part upon whether Markel will be successful in integrating Alterra's businesses in a timely and efficient manner. Markel may not be able to accomplish this integration process smoothly or successfully. The integration of certain operations following the Alterra Acquisition will take time and will require the dedication of significant management resources, which may temporarily distract management's attention from the routine business of the combined company. Any delay or inability of management to successfully integrate the operations of the two companies could compromise the combined company's potential to achieve the long-term strategic benefits of the Alterra Acquisition and could have a material adverse effect on the business, financial condition and operating results of the combined company and the market price of the combined company's shares of common stock.

In addition, the combined company will incur integration and restructuring costs following the completion of the Alterra Acquisition as it integrates the businesses of Alterra. Although the parties expect that the realization of efficiencies related to the integration of the businesses will offset incremental transaction, integration and restructuring costs over time, Markel cannot give any assurance that this net benefit will be achieved in the near term, if at all.

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Markel, Alterra or the combined company may lose employees due to uncertainties associated with the Alterra Acquisition and may not be able to hire qualified new employees. The success of the combined company after the Alterra Acquisition will depend in part upon the ability of Markel and Alterra to retain key employees. Competition for qualified personnel can be intense. In addition, key employees may depart because of issues relating to the uncertainty or difficulty of integration or a desire not to remain with the combined company. Accordingly, no assurance can be given that Markel, Alterra or the combined company will be able to attract, retain or motivate key employees or qualified new employees. If, despite retention efforts, key employees depart because of issues relating to the uncertainty and difficulty of integration, the combined company's business could be adversely impacted.

The occurrence of severe catastrophic events may cause the combined company's financial results to be volatile and may affect the financial results of the combined company differently than such an event would have affected the financial results of either Markel or Alterra on a stand-alone basis. Because the combined company will, among other things, underwrite property catastrophe insurance and reinsurance and have large aggregate exposures to natural and man-made disasters, management expects that the combined company's loss experience generally will include infrequent events of great severity. Consequently, the occurrence of losses from catastrophic events is likely to cause substantial volatility in the combined company's financial results. In addition, because catastrophes will be an inherent risk of the combined company's business, a major event or series of events could have a material adverse effect on the combined company's financial condition and results of operations, possibly to the extent of eliminating the combined company's shareholders' equity. Increases in the values and concentrations of insured property and the effects of inflation have resulted in increased severity of industry losses in recent years, and those factors are expected to increase the severity of catastrophe losses in the future. Upon closing, the combined company's exposure to natural and man-made disasters will be different than the exposure of Markel before the Alterra Acquisition.

Alterra's counterparties to contracts and arrangements may acquire certain rights upon the Alterra Acquisition, which could negatively affect the combined company following the Alterra Acquisition. Alterra or its subsidiaries are parties to numerous contracts, agreements, licenses, permits, authorizations and other arrangements that contain provisions giving counterparties certain rights (including, in some cases, termination rights) upon a "change in control" of Alterra or its subsidiaries. The definition of "change in control" varies from contract to contract, ranging from a narrow to a broad definition, and in some cases, the "change in control" provisions may be implicated by the Alterra Acquisition. If a change in control occurs, cedants may be permitted to cancel contracts on a cut-off or run-off basis, and Alterra or certain of its affiliates may be required to provide collateral to secure premium and reserve balances or may be required to cancel and commute a contract, subject to an agreement between the parties that may be settled in arbitration. If a contract is cancelled on a cut-off basis, Alterra may be required to return unearned premiums, net of commissions. In addition, contracts may provide a ceding company with multiple options, such as collateralization or commutation, that would be triggered by a change in control. Collateral requirements may take the form of trust agreements or be funded by securities held or letters of credit. Upon commutation, the amount to be paid to settle the liability for gross loss reserves would typically consider a discount to the financial statement loss reserve value, reflecting the time value of money resident in the ultimate settlement of such loss reserves. In certain instances, contracts contain dual triggers, such as a change in control and a ratings downgrade, both of which must be satisfied for the contractual right to be exercisable.

Whether a ceding company would have cancellation rights in connection with the Alterra Acquisition depends upon the language of its agreement with Alterra or its applicable subsidiaries. Whether a ceding company exercises any cancellation rights it has would depend on, among other factors, such ceding company's views with respect to the financial strength and business reputation of the combined company, the extent to which such ceding company currently has reinsurance coverage with the combined company's affiliates, the prevailing market conditions, the pricing and availability of replacement reinsurance coverage and the combined company's ratings following the Alterra Acquisition. Alterra cannot currently predict the effects, if any, if the Alterra Acquisition is deemed to constitute a change in control under contracts and other arrangements, including the extent to which cancellation rights would be exercised, if at all, nor the effect on the combined company's financial condition, results of operations, or cash flows, but such effect could be material.

Associates

At December 31, 2012, we had approximately 6,400 employees, of whom approximately 2,800 were employed within our insurance operations and approximately 3,600 were employed within our non-insurance operations.

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SELECTED FINANCIAL DATA (dollars in millions, except per share data) [1]

	2012		2011		2010	
Results of Operations						
Earned premiums	$2,147		$1,979		$1,731	
Net investment income	282		264		273	
Total operating revenues	3,000		2,630		2,225	
Net income (loss) to shareholders	253		142		267	
Comprehensive income (loss) to shareholders	504		252		431	
Diluted net income (loss) per share	$25.89		$14.60		$27.27	
Financial Position						
Total investments and cash and cash equivalents	$9,333		$8,728		$8,224	
Total assets	12,557		11,532		10,826	
Unpaid losses and loss adjustment expenses	5,371		5,399		5,398	
Senior long-term debt and other debt	1,493		1,294		1,016	
Shareholders' equity	3,889		3,388		3,172	
Common shares outstanding (at year end, in thousands)	9,629		9,621		9,718	
OPERATING PERFORMANCE MEASURES [1, 2]						
Operating Data						
Book value per common share outstanding	$403.85		$352.10		$326.36	
Growth (decline) in book value per share	15	%	8	%	16	%
5-Year CAGR in book value per share [3]	9	%	9	%	13	%
Closing stock price	$433.42		$414.67		$378.13	
Ratio Analysis						
U.S. GAAP combined ratio [4]	97	%	102	%	97	%
Investment yield [5]	4	%	4	%	4	%
Taxable equivalent total investment return [6]	9	%	7	%	8	%
Investment leverage [7]	2.4		2.6		2.6	
Debt to capital	28	%	28	%	24	%

(1) Effective January 1, 2012, we prospectively adopted Financial Accounting Standards Board Accounting Standards Update No. 2010-26, Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts. See note 1(r) in the notes to consolidated financial statements.

(2) Operating Performance Measures provide a basis for management to evaluate our performance. The method we use to compute these measures may differ from the methods used by other companies. See further discussion of management's evaluation of these measures in Management's Discussion & Analysis of Financial Condition and Results of Operations.

(3) CAGR—compound annual growth rate.

(4) The U.S. GAAP combined ratio measures the relationship of incurred losses, loss adjustment expenses and underwriting, acquisition and insurance expenses to earned premiums.

(5) Investment yield reflects net investment income as a percentage of average invested assets.

(6) Taxable equivalent total investment return includes net investment income, realized investment gains or losses, the change in fair value of the investment portfolio and the effect of foreign currency exchange rate movements during the period as a percentage of average invested assets. Tax-exempt interest and dividend payments are grossed up using the U.S. corporate tax rate to reflect an equivalent taxable yield.

(7) Investment leverage represents total invested assets divided by shareholders' equity.

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2009	2008		2007	2006	2005	2004	2003	10-Year CAGR (3)	
$1,816	$2,022		$2,117	$2,184	$1,938	$2,054	$1,864	3	%
260	282		305	269	242	204	183	5	%
2,069	1,977		2,551	2,576	2,200	2,262	2,092	5	%
202	(59	)	406	393	148	165	123	—	
591	(403	)	337	551	64	273	222	—	
$20.52	$(5.95	)	$40.64	$39.40	$14.80	$16.41	$12.31	—	
$7,849	$6,893		$7,775	$7,524	$6,588	$6,317	$5,350	8	%
10,242	9,512		10,164	10,117	9,814	9,398	8,532	5	%
5,427	5,492		5,526	5,584	5,864	5,482	4,930	2	%
964	694		691	866	849	855	763	—	
2,774	2,181								