

ALLSTATE CORP
Form 10-Q
October 27, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2010

OR

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

For the transition period from _____ to _____

Commission file number 1-11840

THE ALLSTATE CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

36-3871531

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(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

2775 Sanders Road, Northbrook, Illinois

(Address of principal executive offices)

60062

(Zip Code)

(847) 402-5000

(Registrant's telephone number, including area code)

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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes X No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer X Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

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

Yes ☐ No X

As of October 22, 2010, the registrant had 538,183,935 common shares, \$.01 par value, outstanding.

THE ALLSTATE CORPORATION

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September 30, 2010

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

THE ALLSTATE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(\$ in millions, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(unaudited)		(unaudited)	
Revenues				
Property-liability insurance premiums	\$ 6,499	\$ 6,535	\$ 19,515	\$ 19,677
Life and annuity premiums and contract charges	548	482	1,637	1,460
Net investment income	1,005	1,084	3,104	3,368
Realized capital gains and losses:				
Total other-than-temporary impairment losses	(99)	(539)	(637)	(1,735)
Portion of loss recognized in other comprehensive income	(68)	147	(91)	301
Net other-than-temporary impairment losses recognized in earnings	(167)	(392)	(728)	(1,434)
Sales and other realized capital gains and losses	23	(127)	(215)	884
Total realized capital gains and losses	(144)	(519)	(943)	(550)
	7,908	7,582	23,313	23,955
Costs and expenses				
Property-liability insurance claims and claims expense	4,603	4,573	14,109	14,295
Life and annuity contract benefits	445	382	1,372	1,176
Interest credited to contractholder funds	445	496	1,358	1,636
Amortization of deferred policy acquisition costs	1,006	1,023	2,969	3,649
Operating costs and expenses	828	744	2,446	2,247
Restructuring and related charges	9	35	33	112
Interest expense	91	106	275	291
	7,427	7,359	22,562	23,406
Gain on disposition of operations	9	2	12	6
Income from operations before income tax expense	490	225	763	555
Income tax expense	123	4	131	219
Net income	\$ 367	\$ 221	\$ 632	\$ 336
Earnings per share:				
Net income per share - Basic	\$ 0.68	\$ 0.41	\$ 1.17	\$ 0.62
Weighted average shares - Basic	540.9	539.9	540.6	539.5
Net income per share - Diluted	\$ 0.68	\$ 0.41	\$ 1.16	\$ 0.62
Weighted average shares - Diluted	543.0	541.5	542.7	540.5
Cash dividends declared per share	\$ 0.20	\$ 0.20	\$ 0.60	\$ 0.60

See notes to condensed consolidated financial statements.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(\$ in millions, except par value data)

	September 30, 2010 (unaudited)	December 31, 2009
Assets		
Investments:		
Fixed income securities, at fair value (amortized cost \$80,786 and \$81,243)	\$ 83,193	\$ 78,766
Equity securities, at fair value (cost \$3,447 and \$4,845)	3,707	5,024
Mortgage loans	6,961	7,935
Limited partnership interests	3,454	2,744
Short-term, at fair value (amortized cost \$2,776 and \$3,056)	2,776	3,056
Other	2,123	2,308
Total investments	102,214	99,833
Cash	500	612
Premium installment receivables, net	4,981	4,839
Deferred policy acquisition costs	4,671	5,470
Reinsurance recoverables, net	6,597	6,355
Accrued investment income	847	864
Deferred income taxes	670	1,870
Property and equipment, net	922	990
Goodwill	874	875
Other assets	1,799	1,872
Separate Accounts	8,459	9,072
Total assets	\$ 132,534	\$ 132,652
Liabilities		
Reserve for property-liability insurance claims and claims expense	\$ 19,294	\$ 19,167
Reserve for life-contingent contract benefits	13,955	12,910
Contractholder funds	48,936	52,582
Unearned premiums	10,001	9,822
Claim payments outstanding	733	742
Other liabilities and accrued expenses	5,945	5,726
Long-term debt	5,909	5,910
Separate Accounts	8,459	9,072
Total liabilities	113,232	115,931
Commitments and Contingent Liabilities (Note 10)		
Equity		
Preferred stock, \$1 par value, 25 million shares authorized, none issued		
Common stock, \$.01 par value, 2.0 billion shares authorized and 900 million issued, 538 million and 537 million shares outstanding	9	9
Additional capital paid-in	3,165	3,172
Retained income	31,781	31,492
Deferred ESOP expense	(45)	(47)
Treasury stock, at cost (362 million and 363 million shares)	(15,755)	(15,828)
Accumulated other comprehensive income:		
Unrealized net capital gains and losses:		
Unrealized net capital losses on fixed income securities with OTTI	(200)	(441)
Other unrealized net capital gains and losses	1,919	(1,072)
Unrealized adjustment to DAC, DSI and insurance reserves	(427)	643
Total unrealized net capital gains and losses	1,292	(870)
Unrealized foreign currency translation adjustments	54	46
Unrecognized pension and other postretirement benefit cost	(1,227)	(1,282)
Total accumulated other comprehensive income (loss)	119	(2,106)
Total shareholders' equity	19,274	16,692
Noncontrolling interest	28	29
Total equity	19,302	16,721
Total liabilities and equity	\$ 132,534	\$ 132,652

See notes to condensed consolidated financial statements.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(\$ in millions)

	Nine Months Ended September 30,	
	2010	2009
	(unaudited)	
Cash flows from operating activities		
Net income	\$ 632	\$ 336
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and other non-cash items	55	(87)
Realized capital gains and losses	943	550
Gain on disposition of operations	(12)	(6)
Interest credited to contractholder funds	1,358	1,636
Changes in:		
Policy benefits and other insurance reserves	143	(460)
Unearned premiums	172	6
Deferred policy acquisition costs	(138)	471
Premium installment receivables, net	(137)	(108)
Reinsurance recoverables, net	(229)	(101)
Income taxes	178	1,175
Other operating assets and liabilities	58	103
Net cash provided by operating activities	3,023	3,515
Cash flows from investing activities		
Proceeds from sales		
Fixed income securities	17,345	16,098
Equity securities	4,262	4,636
Limited partnership interests	387	293
Mortgage loans	121	140
Other investments	98	429
Investment collections		
Fixed income securities	3,672	3,947
Mortgage loans	784	1,093
Other investments	96	99
Investment purchases		
Fixed income securities	(20,712)	(22,694)
Equity securities	(2,721)	(5,991)
Limited partnership interests	(1,040)	(674)
Mortgage loans	(55)	(23)
Other investments	(99)	(54)
Change in short-term investments, net	104	5,437
Change in other investments, net	(464)	(144)
Disposition of operations	7	12
Purchases of property and equipment, net	(114)	(143)
Net cash provided by investing activities	1,671	2,461
Cash flows from financing activities		
Proceeds from issuance of long-term debt		1,003
Repayment of long-term debt	(1)	(1)
Contractholder fund deposits	2,297	3,252
Contractholder fund withdrawals	(6,779)	(9,485)
Dividends paid	(322)	(434)
Treasury stock purchases	(5)	(3)
Shares reissued under equity incentive plans, net	26	2
Excess tax benefits on share-based payment arrangements	(7)	(6)
Other	(15)	8
Net cash used in financing activities	(4,806)	(5,664)
Net (decrease) increase in cash	(112)	312
Cash at beginning of period	612	415
Cash at end of period	\$ 500	\$ 727

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See notes to condensed consolidated financial statements.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. General

Basis of presentation

The accompanying condensed consolidated financial statements include the accounts of The Allstate Corporation and its wholly owned subsidiaries, primarily Allstate Insurance Company (AIC), a property-liability insurance company with various property-liability and life and investment subsidiaries, including Allstate Life Insurance Company (ALIC) (collectively referred to as the Company or Allstate).

The condensed consolidated financial statements and notes as of September 30, 2010, and for the three-month and nine-month periods ended September 30, 2010 and 2009 are unaudited. The condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring accruals), which are, in the opinion of management, necessary for the fair presentation of the financial position, results of operations and cash flows for the interim periods. These condensed consolidated financial statements and notes should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009. The results of operations for the interim periods should not be considered indicative of results to be expected for the full year.

Adopted accounting standards

Disclosures about Fair Value Measurements

In January 2010, the Financial Accounting Standards Board (FASB) issued new accounting guidance which expands disclosure requirements relating to fair value measurements. The guidance adds requirements for disclosing amounts of and reasons for significant transfers into and out of Levels 1 and 2 and requires gross rather than net disclosures about purchases, sales, issuances and settlements relating to Level 3 measurements. The guidance also provides clarification that fair value measurement disclosures are required for each class of assets and liabilities. Disclosures about the valuation techniques and inputs used to measure fair value for measurements that fall in either Level 2 or Level 3 are also required. The Company adopted the provisions of the new guidance as of March 31, 2010, except for disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements, which are required for fiscal years beginning after December 15, 2010. Disclosures are not required for earlier periods presented for comparative purposes. The new guidance affects disclosures only; and therefore, the adoption had no impact on the Company's results of operations or financial position.

Consolidation of Variable Interest Entities

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In June 2009, the FASB issued new accounting guidance which requires an entity to perform a qualitative analysis to determine whether it holds a controlling financial interest (i.e., is a primary beneficiary) in a variable interest entity (VIE). The analysis identifies the primary beneficiary of a VIE as the entity that has both the power to direct the activities of the VIE that most significantly impact the economic performance of the VIE and the obligation to absorb losses, or the right to receive benefits, that could potentially be significant to the VIE. The Company adopted the new guidance as of January 1, 2010. The adoption resulted in the consolidation of four VIEs for which the Company concluded it is the primary beneficiary as of January 1, 2010.

Two of the consolidated VIEs hold investments managed by Allstate Investment Management Company (AIMCO), a subsidiary of the Company. Consolidation as of January 1, 2010 resulted in an increase in total assets of \$696 million, an increase in total liabilities of \$679 million, an increase in retained income of \$7 million and an increase in noncontrolling interest of \$10 million. During the first quarter of 2010, the Company sold substantially all its variable interests in these two VIEs. As a result, the Company deconsolidated the VIEs as of March 26, 2010. The Condensed Consolidated Statement of Operations for the nine months ended September 30, 2010 reflects the effect of the consolidation for the portion of the period the Company was the primary beneficiary, which was not material.

The adoption also resulted in the consolidation of two insurance company affiliates, Allstate Texas Lloyds and Allstate County Mutual Insurance Company, that underwrite homeowners and auto insurance policies, respectively, and reinsure all of their net business to AIC. Consolidation as of January 1, 2010 resulted in an increase in total assets of \$38 million, an increase in total liabilities of \$34 million, an increase in retained income of \$3 million and an increase in unrealized net capital gains and losses of \$1 million.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

In the normal course of investing activities, the Company invests in variable interests issued by VIEs. These variable interests include structured investments such as residential mortgage-backed securities, commercial mortgage-backed securities and asset-backed securities as well as limited partnerships, special purpose entities and trusts. For these variable interests, the Company concluded it is not the primary beneficiary due to the amount of the Company's interest in the VIEs and the Company's lack of power to direct the activities that are most significant to the economic performance of the VIEs. The Company's maximum exposure to loss on these interests is limited to the amount of the Company's investment, including future funding commitments, as applicable.

Embedded Credit Derivatives Scope Exception

In March 2010, the FASB issued accounting guidance clarifying the scope exception for embedded credit derivative features, including those in certain collateralized debt obligations and synthetic collateralized debt obligations. Embedded credit derivative features related to the transfer of credit risk that is only in the form of subordination of one financial instrument to another continue to qualify for the scope exception. Other embedded credit derivative features must be analyzed for potential bifurcation and separate accounting as a derivative, with periodic changes in fair value recorded in net income. The adoption of the new guidance as of July 1, 2010 resulted in the bifurcation of the credit default swaps embedded in synthetic collateralized debt obligations purchased after January 1, 2007, and the related net unrealized capital losses were reclassified from accumulated other comprehensive income to retained income. The cumulative effect of adoption, net of related deferred policy acquisition costs (DAC), deferred sales inducement costs (DSI) and tax adjustments, was a \$19 million increase in unrealized net capital gains and losses, a \$9 million decrease in total assets and a \$28 million decrease in retained income.

Pending accounting standards

Consolidation Analysis Considering Investments Held through Separate Accounts

In April 2010, the FASB issued guidance clarifying that an insurer is not required to combine interests in investments held in a qualifying separate account with its interests in the same investments held in the general account when performing a consolidation evaluation. The guidance is effective for fiscal years and interim periods beginning after December 15, 2010 with early adoption permitted. The adoption of this guidance is not expected to have a material impact on the Company's results of operations or financial position.

Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses

In July 2010, the FASB issued guidance requiring expanded disclosures relating to the credit quality of financing receivables and the related allowances for credit losses. The new guidance requires a greater level of disaggregated information, as well as additional disclosures about credit quality indicators, past due information and modifications of its financing receivables. The new guidance is effective for reporting periods

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ending after December 15, 2010. The new guidance affects disclosures only; and therefore, the adoption will have no impact on the Company's results of operations or financial position.

Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts

In October 2010, the FASB issued guidance modifying the definition of the types of costs incurred by insurance entities that can be capitalized in the acquisition of new and renewal contracts. The guidance specifies that incremental direct costs of contract acquisition attributable to successful efforts should be included as deferred acquisition costs. The guidance also specifies that deferred acquisition costs include advertising costs only when the direct-response advertising accounting criteria are met. The new guidance is effective for reporting periods beginning after December 15, 2011 and should be applied prospectively, with retrospective application permitted. If application of the guidance would result in the capitalization of acquisition costs that had not previously been capitalized prior to adoption, the entity may elect not to capitalize those additional costs. The Company is in process of evaluating the impact of adoption on the Company's results of operations and financial position.

2. Earnings per share

Basic earnings per share is computed using the weighted average number of common shares outstanding, including unvested participating restricted stock units. Diluted earnings per share is computed using the weighted

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

average number of common and dilutive potential common shares outstanding. For the Company, dilutive potential common shares consist of outstanding stock options and unvested non-participating restricted stock units.

The computation of basic and diluted earnings per share is presented in the following table.

(\$ in millions, except per share data)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Numerator:				
Net income	\$ 367	\$ 221	\$ 632	\$ 336
Denominator:				
Weighted average common shares outstanding	540.9	539.9	540.6	539.5
Effect of dilutive potential common shares:				
Stock options	1.9	1.6	2.0	1.0
Restricted stock units (non-participating)	0.2	--	0.1	--
Weighted average common and dilutive potential common shares outstanding	543.0	541.5	542.7	540.5
Earnings per share - Basic	\$ 0.68	\$ 0.41	\$ 1.17	\$ 0.62
Earnings per share - Diluted	\$ 0.68	\$ 0.41	\$ 1.16	\$ 0.62

The effect of dilutive potential common shares does not include the effect of options with an anti-dilutive effect on earnings per share because their exercise prices exceed the average market price of Allstate common shares during the period or for which the unrecognized compensation cost would have an anti-dilutive effect. Options to purchase 27.6 million and 25.0 million Allstate common shares, with exercise prices ranging from \$27.36 to \$62.84 and \$23.13 to \$64.53, were outstanding at September 30, 2010 and 2009, respectively, but were not included in the computation of diluted earnings per share for the three-month periods then ended. Options to purchase 26.6 million and 26.2 million Allstate common shares, with exercise prices ranging from \$27.36 to \$64.53 and \$23.13 to \$65.38, were outstanding at September 30, 2010 and 2009, respectively, but were not included in the computation of diluted earnings per share for the nine-month periods then ended.

3. Supplemental Cash Flow Information

Non-cash investment exchanges, including modifications of certain mortgage loans, fixed income securities, limited partnerships and other investments, as well as mergers completed with equity securities, totaled \$544 million and \$342 million for the nine months ended September 30, 2010 and 2009, respectively.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Liabilities for collateral received in conjunction with the Company's securities lending and over-the-counter (OTC) derivatives are reported in other liabilities and accrued expenses or other investments in the Condensed Consolidated Statements of Financial Position. The accompanying cash flows are included in cash flows from operating activities in the Condensed Consolidated Statements of Cash Flows along with the activities resulting from management of the proceeds, which are as follows:

(\$ in millions)	Nine months ended September 30,	
	2010	2009
Net change in proceeds managed		
Net change in short-term investments	\$ 187	\$ (190)
Operating cash flow provided (used)	187	(190)
Net change in cash	2	--
Net change in proceeds managed	\$ 189	\$ (190)
Net change in liabilities		
Liabilities for collateral, beginning of year	\$ (658)	\$ (340)
Liabilities for collateral, end of period	(469)	(530)
Operating cash flow (used) provided	\$ (189)	\$ 190

4. Investments

Fair values

The amortized cost, gross unrealized gains and losses and fair value for fixed income securities are as follows:

(\$ in millions)	Amortized cost	Gross unrealized Gains	Losses	Fair value
At September 30, 2010				
U.S. government and agencies	\$ 10,721	\$ 533	\$ (1)	\$ 11,253
Municipal	16,366	803	(401)	16,768
Corporate	34,870	2,618	(284)	37,204
Foreign government	2,946	482	--	3,428
Residential mortgage-backed securities (RMBS)	9,192	245	(938)	8,499
Commercial mortgage-backed securities (CMBS)	2,375	59	(441)	1,993
Asset-backed securities (ABS)	4,280	105	(375)	4,010
Redeemable preferred stock	36	2	--	38
Total fixed income securities	\$ 80,786	\$ 4,847	\$ (2,440)	\$ 83,193
At December 31, 2009				
U.S. government and agencies	\$ 7,333	\$ 219	\$ (16)	\$ 7,536

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Municipal	21,683	537	(940)	21,280
Corporate	32,770	1,192	(847)	33,115
Foreign government	2,906	306	(15)	3,197
RMBS	9,487	130	(1,630)	7,987
CMBS	3,511	30	(955)	2,586
ABS	3,514	62	(550)	3,026
Redeemable preferred stock	39	1	(1)	39
Total fixed income securities	\$ 81,243	\$ 2,477	\$ (4,954)	\$ 78,766

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Scheduled maturities

The scheduled maturities for fixed income securities are as follows at September 30, 2010:

(\$ in millions)	Amortized cost	Fair value
Due in one year or less	\$ 3,338	\$ 3,389
Due after one year through five years	25,627	26,746
Due after five years through ten years	15,835	17,386
Due after ten years	22,514	23,163
	67,314	70,684
RMBS and ABS	13,472	12,509
Total	\$ 80,786	\$ 83,193

Actual maturities may differ from those scheduled as a result of prepayments by the issuers. Because of the potential for prepayment on RMBS and ABS, they are not categorized by contractual maturity. CMBS are categorized by contractual maturity because they generally are not subject to prepayment risk.

Net investment income

Net investment income is as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Fixed income securities	\$ 926	\$ 987	\$ 2,840	\$ 3,022
Equity securities	17	15	63	50
Mortgage loans	92	121	295	389
Limited partnership interests	6	4	19	11
Short-term investments	2	4	6	23
Other	5	(4)	12	(7)
Investment income, before expense	1,048	1,127	3,235	3,488
Investment expense	(43)	(43)	(131)	(120)
Net investment income	\$ 1,005	\$ 1,084	\$ 3,104	\$ 3,368

Realized capital gains and losses

Realized capital gains and losses by security type are as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Fixed income securities	\$ 84	\$ (33)	\$ (240)	\$ 89
Equity securities	83	(21)	142	(157)
Mortgage loans	(1)	(66)	(54)	(114)
Limited partnership interests	(20)	(20)	(15)	(443)
Derivatives	(286)	(364)	(779)	151
Other	(4)	(15)	3	(76)
Realized capital gains and losses	\$ (144)	\$ (519)	\$ (943)	\$ (550)

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Realized capital gains and losses by transaction type are as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Impairment write-downs	\$ (137)	\$ (381)	\$ (599)	\$ (1,292)
Change in intent write-downs	(30)	(11)	(129)	(142)
Net other-than-temporary impairment losses recognized in earnings	(167)	(392)	(728)	(1,434)
Sales	319	201	552	882
Valuation of derivative instruments	(133)	(269)	(571)	201
Settlements of derivative instruments	(152)	(92)	(209)	(52)
EMA limited partnership income	(11)	33	13	(147)
Realized capital gains and losses	\$ (144)	\$ (519)	\$ (943)	\$ (550)

Gross gains of \$387 million and \$341 million and gross losses of \$173 million and \$144 million were realized on sales of fixed income securities during the three months ended September 30, 2010 and 2009, respectively. Gross gains of \$673 million and \$1.12 billion and gross losses of \$360 million and \$303 million were realized on sales of fixed income securities during the nine months ended September 30, 2010 and 2009, respectively.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Other-than-temporary impairment losses by asset type are as follows:

(\$ in millions)	Three months ended September 30, 2010			Nine months ended September 30, 2010		
	Gross	Included in OCI	Net	Gross	Included in OCI	Net
Fixed income securities:						
Municipal	\$ (1)	\$ --	\$ (1)	\$ (106)	\$ 4	\$ (102)
Corporate	(14)	(1)	(15)	(67)	1	(66)
RMBS	(56)	(41)	(97)	(268)	(43)	(311)
CMBS	(1)	(26)	(27)	(44)	(37)	(81)
ABS	--	--	--	(9)	(16)	(25)
Total fixed income securities	(72)	(68)	(140)	(494)	(91)	(585)
Equity securities	(14)	--	(14)	(51)	--	(51)
Mortgage loans	(3)	--	(3)	(50)	--	(50)
Limited partnership interests	(10)	--	(10)	(42)	--	(42)
Other-than-temporary impairment losses	\$ (99)	\$ (68)	\$ (167)	\$ (637)	\$ (91)	\$ (728)

	Three months ended September 30, 2009			Nine months ended September 30, 2009		
	Gross	Included in OCI	Net	Gross	Included in OCI	Net
Fixed income securities:						
Municipal	\$ (6)	\$ 2	\$ (4)	\$ (92)	\$ 6	\$ (86)
Corporate	(112)	(1)	(113)	(204)	(10)	(214)
Foreign government	--	--	--	(17)	--	(17)
RMBS	(174)	115	(59)	(433)	266	(167)
CMBS	(90)	62	(28)	(142)	61	(81)
ABS	(10)	(31)	(41)	(185)	(22)	(207)
Total fixed income securities	(392)	147	(245)	(1,073)	301	(772)
Equity securities	(61)	--	(61)	(247)	--	(247)
Mortgage loans	(31)	--	(31)	(80)	--	(80)
Limited partnership interests	(53)	--	(53)	(296)	--	(296)
Other	(2)	--	(2)	(39)	--	(39)
Other-than-temporary impairment losses	\$ (539)	\$ 147	\$ (392)	\$ (1,735)	\$ 301	\$ (1,434)

The total amount of other-than-temporary impairment losses included in accumulated other comprehensive income for fixed income securities, which were not included in earnings, are presented in the following table. The amount excludes \$330 million and \$192 million as of September 30, 2010 and December 31, 2009, respectively, of net unrealized gains related to changes in valuation of the fixed income securities subsequent to the impairment measurement date.

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(\$ in millions)

	September 30, 2010	December 31, 2009
Municipal	\$ (8)	\$ (10)
Corporate	(48)	(51)
RMBS	(484)	(594)
CMBS	(58)	(127)
ABS	(40)	(89)
Total	\$ (638)	\$ (871)

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Rollforwards of the cumulative credit losses recognized in earnings for fixed income securities held as of the end of the period are as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Beginning balance	\$ (1,309)	\$ (1,506)	\$ (1,187)	\$ --
Beginning balance of cumulative credit loss for securities held at April 1, 2009	--	--	--	(1,357)
Cumulative effect of change in accounting principle	81	--	81	--
Additional credit loss for securities previously other-than-temporarily impaired	(101)	(88)	(265)	(122)
Additional credit loss for securities not previously other-than-temporarily impaired	(9)	(157)	(197)	(315)
Reduction in credit loss for securities disposed or collected	104	396	330	439
Reduction in credit loss for securities other-than-temporarily impaired to fair value	42	--	43	--
Change in credit loss due to accretion of increase in cash flows and time value of cash flows for securities previously other-than-temporarily impaired	1	--	4	--
Ending balance	\$ (1,191)	\$ (1,355)	\$ (1,191)	\$ (1,355)

The Company uses its best estimate of future cash flows expected to be collected from the fixed income security, discounted at the security's original or current effective rate, as appropriate, to calculate a recovery value and determine whether a credit loss exists. The determination of cash flow estimates is inherently subjective and methodologies may vary depending on facts and circumstances specific to the security. All reasonably available information relevant to the collectability of the security, including past events, current conditions, and reasonable and supportable assumptions and forecasts, are considered when developing the estimate of cash flows expected to be collected. That information generally includes, but is not limited to, the remaining payment terms of the security, prepayment speeds, foreign exchange rates, the financial condition and future earnings potential of the issue or issuer, expected defaults, expected recoveries, the value of underlying collateral, vintage, geographic concentration, available reserves or escrows, current subordination levels, third party guarantees and other credit enhancements. Other information, such as industry analyst reports and forecasts, sector credit ratings, financial condition of the bond insurer for insured fixed income securities, and other market data relevant to the realizability of contractual cash flows, may also be considered. The estimated fair value of collateral will be used to estimate recovery value if the Company determines that the security is dependent on the liquidation of collateral for ultimate settlement. If the estimated recovery value is less than the amortized cost of the security, a credit loss exists and an other-than-temporary impairment for the difference between the estimated recovery value and amortized cost is recorded in earnings. The portion of the unrealized loss related to factors other than credit remains classified in accumulated other comprehensive income. If the Company determines that the fixed income security does not have sufficient cash flow or other information to estimate a recovery value for the security, the Company may conclude that the entire decline in fair value is deemed to be credit related and the loss is recorded in earnings.

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Unrealized net capital gains and losses

Unrealized net capital gains and losses included in accumulated other comprehensive income are as follows:

(\$ in millions)		Fair		Gross unrealized		Unrealized net
At September 30, 2010		value		Gains	Losses	gains (losses)
Fixed income securities (1)	\$	83,193	\$	4,847	\$ (2,440)	\$ 2,407
Equity securities		3,707		363	(103)	260
Short-term investments		2,776		--	--	--
Derivative instruments (2)		(12)		2	(19)	(17)
Unrealized net capital gains and losses, pre-tax						2,650
Amounts recognized for:						
Insurance reserves (3)						(608)
DAC and DSI (4)						(49)
Amounts recognized						(657)
Deferred income taxes						(701)
Unrealized net capital gains and losses, after-tax						\$ 1,292

(1) Unrealized net capital gains and losses for fixed income securities as of September 30, 2010 comprises \$(308) million related to unrealized net capital losses on fixed income securities with OTTI and \$2,715 million related to other unrealized net capital gains and losses.

(2) Included in the fair value of derivative instruments are \$2 million classified as assets and \$14 million classified as liabilities.

(3) The insurance reserves adjustment represents the amount by which the reserve balance would increase if the net unrealized gains in the applicable product portfolios were realized and reinvested at current lower interest rates, resulting in a premium deficiency. Although the Company evaluates premium deficiencies on the combined performance of life insurance and immediate annuities with life contingencies, the adjustment primarily relates to structured settlement annuities with life contingencies, in addition to annuity buy-outs and certain payout annuities with life contingencies.

(4) The DAC and DSI adjustment balance represents the amount by which the amortization of DAC and DSI would increase or decrease if the unrealized gains or losses in the respective product portfolios were realized.

		Fair		Gross unrealized		Unrealized net
At December 31, 2009		value		Gains	Losses	gains (losses)
Fixed income securities (1)	\$	78,766	\$	2,477	\$ (4,954)	\$ (2,477)
Equity securities		5,024		381	(202)	179
Short-term investments		3,056		--	--	--
Derivative instruments (2)		(20)		2	(25)	(23)
Unrealized net capital gains and losses, pre-tax						(2,321)
Amounts recognized for:						
Insurance reserves						--

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DAC and DSI	990
Amounts recognized	990
Deferred income taxes	461
Unrealized net capital gains and losses, after-tax	\$ (870)

(1) Unrealized net capital gains and losses for fixed income securities as of December 31, 2009 comprises \$(679) million related to unrealized net capital losses on fixed income securities with OTTI and \$(1,798) million related to other unrealized net capital gains and losses.

(2) Included in the fair value of derivative instruments are \$(2) million classified as assets and \$18 million classified as liabilities.

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Change in unrealized net capital gains and losses

The change in unrealized net capital gains and losses for the nine months ended September 30, 2010 is as follows:

(\$ in millions)

Fixed income securities	\$	4,884
Equity securities		81
Derivative instruments		6
Total		4,971
Amounts recognized for:		
Insurance reserves		(608)
DAC and DSI		(1,039)
Decrease in amounts recognized		(1,647)
Deferred income taxes		(1,162)
Increase in unrealized net capital gains and losses	\$	2,162

Portfolio monitoring

The Company has a comprehensive portfolio monitoring process to identify and evaluate each fixed income and equity security whose carrying value may be other-than-temporarily impaired.

For each fixed income security in an unrealized loss position, the Company assesses whether management with the appropriate authority has made the decision to sell or whether it is more likely than not the Company will be required to sell the security before recovery of the amortized cost basis for reasons such as liquidity, contractual or regulatory purposes. If a security meets either of these criteria, the security's decline in fair value is considered other than temporary and is recorded in earnings.

If the Company has not made the decision to sell the fixed income security and it is not more likely than not the Company will be required to sell the fixed income security before recovery of its amortized cost basis, the Company evaluates whether it expects to receive cash flows sufficient to recover the entire amortized cost basis of the security. The Company calculates the estimated recovery value by discounting the best estimate of future cash flows at the security's original or current effective rate, as appropriate, and compares this to the amortized cost of the security. If the Company does not expect to receive cash flows sufficient to recover the entire amortized cost basis of the fixed income security, the credit loss component of the impairment is recorded in earnings, with the remaining amount of the unrealized loss related to other factors recognized in other comprehensive income.

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For equity securities, the Company considers various factors, including whether it has the intent and ability to hold the equity security for a period of time sufficient to recover its cost basis. Where the Company lacks the intent and ability to hold to recovery, or believes the recovery period is extended, the equity security's decline in fair value is considered other than temporary and is recorded in earnings. For equity securities managed by a third party, the Company has contractually retained its decision making authority as it pertains to selling equity securities that are in an unrealized loss position.

The Company's portfolio monitoring process includes a quarterly review of all securities to identify instances where the fair value of a security compared to its amortized cost (for fixed income securities) or cost (for equity securities) is below established thresholds. The process also includes the monitoring of other impairment indicators such as ratings, ratings downgrades and payment defaults. The securities identified, in addition to other securities for which the Company may have a concern, are evaluated for potential other-than-temporary impairment using all reasonably available information relevant to the collectability or recovery of the security. Inherent in the Company's evaluation of other-than-temporary impairment for these fixed income and equity securities are assumptions and estimates about the financial condition and future earnings potential of the issue or issuer. Some of the factors considered in evaluating whether a decline in fair value is other than temporary are: 1) the financial condition, near-term and long-term prospects of the issue or issuer, including relevant industry specific market conditions and trends, geographic location and implications of rating agency actions and offering prices; 2) the specific reasons that a security is in an unrealized loss position, including overall market conditions which could affect liquidity; and 3) the length of time and extent to which the fair value has been less than amortized cost or cost.

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The following table summarizes the gross unrealized losses and fair value of fixed income and equity securities by the length of time that individual securities have been in a continuous unrealized loss position.

(\$ in millions)	Less than 12 months			12 months or more			Total
	Number of issues	Fair value	Unrealized losses	Number of issues	Fair value	Unrealized losses	unrealized losses
At September 30, 2010							
Fixed income securities							
U.S. government and agencies	6	\$ 633	\$ (1)	--	\$ --	\$ --	(1)
Municipal	84	338	(4)	431	3,003	(397)	(401)
Corporate	82	1,026	(42)	189	2,512	(242)	(284)
Foreign government	1	2	--	2	11	--	--
RMBS	266	358	(5)	370	2,050	(933)	(938)
CMBS	4	31	(1)	144	1,015	(440)	(441)
ABS	50	534	(17)	137	1,249	(358)	(375)
Redeemable preferred stock	--	--	--	1	--	--	--
Total fixed income securities (1)	493	2,922	(70)	1,274	9,840	(2,370)	(2,440)
Equity securities	1,427	992	(92)	11	71	(11)	(103)
Total fixed income and equity securities	1,920	\$ 3,914	\$ (162)	1,285	\$ 9,911	\$ (2,381)	\$ (2,543)
Investment grade fixed income securities	439	\$ 2,621	\$ (58)	868	\$ 7,111	\$ (1,153)	\$ (1,211)
Below investment grade fixed income securities	54	301	(12)	406	2,729	(1,217)	(1,229)
Total fixed income securities	493	\$ 2,922	\$ (70)	1,274	\$ 9,840	\$ (2,370)	\$ (2,440)
At December 31, 2009							
Fixed income securities							
U.S. government and agencies	38	\$ 3,523	\$ (16)	--	\$ --	\$ --	(16)
Municipal	761	3,646	(123)	747	5,024	(817)	(940)
Corporate	399	5,072	(178)	421	5,140	(669)	(847)
Foreign government	50	505	(15)	1	1	--	(15)
RMBS	387	1,092	(23)	453	2,611	(1,607)	(1,630)
CMBS	25	232	(4)	259	1,790	(951)	(955)
ABS	39	352	(20)	173	1,519	(530)	(550)
Redeemable preferred stock	1	--	--	1	21	(1)	(1)
Total fixed income securities (1)	1,700	14,422	(379)	2,055	16,106	(4,575)	(4,954)
Equity securities	1,665	1,349	(113)	28	450	(89)	(202)
Total fixed income and equity securities	3,365	\$ 15,771	\$ (492)	2,083	\$ 16,556	\$ (4,664)	\$ (5,156)
Investment grade fixed income securities	1,587	\$ 13,891	\$ (293)	1,561	\$ 13,127	\$ (2,848)	\$ (3,141)
Below investment grade fixed income securities	113	531	(86)	494	2,979	(1,727)	(1,813)
Total fixed income securities	1,700	\$ 14,422	\$ (379)	2,055	\$ 16,106	\$ (4,575)	\$ (4,954)

(1) Gross unrealized losses resulting from factors other than credit on fixed income securities with other-than-temporary impairments for which the Company has recorded a credit loss in earnings total \$4 million for the less than 12 month category and \$428 million for the 12 months or greater category as of September 30, 2010 and \$20 million for the less than 12 month category and \$729 million for the 12 months or greater category as of December 31, 2009.

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As of September 30, 2010, \$728 million of unrealized losses are related to securities with an unrealized loss position less than 20% of amortized cost or cost, the degree of which suggests that these securities do not pose a high risk of being other-than-temporarily impaired. Of the \$728 million, \$494 million are related to unrealized losses on investment grade fixed income securities. Investment grade is defined as a security having a rating of Aaa, Aa, A or Baa from Moody's, a rating of AAA, AA, A or BBB from Standard & Poor's (S&P), Fitch, Dominion or Realpoint, a rating of aaa, aa, a or bbb from A.M. Best, or a comparable internal rating if an externally provided rating is not available. Unrealized losses on investment grade securities are principally related to widening credit spreads or, in some instances, rising interest rates since the time of initial purchase.

As of September 30, 2010, the remaining \$1.81 billion of unrealized losses are related to securities in unrealized loss positions greater than or equal to 20% of amortized cost or cost. Investment grade securities comprising \$717 million of these unrealized losses were evaluated based on factors such as expected cash flows and the financial condition and near-term and long-term prospects of the issue or issuer and were determined to have adequate

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resources to fulfill contractual obligations. Of the \$1.81 billion, \$1.06 billion are related to below investment grade fixed income securities and \$32 million are related to equity securities. Of these amounts, \$1.03 billion of the below investment grade fixed income securities had been in an unrealized loss position for a period of twelve or more consecutive months as of September 30, 2010. Unrealized losses on below investment grade securities are principally related to RMBS, CMBS and ABS and were the result of wider credit spreads resulting from larger risk premiums since the time of initial purchase, largely due to macroeconomic conditions and credit market deterioration, including the impact of declining residential and commercial real estate valuations.

RMBS, CMBS and ABS securities in an unrealized loss position were evaluated based on actual and projected collateral losses relative to the securities' positions in the respective securitization trusts, security specific expectations of cash flows, and credit ratings. This evaluation also takes into consideration credit enhancement, measured in terms of (i) subordination from other classes of securities in the trust that are contractually obligated to absorb losses before the class of security the Company owns, (ii) the expected impact of other structural features embedded in the securitization trust beneficial to the class of securities the Company owns, such as overcollateralization and excess spread, and (iii) for RMBS and ABS in an unrealized loss position, credit enhancements from reliable bond insurers, where applicable. Municipal bonds in an unrealized loss position were evaluated based on the quality of the underlying securities, taking into consideration credit enhancements from reliable bond insurers, where applicable. Unrealized losses on equity securities are primarily related to equity market fluctuations.

As of September 30, 2010, the Company has not made the decision to sell and it is not more likely than not the Company will be required to sell fixed income securities with unrealized losses before recovery of the amortized cost basis. As of September 30, 2010, the Company had the intent and ability to hold equity securities with unrealized losses for a period of time sufficient for them to recover.

Limited partnership impairment

As of September 30, 2010 and December 31, 2009, the carrying value of equity method limited partnership interests totaled \$2.19 billion and \$1.64 billion, respectively. The Company recognizes an impairment loss for equity method investments when evidence demonstrates that it is other-than-temporarily impaired. Evidence of a loss in value that is other than temporary may include the absence of an ability to recover the carrying amount of the investment or the inability of the investee to sustain a level of earnings that would justify the carrying amount of the investment. The Company had no write-downs related to equity method limited partnership interests for the three months ended September 30, 2010 and 2009. The Company had write-downs related to equity method limited partnership interests of \$1 million and \$10 million for the nine months ended September 30, 2010 and 2009, respectively.

As of September 30, 2010 and December 31, 2009, the carrying value for cost method limited partnership interests was \$1.26 billion and \$1.10 billion, respectively. To determine if an other-than-temporary impairment has occurred, the Company evaluates whether an impairment indicator has occurred in the period that may have a significant adverse effect on the carrying value of the investment. Impairment indicators may include: significantly reduced valuations of the investments held by limited partnerships; actual recent cash flows received being significantly less than expected cash flows; reduced valuations based on financing completed at a lower value; completed sale of a material underlying investment at a price significantly lower than expected; or any other adverse events since the last financial statements received that might affect the fair value of the investee's capital. Additionally, the Company's portfolio monitoring process includes a quarterly review of all cost method limited partnerships to identify instances where the net asset value is below established thresholds for certain periods of time, as

well as investments that are performing below expectations, for further impairment consideration. If a cost method limited partnership is other-than-temporarily impaired, the carrying value is written down to fair value, generally estimated to be equivalent to the reported net asset value of the underlying funds. The Company had write-downs related to cost method investments of \$10 million and \$53 million for the three months ended September 30, 2010 and 2009, respectively, and \$41 million and \$286 million for the nine months ended September 30, 2010 and 2009, respectively.

5. Fair Value of Assets and Liabilities

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The hierarchy for inputs used in

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determining fair value maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available. Assets and liabilities recorded on the Condensed Consolidated Statements of Financial Position at fair value are categorized in the fair value hierarchy based on the observability of inputs to the valuation techniques as follows:

Level 1: Assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Company can access.

Level 2: Assets and liabilities whose values are based on the following:

- (a) Quoted prices for similar assets or liabilities in active markets;
- (b) Quoted prices for identical or similar assets or liabilities in markets that are not active; or
- (c) Valuation models whose inputs are observable, directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. Unobservable inputs reflect the Company's estimates of the assumptions that market participants would use in valuing the assets and liabilities.

The availability of observable inputs varies by instrument. In situations where fair value is based on internally developed pricing models or inputs that are unobservable in the market, the determination of fair value requires more judgment. The degree of judgment exercised by the Company in determining fair value is typically greatest for instruments categorized in Level 3. In many instances, valuation inputs used to measure fair value fall into different levels of the fair value hierarchy. The category level in the fair value hierarchy is determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company uses prices and inputs that are current as of the measurement date, including during periods of market disruption. In periods of market disruption, the ability to observe prices and inputs may be reduced for many instruments.

The Company has two types of situations where investments are classified as Level 3 in the fair value hierarchy. The first is where quotes continue to be received from independent third-party valuation service providers and all significant inputs are market observable; however, there has been a significant decrease in the volume and level of activity for the asset when compared to normal market activity such that the degree of

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market observability has declined to a point where categorization as a Level 3 measurement is considered appropriate. The indicators considered in determining whether a significant decrease in the volume and level of activity for a specific asset has occurred include the level of new issuances in the primary market, trading volume in the secondary market, the level of credit spreads over historical levels, applicable bid-ask spreads, and price consensus among market participants and other pricing sources.

The second situation where the Company classifies securities in Level 3 is where specific inputs significant to the fair value estimation models are not market observable. This occurs in two primary instances. The first relates to the Company's use of broker quotes. The second relates to auction rate securities (ARS) backed by student loans for which a key input, the anticipated date liquidity will return to this market, is not market observable.

Certain assets are not carried at fair value on a recurring basis, including investments such as mortgage loans, limited partnership interests, bank loans and policy loans. Accordingly, such investments are only included in the fair value hierarchy disclosure when the investment is subject to remeasurement at fair value after initial recognition and the resulting remeasurement is reflected in the condensed consolidated financial statements. In addition, derivatives embedded in fixed income securities are not disclosed in the hierarchy as free-standing derivatives since they are presented with the host contracts in fixed income securities. As of September 30, 2010, 74.4% of total assets are measured at fair value and 0.7% of total liabilities are measured at fair value.

In determining fair value, the Company principally uses the market approach which generally utilizes market transaction data for the same or similar instruments. To a lesser extent, the Company uses the income approach which involves determining fair values from discounted cash flow methodologies. For the majority of Level 2 and Level 3 valuations, a combination of the market and income approaches is used.

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Summary of significant valuation techniques for assets and liabilities measured at fair value on a recurring basis

Level 1 measurements

- Fixed income securities: Comprise U.S. Treasuries. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.

- Equity securities: Comprise actively traded, exchange-listed U.S. and international equity securities. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.

- Short-term: Comprise actively traded money market funds that have daily quoted net asset values for identical assets that the Company can access.

- Separate account assets: Comprise actively traded mutual funds that have daily quoted net asset values for identical assets that the Company can access. Net asset values for the actively traded mutual funds in which the separate account assets are invested are obtained daily from the fund managers.

Level 2 measurements

- Fixed income securities:

U.S. government and agencies: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields and credit spreads.

Municipal: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields and credit spreads.

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Corporate, including privately placed: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields and credit spreads. Also included are privately placed securities valued using a discounted cash flow model that is widely accepted in the financial services industry and uses market observable inputs and inputs derived principally from, or corroborated by, observable market data. The primary inputs to the discounted cash flow model include an interest rate yield curve, as well as published credit spreads for similar assets in markets that are not active that incorporate the credit quality and industry sector of the issuer.

Foreign government: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields and credit spreads.

RMBS - U.S. government sponsored entities (U.S. Agency), Prime residential mortgage-backed securities (Prime) and Alt-A residential mortgage-backed securities (Alt-A); ABS - auto and student loans and other: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields, prepayment speeds, collateral performance and credit spreads.

Redeemable preferred stock: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields, underlying stock prices and credit spreads.

CMBS: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields, collateral performance and credit spreads.

- Equity securities: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active.

- Short-term: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields and credit spreads. For certain short-term investments, amortized cost is used as the best estimate of fair value.

- Other investments: Free-standing exchange listed derivatives that are not actively traded are valued based on quoted prices for identical instruments in markets that are not active.

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OTC derivatives, including interest rate swaps, foreign currency swaps, foreign exchange forward contracts, and certain credit default swaps, are valued using models that rely on inputs such as interest rate yield curves, currency rates, and counterparty credit spreads that are observable for substantially the full term of the contract. The valuation techniques underlying the models are widely accepted in the financial services industry and do not involve significant judgment.

- Contractholder funds: Derivatives embedded in certain annuity contracts are valued based on internal models that rely on inputs such as interest rate yield curves and equity index volatility assumptions that are market observable for substantially the full term of the contract. The valuation techniques are widely accepted in the financial services industry and do not include significant judgment.

Level 3 measurements

- Fixed income securities:

Municipal: ARS primarily backed by student loans that have become illiquid due to failures in the auction market are valued using a discounted cash flow model that is widely accepted in the financial services industry and uses significant non-market observable inputs, including estimates of future coupon rates if auction failures continue, maturity assumptions and illiquidity premium. Also included are municipal bonds that are not rated by third party credit rating agencies but are rated by the National Association of Insurance Commissioners (NAIC), and other high-yield municipal bonds. The primary inputs to the valuation of these municipal bonds include quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2 fair value measurements, contractual cash flows, benchmark yields and credit spreads.

Corporate, including privately placed: Primarily valued based on non-binding broker quotes. Also included are equity-indexed notes which are valued using a discounted cash flow model that is widely accepted in the financial services industry and uses significant non-market observable inputs, such as volatility. Other inputs include an interest rate yield curve, as well as published credit spreads for similar assets that incorporate the credit quality and industry sector of the issuer.

RMBS - Subprime residential mortgage-backed securities (Subprime) and Alt-A: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2 fair value measurements, contractual cash flows, benchmark yields, prepayment speeds, collateral performance and credit spreads. Also included are Subprime and Alt-A securities that are valued based on non-binding broker quotes. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, Subprime and certain Alt-A securities are categorized as Level 3.

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Foreign government: Valued based on non-binding broker quotes.

CMBS: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2 fair value measurements, contractual cash flows, benchmark yields, collateral performance and credit spreads. Also included are CMBS that are valued based on non-binding broker quotes. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, certain CMBS are categorized as Level 3.

ABS - Collateralized debt obligations (CDO): Valued based on non-binding broker quotes received from brokers who are familiar with the investments. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, all CDO are categorized as Level 3.

ABS - student loans and other: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2 fair value measurements, contractual cash flows, benchmark yields, prepayment speeds, collateral performance and credit spreads. Also included are ABS that are valued based on non-binding broker quotes. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in

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liquidity that has been experienced in the market for these securities, certain ABS are categorized as Level 3.

- **Other investments:** Certain OTC derivatives, such as interest rate caps and floors, certain credit default swaps and OTC options (including swaptions), are valued using models that are widely accepted in the financial services industry. These are categorized as Level 3 as a result of the significance of non-market observable inputs such as volatility. Other primary inputs include interest rate yield curves and credit spreads.
- **Contractholder funds:** Derivatives embedded in certain annuity contracts are valued internally using models widely accepted in the financial services industry that determine a single best estimate of fair value for the embedded derivatives within a block of contractholder liabilities. The models use stochastically determined cash flows based on the contractual elements of embedded derivatives and other applicable market data. These are categorized as Level 3 as a result of the significance of non-market observable inputs.

Assets and liabilities measured at fair value on a non-recurring basis

Mortgage loans written-down to fair value in connection with recognizing impairments are valued based on the fair value of the underlying collateral. Limited partnership interests written-down to fair value in connection with recognizing other-than-temporary impairments are valued using net asset values.

The following table summarizes the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis as of September 30, 2010:

(\$ in millions)	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Counterparty and cash collateral netting	Balance as of September 30, 2010
Assets					
Fixed income securities:					
U.S. government and agencies	\$ 6,912	\$ 4,341	\$ --		\$ 11,253
Municipal	--	14,624	2,144		16,768
Corporate	--	35,027	2,177		37,204
Foreign government	--	3,428	--		3,428
RMBS	--	6,615	1,884		8,499
CMBS	--	1,127	866		1,993
ABS	--	1,658	2,352		4,010

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Redeemable preferred stock	--	37	1		38
Total fixed income securities	6,912	66,857	9,424		83,193
Equity securities	3,463	179	65		3,707
Short-term investments	253	2,523	--		2,776
Other investments:					
Free-standing derivatives	--	568	11	\$ (263)	316
Separate account assets	8,459	--	--	--	8,459
Other assets	--	--	2	--	2
Total recurring basis assets	19,087	70,127	9,502	(263)	98,453
Non-recurring basis (1)	--	--	95	--	95
Total assets at fair value	\$ 19,087	\$ 70,127	\$ 9,597	\$ (263)	\$ 98,548
% of total assets at fair value	19.4 %	71.2 %	9.7 %	(0.3) %	100.0 %
Liabilities					
Contractholder funds:					
Derivatives embedded in annuity contracts	\$ --	\$ (145)	\$ (142)	--	\$ (287)
Other liabilities:					
Free-standing derivatives	(2)	(652)	(106)	\$ 259	(501)
Total liabilities at fair value	\$ (2)	\$ (797)	\$ (248)	\$ 259	\$ (788)
% of total liabilities at fair value	0.3 %	101.1 %	31.5 %	(32.9) %	100.0 %

(1) Includes \$55 million of mortgage loans, \$34 million of limited partnership interests and \$6 million of other investments written-down to fair value in connection with recognizing other-than-temporary impairments.

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The following table summarizes the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2009:

(\$ in millions)	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Counterparty and cash collateral netting	Balance as of December 31, 2009
Assets					
Fixed income securities:					
U.S. government and agencies	\$ 4,415	\$ 3,121	\$ --		\$ 7,536
Municipal	--	18,574	2,706		21,280
Corporate	--	30,874	2,241		33,115
Foreign government	--	3,177	20		3,197
RMBS	--	6,316	1,671		7,987
CMBS	--	1,182	1,404		2,586
ABS	--	1,025	2,001		3,026
Redeemable preferred stock	--	37	2		39
Total fixed income securities	4,415	64,306	10,045		78,766
Equity securities	4,821	134	69		5,024
Short-term investments	278	2,778	--		3,056
Other investments:					
Free-standing derivatives	--	882	146	\$ (482)	546
Separate account assets	9,072	--	--		9,072
Other assets	--	--	2		2
Total recurring basis assets	18,586	68,100	10,262	(482)	96,466
Non-recurring basis (1)	--	--	235		235
Total assets at fair value	\$ 18,586	\$ 68,100	\$ 10,497	\$ (482)	\$ 96,701
% of total assets at fair value	19.2 %	70.4 %	10.9 %	(0.5) %	100.0 %
Liabilities					
Contractholder funds:					
Derivatives embedded in annuity contracts	\$ --	\$ (217)	\$ (110)		\$ (327)
Other liabilities:					
Free-standing derivatives	(2)	(596)	(91)	\$ 276	(413)
Total liabilities at fair value	\$ (2)	\$ (813)	\$ (201)	\$ 276	\$ (740)
% of total liabilities at fair value	0.3 %	109.9 %	27.1 %	(37.3) %	100.0 %

(1) Includes \$211 million of mortgage loans and \$24 million of limited partnership interests written-down to fair value in connection with recognizing other-than-temporary impairments.

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The following table presents the rollforward of Level 3 assets and liabilities held at fair value on a recurring basis during the three months ended September 30, 2010.

(\$ in millions)	Total realized and unrealized gains (losses) included in:						
	Balance as of June 30, 2010	Net income (1)	OCI on Statement of Financial Position	Purchases, sales, issuances and settlements, net	Transfers into Level 3	Transfers out of Level 3	Balance as of September 30, 2010
Assets							
Fixed income securities:							
Municipal	\$ 2,197	\$ 13	\$ 18	\$ (87)	\$ 5	\$ (2)	\$ 2,144
Corporate	2,225	8	77	(96)	192	(229)	2,177
RMBS	2,010	(102)	206	(230)	--	--	1,884
CMBS	880	(66)	134	(120)	38	--	866
ABS	2,430	18	73	64	--	(233)	2,352
Redeemable preferred stock	1	--	--	--	--	--	1
Total fixed income securities	9,743	(129)	508	(469)	235	(464)	9,424
Equity securities	66	14	--	(15)	--	--	65
Other investments:							
Free-standing derivatives, net	(99)	(10)	--	14	--	--	(95) (2)
Other assets	2	--	--	--	--	--	2
Total recurring Level 3 assets	\$ 9,712	\$ (125)	\$ 508	\$ (470)	\$ 235	\$ (464)	\$ 9,396
Liabilities							
Contractholder funds:							
Derivatives embedded in annuity contracts	\$ (119)	\$ (23)	\$ --	\$ --	\$ --	\$ --	\$ (142)
Total recurring Level 3 liabilities	\$ (119)	\$ (23)	\$ --	\$ --	\$ --	\$ --	\$ (142)

(1) The effect to net income totals \$(148) million and is reported in the Condensed Consolidated Statements of Operations as follows: \$(136) million in realized capital gains and losses, \$11 million in net investment income and \$23 million in life and annuity contract benefits.

(2) Comprises \$11 million of assets and \$106 million of liabilities.

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The following table presents the rollforward of Level 3 assets and liabilities held at fair value on a recurring basis during the nine months ended September 30, 2010.

(\$ in millions)	Total realized and unrealized gains (losses) included in:							Balance as of September 30, 2010
	Balance as of December 31, 2009	Net income (1)	OCI on Statement of Financial Position	Purchases, sales, issuances and settlements, net	Transfers into Level 3	Transfers out of Level 3		
Assets								
Fixed income securities:								
Municipal	\$ 2,706	\$ (34)	\$ 76	\$ (539)	\$ 21	\$ (86)	\$ 2,144	
Corporate	2,241	(29)	178	(62)	355	(506)	2,177	
Foreign government	20	--	--	(20)	--	--	--	
RMBS	1,671	(271)	549	(51)	--	(14)	1,884	
CMBS	1,404	(173)	434	(448)	62	(413)	866	
ABS	2,001	36	172	536	--	(393)	2,352	
Redeemable preferred stock	2	--	--	(1)	--	--	1	
Total fixed income securities	10,045	(471)	1,409	(585)	438	(1,412)	9,424	
Equity securities	69	8	4	(12)	--	(4)	65	
Other investments:								
Free-standing derivatives, net	55	(242)	--	92	--	--	(95) (2)	
Other assets	2	--	--	--	--	--	2	
Total recurring Level 3 assets	\$ 10,171	\$ (705)	\$ 1,413	\$ (505)	\$ 438	\$ (1,416)	\$ 9,396	
Liabilities								
Contractholder funds:								
Derivatives embedded in annuity contracts	\$ (110)	\$ (35)	\$ --	\$ 3	\$ --	\$ --	\$ (142)	
Total recurring Level 3 liabilities	\$ (110)	\$ (35)	\$ --	\$ 3	\$ --	\$ --	\$ (142)	

(1) The effect to net income totals \$(740) million and is reported in the Condensed Consolidated Statements of Operations as follows: \$(767) million in realized capital gains and losses, \$65 million in net investment income, \$3 million in interest credited to contractholder funds and \$35 million in life and annuity contract benefits.

(2) Comprises \$11 million of assets and \$106 million of liabilities.

Transfers between level categorizations may occur due to changes in the availability of market observable inputs, which generally are caused by changes in market conditions such as liquidity, trading volume or bid-ask spreads. Transfers between level categorizations may also occur due to changes in the valuation source. For example, in situations where a fair value quote is not provided by the Company's independent third-party valuation service provider and as a result the price is stale or has been replaced with a broker quote, the security is transferred into Level 3. Transfers in and out of level categorizations are reported as having occurred at the beginning of the quarter in which the transfer occurred. Therefore, for all transfers into Level 3, all realized and changes in unrealized gains and losses in the quarter of transfer are reflected in the Level 3 rollforward table.

There were no transfers between Level 1 and Level 2 during the three and nine months ended September 30, 2010.

During the three and nine months ended September 30, 2010, certain CMBS and ABS were transferred into Level 2 from Level 3 as a result of increased liquidity in the market and the availability of market observable quoted prices for similar assets. When transferring these securities into Level 2, the Company did not change the source of fair value estimates or modify the estimates received from independent third-party valuation service providers or the internal valuation approach. Accordingly, for securities included within this group, there was no change in fair value in conjunction with the transfer resulting in a realized or unrealized gain or loss.

Transfers into Level 3 during the three and nine months ended September 30, 2010, including those related to Corporate fixed income securities, included situations where a fair value quote was not provided by the Company's independent third-party valuation service provider and as a result the price was stale or had been replaced with a

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broker quote resulting in the security being classified as Level 3. Transfers out of Level 3 during the three and nine months ended September 30, 2010, including those related to Corporate fixed income securities, included situations where a broker quote was used in the prior period and a fair value quote became available from the Company's independent third-party valuation service provider in the current period. A quote utilizing the new pricing source was not available as of the prior period, and any gains or losses related to the change in valuation source for individual securities were not significant.

The following table provides the total gains and (losses) included in net income during the period for Level 3 assets and liabilities still held at September 30, 2010.

(\$ in millions)	Three months ended September 30, 2010		Nine months ended September 30, 2010	
Assets				
Fixed income securities:				
Municipal	\$	1	\$	(24)
Corporate		(1)		(42)
RMBS		(83)		(214)
CMBS		(22)		(42)
ABS		28		53
Total fixed income securities		(77)		(269)
Equity securities		(1)		(8)
Other investments:				
Free-standing derivatives, net		28		(113)
Total recurring Level 3 assets	\$	(50)	\$	(390)
Liabilities				
Contractholder funds:				
Derivatives embedded in annuity contracts	\$	(23)	\$	(35)
Total recurring Level 3 liabilities	\$	(23)	\$	(35)

The amounts in the table above represent gains and losses included in net income during the period presented for the period of time that the asset or liability was determined to be in Level 3. These gains and losses total \$(73) million for the three months ended September 30, 2010 and are reported in the Condensed Consolidated Statements of Operations as follows: \$(57) million in realized capital gains and losses, \$6 million in net investment income, \$(1) million in interest credited to contractholder funds and \$23 million in life and annuity contract benefits. These gains and losses total \$(425) million for the nine months ended September 30, 2010 and are reported in the Condensed Consolidated Statements of Operations as follows: \$(426) million in realized capital gains and losses, \$41 million in net investment income, \$5 million in interest credited to contractholder funds and \$35 million in life and annuity contract benefits.

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The following table presents the rollforward of Level 3 assets and liabilities held at fair value on a recurring basis during the three months ended September 30, 2009.

(\$ in millions)

	Total realized and unrealized gains (losses) included in:					Total gains (losses) included in net income for financial instruments still held at September 30, 2009 (3)	
	Balance as of June 30, 2009	Net income (1)	OCI on Statement of Financial Position	Purchases, sales, issuances and settlements, net	Net transfers in and/or (out) of Level 3	Balance as of September 30, 2009	
Assets							
Fixed income securities:							
Municipal	\$ 2,513	\$ (1)	\$ 131	\$ (72)	\$ 136	\$ 2,707	\$ --
Corporate	9,837	2	559	(370)	(50)	9,978	(10)
Foreign government	--	--	--	80	--	80	--
RMBS	2,377	(46)	267	(150)	(738)	1,710	(51)
CMBS	944	(57)	420	(56)	136	1,387	(17)
ABS	1,728	(6)	388	(2)	(333)	1,775	(38)
Redeemable preferred stock	2	--	--	--	--	2	--
Total fixed income securities	17,401	(108)	1,765	(570)	(849)	17,639	(116)
Equity securities	70	--	(2)	--	--	68	--
Other investments:							
Free-standing derivatives, net	159	(151)	--	(16)	--	(8) (2)	(128)
Other assets	2	--	--	--	--	2	--
Total recurring Level 3 assets	\$ 17,632	\$ (259)	\$ 1,763	\$ (586)	\$ (849)	\$ 17,701	\$ (244)
Liabilities							
Contractholder funds:							
Derivatives embedded in annuity contracts	\$ (155)	\$ 36	\$ --	\$ (1)	\$ --	\$ (120)	\$ 36
Total recurring Level 3 liabilities	\$ (155)	\$ 36	\$ --	\$ (1)	\$ --	\$ (120)	\$ 36

(1) The effect to net income totals \$(223) million and is reported in the Condensed Consolidated Statements of Operations as follows: \$(273) million in realized capital gains and losses, \$13 million in net investment income, \$(1) million in interest credited to contractholder funds and \$(36) million in life and annuity contract benefits.

(2) Comprises \$96 million of assets and \$104 million of liabilities.

(3) The amounts represent gains and losses included in net income for the period of time that the asset or liability was determined to be in Level 3. These gains and losses total \$(208) million and are reported in the Condensed Consolidated Statements of Operations as follows: \$(257) million in realized capital gains and losses, \$11 million in net investment income, \$(2) million in interest credited to contractholder funds, and \$(36) million in life and annuity contract benefits.

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The following table presents the rollforward of Level 3 assets and liabilities held at fair value on a recurring basis during the nine months ended September 30, 2009.

(\$ in millions)	Total realized and unrealized gains (losses) included in:						Total gains (losses) included in net income for financial instruments still held at September 30, 2009 (3)
	Balance as of December 31, 2008	Net income (1)	OCI on Statement of Financial Position	Purchases, sales, issuances and settlements, net	Net transfers in and/or (out) of Level 3	Balance as of September 30, 2009	
Assets							
Fixed income securities:							
Municipal	\$ 2,463	\$ (4)	\$ 192	\$ (107)	\$ 163	\$ 2,707	\$ (5)
Corporate	10,195	(50)	1,197	(1,250)	(114)	9,978	(53)
Foreign government	--	--	--	80	--	80	--
RMBS	2,988	(105)	58	(293)	(938)	1,710	(84)
CMBS	457	(163)	592	(60)	561	1,387	(131)
ABS	1,714	(172)	676	7	(450)	1,775	(171)
Redeemable preferred stock	2	--	--	--	--	2	--
Total fixed income securities	17,819	(494)	2,715	(1,623)	(778)	17,639	(444)
Equity securities	74	--	(6)	3	(3)	68	--
Other investments:							
Free-standing derivatives, net	(101)	68	--	25	--	(8) (2)	126
Other assets	1	1	--	--	--	2	1
Total recurring Level 3 assets	\$ 17,793	\$ (425)	\$ 2,709	\$ (1,595)	\$ (781)	\$ 17,701	\$ (317)
Liabilities							
Contractholder funds:							
Derivatives embedded in annuity contracts	\$ (265)	\$ 141	\$ --	\$ 4	\$ --	\$ (120)	\$ 141
Total recurring Level 3 liabilities	\$ (265)	\$ 141	\$ --	\$ 4	\$ --	\$ (120)	\$ 141

(1) The effect to net income totals \$(284) million and is reported in the Condensed Consolidated Statements of Operations as follows: \$(503) million in realized capital gains and losses, \$78 million in net investment income, and \$(141) million in life and annuity contract benefits.

(2) Comprises \$96 million of assets and \$104 million of liabilities.

(3) The amounts represent gains and losses included in net income for the period of time that the asset or liability was determined to be in Level 3. These gains and losses total \$(176) million and are reported in the Condensed Consolidated Statements of Operations as follows: \$(385) million in realized capital gains and losses, \$65 million in net investment income, \$(3) million in interest credited to contractholder funds, and \$(141) million in life and annuity contract benefits.

Presented below are the carrying values and fair value estimates of financial instruments not carried at fair value on a recurring basis.

Financial assets

(\$ in millions)	September 30, 2010		December 31, 2009	
	Carrying value	Fair value	Carrying value	Fair value
Mortgage loans	\$ 6,961	\$ 6,372	\$ 7,935	\$ 6,336
Limited partnership interests - cost basis	1,261	1,334	1,103	1,098
Bank loans	341	325	420	391

The fair value of mortgage loans is based on discounted contractual cash flows or, if the loans are impaired due to credit reasons, the fair value of collateral less costs to sell. Risk adjusted discount rates are selected using current rates at which similar loans would be made to borrowers with similar characteristics, using similar types of properties as collateral. The fair value of limited partnership interests accounted for on the cost basis is determined using reported net asset values of the underlying funds. The fair value of bank loans, which are reported in other investments on the Condensed Consolidated Statements of Financial Position, are valued based on broker quotes from brokers familiar with the loans and current market conditions.

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Financial liabilities

(\$ in millions)	September 30, 2010		December 31, 2009	
	Carrying value	Fair value	Carrying value	Fair value
Contractholder funds on investment contracts	\$ 36,927	\$ 36,859	\$ 40,943	\$ 39,328
Long-term debt	5,909	6,417	5,910	6,016
Liability for collateral	469	469	658	658

The fair value of contractholder funds on investment contracts is based on the terms of the underlying contracts utilizing prevailing market rates for similar contracts adjusted for the Company's own credit risk. Deferred annuities included in contractholder funds are valued using discounted cash flow models which incorporate market value margins, which are based on the cost of holding economic capital, and the Company's own credit risk. Immediate annuities without life contingencies and fixed rate funding agreements are valued at the present value of future benefits using market implied interest rates which include the Company's own credit risk.

The fair value of long-term debt is based on market observable data (such as the fair value of the debt when traded as an asset) or, in certain cases, is determined using discounted cash flow calculations based on current interest rates for instruments with comparable terms and considers the Company's own credit risk. The liability for collateral is valued at carrying value due to its short-term nature.

6. Derivative Financial Instruments

The Company primarily uses derivatives for risk management, to partially mitigate potential adverse impacts from changes in risk-free interest rates, negative equity market valuations and increases in credit spreads, and asset replication. In addition, the Company has derivatives embedded in non-derivative host contracts that are required to be separated from the host contracts and accounted for at fair value. With the exception of non-hedge derivatives used for asset replication and non-hedge embedded derivatives, all of the Company's derivatives are evaluated for their ongoing effectiveness as either accounting hedge or non-hedge derivative financial instruments on at least a quarterly basis. The Company does not use derivatives for trading purposes. Non-hedge accounting is generally used for portfolio level hedging strategies where the terms of the individual hedged items do not meet the strict homogeneity requirements to permit the application of hedge accounting.

Property-Liability uses interest rate swaption contracts and exchange traded options on interest rate futures to offset potential declining fixed income market values resulting from potential rising interest rates. Property-Liability also uses interest rate swaps to mitigate municipal bond interest rate risk within the municipal bond portfolio. Exchange traded equity put options are utilized by Property-Liability for overall equity portfolio protection from significant declines in equity market values below a targeted level. Equity index futures are used by Property-Liability to offset valuation losses in the equity portfolio during periods of declining equity market values. Credit default swaps are typically used to mitigate the credit risk within the Property-Liability fixed income portfolio.

Portfolio duration management is a risk management strategy that is principally employed by Property-Liability wherein, depending on the current portfolio duration relative to a designated target and the expectations of future interest rate movements, financial futures and interest rate swaps are utilized to change the duration of the portfolio in order to offset the economic effect that interest rates would otherwise have on the fair value of its fixed income securities.

Property-Liability uses futures to hedge the market risk related to deferred compensation liability contracts and forward contracts to hedge foreign currency risk associated with holding foreign currency denominated investments and foreign operations.

Allstate Financial uses foreign currency swaps primarily to reduce the foreign currency risk associated with issuing foreign currency denominated funding agreements and holding foreign currency denominated investments. Credit default swaps are also typically used to mitigate the credit risk within the Allstate Financial fixed income portfolio.

Asset-liability management is a risk management strategy that is principally employed by Allstate Financial to balance the respective interest-rate sensitivities of its assets and liabilities. Depending upon the attributes of the

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assets acquired and liabilities issued, derivative instruments such as interest rate swaps, caps, floors, swaptions and futures are utilized to change the interest rate characteristics of existing assets and liabilities to ensure the relationship is maintained within specified ranges and to reduce exposure to rising or falling interest rates. Allstate Financial uses financial futures and interest rate swaps to hedge anticipated asset purchases and liability issuances and futures and options for hedging the equity exposure contained in its equity indexed annuity product contracts that offer equity returns to contractholders. In addition, Allstate Financial uses interest rate swaps to hedge interest rate risk inherent in funding agreements.

When derivatives meet specific criteria, they may be designated as accounting hedges and accounted for as fair value, cash flow, foreign currency fair value or foreign currency cash flow hedges. Allstate Financial designates certain of its interest rate and foreign currency swap contracts and certain investment risk transfer reinsurance agreements as fair value hedges when the hedging instrument is highly effective in offsetting the risk of changes in the fair value of the hedged item. Allstate Financial designates certain of its foreign currency swap contracts as cash flow hedges when the hedging instrument is highly effective in offsetting the exposure of variations in cash flows for the hedged risk that could affect net income. Amounts are reclassified to net investment income or realized capital gains and losses as the hedged item affects net income.

Asset replication refers to the synthetic creation of assets through the use of derivatives and primarily investment grade host bonds to replicate securities that are either unavailable in the cash markets or more economical to acquire in synthetic form. The Company replicates fixed income securities using a combination of a credit default swap and one or more highly rated fixed income securities to synthetically replicate the economic characteristics of one or more cash market securities. The Company also creates synthetic exposure to equity markets through the use of exchange traded equity index future contracts and an investment grade host bond.

The Company's primary embedded derivatives are conversion options in fixed income securities, which provide the Company with the right to convert the instrument into a predetermined number of shares of common stock; equity options in Allstate Financial annuity product contracts, which provide equity returns to contractholders; equity-indexed notes containing equity call options, which provide a coupon payout that is determined using one or more equity-based indices; and credit default swaps in synthetic collateralized debt obligations, which provide enhanced coupon rates as a result of selling credit protection.

The notional amounts specified in the contracts are used to calculate the exchange of contractual payments under the agreements and are generally not representative of the potential for gain or loss on these agreements. However, the notional amounts specified in credit default swaps where the Company has sold credit protection represent the maximum amount of potential loss, assuming no recoveries.

Fair value, which is equal to the carrying value, is the estimated amount that the Company would receive or pay to terminate the derivative contracts at the reporting date. The carrying value amounts for OTC derivatives are further adjusted for the effects, if any, of legally enforceable master netting agreements and are presented on a net basis, by counterparty agreement, in the Condensed Consolidated Statements of Financial Position. For certain exchange traded derivatives, the exchange requires margin deposits as well as daily cash settlements of margin accounts. As of September 30, 2010, the Company pledged \$71 million of securities and cash in the form of margin deposits.

For those derivatives which qualify for fair value hedge accounting, net income includes the changes in the fair value of both the derivative instrument and the hedged risk, and therefore reflects any hedging ineffectiveness. For cash flow hedges, gains and losses are amortized from accumulated other comprehensive income and are reported in net income in the same period the forecasted transactions being hedged impact net income. For embedded derivatives in fixed income securities, net income includes the change in fair value of the embedded derivative and accretion income related to the host instrument. For non-hedge derivatives, net income includes changes in fair value and accrued periodic settlements, when applicable.

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The following table provides a summary of the volume and fair value positions of derivative instruments as well as their reporting location in the Condensed Consolidated Statements of Financial Position at September 30, 2010.

(\$ in millions, except number of contracts)

	Balance sheet location	Asset derivatives					
		Notional amount	Volume (1)	Fair value, net	Gross asset	Gross liability	
			Number of contracts				
Derivatives designated as accounting hedging instruments							
Interest rate swap agreements	Other investments	\$ 35	n/a	\$ (2)	\$ --	\$ (2)	
Foreign currency swap agreements	Other investments	41	n/a	2	3	(1)	
Total		\$ 76	n/a	\$ --	\$ 3	\$ (3)	
Derivatives not designated as accounting hedging instruments							
Interest rate contracts							
Interest rate swap agreements	Other investments	\$ 574	n/a	\$ 58	\$ 60	\$ (2)	
Interest rate cap and floor agreements	Other investments	61	n/a	--	--	--	
Financial futures contracts and options	Other investments	n/a	2,600	--	--	--	
Financial futures contracts and options	Other assets	n/a	16,040	--	--	--	
Equity and index contracts							
Options, futures and warrants (2)	Other investments	66	43,050	258	258	--	
Options, futures and warrants	Other assets	n/a	1,456	--	--	--	
Foreign currency contracts							
Foreign currency swap agreements	Other investments	40	n/a	--	--	--	
Foreign currency forwards and options	Other investments	77	n/a	--	1	(1)	
Embedded derivative financial instruments							
Conversion options	Fixed income securities	852	n/a	204	206	(2)	
Equity-indexed call options	Fixed income securities	325	n/a	47	47	--	
Credit default swaps	Fixed income securities	181	n/a	(102)	--	(102)	
Other embedded derivative financial instruments	Other investments	1,000	n/a	2	2	--	
Credit default contracts							
Credit default swaps - buying protection	Other investments	146	n/a	--	1	(1)	
Other contracts							
Other contracts	Other investments	13	n/a	--	--	--	
Other contracts	Other assets	5	n/a	2	2	--	
Total		\$ 3,340	63,146	\$ 469	\$ 577	\$ (108)	
Total derivative assets		\$ 3,416	63,146	\$ 469	\$ 580	\$ (111)	

(1) Volume for OTC derivative contracts is represented by their notional amounts. Volume for exchange traded derivatives is represented by the number of contracts, which is the basis on which they are traded. (n/a = not applicable)

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(2) In addition to the number of contracts presented in the table, the Company held 1,432,065 stock warrants. Stock warrants can be converted to cash upon sale of those instruments or exercised for shares of common stock.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

		Liability derivatives					Gross asset	Gross liability
		Balance sheet location	Volume (1)		Fair value, net			
			Notional amount	Number of contracts				
Derivatives designated as accounting hedging instruments								
Interest rate swap agreements		Other liabilities & accrued expenses	\$ 3,621	n/a	\$ (255)	\$ 26	\$ (281)	
Interest rate swap agreements		Contractholder funds	--	n/a	7	7	--	
Foreign currency swap agreements		Other liabilities & accrued expenses	161	n/a	(14)	1	(15)	
Foreign currency and interest rate swap agreements		Other liabilities & accrued expenses	435	n/a	44	44	--	
Foreign currency and interest rate swap agreements		Contractholder funds	--	n/a	20	20	--	
Total			\$ 4,217	n/a	\$ (198)	\$ 98	\$ (296)	
Derivatives not designated as accounting hedging instruments								
Interest rate contracts								
Interest rate swap agreements		Other liabilities & accrued expenses	\$ 5,769	n/a	\$ (70)	\$ 132	\$ (202)	
Interest rate swaption agreements		Other liabilities & accrued expenses	8,750	n/a	8	8	--	
Interest rate cap and floor agreements		Other liabilities & accrued expenses	3,514	n/a	(32)	1	(33)	
Financial futures contracts and options		Other liabilities & accrued expenses	n/a	7,130	--	--	--	
Equity and index contracts								
Options and futures		Other liabilities & accrued expenses	57	25,184	(110)	1	(111)	
Foreign currency contracts								
Foreign currency swap agreements		Other liabilities & accrued expenses	50	n/a	3	3	--	
Foreign currency forwards and options		Other liabilities & accrued expenses	682	n/a	(13)	2	(15)	
Embedded derivative financial instruments								
Guaranteed accumulation benefits		Contractholder funds	1,019	n/a	(87)	--	(87)	
Guaranteed withdrawal benefits		Contractholder funds	720	n/a	(51)	--	(51)	
Equity-indexed options in life and annuity product contracts		Contractholder funds	4,165	n/a	(145)	--	(145)	
Other embedded derivative financial instruments		Contractholder funds	85	n/a	(4)	--	(4)	
Credit default contracts								
Credit default swaps buying protection		Other liabilities & accrued expenses	1,661	n/a	(3)	9	(12)	
Credit default swaps selling protection		Other liabilities & accrued expenses	707	n/a	(82)	2	(84)	
Total			\$ 27,179	32,314	\$ (586)	\$ 158	\$ (744)	
Total derivative liabilities			\$ 31,396	32,314	\$ (784)	\$ 256	\$ (1,040)	
Total derivatives			\$ 34,812	95,460	\$ (315)			

(1) Volume for OTC derivative contracts is represented by their notional amounts. Volume for exchange traded derivatives is represented by the number of contracts, which is the basis on which they are traded. (n/a = not applicable)

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The following table provides a summary of the volume and fair value positions of derivative instruments as well as their reporting location in the Consolidated Statements of Financial Position at December 31, 2009.

(\$ in millions, except number of contracts)

(\$ in millions, except number of contracts)		Asset derivatives					
		Balance sheet location	Notional amount	Volume (1)	Fair value, net	Gross asset	Gross liability
Number of contracts							
Derivatives designated as accounting hedging instruments							
Interest rate swap agreements	Other investments	\$ 45	n/a	\$ (3)	\$	\$ (3)	
Foreign currency swap agreements	Other investments	23	n/a	(2)		(2)	
Total		\$ 68	n/a	\$ (5)	\$	\$ (5)	
Derivatives not designated as accounting hedging instruments							
Interest rate contracts							
Interest rate swap agreements	Other investments	\$ 1,206	n/a	\$ 49	\$ 62	\$ (13)	
Interest rate swaption agreements	Other investments	8,500	n/a	95	95		
Interest rate cap and floor agreements	Other investments	52	n/a	2	2		
Financial futures contracts and options	Other investments	n/a	30,000	12	12		
Financial futures contracts and options	Other assets	n/a	404				
Equity and index contracts							
Options, futures and warrants (2)	Other investments	62	43,850	435	435		
Options, futures and warrants	Other assets	n/a	102				
Foreign currency contracts							
Foreign currency swap agreements	Other investments	53	n/a	1	1		
Foreign currency forwards and options	Other investments	476	n/a	5	8	(3)	
Embedded derivative financial instruments							
Conversion options	Fixed income securities	936	n/a	312	316	(4)	
Equity-indexed call options	Fixed income securities	475	n/a	89	89		
Other embedded derivative financial instruments	Other investments	1,000	n/a	2	2		
Credit default contracts							
Credit default swaps buying protection	Other investments	329	n/a	(6)	2	(8)	
Credit default swaps selling protection	Other investments	93	n/a	(8)	2	(10)	
Other contracts							
Other contracts	Other investments	75	n/a				
Other contracts	Other assets	6	n/a	2	2		
Total		\$ 13,263	74,356	\$ 990	\$ 1,028	\$ (38)	
Total derivative assets		\$ 13,331	74,356	\$ 985	\$ 1,028	\$ (43)	

(1) Volume for OTC derivative contracts is represented by their notional amounts. Volume for exchange traded derivatives is represented by the number of contracts, which is the basis on which they are traded. (n/a = not applicable)

(2) In addition to the number of contracts presented in the table, the Company held 101,255 stock rights and 1,352,432 stock warrants. Stock rights and stock warrants can be converted to cash upon sale of those instruments or exercised for shares of common stock.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

		Liability derivatives					
		Volume (1)		Fair value, net	Gross asset	Gross liability	
Balance sheet location		Notional amount	Number of contracts				
Derivatives designated as accounting hedging instruments							
Interest rate swap agreements	Other liabilities & accrued expenses	\$ 2,443	n/a	\$ (230)	\$ --	\$ (230)	
Foreign currency swap agreements	Other liabilities & accrued expenses	179	n/a	(18)	3	(21)	
Foreign currency and interest rate swap agreements	Other liabilities & accrued expenses	870	n/a	231	231	--	
Foreign currency and interest rate swap agreements	Contractholder funds	--	n/a	44	44	--	
Total		\$ 3,492	n/a	\$ 27	\$ 278	\$ (251)	
Derivatives not designated as accounting hedging instruments							
Interest rate contracts							
Interest rate swap agreements	Other liabilities & accrued expenses	\$ 6,187	n/a	\$ 28	\$ 68	\$ (40)	
Interest rate swaption agreements	Other liabilities & accrued expenses	2,000	n/a	34	34	--	
Interest rate cap and floor agreements	Other liabilities & accrued expenses	3,896	n/a	(16)	9	(25)	
Equity and index contracts							
Options, futures and warrants	Other liabilities & accrued expenses	45	21,098	(214)	3	(217)	
Foreign currency contracts							
Foreign currency swap agreements	Other liabilities & accrued expenses	54	n/a	3	3	--	
Foreign currency forwards and options	Other liabilities & accrued expenses	185	n/a	2	2	--	
Embedded derivative financial instruments							
Guaranteed accumulation benefits	Contractholder funds	1,113	n/a	(66)	--	(66)	
Guaranteed withdrawal benefits	Contractholder funds	810	n/a	(41)	--	(41)	
Equity-indexed options in life and annuity product contracts	Contractholder funds	4,321	n/a	(217)	--	(217)	
Other embedded derivative financial instruments	Contractholder funds	85	n/a	(3)	--	(3)	
Credit default contracts							
Credit default swaps	buying protection	839	n/a	(40)	5	(45)	
Credit default swaps	selling protection	1,195	n/a	(65)	7	(72)	
Total		\$ 20,730	21,098	\$ (595)	\$ 131	\$ (726)	
Total derivative liabilities		\$ 24,222	21,098	\$ (568)	\$ 409	\$ (977)	
Total derivatives		\$ 37,553	95,454	\$ 417			

(1) Volume for OTC derivative contracts is represented by their notional amounts. Volume for exchange traded derivatives is represented by the number of contracts, which is the basis on which they are traded. (n/a = not applicable)

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The following table provides a summary of the impacts of the Company's foreign currency contracts in cash flow hedging relationships in the Condensed Consolidated Statements of Operations and the Condensed Consolidated Statements of Financial Position. Amortization of net gains from accumulated other comprehensive income related to cash flow hedges is expected to be \$2 million during the next twelve months.

(\$ in millions)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Effective portion				
(Loss) gain recognized in OCI on derivatives during the period	\$ (19)	\$ (12)	\$ 9	\$ (36)
Loss recognized in OCI on derivatives during the term of the hedging relationship	(17)	(24)	(17)	(24)
Gain reclassified from AOCI into income (net investment income)	--	1	1	2
(Loss) gain reclassified from AOCI into income (realized capital gains and losses)	--	(2)	2	(1)
Ineffective portion and amount excluded from effectiveness testing				
Gain recognized in income on derivatives (realized capital gains and losses)	--	--	--	--

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

The following tables present gains and losses from valuation, settlements and hedge ineffectiveness reported on derivatives used in fair value hedging relationships and derivatives not designated as accounting hedging instruments in the Condensed Consolidated Statements of Operations.

(\$ in millions)

Three months ended September 30, 2010

	Net investment income	Realized capital gains and losses	Life and annuity contract benefits	Interest credited to contractholder funds	Operating costs and expenses	Total gain (loss) recognized in net income on derivatives
Derivatives in fair value accounting hedging relationships						
Interest rate contracts	\$ (57)	\$ 2	\$ --	\$ 9	\$ --	\$ (46)
Foreign currency and interest rate contracts	--	--	--	25	--	25
Subtotal	(57)	2	--	34	--	(21)
Derivatives not designated as accounting hedging instruments						
Interest rate contracts	--	(183)	--	--	--	(183)
Equity and index contracts	--	(115)	--	70	13	(32)
Embedded derivative financial instruments	--	48	(22)	(39)	--	(13)
Foreign currency contracts	--	(41)	--	--	4	(37)
Credit default contracts	--	5	--	--	--	5
Other contracts	--	(1)	--	1	--	--
Subtotal	--	(287)	(22)	32	17	(260)
Total	\$ (57)	\$ (285)	\$ (22)	\$ 66	\$ 17	\$ (281)

Nine months ended September 30, 2010

	Net investment income	Realized capital gains and losses	Life and annuity contract benefits	Interest credited to contractholder funds	Operating costs and expenses	Total gain (loss) recognized in net income on derivatives
Derivatives in fair value accounting hedging relationships						
Interest rate contracts	\$ (170)	\$ 4	\$ --	\$ 21	\$ --	\$ (145)
Foreign currency and interest rate contracts	--	(1)	--	(15)	--	(16)
Subtotal	(170)	3	--	6	--	(161)
Derivatives not designated as accounting hedging instruments						
Interest rate contracts	--	(621)	--	--	--	(621)
Equity and index contracts	--	(72)	--	34	5	(33)
Embedded derivative financial instruments	--	(71)	(30)	71	--	(30)
Foreign currency contracts	--	(21)	--	--	(2)	(23)

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Credit default contracts	--	2	--	--	--	2
Other contracts	--	--	--	3	--	3
Subtotal	--	(783)	(30)	108	3	(702)
Total	\$ (170)	\$ (780)	\$ (30)	\$ 114	\$ 3	\$ (863)

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Three months ended September 30, 2009

	Net investment income	Realized capital gains and losses	Life and annuity contract benefits	Interest credited to contractholder funds	Operating costs and expenses	Total gain (loss) recognized in net income on derivatives
Derivatives in fair value accounting hedging relationships						
Interest rate contracts	\$ (55)	\$ --	\$ --	\$ --	\$ --	\$ (55)
Foreign currency and interest rate contracts	--	(3)	--	12	--	9
Subtotal	(55)	(3)	--	12	--	(46)
Derivatives not designated as accounting hedging instruments						
Interest rate contracts	--	(398)	--	--	--	(398)
Equity and index contracts	--	(47)	--	68	16	37
Embedded derivative financial instruments	--	88	36	(100)	--	24
Foreign currency contracts	--	4	--	--	3	7
Credit default contracts	--	(6)	--	--	--	(6)
Other contracts	--	--	--	2	--	2
Subtotal	--	(359)	36	(30)	19	(334)
Total	\$ (55)	\$ (362)	\$ 36	\$ (18)	\$ 19	\$ (380)

Nine months ended September 30, 2009

	Net investment income	Realized capital gains and losses	Life and annuity contract benefits	Interest credited to contractholder funds	Operating costs and expenses	Total gain (loss) recognized in net income on derivatives
Derivatives in fair value accounting hedging relationships						
Interest rate contracts	\$ 23	\$ 10	\$ --	\$ (13)	\$ --	\$ 20
Foreign currency and interest rate contracts	--	(6)	--	72	--	66
Subtotal	23	4	--	59	--	86
Derivatives not designated as accounting hedging instruments						
Interest rate contracts	--	181	--	--	--	181
Equity and index contracts	--	(132)	--	77	19	(36)
Embedded derivative financial instruments	--	117	146	(185)	--	78
Foreign currency contracts	--	(2)	--	--	(9)	(11)
Credit default contracts	--	(16)	--	--	--	(16)
Other contracts	(1)	--	--	1	--	--
Subtotal	(1)	148	146	(107)	10	196
Total	\$ 22	\$ 152	\$ 146	\$ (48)	\$ 10	\$ 282

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The following tables provide a summary of the changes in fair value of the Company's fair value hedging relationships in the Condensed Consolidated Statements of Operations.

(\$ in millions)

Location of gain or (loss) recognized in net income on derivatives	Three months ended September 30, 2010			
	Gain (loss) on derivatives		Gain (loss) on hedged risk	
	Interest rate contracts	Foreign currency & interest rate contracts	Contractholder funds	Investments
Interest credited to contractholder funds	\$ 6	\$ 18	\$ (24)	\$ --
Net investment income	(32)	--	--	32
Realized capital gains and losses	2	--	--	--
Total	\$ (24)	\$ 18	\$ (24)	\$ 32

Location of gain or (loss) recognized in net income on derivatives	Nine months ended September 30, 2010			
	Gain (loss) on derivatives		Gain (loss) on hedged risk	
	Interest rate contracts	Foreign currency & interest rate contracts	Contractholder funds	Investments
Interest credited to contractholder funds	\$ 14	\$ (39)	\$ 25	\$ --
Net investment income	(88)	--	--	88
Realized capital gains and losses	4	(1)	--	--
Total	\$ (70)	\$ (40)	\$ 25	\$ 88

Location of gain or (loss) recognized in net income on derivatives	Three months ended September 30, 2009			
	Gain (loss) on derivatives		Gain (loss) on hedged risk	
	Interest rate contracts	Foreign currency & interest rate contracts	Contractholder funds	Investments
Interest credited to contractholder funds	\$ --	\$ 1	\$ (1)	\$ --
Net investment income	(21)	--	--	21
Realized capital gains and losses	--	(3)	--	--
Total	\$ (21)	\$ (2)	\$ (1)	\$ 21

Location of gain or (loss) recognized in net income on derivatives	Nine months ended September 30, 2009			
	Gain (loss) on derivatives		Gain (loss) on hedged risk	
	Interest rate contracts	Foreign currency & interest rate contracts	Contractholder funds	Investments
Interest credited to contractholder funds	\$ (26)	\$ 45	\$ (19)	\$ --
Net investment income	124	--	--	(124)

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Realized capital gains and losses		10		(6)		--		--
Total	\$	108	\$	39	\$	(19)	\$	(124)

The Company manages its exposure to credit risk by utilizing highly rated counterparties, establishing risk control limits, executing legally enforceable master netting agreements (MNAs) and obtaining collateral where appropriate. The Company uses MNAs for OTC derivative transactions, including interest rate swap, foreign currency swap, interest rate cap, interest rate floor, credit default swap, forward and certain option agreements (including swaptions). These agreements permit either party to net payments due for transactions covered by the agreements. Under the provisions of the agreements, collateral is either pledged or obtained when certain predetermined exposure limits are exceeded. As of September 30, 2010, counterparties pledged \$4 million in cash and \$13 million in securities to the Company, and the Company pledged \$364 million in securities to counterparties which includes \$275 million of collateral posted under MNAs for contracts containing credit-risk-contingent provisions that are in a liability position and \$89 million of collateral posted under MNAs for contracts without credit-risk-contingent liabilities. The Company has not incurred any losses on derivative financial instruments due to counterparty nonperformance. Other derivatives, including futures and certain option contracts, are traded on

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organized exchanges which require margin deposits and guarantee the execution of trades, thereby mitigating any potential credit risk.

Counterparty credit exposure represents the Company's potential loss if all of the counterparties concurrently fail to perform under the contractual terms of the contracts and all collateral, if any, becomes worthless. This exposure is measured by the fair value of OTC derivative contracts with a positive fair value at the reporting date reduced by the effect, if any, of legally enforceable master netting agreements.

The following table summarizes the counterparty credit exposure by counterparty credit rating as it relates to interest rate swap, foreign currency swap, interest rate cap, interest rate floor, free-standing credit default swap, forward and certain option agreements (including swaptions).

(\$ in millions)		September 30, 2010			December 31, 2009				
	Number of counterparties	Notional amount	Credit exposure	Exposure, net of collateral		Number of counterparties	Notional amount	Credit exposure	Exposure, net of collateral
Rating (1)		amount (2)	(2)	(2)			amount (2)	(2)	(2)
AA-	1	\$ 672	\$ 23	\$ 11	2	\$ 3,269	\$ 26	\$ 1	
A+	2	190	3	--	5	12,359	204	57	
A	3	932	5	5	3	2,551	62	30	
A-	1	89	34	34	1	145	23	23	
Total	7	\$ 1,883	\$ 65	\$ 50	11	\$ 18,324	\$ 315	\$ 111	

(1) Rating is the lower of S&P or Moody's ratings.

(2) Only OTC derivatives with a net positive fair value are included for each counterparty.

Market risk is the risk that the Company will incur losses due to adverse changes in market rates and prices. Market risk exists for all of the derivative financial instruments the Company currently holds, as these instruments may become less valuable due to adverse changes in market conditions. To limit this risk, the Company's senior management has established risk control limits. In addition, changes in fair value of the derivative financial instruments that the Company uses for risk management purposes are generally offset by the change in the fair value or cash flows of the hedged risk component of the related assets, liabilities or forecasted transactions.

Certain of the Company's derivative instruments contain credit-risk-contingent termination events, cross-default provisions and credit support annex agreements. Credit-risk-contingent termination events allow the counterparties to terminate the derivative on certain dates if AIC's, ALIC's or Allstate Life Insurance Company of New York's (ALNY's) financial strength credit ratings by Moody's or S&P fall below a certain level or in the event AIC, ALIC or ALNY are no longer rated by both Moody's and S&P. Credit-risk-contingent cross-default provisions allow the counterparties to terminate the derivative instruments if the Company defaults by pre-determined threshold amounts on certain debt instruments. Credit-risk-contingent credit support annex agreements specify the amount of collateral the Company must post to counterparties based on AIC's, ALIC's or ALNY's financial strength credit ratings by Moody's or S&P, or in the event AIC, ALIC or ALNY are no longer rated by both Moody's and S&P.

The following summarizes the fair value of derivative instruments with termination, cross-default or collateral credit-risk-contingent features that are in a liability position, as well as the fair value of assets and collateral that are netted against the liability in accordance with provisions within legally enforceable MNAs.

(\$ in millions)	September 30, 2010	December 31, 2009
Gross liability fair value of contracts containing credit-risk-contingent features	\$ 566	\$ 429
Gross asset fair value of contracts containing credit-risk-contingent features and subject to MNAs	(248)	(265)
Collateral posted under MNAs for contracts containing credit-risk-contingent features	(275)	(122)
Maximum amount of additional exposure for contracts with credit-risk-contingent features if all features were triggered concurrently	\$ 43	\$ 42

Credit derivatives - selling protection

Free-standing credit default swaps (CDS) are utilized for selling credit protection against a specified credit event. A credit default swap is a derivative instrument, representing an agreement between two parties to exchange the credit risk of a specified entity (or a group of entities), or an index based on the credit risk of a group of entities

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(all commonly referred to as the reference entity or a portfolio of reference entities), in return for a periodic premium. In selling protection, CDS are used to replicate fixed income securities and to complement the cash market when credit exposure to certain issuers is not available or when the derivative alternative is less expensive than the cash market alternative. CDS typically have a five-year term.

The following table shows the CDS notional amounts by credit rating and fair value of protection sold as of September 30, 2010:

(\$ in millions)		Notional amount					
	AA	A	BBB	BB and lower	Total	Fair value	
Single name							
Investment grade corporate debt	\$ 50	\$ 146	\$ 150	\$ 20	\$ 366	\$	(9)
High yield debt	--	--	--	6	6		--
Municipal	170	--	--	--	170		(15)
Subtotal	220	146	150	26	542		(24)
Baskets							
Tranche							
Investment grade corporate debt	--	--	--	65	65		(22)
First-to-default							
Municipal	--	100	--	--	100		(36)
Subtotal	--	100	--	65	165		(58)
Total	\$ 220	\$ 246	\$ 150	\$ 91	\$ 707	\$	(82)

The following table shows the CDS notional amounts by credit rating and fair value of protection sold as of December 31, 2009:

(\$ in millions)		Notional amount					
	AA	A	BBB	BB and lower	Total	Fair value	
Single name							
Investment grade corporate debt	\$ 63	\$ 86	\$ 84	\$ 30	\$ 263	\$	(12)
High yield debt	--	--	--	10	10		--
Municipal	135	--	--	--	135		(10)
Subtotal	198	86	84	40	408		(22)
Baskets							
Tranche							
Investment grade corporate debt	--	--	--	65	65		(27)
First-to-default							
	--	45	15	--	60		--

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Investment grade corporate debt						
Municipal	20	135	--	--	155	(28)
Subtotal	20	180	15	65	280	(55)
Index						
Investment grade corporate debt	14	159	408	19	600	4
Total	\$ 232	\$ 425	\$ 507	\$ 124	\$ 1,288	\$ (73)

In selling protection with CDS, the Company sells credit protection on an identified single name, a basket of names in a first-to-default (FTD) structure or a specific tranche of a basket, or credit derivative index (CDX) that is generally investment grade, and in return receives periodic premiums through expiration or termination of the agreement. With single name CDS, this premium or credit spread generally corresponds to the difference between

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the yield on the reference entity's public fixed maturity cash instruments and swap rates at the time the agreement is executed. With a FTD basket or a tranche of a basket, because of the additional credit risk inherent in a basket of named reference entities, the premium generally corresponds to a high proportion of the sum of the credit spreads of the names in the basket and the correlation between the names. CDX index is utilized to take a position on multiple (generally 125) reference entities. Credit events are typically defined as bankruptcy, failure to pay, or restructuring, depending on the nature of the reference entities. If a credit event occurs, the Company settles with the counterparty, either through physical settlement or cash settlement. In a physical settlement, a reference asset is delivered by the buyer of protection to the Company, in exchange for cash payment at par, whereas in a cash settlement, the Company pays the difference between par and the prescribed value of the reference asset. When a credit event occurs in a single name or FTD basket (for FTD, the first credit event occurring for any one name in the basket), the contract terminates at the time of settlement. When a credit event occurs in a tranche of a basket, there is no immediate impact to the Company until cumulative losses in the basket exceed the contractual subordination. To date, realized losses have not exceeded the subordination. For CDX index, the reference entity's name incurring the credit event is removed from the index while the contract continues until expiration. The maximum payout on a CDS is the contract notional amount. A physical settlement may afford the Company with recovery rights as the new owner of the asset.

The Company monitors risk associated with credit derivatives through individual name credit limits at both a credit derivative and a combined cash instrument/credit derivative level. The ratings of individual names for which protection has been sold are also monitored.

In addition to the CDS described above, the Company's synthetic collateralized debt obligations contain embedded credit default swaps which sell protection on a basket of reference entities. The synthetic collateralized debt obligations are fully funded; therefore, the Company is not obligated to contribute additional funds when credit events occur related to the reference entities named in the embedded credit default swaps. The Company's maximum amount at risk equals the amount of its aggregate initial investment in the synthetic collateralized debt obligations.

7. Reserve for Property-Liability Insurance Claims and Claims Expense

The Company establishes reserves for claims and claims expense (loss) on reported and unreported claims of insured losses. The Company's reserving process takes into account known facts and interpretations of circumstances and factors including the Company's experience with similar cases, actual claims paid, historical trends involving claim payment patterns and pending levels of unpaid claims, loss management programs, product mix and contractual terms, changes in law and regulation, judicial decisions, and economic conditions. In the normal course of business, the Company may also supplement its claims processes by utilizing third party adjusters, appraisers, engineers, inspectors, and other professionals and information sources to assess and settle catastrophe and non-catastrophe related claims. The effects of inflation are implicitly considered in the reserving process.

Because reserves are estimates of unpaid portions of losses that have occurred, including incurred but not reported losses, the establishment of appropriate reserves, including reserves for catastrophes, is an inherently uncertain and complex process. The ultimate cost of losses may vary materially from recorded amounts, which are based on management's best estimates. The highest degree of uncertainty is associated with reserves for losses incurred in the current reporting period as it contains the greatest proportion of losses that have not been reported or settled. The Company regularly updates its reserve estimates as new information becomes available and as events unfold that may affect the resolution of unsettled claims. Changes in prior year reserve estimates, which may be material, are reported in property-liability insurance claims and

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claims expense in the Condensed Consolidated Statements of Operations in the period such changes are determined.

Management believes that the reserve for property-liability insurance claims and claims expense, net of reinsurance recoverables, is appropriately established in the aggregate and adequate to cover the ultimate net cost of reported and unreported claims arising from losses which had occurred by the date of the Condensed Consolidated Statements of Financial Position based on available facts, technology, laws and regulations.

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8. Reinsurance

Property-liability insurance premiums and life and annuity premiums and contract charges have been reduced by the reinsurance ceded amounts shown in the following table:

(\$ in millions)	Three months ended				Nine months ended			
	September 30,				September 30,			
	2010		2009		2010		2009	
Property-liability insurance premiums earned	\$	270	\$	269	\$	811	\$	798
Life and annuity premiums and contract charges		192		206		585		612

Property-liability insurance claims and claims expense and life and annuity contract benefits and interest credited to contractholder funds have been reduced by the reinsurance ceded amounts shown in the following table:

(\$ in millions)	Three months ended				Nine months ended			
	September 30,				September 30,			
	2010		2009		2010		2009	
Property-liability insurance claims and claims expense	\$	11	\$	64	\$	202	\$	242
Life and annuity contract benefits (1)		267		(1)		616		617
Interest credited to contractholder funds		8		9		24		24

(1) The three months ended September 30, 2009 include a \$166 million decrease in the reinsurance recoverables related to the ceded variable annuity contract guarantees as a result of improved equity market conditions during 2009.

9. Company Restructuring

The Company undertakes various programs to reduce expenses. These programs generally involve a reduction in staffing levels, and in certain cases, office closures. Restructuring and related charges include employee termination and relocation benefits, and post-exit rent expenses in connection with these programs, and non-cash charges resulting from pension benefit payments made to agents in connection with the 1999 reorganization of Allstate's multiple agency programs to a single exclusive agency program. In the nine months ended September 30, 2010, restructuring programs primarily relate to Allstate Protection's claim and field sales office consolidations and realignment of litigation services. The expenses related to these activities are included in the Condensed Consolidated Statements of Operations as restructuring and related charges, and totaled \$9 million and \$35 million during the three months ended September 30, 2010 and 2009, respectively, and \$33 million and \$112 million for the nine months ended September 30, 2010 and 2009, respectively.

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The following table presents changes in the restructuring liability during the nine months ended September 30, 2010.

(\$ in millions)		Employee costs		Exit costs		Total liability
Balance at December 31, 2009	\$	45	\$	6	\$	51
Expense incurred		19		1		20
Adjustments to liability		(6)		--		(6)
Payments applied against liability		(24)		(2)		(26)
Balance at September 30, 2010	\$	34	\$	5	\$	39

The payments applied against the liability for employee costs primarily reflect severance costs, and the payments for exit costs generally consist of post-exit rent expenses and contract termination penalties. As of September 30, 2010, the cumulative amount incurred to date for active programs totaled \$170 million for employee costs and \$46 million for exit costs.

10. Guarantees and Contingent Liabilities

State facility assessments

The Company is required to participate in assigned risk plans, reinsurance facilities and joint underwriting associations in various states that provide insurance coverage to individuals or entities that otherwise are unable to

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purchase such coverage from private insurers. Because of the Company's participation, it may be exposed to losses that surpass the capitalization of these facilities and/or to assessments from these facilities.

Shared markets

As a condition of maintaining its licenses to write personal property and casualty insurance in various states, the Company is required to participate in assigned risk plans, reinsurance facilities and joint underwriting associations that provide various types of insurance coverage to individuals or entities that otherwise are unable to purchase such coverage from private insurers. Underwriting results related to these arrangements, which tend to be adverse, have been immaterial to the Company's results of operations.

Guarantees

The Company owns certain fixed income securities that obligate the Company to exchange credit risk or to forfeit principal due, depending on the nature or occurrence of specified credit events for the reference entities. In the event all such specified credit events were to occur, the Company's maximum amount at risk on these fixed income securities, as measured by the amount of the aggregate initial investment, was \$111 million at September 30, 2010. The obligations associated with these fixed income securities expire at various dates on or before July 26, 2016.

Related to the disposal through reinsurance of substantially all of Allstate Financial's variable annuity business to The Prudential Insurance Company of America, a subsidiary of Prudential Financial, Inc. (collectively "Prudential") in 2006, the Company and its consolidated subsidiaries, ALIC and ALNY, have agreed to indemnify Prudential for certain pre-closing contingent liabilities (including extra-contractual liabilities of ALIC and ALNY and liabilities specifically excluded from the transaction) that ALIC and ALNY have agreed to retain. In addition, the Company, ALIC and ALNY will each indemnify Prudential for certain post-closing liabilities that may arise from the acts of ALIC, ALNY and their agents, including in connection with ALIC's and ALNY's provision of transition services. The reinsurance agreements contain no limitations or indemnifications with regard to insurance risk transfer, and transferred all of the future risks and responsibilities for performance on the underlying variable annuity contracts to Prudential, including those related to benefit guarantees. Management does not believe this agreement will have a material adverse effect on results of operations, cash flows or financial position of the Company.

The Company provides residual value guarantees on Company leased automobiles. If all outstanding leases were terminated effective September 30, 2010, the Company's maximum obligation pursuant to these guarantees, assuming the automobiles have no residual value, would be \$11 million at September 30, 2010. The remaining term of each residual value guarantee is equal to the term of the underlying lease that ranges from less than one year to three years. Historically, the Company has not made any material payments pursuant to these guarantees.

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In the normal course of business, the Company provides standard indemnifications to contractual counterparties in connection with numerous transactions, including acquisitions and divestitures. The types of indemnifications typically provided include indemnifications for breaches of representations and warranties, taxes and certain other liabilities, such as third party lawsuits. The indemnification clauses are often standard contractual terms and are entered into in the normal course of business based on an assessment that the risk of loss would be remote. The terms of the indemnifications vary in duration and nature. In many cases, the maximum obligation is not explicitly stated and the contingencies triggering the obligation to indemnify have not occurred and are not expected to occur. Consequently, the maximum amount of the obligation under such indemnifications is not determinable. Historically, the Company has not made any material payments pursuant to these obligations.

The aggregate liability balance related to all guarantees was not material as of September 30, 2010.

Regulation and Compliance

The Company is subject to changing social, economic and regulatory conditions. From time to time, regulatory authorities or legislative bodies seek to influence and restrict premium rates, require premium refunds to policyholders, require reinstatement of terminated policies, restrict the ability of insurers to cancel or non-renew policies, require insurers to continue to write new policies or limit their ability to write new policies, limit insurers' ability to change coverage terms or to impose underwriting standards, impose additional regulations regarding agent and broker compensation, regulate the nature of and amount of investments, and otherwise expand overall regulation

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of insurance products and the insurance industry. The Company has established procedures and policies to facilitate compliance with laws and regulations, to foster prudent business operations, and to support financial reporting. The Company routinely reviews its practices to validate compliance with laws and regulations and with internal procedures and policies. As a result of these reviews, from time to time the Company may decide to modify some of its procedures and policies. Such modifications, and the reviews that led to them, may be accompanied by payments being made and costs being incurred. The ultimate changes and eventual effects of these actions on the Company's business, if any, are uncertain.

A multi-state market conduct examination of Allstate's claims handling practices has been underway with Florida, Illinois, Iowa, and New York serving as lead states. The Illinois Department of Insurance issued the official notice of the examination on March 30, 2009. The exam concluded with the state regulatory authorities finding no institutional issues involving underpayment of claims. Moreover, no violations were cited regarding Allstate's claims adjusting practices, and no fines or penalties were assessed. Allstate has agreed to adopt certain enhancements to its business practices such as undertaking certain work in connection with its claim processes including, for example, consolidating materials detailing the primary functions of its bodily injury practices into a single manual and centralizing the oversight of some practices. Allstate has also agreed to contribute a non-material amount towards the development and training of insurance department examination personnel to support the review and evaluation of the insurance industry's use of software technology in adjusting claims. Forty-five states have agreed with the conclusions and resolution of this exam.

Legal and regulatory proceedings and inquiries

Background

The Company and certain subsidiaries are involved in a number of lawsuits, regulatory inquiries, and other legal proceedings arising out of various aspects of its business. As background to both the Claims related proceedings and Other proceedings subsections below, please note the following:

- These matters raise difficult and complicated factual and legal issues and are subject to many uncertainties and complexities, including the underlying facts of each matter; novel legal issues; variations between jurisdictions in which matters are being litigated, heard, or investigated; differences in applicable laws and judicial interpretations; the length of time before many of these matters might be resolved by settlement, through litigation, or otherwise; the fact that some of the lawsuits are putative class actions in which a class has not been certified and in which the purported class may not be clearly defined; the fact that some of the lawsuits involve multi-state class actions in which the applicable law(s) for the claims at issue is in dispute and therefore unclear; and the current challenging legal environment faced by large corporations and insurance companies.

- The outcome of these matters may be affected by decisions, verdicts, and settlements, and the timing of such decisions, verdicts, and settlements, in other individual and class action lawsuits that involve the Company, other insurers, or other entities and by other legal,

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governmental, and regulatory actions that involve the Company, other insurers, or other entities. The outcome may also be affected by future state or federal legislation, the timing or substance of which cannot be predicted.

- In the lawsuits, plaintiffs seek a variety of remedies which may include equitable relief in the form of injunctive and other remedies and monetary relief in the form of contractual and extra-contractual damages. In some cases, the monetary damages sought may include punitive or treble damages. Often specific information about the relief sought, such as the amount of damages, is not available because plaintiffs have not requested specific relief in their pleadings. When specific monetary demands are made, they are often set just below a state court jurisdictional limit in order to seek the maximum amount available in state court, regardless of the specifics of the case, while still avoiding the risk of removal to federal court. In Allstate's experience, monetary demands in pleadings bear little relation to the ultimate loss, if any, to the Company.

- In connection with regulatory examinations and proceedings, government authorities may seek various forms of relief, including penalties, restitution, and changes in business practices. The Company may not be advised of the nature and extent of relief sought until the final stages of the examination or proceeding.

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- For the reasons specified above, it is often not possible to make meaningful estimates of the amount or range of loss that could result from the matters described below in the *Claims related proceedings* and *Other proceedings* subsections. The Company reviews these matters on an ongoing basis and follows appropriate accounting guidance when making accrual and disclosure decisions. When assessing reasonably possible and probable outcomes, the Company bases its decisions on its assessment of the ultimate outcome following all appeals.
- Due to the complexity and scope of the matters disclosed in the *Claims related proceedings* and *Other proceedings* subsections below and the many uncertainties that exist, the ultimate outcome of these matters cannot be reasonably predicted. In the event of an unfavorable outcome in one or more of these matters, the ultimate liability may be in excess of amounts currently reserved, if any, and may be material to the Company's operating results or cash flows for a particular quarterly or annual period. However, based on information currently known to it, management believes that the ultimate outcome of all matters described below, as they are resolved over time, is not likely to have a material adverse effect on the financial position of the Company.

Claims related proceedings

The Company is vigorously defending a number of matters in various stages of development filed in the aftermath of Hurricane Katrina, including individual lawsuits and a statewide putative class action in Louisiana. The Louisiana Attorney General filed a putative class action lawsuit in state court against Allstate and other insurers on behalf of Road Home fund recipients alleging that the insurers have failed to pay all damages owed under their policies. The insurers removed the matter to federal court. The district court denied plaintiffs' motion to remand the matter to state court and the U.S. Court of Appeals for the Fifth Circuit (*Fifth Circuit*) affirmed that ruling. The defendants filed a motion to dismiss and the plaintiffs filed a motion to remand the claims involving a Road Home subrogation agreement. In March 2009, the district court denied the State's request that its claims be remanded to state court. As for the defendant insurers' motion, the judge granted it in part and denied it in part. Dismissal of all of the extra-contractual claims, including the bad faith and breach of fiduciary duty claims, was granted. Dismissal also was granted of all claims based on the Valued Policy Law and all flood loss claims based on the levee breaches finding that the insurers flood exclusions precluded coverage. The remaining claims are for breach of contract and for declaratory relief on the alleged underpayment of claims by the insurers. The judge did not dismiss the class action allegations. The defendants also had moved to dismiss the complaint on grounds that the State had no standing to bring the lawsuit as an assignee of insureds because of anti-assignment language in the insurers policies. The judge denied the defendants' motion for reconsideration on the assignment issue but found the matter was ripe for consideration by the federal appellate court. The defendants have filed a petition for permission to appeal to the Fifth Circuit. The Fifth Circuit has accepted review. After the Fifth Circuit accepted review, plaintiffs filed a motion to remand the case to state court, asserting that the class claims on which federal jurisdiction was premised have now effectively been dismissed as a result of a ruling in a related case. The Fifth Circuit has denied the motion for remand, without prejudice to plaintiffs' right to refile the motion for remand after the Fifth Circuit disposes of the pending appeal. On July 28, 2010, the Fifth Circuit issued an order stating that since there is no controlling Louisiana Supreme Court precedent on the issue of whether an insurance policy's anti-assignment clause prohibits post-loss assignments, the Fifth Circuit is certifying that issue to the Louisiana Supreme Court. The Louisiana Supreme Court may rule based on the pleadings that have been filed with the Fifth Circuit, or it may request additional briefing as well as oral argument.

There are one nationwide and several statewide class action lawsuits pending against Allstate alleging that it failed to properly pay general contractors overhead and profit on many homeowner structural loss claims. Most of these lawsuits contain counts for breach of contract, as well as one or more counts asserting other theories of liability such as bad faith, fraud, unjust enrichment, or unfair claims practices. General contractors overhead and profit is an amount that is added to payments on claims where the services of a general contractor are reasonably likely

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to be required. To a large degree, these lawsuits mirror similar lawsuits filed against other carriers in the industry, some of which have settled. These lawsuits are pending in various state and federal courts, and they are in different stages of development. No classes have been certified against Allstate. The Company has extended an offer of settlement on a 48-state basis in the nationwide class action that appears acceptable to the plaintiffs. Many terms and conditions of such a settlement are still to be worked out, and any final agreement to settle will be subject to the approval of the court. The settlement was accrued as a prior year reserve reestimate in property-liability insurance claims and claims expense in the third quarter of 2010.

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Allstate has been vigorously defending a lawsuit involving worker classification issues. This lawsuit is a certified class action challenging a state wage and hour law. In this case, plaintiffs sought monetary relief, such as penalties and liquidated damages, and non-monetary relief, such as injunctive relief. In December 2009, the liability phase of the case was tried and, on July 6, 2010, the court issued its decision finding in favor of Allstate on all claims. The plaintiffs are appealing the decision.

Other proceedings

The Company is defending certain matters relating to the Company's agency program reorganization announced in 1999. These matters are in various stages of development.

- These matters include a lawsuit filed in 2001 by the U.S. Equal Employment Opportunity Commission (EEOC) alleging retaliation under federal civil rights laws (the EEOC I suit) and a class action filed in 2001 by former employee agents alleging retaliation and age discrimination under the Age Discrimination in Employment Act (ADEA), breach of contract and ERISA violations (the Romero I suit). In 2004, in the consolidated EEOC I and Romero I litigation, the trial court issued a memorandum and order that, among other things, certified classes of agents, including a mandatory class of agents who had signed a release, for purposes of effecting the court's declaratory judgment that the release is voidable at the option of the release signer. The court also ordered that an agent who voids the release must return to Allstate any and all benefits received by the [agent] in exchange for signing the release. The court also stated that, on the undisputed facts of record, there is no basis for claims of age discrimination. The EEOC and plaintiffs asked the court to clarify and/or reconsider its memorandum and order and in January 2007, the judge denied their request. In June 2007, the court granted the Company's motions for summary judgment. Following plaintiffs' filing of a notice of appeal, the U.S. Court of Appeals for the Third Circuit (Third Circuit) issued an order in December 2007 stating that the notice of appeal was not taken from a final order within the meaning of the federal law and thus not appealable at this time. In March 2008, the Third Circuit decided that the appeal should not summarily be dismissed and that the question of whether the matter is appealable at this time will be addressed by the Third Circuit along with the merits of the appeal. In July 2009, the Third Circuit vacated the decision which granted the Company's summary judgment motions, remanded the cases to the trial court for additional discovery, and directed that the cases be reassigned to another trial court judge. In January 2010, the cases were assigned to a new judge for further proceedings in the trial court.

- A putative nationwide class action has also been filed by former employee agents alleging various violations of ERISA, including a worker classification issue. These plaintiffs are challenging certain amendments to the Agents Pension Plan and are seeking to have exclusive agent independent contractors treated as employees for benefit purposes. This matter was dismissed with prejudice by the trial court, was the subject of further proceedings on appeal, and was reversed and remanded to the trial court in 2005. In June 2007, the court granted the Company's motion to dismiss the case. Following plaintiffs' filing of a notice of appeal, the Third Circuit issued an order in December 2007 stating that the notice of appeal was not taken from a final order within the meaning of the federal law and thus not appealable at this time. In March 2008, the Third Circuit decided that the appeal should not summarily be dismissed and that the question of whether the matter is appealable at this time will be addressed by the Third Circuit along with the merits of the appeal. In July 2009, the Third Circuit vacated the decision which granted the Company's motion to dismiss the case, remanded the case to the trial court for additional discovery, and directed that the case be reassigned to another trial court judge. In January 2010, the case was assigned to a new judge for further proceedings in the trial court.

In these agency program reorganization matters, plaintiffs seek compensatory and punitive damages, and equitable relief. Allstate has been vigorously defending these lawsuits and other matters related to its agency program reorganization.

Other Matters

Various other legal, governmental, and regulatory actions, including state market conduct exams, and other governmental and regulatory inquiries are currently pending that involve the Company and specific aspects of its conduct of business. Like other members of the insurance industry, the Company is the target of a number of class action lawsuits and other types of proceedings, some of which involve claims for substantial or indeterminate

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amounts. These actions are based on a variety of issues and target a range of the Company's practices. The outcome of these disputes is currently unpredictable.

One or more of these matters could have an adverse effect on the Company's operating results or cash flows for a particular quarterly or annual period. However, based on information currently known to it, management believes that the ultimate outcome of all matters described in this

Other Matters subsection, in excess of amounts currently reserved, if any, as they are resolved over time, is not likely to have a material effect on the operating results, cash flows or financial position of the Company.

Asbestos and environmental

Allstate's reserves for asbestos claims were \$1.13 billion and \$1.18 billion, net of reinsurance recoverables of \$565 million and \$600 million, at September 30, 2010 and December 31, 2009, respectively. Reserves for environmental claims were \$205 million and \$198 million, net of reinsurance recoverables of \$47 million and \$49 million, at September 30, 2010 and December 31, 2009, respectively. Approximately 59% and 62% of the total net asbestos and environmental reserves at September 30, 2010 and December 31, 2009, respectively, were for incurred but not reported estimated losses.

Management believes its net loss reserves for asbestos, environmental and other discontinued lines exposures are appropriately established based on available facts, technology, laws and regulations. However, establishing net loss reserves for asbestos, environmental and other discontinued lines claims is subject to uncertainties that are much greater than those presented by other types of claims. The ultimate cost of losses may vary materially from recorded amounts, which are based on management's best estimate. Among the complications are lack of historical data, long reporting delays, uncertainty as to the number and identity of insureds with potential exposure and unresolved legal issues regarding policy coverage; unresolved legal issues regarding the determination, availability and timing of exhaustion of policy limits; plaintiffs' evolving and expanding theories of liability; availability and collectability of recoveries from reinsurance; retrospectively determined premiums and other contractual agreements; estimates of the extent and timing of any contractual liability; the impact of bankruptcy protection sought by various asbestos producers and other asbestos defendants; and other uncertainties. There are also complex legal issues concerning the interpretation of various insurance policy provisions and whether those losses are covered, or were ever intended to be covered, and could be recoverable through retrospectively determined premium, reinsurance or other contractual agreements. Courts have reached different and sometimes inconsistent conclusions as to when losses are deemed to have occurred and which policies provide coverage; what types of losses are covered; whether there is an insurer obligation to defend; how policy limits are determined; how policy exclusions and conditions are applied and interpreted; and whether clean-up costs represent insured property damage. Management believes these issues are not likely to be resolved in the near future, and the ultimate costs may vary materially from the amounts currently recorded resulting in material changes in loss reserves. In addition, while the Company believes that improved actuarial techniques and databases have assisted in its ability to estimate asbestos, environmental, and other discontinued lines net loss reserves, these refinements may subsequently prove to be inadequate indicators of the extent of probable losses. Due to the uncertainties and factors described above, management believes it is not practicable to develop a meaningful range for any such additional net loss reserves that may be required.

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11. Income Taxes

A reconciliation of the statutory federal income tax rate to the effective income tax rate on income from operations for the nine months ended September 30 is as follows:

(\$ in millions)	2010		2009	
Statutory federal income tax rate - expense	\$ 267	35.0 %	\$ 194	35.0 %
Tax-exempt income	(139)	(18.2)	(197)	(35.6)
Dividends received deduction	(13)	(1.7)	(11)	(2.1)
Deferred foreign tax credit	4	0.5	12	2.1
Adjustment to prior year tax liabilities	(4)	(0.5)	(21)	(3.7)
Other	16	2.1	(6)	(1.1)
Valuation allowance	--	--	248	44.7
Effective income tax rate - expense	\$ 131	17.2 %	\$ 219	39.3 %

Income tax expense for the nine months ended September 30, 2009 included expense of \$254 million attributable to an increase in the valuation allowance relating to the deferred tax asset on capital losses.

12. Components of Net Periodic Pension and Postretirement Benefit Costs

The components of net periodic cost for the Company's pension and postretirement benefit plans are as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Pension benefits				
Service cost	\$ 38	\$ 32	\$ 113	\$ 95
Interest cost	80	83	240	248
Expected return on plan assets	(83)	(100)	(248)	(298)
Amortization of:				
Prior service credit	(1)	(1)	(2)	(2)
Net actuarial loss	40	5	119	13
Settlement loss	13	15	39	47

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Net periodic pension cost	\$	87	\$	34	\$	261	\$	103
Postretirement benefits								
Service cost	\$	3	\$	3	\$	9	\$	10
Interest cost		10		13		30		42
Amortization of:								
Prior service credit		(6)		(2)		(17)		(1)
Net actuarial gain		(5)		(7)		(16)		(23)
Net periodic postretirement benefit cost	\$	2	\$	7	\$	6	\$	28

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13. Business Segments

Summarized revenue data for each of the Company's business segments are as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Revenues				
<i>Property-Liability</i>				
Property-liability insurance premiums				
Standard auto	\$ 4,134	\$ 4,167	\$ 12,425	\$ 12,493
Non-standard auto	224	237	688	730
Total auto	4,358	4,404	13,113	13,223
Homeowners	1,526	1,504	4,554	4,562
Other personal lines	614	627	1,847	1,893
Allstate Protection	6,498	6,535	19,514	19,678
Discontinued Lines and Coverages	1	--	1	(1)
Total property-liability insurance premiums	6,499	6,535	19,515	19,677
Net investment income	284	326	898	1,004
Realized capital gains and losses	(107)	(290)	(403)	(403)
Total Property-Liability	6,676	6,571	20,010	20,278
<i>Allstate Financial</i>				
Life and annuity premiums and contract charges				
Traditional life insurance	107	103	317	303
Immediate annuities with life contingencies	26	15	84	83
Accident and health	157	114	464	340
Total life and annuity premiums	290	232	865	726
Interest-sensitive life insurance	249	238	740	699
Fixed annuities	9	12	32	35
Total contract charges	258	250	772	734
Total life and annuity premiums and contract charges	548	482	1,637	1,460
Net investment income	707	744	2,161	2,327
Realized capital gains and losses	(38)	(234)	(553)	(156)
Total Allstate Financial	1,217	992	3,245	3,631
<i>Corporate and Other</i>				
Service fees	2	3	8	7
Net investment income	14	14	45	37
Realized capital gains and losses	1	5	13	9
Total Corporate and Other before reclassification of service fees	17	22	66	53
Reclassification of service fees (1)	(2)	(3)	(8)	(7)
Total Corporate and Other	15	19	58	46

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Consolidated revenues	\$	7,908	\$	7,582	\$	23,313	\$	23,955
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(1) For presentation in the Condensed Consolidated Statements of Operations, service fees of the Corporate and Other segment are reclassified to operating costs and expenses.

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Summarized financial performance data for each of the Company's reportable segments are as follows:

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Net income				
<i>Property-Liability</i>				
Underwriting income (loss)				
Allstate Protection	\$ 287	\$ 363	\$ 571	\$ 578
Discontinued Lines and Coverages	(21)	(17)	(27)	(27)
Total underwriting income	266	346	544	551
Net investment income	284	326	898	1,004
Income tax expense on operations	(154)	(170)	(391)	(346)
Realized capital gains and losses, after-tax	(69)	(188)	(261)	(373)
Gain on disposition of operations, after-tax	4	--	4	--
Property-Liability net income	331	314	794	836
<i>Allstate Financial</i>				
Life and annuity premiums and contract charges	548	482	1,637	1,460
Net investment income	707	744	2,161	2,327
Periodic settlements and accruals on non-hedge derivative financial instruments	10	2	38	--
Contract benefits and interest credited to contractholder funds	(891)	(879)	(2,731)	(2,735)
Operating costs and expenses and amortization of deferred policy acquisition costs	(219)	(207)	(554)	(672)
Restructuring and related charges	--	(4)	1	(24)
Income tax expense on operations	(47)	(43)	(180)	(111)
Operating income	108	95	372	245
Realized capital gains and losses, after-tax	(25)	(151)	(360)	(239)
DAC and DSI accretion (amortization) related to realized capital gains and losses, after-tax	7	18	9	(132)
DAC and DSI unlocking related to realized capital gains and losses, after-tax	--	--	(18)	(224)
Reclassification of periodic settlements and accruals on non-hedge financial instruments, after-tax	(7)	(1)	(25)	--
Gain on disposition of operations, after-tax	2	1	4	4
Allstate Financial net income (loss)	85	(38)	(18)	(346)
<i>Corporate and Other</i>				
Service fees (1)	2	3	8	7
Net investment income	14	14	45	37
Operating costs and expenses (1)	(97)	(112)	(301)	(309)
Income tax benefit on operations	31	37	96	105
Operating loss	(50)	(58)	(152)	(160)
Realized capital gains and losses, after-tax	1	3	8	6
Corporate and Other net loss	(49)	(55)	(144)	(154)
Consolidated net income	\$ 367	\$ 221	\$ 632	\$ 336

(1) For presentation in the Condensed Consolidated Statements of Operations, service fees of the Corporate and Other segment are reclassified to operating costs and expenses.

THE ALLSTATE CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

14. Other Comprehensive Income

The components of other comprehensive income on a pre-tax and after-tax basis are as follows:

(\$ in millions)	Three months ended September 30,					
	2010		2009			
	Pre-tax	Tax	After-tax	Pre-tax	Tax	After-tax
Unrealized net holding gains and losses arising during the period, net of related offsets	\$ 1,593	\$ (557)	\$ 1,036	\$ 3,354	\$ (1,185)	\$ 2,169
Less: reclassification adjustment of realized capital gains and losses	140	(49)	91	(85)	30	(55)
Unrealized net capital gains and losses	1,453	(508)	945	3,439	(1,215)	2,224
Unrealized foreign currency translation adjustments	17	(6)	11	39	(14)	25
Unrecognized pension and other postretirement benefit cost	26	(9)	17	122	(67)	55
Other comprehensive income	\$ 1,496	\$ (523)	973	\$ 3,600	\$ (1,296)	2,304
Net income			367			221
Comprehensive income			\$ 1,340			\$ 2,525

	Nine months ended September 30,					
	2010		2009			
	Pre-tax	Tax	After-tax	Pre-tax	Tax	After-tax
Unrealized net holding gains and losses arising during the period, net of related offsets	\$ 3,134	\$ (1,096)	\$ 2,038	\$ 6,168	\$ (2,156)	\$ 4,012
Less: reclassification adjustment of realized capital gains and losses	(161)	56	(105)	(640)	224	(416)
Unrealized net capital gains and losses	3,295	(1,152)	2,143	6,808	(2,380)	4,428
Unrealized foreign currency translation adjustments	12	(4)	8	57	(20)	37
Unrecognized pension and other postretirement benefit cost	83	(28)	55	109	(63)	46
Other comprehensive income	\$ 3,390	\$ (1,184)	2,206	\$ 6,974	\$ (2,463)	4,511
Net income			632			336
Comprehensive income			\$ 2,838			\$ 4,847

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

The Allstate Corporation

Northbrook, IL 60062

We have reviewed the accompanying condensed consolidated statement of financial position of The Allstate Corporation and subsidiaries (the Company) as of September 30, 2010, and the related condensed consolidated statements of operations for the three-month and nine-month periods ended September 30, 2010 and 2009, and the condensed consolidated statements of cash flows for the nine-month periods ended September 30, 2010 and 2009. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of financial position of The Allstate Corporation and subsidiaries as of December 31, 2009, and the related consolidated statements of operations, comprehensive income, shareholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated February 25, 2010, which report includes an explanatory paragraph relating to a change in the Company's recognition and presentation for other-than-temporary impairments of debt securities in 2009, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated statement of financial position as of December 31, 2009 is fairly stated, in all material respects, in relation to the consolidated statement of financial position from which it has been derived.

/s/ Deloitte & Touche LLP

Chicago, Illinois

October 27, 2010

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

OVERVIEW

The following discussion highlights significant factors influencing the consolidated financial position and results of operations of The Allstate Corporation (referred to in this document as "we", "our", "us", "the Company" or "Allstate"). It should be read in conjunction with the condensed consolidated financial statements and notes thereto found under Part I, Item 1, contained herein, and with the discussion, analysis, consolidated financial statements and notes thereto in Part I, Item 1, and Part II, Item 7, and Item 8, of The Allstate Corporation Annual Report on Form 10-K for 2009. Further analysis of our insurance segments is provided in the Property-Liability Operations (which includes the Allstate Protection and the Discontinued Lines and Coverages segments) and in the Allstate Financial Segment sections of Management's Discussion and Analysis ("MD&A"). The segments are consistent with the way in which we use financial information to evaluate business performance and to determine the allocation of resources.

Allstate is focused on three priorities: improve customer loyalty, reinvent protection and retirement for the consumer and grow our businesses.

HIGHLIGHTS

- Consolidated net income was \$367 million in the third quarter of 2010 compared to \$221 million in the third quarter of 2009, and \$632 million in the first nine months of 2010 compared to \$336 million in the first nine months of 2009. Net income per diluted share was \$0.68 in the third quarter of 2010 compared to \$0.41 in the third quarter of 2009, and \$1.16 in the first nine months of 2010 compared to \$0.62 in the first nine months of 2009.
- Property-Liability net income was \$331 million in the third quarter of 2010 compared to \$314 million in the third quarter of 2009, and \$794 million in the first nine months of 2010 compared to \$836 million in the first nine months of 2009.
- The Property-Liability combined ratio was 95.9 in the third quarter of 2010 compared to 94.7 in the third quarter of 2009, and 97.2 in the first nine months of both 2010 and 2009.
- Allstate Financial had a net income of \$85 million in the third quarter of 2010 compared to a net loss of \$38 million in the third quarter of 2009, and a net loss of \$18 million in the first nine months of 2010 compared to a net loss of \$346 million in the first nine months of 2009.
- Total revenues were \$7.91 billion in the third quarter of 2010 compared to \$7.58 billion in the third quarter of 2009, and \$23.31 billion in the first nine months of 2010 compared to \$23.96 billion in the first nine months of 2009.
- Property-Liability premiums earned in the third quarter of 2010 totaled \$6.50 billion, a decrease of 0.6% from \$6.54 billion in the third quarter of 2009, and \$19.52 billion in the first nine months of 2010, a decrease of 0.8% from \$19.68 billion in the first nine months of 2009.
- Net realized capital losses were \$144 million in the third quarter of 2010 compared to \$519 million in the third quarter of 2009, and net realized capital losses were \$943 million in the first nine months of 2010 compared to \$550 million in the first nine months of 2009.
- Investments as of September 30, 2010 totaled \$102.21 billion, an increase of 2.4% from \$99.83 billion as of December 31, 2009. Net investment income in the third quarter of 2010 was \$1.01 billion, a decrease of 7.3% from \$1.08 billion in the third quarter of 2009, and \$3.10 billion in the first nine months of 2010, a decrease of 7.8% from \$3.37 billion in the first nine months of 2009.

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- Book value per diluted share (ratio of shareholders' equity to total shares outstanding and dilutive potential shares outstanding) was \$35.48 as of September 30, 2010, an increase of 9.9% from \$32.29 as of September 30, 2009 and an increase of 15.0% from \$30.84 as of December 31, 2009.
- For the twelve months ended September 30, 2010, return on the average of beginning and ending period shareholders' equity was 6.3%, an increase of 10.9 points from (4.6)% for the twelve months ended September 30, 2009.
- At September 30, 2010, we had \$19.27 billion in capital. This total included \$3.53 billion in deployable invested assets at the parent holding company level.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

CONSOLIDATED NET INCOME

(\$ in millions)

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Revenues				
Property-liability insurance premiums	\$ 6,499	\$ 6,535	\$ 19,515	\$ 19,677
Life and annuity premiums and contract charges	548	482	1,637	1,460
Net investment income	1,005	1,084	3,104	3,368
Realized capital gains and losses:				
Total other-than-temporary impairment losses	(99)	(539)	(637)	(1,735)
Portion of loss recognized in other comprehensive income	(68)	147	(91)	301
Net other-than-temporary impairment losses recognized in earnings	(167)	(392)	(728)	(1,434)
Sales and other realized capital gains and losses	23	(127)	(215)	884
Total realized capital gains and losses	(144)	(519)	(943)	(550)
Total revenues	7,908	7,582	23,313	23,955
Costs and expenses				
Property-liability insurance claims and claims expense	(4,603)	(4,573)	(14,109)	(14,295)
Life and annuity contract benefits	(445)	(382)	(1,372)	(1,176)
Interest credited to contractholder funds	(445)	(496)	(1,358)	(1,636)
Amortization of deferred policy acquisition costs	(1,006)	(1,023)	(2,969)	(3,649)
Operating costs and expenses	(828)	(744)	(2,446)	(2,247)
Restructuring and related charges	(9)	(35)	(33)	(112)
Interest expense	(91)	(106)	(275)	(291)
Total costs and expenses	(7,427)	(7,359)	(22,562)	(23,406)
Gain on disposition of operations	9	2	12	6
Income tax expense	(123)	(4)	(131)	(219)
Net income	\$ 367	\$ 221	\$ 632	\$ 336
Property-Liability	\$ 331	\$ 314	\$ 794	\$ 836
Allstate Financial	85	(38)	(18)	(346)
Corporate and Other	(49)	(55)	(144)	(154)
Net income	\$ 367	\$ 221	\$ 632	\$ 336

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

PROPERTY-LIABILITY HIGHLIGHTS

- Premiums written, an operating measure that is defined and reconciled to premiums earned in the Property-Liability Operations section of the MD&A, decreased 0.6% to \$6.77 billion in the third quarter of 2010 from \$6.81 billion in the third quarter of 2009, and 0.1% to \$19.67 billion in the first nine months of 2010 from \$19.69 billion in the first nine months of 2009.

Allstate brand standard auto premiums written decreased 0.5% to \$4.03 billion in the third quarter of 2010 from \$4.05 billion in the third quarter of 2009, and increased 0.8% to \$12.00 billion in the first nine months of 2010 from \$11.90 billion in the first nine months of 2009.

Allstate brand homeowners premiums written increased 2.4% to \$1.61 billion in the third quarter of 2010 from \$1.57 billion in the third quarter of 2009, and increased 2.1% to \$4.36 billion in the first nine months of 2010 from \$4.28 billion in the first nine months of 2009.

Encompass brand premiums written decreased 16.7% to \$290 million in the third quarter of 2010 from \$348 million in the third quarter of 2009, and 19.4% to \$841 million in the first nine months of 2010 from \$1.04 billion in the first nine months of 2009.

- Premium operating measures and statistics contributing to overall Allstate brand standard auto premiums written were the following:

1.7% decrease in policies in force (PIF) as of September 30, 2010 compared to September 30, 2009

1.4% increase in the six month policy term average gross premium before reinsurance to \$441 in the third quarter of 2010 from \$435 in the third quarter of 2009, and 2.5% increase in the six month policy term average gross premium before reinsurance to \$443 in the first nine months of 2010 from \$432 in the first nine months of 2009

0.4 point decrease in the six month renewal ratio to 88.7% in the third quarter of 2010 compared to 89.1% in the third quarter of 2009, and the six month renewal ratio of 88.8% in the first nine months of 2010 was comparable to the first nine months of 2009

2.5% increase in new issued applications in the third quarter of 2010 compared to the same period of 2009, and 2.7% decrease in new issued applications in the first nine months of 2010 compared to the same period of 2009

- Premium operating measures and statistics contributing to overall Allstate brand homeowners premiums written increase were the following:

4.1% decrease in PIF as of September 30, 2010 compared to September 30, 2009

7.2% increase in the twelve month policy term average gross premium before reinsurance to \$953 in the third quarter of 2010 from \$889 in the third quarter of 2009, and 6.7% increase in the twelve month policy term average gross premium before reinsurance to \$937 in the first nine months of 2010 from \$878 in the first nine months of 2009

0.1 point increase in the twelve month renewal ratio to 88.6% in the third quarter of 2010 compared to 88.5% in the third quarter of 2009, and 0.3 point increase in the twelve month renewal ratio to 88.3% in the first nine months of 2010 compared to 88.0% in the first nine months of 2009

5.4% and 2.4% decrease in new issued applications in the third quarter and first nine months of 2010, respectively, compared to the same period of 2009

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\$15 million decrease in catastrophe reinsurance costs to \$127 million in the third quarter of 2010 from \$142 million in the third quarter of 2009, and \$24 million decrease in catastrophe reinsurance costs to \$398 million in the first nine months of 2010 from \$422 million in the first nine months of 2009

- Factors comprising the Allstate brand standard auto loss ratio increase of 0.1 points to 68.7 in the third quarter of 2010 from 68.6 in the third quarter of 2009, and an increase of 0.1 points to 69.5 in the first nine months of 2010 from 69.4 in the first nine months of 2009 were the following:

3.7% and 1.8% increase in standard auto claim frequency (rate of claim occurrence per policy in force) for property damage in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

7.5% and 5.7% increase in standard auto claim frequency for bodily injury in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

1.0% increase and 0.1% decrease in auto paid claim severities (average cost per claim) for property damage in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

1.1% increase and 0.4% decrease in auto paid claim severities for bodily injury in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

- Factors comprising the Allstate brand homeowners loss ratio, which includes catastrophes, an increase of 5.1 points to 80.5 in the third quarter of 2010 from 75.4 in the third quarter of 2009, and a decrease of 1.0 points to 83.5 in the first nine months of 2010 from 84.5 in the first nine months of 2009 were the following:

0.8 point increase in the effect of catastrophe losses to 23.1 points in the third quarter of 2010 compared to 22.3 points in the third quarter of 2009, and 0.3 point decrease in the effect of catastrophe losses to 31.6 points in the first nine months of 2010 compared to 31.9 points in the first nine months of 2009

2.3% decrease and 1.2% increase in homeowner claim frequency, excluding catastrophes, in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

2.1% and 0.6% increase in paid claim severity, excluding catastrophes, in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

- Factors comprising the \$21 million decrease in catastrophe losses to \$386 million in the third quarter of 2010 compared to \$407 million in the third quarter of 2009, and \$71 million decrease to \$1.67 billion in the first nine months of 2010 compared to \$1.74 billion in the first nine months of 2009 were the following:

\$42 million of favorable prior year reserve reestimates in the third quarter of 2010 compared to \$80 million favorable prior year reserve reestimates in the third quarter of 2009, primarily related to recovered subrogation, and \$140 million favorable prior year reserve reestimates in the first nine months of 2010 which is comparable to 2009

\$57 million of unfavorable prior quarter reserve reestimates in the third quarter of 2010 compared to \$86 million unfavorable prior quarter reserve reestimates in the third quarter of 2009

29 events with \$371 million of losses in the third quarter of 2010 compared to 24 events with losses of \$401 million in the third quarter of 2009, and 70 events with losses of \$1.81 billion in the first nine months of 2010 compared to 69 events with losses of \$1.88 billion in the first nine months of 2009

- Factors comprising prior year reserve reestimates of \$11 million unfavorable in the third quarter of 2010 compared to \$52 million favorable in the third quarter of 2009, and prior year reserve reestimates of \$162 million favorable in the first nine months of 2010 compared to \$87 million favorable in the first nine months of 2009 included:

prior year reserve reestimates related to auto, homeowners and other personal lines in the third quarter of 2010 contributed \$40 million favorable, \$67 million unfavorable and \$38 million favorable, respectively, compared to prior year reserve reestimates in the third quarter of 2009 of \$11 million unfavorable, \$75 million favorable and \$3 million favorable, respectively. Prior year reserve reestimates related to auto, homeowners and other personal lines in the first nine months of 2010 contributed \$120 million favorable, \$2 million favorable and \$65 million favorable, respectively, compared to prior year reserve reestimates in the first nine months of 2009 of \$28 million favorable, \$118 million favorable and \$38 million unfavorable, respectively.

prior year reserve reestimates in the third quarter of 2010 are attributable to a \$70 million litigation settlement largely offset by favorable prior year catastrophe reestimates and severity development that was better than expected. Prior year reestimates in the first nine months of 2010 are attributable to favorable prior year catastrophe reestimates and severity development that was better than expected, partially offset by the litigation settlement.

- Our 2010 annual review resulted in asbestos reserve reestimates of \$5 million unfavorable in the third quarter of 2010 compared to \$8 million favorable in the third quarter of 2009, and environmental reserve reestimates of \$18 million unfavorable in the third quarter of 2010 compared to \$13 million unfavorable in the third quarter of 2009.

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- Property-Liability underwriting income was \$266 million in the third quarter of 2010 compared to \$346 million in the third quarter of 2009, and \$544 million in the first nine months of 2010 compared to \$551 million in the first nine months of 2009. Underwriting income, a measure not based on accounting principles generally accepted in the United States of America (GAAP), is defined below.
- Property-Liability investments as of September 30, 2010 were \$35.75 billion, an increase of 3.5% from \$34.53 billion as of December 31, 2009. Net investment income was \$284 million in the third quarter of 2010, a decrease of 12.9% from \$326 million in the third quarter of 2009, and \$898 million in the first nine months of 2010, a decrease of 10.6% from \$1.00 billion in the first nine months of 2009.
- Net realized capital losses were \$107 million in the third quarter of 2010 compared to \$290 million in the third quarter of 2009, and net realized capital losses were \$403 million in the first nine months of both 2010 and 2009.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

PROPERTY-LIABILITY OPERATIONS

Overview Our Property-Liability operations consist of two business segments: Allstate Protection and Discontinued Lines and Coverages. Allstate Protection comprises two brands, the Allstate brand and Encompass® brand. Allstate Protection is principally engaged in the sale of personal property and casualty insurance, primarily private passenger auto and homeowners insurance, to individuals in the United States and Canada. Discontinued Lines and Coverages includes results from insurance coverage that we no longer write and results for certain commercial and other businesses in run-off. These segments are consistent with the groupings of financial information that management uses to evaluate performance and to determine the allocation of resources.

Underwriting income, a measure that is not based on GAAP and is reconciled to net income below, is calculated as premiums earned, less claims and claims expense (losses), amortization of deferred policy acquisition costs (DAC), operating costs and expenses and restructuring and related charges, as determined using GAAP. We use this measure in our evaluation of results of operations to analyze the profitability of the Property-Liability insurance operations separately from investment results. It is also an integral component of incentive compensation. It is useful for investors to evaluate the components of income separately and in the aggregate when reviewing performance. Net income is the GAAP measure most directly comparable to underwriting income. Underwriting income should not be considered as a substitute for net income and does not reflect the overall profitability of the business.

The table below includes GAAP operating ratios we use to measure our profitability. We believe that they enhance an investor's understanding of our profitability. They are calculated as follows:

- Claims and claims expense (loss) ratio - the ratio of claims and claims expense to premiums earned. Loss ratios include the impact of catastrophe losses.
- Expense ratio - the ratio of amortization of DAC, operating costs and expenses, and restructuring and related charges to premiums earned.
- Combined ratio - the ratio of claims and claims expense, amortization of DAC, operating costs and expenses, and restructuring and related charges to premiums earned. The combined ratio is the sum of the loss ratio and the expense ratio. The difference between 100% and the combined ratio represents underwriting income as a percentage of premiums earned.

We have also calculated the following impacts of specific items on the GAAP operating ratios because of the volatility of these items between fiscal periods.

- Effect of catastrophe losses on combined ratio - the percentage of catastrophe losses included in claims and claims expense to premiums earned. This ratio includes prior year reserve reestimates of catastrophe losses.

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- Effect of prior year reserve reestimates on combined ratio - the percentage of prior year reserve reestimates included in claims and claims expense to premiums earned. This ratio includes prior year reserve reestimates of catastrophe losses.
- Effect of restructuring and related charges on combined ratio - the percentage of restructuring and related charges to premiums earned.
- Effect of Discontinued Lines and Coverages on combined ratio - the ratio of claims and claims expense and other costs and expenses in the Discontinued Lines and Coverages segment to Property-Liability premiums earned. The sum of the effect of Discontinued Lines and Coverages on the combined ratio and the Allstate Protection combined ratio is equal to the Property-Liability combined ratio.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

Summarized financial data, a reconciliation of underwriting income to net income, and GAAP operating ratios for our Property-Liability operations are presented in the following table.

(\$ in millions, except ratios)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Premiums written	\$ 6,767	\$ 6,810	\$ 19,665	\$ 19,694
Revenues				
Premiums earned	\$ 6,499	\$ 6,535	\$ 19,515	\$ 19,677
Net investment income	284	326	898	1,004
Realized capital gains and losses	(107)	(290)	(403)	(403)
Total revenues	6,676	6,571	20,010	20,278
Costs and expenses				
Claims and claims expense	(4,603)	(4,573)	(14,109)	(14,295)
Amortization of DAC	(915)	(943)	(2,754)	(2,832)
Operating costs and expenses	(706)	(642)	(2,074)	(1,911)
Restructuring and related charges	(9)	(31)	(34)	(88)
Total costs and expenses	(6,233)	(6,189)	(18,971)	(19,126)
Gain on disposition of operations	5	--	5	--
Income tax expense	(117)	(68)	(250)	(316)
Net income	\$ 331	\$ 314	\$ 794	\$ 836
Underwriting income	\$ 266	\$ 346	\$ 544	\$ 551
Net investment income	284	326	898	1,004
Income tax expense on operations	(154)	(170)	(391)	(346)
Realized capital gains and losses, after-tax	(69)	(188)	(261)	(373)
Gain on disposition of operations, after-tax	4	--	4	--
Net income	\$ 331	\$ 314	\$ 794	\$ 836
Catastrophe losses (1)	\$ 386	\$ 407	\$ 1,670	\$ 1,741
GAAP operating ratios				
Claims and claims expense ratio	70.8	70.0	72.3	72.6
Expense ratio	25.1	24.7	24.9	24.6
Combined ratio	95.9	94.7	97.2	97.2
Effect of catastrophe losses on combined ratio (1)	5.9	6.2	8.6	8.8
Effect of prior year reserve reestimates on combined ratio (1)	0.2	(0.7)	(0.9)	(0.4)
Effect of restructuring and related charges on combined ratio	0.1	0.5	0.2	0.4
Effect of Discontinued Lines and Coverages on combined ratio	0.3	0.3	0.1	0.1

(1) Prior year reserve reestimates included in catastrophe losses totaled \$42 million and \$140 million favorable in the three months and nine months ended September 30 2010, respectively, compared to \$80 million and \$139 million favorable in the three months and nine months ended September 30, 2009, respectively.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

Premiums written, an operating measure, is the amount of premiums charged for policies issued during a fiscal period. Premiums earned is a GAAP measure. Premiums are considered earned and are included in the financial results on a pro-rata basis over the policy period. The portion of premiums written applicable to the unexpired terms of the policies is recorded as unearned premiums on our Condensed Consolidated Statements of Financial Position.

A reconciliation of premiums written to premiums earned is shown in the following table.

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Premiums written:				
Allstate Protection	\$ 6,767	\$ 6,810	\$ 19,665	\$ 19,695
Discontinued Lines and Coverages	--	--	--	(1)
Property-Liability premiums written	6,767	6,810	19,665	19,694
Increase in unearned premiums	(319)	(315)	(184)	(48)
Other	51	40	34	31
Property-Liability premiums earned	\$ 6,499	\$ 6,535	\$ 19,515	\$ 19,677
Premiums earned:				
Allstate Protection	\$ 6,498	\$ 6,535	\$ 19,514	\$ 19,678
Discontinued Lines and Coverages	1	--	1	(1)
Property-Liability	\$ 6,499	\$ 6,535	\$ 19,515	\$ 19,677

ALLSTATE PROTECTION SEGMENT

Premiums written by brand are shown in the following table.

(\$ in millions)	Allstate brand		Three months ended September 30,		Allstate Protection	
	2010	2009	2010	2009	2010	2009
Standard auto	\$ 4,028	\$ 4,049	\$ 166	\$ 208	\$ 4,194	\$ 4,257
Non-standard auto	223	235	1	6	224	241
Homeowners	1,610	1,573	98	110	1,708	1,683
Other personal lines (1)	616	605	25	24	641	629
Total	\$ 6,477	\$ 6,462	\$ 290	\$ 348	\$ 6,767	\$ 6,810

	Allstate brand		Nine months ended September 30,		Allstate Protection	
	2010	2009	2010	2009	2010	2009
Standard auto	\$ 11,999	\$ 11,903	\$ 495	\$ 629	\$ 12,494	\$ 12,532
Non-standard auto	680	708	5	19	685	727
Homeowners	4,364	4,276	272	319	4,636	4,595

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Other personal lines (1)	1,781	1,764	69	77	1,850	1,841
Total	\$ 18,824	\$ 18,651	\$ 841	\$ 1,044	\$ 19,665	\$ 19,695

(1) Other personal lines include commercial, condominium, renters, involuntary auto and other personal lines.

Allstate brand premiums written, excluding Allstate Canada, by the direct channel increased 15.4% to \$195 million in the third quarter of 2010 from \$169 million in the third quarter of 2009, and 21.7% to \$561 million in the first nine months of 2010 from \$461 million in the first nine months of 2009. Both periods are impacted by profitability management actions taken in New York, Florida, California and North Carolina. The direct channel includes call centers and the internet.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2010 AND 2009

Premiums earned by brand are shown in the following table.

(\$ in millions)	Three months ended September 30,					
	Allstate brand		Encompass brand		Allstate Protection	
	2010	2009	2010	2009	2010	2009
Standard auto	\$ 3,961	\$ 3,946	\$ 173	\$ 221	\$ 4,134	\$ 4,167
Non-standard auto	222	231	2	6	224	237
Homeowners	1,430	1,396	96	108	1,526	1,504
Other personal lines	591	601	23	26	614	627
Total	\$ 6,204	\$ 6,174	\$ 294	\$ 361	\$ 6,498	\$ 6,535

	Nine months ended September 30,					
	Allstate brand		Encompass brand		Allstate Protection	
	2010	2009	2010	2009	2010	2009
Standard auto	\$ 11,873	\$ 11,791	\$ 552	\$ 702	\$ 12,425	\$ 12,493
Non-standard auto	680	708	8	22	688	730
Homeowners	4,262	4,222	292	340	4,554	4,562
Other personal lines	1,775	1,811	72	82	1,847	1,893
Total	\$ 18,590	\$ 18,532	\$ 924	\$ 1,146	\$ 19,514	\$ 19,678

Premium operating measures and statistics that are used to analyze the business are calculated and described below. Measures and statistics presented for Allstate brand exclude Allstate Canada, loan protection and specialty auto.

- **PIF:** Policy counts are based on items rather than customers. A multi-car customer would generate multiple item (policy) counts, even if all cars were insured under one policy.
- **Average premium-gross written:** Gross premiums written divided by issued item count. Gross premiums written include the impacts from discounts and surcharges, and exclude the impacts from mid-term premium adjustments, ceded reinsurance premiums, and premium refund accruals. Allstate brand average gross premiums represent the appropriate policy term for each line, which is 6 months for standard and non-standard auto and 12 months for homeowners. Encompass brand average gross premiums represent the appropriate policy term for each line, which is 12 months for standard auto and homeowners and 6 months for non-standard auto.
- **Renewal ratio:** Renewal policies issued during the period, based on contract effective dates, divided by the total policies issued 6 months prior for standard and non-standard auto (12 months prior for Encompass brand standard auto) or 12 months prior for homeowners.
- **New issued applications:** Item counts of automobiles or homeowners insurance applications for insurance policies that were issued during the period. Does not include automobiles that are added by existing customers.

Standard auto premiums written totaled \$4.19 billion in the third quarter of 2010, a decrease of 1.5% from \$4.26 billion in the third quarter of 2009, and \$12.49 billion in the first nine months of 2010, a decrease of 0.3% from \$12.53 billion in the first nine months of 2009.

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Standard Auto	Allstate brand		Encompass brand	
	2010	2009	2010	2009
Three months ended September 30,				
PIF (thousands)	17,479	17,774	710	921
Average premium-gross written (1)	\$ 441	\$ 435	\$ 974	\$ 981
Renewal ratio (%) (1)	88.7	89.1	67.4	69.1
Nine months ended September 30,				
PIF (thousands)	17,479	17,774	710	921
Average premium-gross written (1)	\$ 443	\$ 432	\$ 986	\$ 968
Renewal ratio (%) (1)	88.8	88.9	67.7	69.6

(1) Policy term is six months for Allstate brand and twelve months for Encompass brand.

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Allstate brand standard auto premiums written totaled \$4.03 billion in the third quarter of 2010, a decrease of 0.5% from \$4.05 billion in the third quarter of 2009, and \$12.00 billion in the first nine months of 2010, an increase of 0.8% from \$11.90 billion in the first nine months of 2009. Contributing to the Allstate brand standard auto premiums written were the following:

decrease in PIF as of September 30, 2010 compared to September 30, 2009, due to fewer policies available to renew and impacts from industry trends reflecting declines in vehicle registrations and vehicle sales per households

2.5% increase in new issued applications on a countrywide basis to 537 thousand in the third quarter of 2010 from 524 thousand in the third quarter of 2009. A 2.7% decrease to 1,499 thousand in the first nine months of 2010 from 1,541 thousand in the first nine months of 2009 impacted by decreases in Florida and California, due in part to rate actions that were approved in 2009 in these markets and other actions to improve profitability. Excluding Florida and California, new issued applications on a countrywide basis increased 13.5% to 428 thousand in the third quarter of 2010 from 377 thousand in the third quarter of 2009, and increased 11.1% to 1,185 thousand in the first nine months of 2010 from 1,067 thousand in the first nine months of 2009. New issued application increased in 39 states, most of which offer an auto discount (the Preferred Package Discount) for our target customer (multi-car residence owner).

increased average gross premium in the third quarter and first nine months of 2010 compared to the same periods of 2009, primarily due to rate changes, partially offset by customers electing to lower coverage levels of their policy

0.4 point decrease in the renewal ratio in the third quarter of 2010 compared to the same period of 2009, primarily due to profitability management actions in California, Georgia, New York and North Carolina, and the renewal ratio in the first nine months of 2010 was comparable to the same period of 2009

The level of Encompass premiums written continues to be impacted by comprehensive actions designed to improve Encompass brand profitability.

Rate changes that are indicated based on loss trend analysis to achieve a targeted return will continue to be pursued. The following table shows the rate changes that were approved for standard auto and does not include rating plan enhancements, including the introduction of discounts and surcharges, that result in no change in the overall rate level in the state. These rate changes do not reflect initial rates filed for insurance subsidiaries initially writing business in a state.

	Three months ended September 30,					
	# of States		Countrywide(%) (1)		State Specific(%) (2) (3)	
	2010	2009	2010	2009	2010	2009
Allstate brand	21 (5)	15	0.5	1.4	2.8	6.5
Encompass brand	12	13	(0.1)	1.6	(1.3)	9.6

	Nine months ended September 30,					
	# of States		Countrywide(%) (1)		State Specific(%) (2) (3)	
	2010	2009	2010	2009	2010	2009
Allstate brand (4)	43 (5)	33	1.0	3.1	2.0	6.1

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Encompass brand	22	35	1.2	6.1	2.6	9.1
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- (1) Represents the impact in the states where rate changes were approved during the three months and nine months ended September 30, 2010 and 2009, respectively, as a percentage of total countrywide prior year-end premiums written.
- (2) Represents the impact in the states where rate changes were approved during the three months and nine months ended September 30, 2010 and 2009, respectively, as a percentage of its respective total prior year-end premiums written in those states.
- (3) Based on historical premiums written in those states, rate changes approved for standard auto totaled \$80 million and \$163 million in the three months and nine months ended September 30, 2010, respectively, compared to \$238 million and \$544 million in the three months and nine months ended September 30, 2009, respectively.
- (4) Includes Washington D.C.
- (5) Includes targeted rate decreases in certain markets to improve our competitive position for target customers (multi-car residence owners).

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Non-standard auto premiums written totaled \$224 million in the third quarter of 2010, a decrease of 7.1% from \$241 million in the third quarter of 2009, and \$685 million in the first nine months of 2010, a decrease of 5.8% from \$727 million in the first nine months of 2009.

<u>Non-Standard Auto</u>	Allstate brand		Encompass brand	
	2010	2009	2010	2009
Three months ended September 30,				
PIF (thousands)	671	733	6	25
Average premium-gross written	\$ 630	\$ 613	\$ 387	\$ 470
Renewal ratio (%)	70.8	72.6	42.5	70.5
Nine months ended September 30,				
PIF (thousands)	671	733	6	25
Average premium-gross written	\$ 623	\$ 613	\$ 425	\$ 480
Renewal ratio (%)	71.7	72.5	44.6	69.5

Allstate brand non-standard auto premiums written totaled \$223 million in the third quarter of 2010, a decrease of 5.1% from \$235 million in the third quarter of 2009, and \$680 million in the first nine months of 2010, a decrease of 4.0% from \$708 million in the first nine months of 2009. Contributing to the Allstate brand non-standard auto premiums written decrease in the third quarter and first nine months of 2010 compared to the same periods of 2009 were the following:

decrease in PIF as of September 30, 2010 compared to September 30, 2009, due to a decline in the number of policies available to renew and fewer new issued applications

23.1% decrease in new issued applications to 70 thousand in the third quarter of 2010 from 91 thousand in the third quarter of 2009, and 11.8% decrease to 246 thousand in the first nine months of 2010 from 279 thousand in the first nine months of 2009

increase in average gross premium in the third quarter and first nine months of 2010 compared to the same periods of 2009

1.8 point and 0.8 point decrease in the renewal ratio in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

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Rate changes that are indicated based on loss trend analysis to achieve a targeted return will continue to be pursued. The following table shows the rate changes that were approved for non-standard auto and does not include rating plan enhancements, including the introduction of discounts and surcharges, that result in no change in the overall rate level in the state. These rate changes do not reflect initial rates filed for insurance subsidiaries initially writing business in a state.

	Three months ended September 30,					
	# of States		Countrywide(%) (1)		State Specific(%) (2) (3)	
	2010	2009	2010	2009	2010	2009
Allstate brand	4	4	0.7	1.2	5.8	5.5
Encompass brand	--	--	--	--	--	--

	Nine months ended September 30,					
	# of States		Countrywide(%) (1)		State Specific(%) (2) (3)	
	2010	2009	2010	2009	2010	2009
Allstate brand	10 (4)	9	4.2	1.5	10.5	4.5
Encompass brand	--	1	--	0.9	--	31.7

- (1) Represents the impact in the states where rate changes were approved during the three months and nine months ended September 30, 2010 and 2009, respectively, as a percentage of total countrywide prior year-end premiums written.
- (2) Represents the impact in the states where rate changes were approved during the three months and nine months ended September 30, 2010 and 2009, respectively, as a percentage of its respective total prior year-end premiums written in those states.
- (3) Based on historical premiums written in those states, rate changes approved for non-standard auto totaled \$6 million and \$38 million in the three months and nine months ended September 30, 2010, respectively, compared to \$12 million and \$15 million in the three months and nine months ended September 30, 2009, respectively.
- (4) Includes Washington D.C.

Homeowners premiums written totaled \$1.71 billion in the third quarter of 2010, an increase of 1.5% from \$1.68 billion in the third quarter of 2009, and \$4.64 billion in the first nine months of 2010, an increase of 0.9% from \$4.60 billion in the first nine months of 2009. Excluding the cost of catastrophe reinsurance, premiums written increased 0.5% and 0.3% in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009.

<u>Homeowners</u>	Allstate brand		Encompass brand	
	2010	2009	2010	2009
Three months ended September 30,				
PIF (thousands)	6,740	7,027	322	391
Average premium-gross written (12 months) \$	953	\$ 889	\$ 1,311	\$ 1,279
Renewal ratio (%)	88.6	88.5	76.5	79.3
Nine months ended September 30,				
PIF (thousands)	6,740	7,027	322	391
Average premium-gross written (12 months) \$	937	\$ 878	\$ 1,304	\$ 1,262
Renewal ratio (%)	88.3	88.0	76.7	79.4

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Allstate brand homeowners premiums written totaled \$1.61 billion in the third quarter of 2010, an increase of 2.4% from \$1.57 billion in the third quarter of 2009, and \$4.36 billion in the first nine months of 2010, an increase of 2.1% from \$4.28 billion in the first nine months of 2009. Contributing to the Allstate brand homeowners premiums written increase in the third quarter and first nine months of 2010 compared to the same periods of 2009 were the following:

decrease in PIF of 4.1% as of September 30, 2010 compared to September 30, 2009, due to fewer policies available to renew and fewer new issued applications

5.4% decrease in new issued applications to 140 thousand in the third quarter of 2010 from 148 thousand in the third quarter of 2009 and 2.4% decrease to 410 thousand in the first nine months of 2010 from 420 thousand in the first nine months of 2009. Our Castle Key Indemnity Company subsidiary continues to have a favorable impact on new issued applications, due to a 2008 regulatory consent decree to sell 50,000 new homeowners policies in Florida by November 2011. Excluding Florida, new issued applications on a countrywide basis decreased 16.2% to 124 thousand in the third quarter of 2010 from 148 thousand in the third quarter of 2009, and 10.7% to 375 thousand in the first nine months of 2010 from 420 thousand in the first nine months of 2009.

increase in average gross premium in the third quarter and first nine months of 2010 compared to the same periods of 2009, primarily due to rate changes

0.1 point and 0.3 point increase in the renewal ratio in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009

decrease in the net cost of our catastrophe reinsurance program in both the third quarter and first nine months of 2010 compared to the same periods of 2009

As of September 30, 2010, an increased Home and Auto discount is now available in 38 states. This has successfully shifted our mix of new business towards multi-line customers.

Rate changes that are indicated based on loss trend analysis to achieve a targeted return will continue to be pursued. The following table shows the rate changes that were approved for homeowners, including rate changes approved based on our net cost of reinsurance, and does not include rating plan enhancements, including the introduction of discounts and surcharges, that result in no change in the overall rate level in the state.

	# of States		Three months ended September 30,			
			Countrywide(%) (1)		State Specific(%)	
	2010	2009	2010	2009	(2) (3)	
					2010	2009
Allstate brand	15	19 (4)	1.0	2.4	4.2	6.9
Encompass brand	8 (4)	17	--	2.0	(0.1)	4.8
	# of States		Nine months ended September 30,			
			Countrywide(%) (1)		State Specific(%) (2) (3)	
	2010	2009	2010	2009	2010	2009

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	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Allstate brand (4)	26	33	3.8	6.6	9.4	9.9
Encompass brand (4)	18	33	0.6	4.1	1.8	6.0

- (1) Represents the impact in the states where rate changes were approved during the three months and nine months ended September 30, 2010 and 2009, respectively, as a percentage of total countrywide prior year-end premiums written.
- (2) Represents the impact in the states where rate changes were approved during the three months and nine months ended September 30, 2010 and 2009, respectively, as a percentage of its respective total prior year-end premiums written in those states.
- (3) Based on historical premiums written in those states, rate changes approved for homeowners totaled \$59 million and \$233 million in the three months and nine months ended September 30, 2010, respectively, compared to \$158 million and \$420 million in the three months and nine months ended September 30, 2009, respectively.
- (4) Includes Washington D.C.

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Underwriting results are shown in the following table.

(\$ in millions)	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Premiums written	\$ 6,767	\$ 6,810	\$ 19,665	\$ 19,695
Premiums earned	\$ 6,498	\$ 6,535	\$ 19,514	\$ 19,678
Claims and claims expense	(4,582)	(4,557)	(14,085)	(14,274)
Amortization of DAC	(915)	(943)	(2,754)	(2,832)
Other costs and expenses	(705)	(641)	(2,070)	(1,906)
Restructuring and related charges	(9)	(31)	(34)	(88)
Underwriting income	\$ 287	\$ 363	\$ 571	\$ 578
Catastrophe losses	\$ 386	\$ 407	\$ 1,670	\$ 1,741
Underwriting income (loss) by line of business				
Standard auto	\$ 258	\$ 284	\$ 688	\$ 743
Non-standard auto	23	24	48	64
Homeowners	(63)	27	(312)	(293)
Other personal lines	69	28	147	64
Underwriting income	\$ 287	\$ 363	\$ 571	\$ 578
Underwriting income (loss) by brand				
Allstate brand	\$ 292	\$ 364	\$ 611	\$ 576
Encompass brand	(5)	(1)	(40)	2
Underwriting income	\$ 287	\$ 363	\$ 571	\$ 578

Allstate Protection experienced underwriting income of \$287 million in the third quarter of 2010 compared to \$363 million in the third quarter of 2009, and \$571 million in the first nine months of 2010 compared to \$578 million in the first nine months of 2009. The decrease in the third quarter of 2010 compared to the same period of 2009 was primarily due to decreases in homeowners and standard auto underwriting income, partially offset by increases in other personal lines underwriting income. Homeowners underwriting loss was \$63 million in the third quarter of 2010 compared to an underwriting income of \$27 million in the third quarter of 2009 primarily due to increases in expenses and catastrophe losses, including prior year reserve reestimates for catastrophes, and a \$70 million unfavorable prior year reserve reestimate related to a litigation settlement, partially offset by average earned premiums increasing faster than loss costs. Standard auto underwriting income decreased 9.2% to an underwriting income of \$258 million in the third quarter of 2010 from an underwriting income of \$284 million in the third quarter of 2009 primarily due to increases in auto claim frequency and expenses, partially offset by favorable reserve reestimates and decreases in catastrophe losses. Other personal lines underwriting income increased 146.4% to an underwriting income of \$69 million in the third quarter of 2010 from an underwriting income of \$28 million in the third quarter of 2009 primarily due to increases in favorable reserve reestimates.

The Allstate Protection underwriting income decreased in the first nine months of 2010 compared to the same period of 2009 primarily due to decreases in standard auto underwriting income, increases in homeowners underwriting losses and decreases in non-standard auto underwriting income, partially offset by increases in other personal lines underwriting income. Standard auto underwriting income decreased 7.4% to an underwriting income of \$688 million in the first nine months of 2010 from an underwriting income of \$743 in the first nine months of 2009 primarily due to increases in auto claim frequency and expenses, partially offset by favorable reserve reestimates and decreases in catastrophe

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losses. Homeowners underwriting loss increased 6.5% to an underwriting loss of \$312 million in the first nine months of 2010 from an underwriting loss of \$293 million in the first nine months of 2009 primarily due to a \$70 million unfavorable prior year reserve reestimate related to a litigation settlement and increases in expenses and catastrophe losses, including prior year reestimates, partially offset by average earned premiums increasing faster than loss costs. Non-standard auto underwriting income decreased 25.0% to an underwriting income of \$48 million in the first nine months of 2010 from an underwriting income of

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\$64 million in the first nine months of 2009 primarily due to decreases in premiums earned and increases in auto claim frequency, partially offset by favorable reserve reestimates and decreases in catastrophe losses. Other personal lines underwriting income increased 129.7% to an underwriting income of \$147 million in the first nine months of 2010 from an underwriting income of \$64 million in the first nine months of 2009 primarily due to increases in favorable reserve reestimates.

Catastrophe losses in the third quarter and first nine months of 2010 were \$386 million and \$1.67 billion, respectively, as detailed in the table below. This compares to catastrophe losses in the third quarter and first nine months of 2009 of \$407 million and \$1.74 billion, respectively.

We define a catastrophe as an event that produces pre-tax losses before reinsurance in excess of \$1 million and involves multiple first party policyholders, or an event that produces a number of claims in excess of a preset, per-event threshold of average claims in a specific area, occurring within a certain amount of time following the event. Catastrophes are caused by various natural events including high winds, winter storms, tornadoes, hailstorms, wildfires, tropical storms, hurricanes, earthquakes and volcanoes. We are also exposed to man-made catastrophic events, such as certain acts of terrorism or industrial accidents. The nature and level of catastrophes in any future period cannot be reliably predicted.

Catastrophe losses related to events that occurred by the size of the event are shown in the following table.

(\$ in millions)

	Number of events		Three months ended September 30, 2010		Combined ratio impact	Average catastrophe loss per event
			Claims and claims expense			
Size of catastrophe						
\$50 million to \$100 million	1	3.4%	\$ 66	17.1%	1.0	\$ 66
Less than \$50 million	28	96.6	305	79.0	4.7	11
Total	29	100.0%	371	96.1	5.7	13
Prior year reserve reestimates			(42)	(10.9)	(0.6)	
Prior quarter reserve reestimates			57	14.8	0.8	
Total catastrophe losses			\$ 386	100.0%	5.9	
	Number of events		Nine months ended September 30, 2010		Combined ratio impact	Average catastrophe loss per event
			Claims and claims expense			
Size of catastrophe						
\$101 million to \$250 million	3	4.3%	\$ 485	29.1%	2.5	\$ 162
\$50 million to \$100 million	8	11.4	538	32.2	2.8	67
Less than \$50 million	59	84.3	787	47.1	4.0	13
Total	70	100.0%	1,810	108.4	9.3	26
Prior year reserve reestimates			(140)	(8.4)	(0.7)	
Total catastrophe losses			\$ 1,670	100.0%	8.6	

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Catastrophe losses incurred by the type of event are shown in the following table.

(\$ in millions)

	2010	Three months ended September 30,			Number of events	2010	2009	Number of events	2010	2009	Number of events	2010	2009	Number of events
		2010	2009	2009										
Hurricanes/Tropical storms	\$	18	1	\$	--	--	\$	18	1	\$	--	--	--	--
Tornadoes		5	1	--	--	138		6	332		4			
Wind/Hail		327	25	384	22	1,384		55	1,334		57			
Other events		21	2	17	2	270		8	214		8			
Prior year reserve reestimates		(42)		(80)		(140)			(139)					
Prior quarter reserve reestimates		57		86		--			--					
Total catastrophe losses	\$	386	29	\$	407	24	\$	1,670	70	\$	1,741			69

Combined ratio Loss ratios are a measure of profitability. Loss ratios by product, and expense and combined ratios by brand, are shown in the following table. These ratios are defined in the Property-Liability Operations section of the MD&A.

	Three months ended September 30,								Nine months ended September 30,							
	Loss ratio (1)				Effect of catastrophe losses on the loss ratio				Effect of pre-tax reserve reestimates on the combined ratio				Loss ratio (1)			
	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009
Allstate brand loss ratio:																
Standard auto	68.7	68.6	0.4	1.3	(0.6)	0.3	69.5	69.4	1.0	1.7	(0.9)	(0.1)				
Non-standard auto	61.7	63.6	--	0.4	(6.8)	(3.9)	66.5	66.4	0.3	0.8	(4.3)	(2.3)				
Homeowners	80.5	75.4	23.1	22.3	5.2	(5.2)	83.5	84.5	31.6	31.9	0.2	(2.4)				
Other personal lines	61.4	64.1	4.4	4.0	(6.3)	(0.8)	63.5	67.5	6.6	7.2	(3.6)	1.7				
Total Allstate brand loss ratio	70.5	69.5	6.0	6.3	--	(1.2)	72.0	72.5	8.5	9.1	(1.0)	(0.6)				
Allstate brand expense ratio	24.8	24.6					24.7	24.4								
Allstate brand combined ratio	95.3	94.1					96.7	96.9								
Encompass brand loss ratio:																
Standard auto	75.7	76.9	0.6	0.5	(1.7)	3.6	75.2	74.8	0.7	0.6	1.8	1.0				
Non-standard auto	100.0	66.7	--	--	--	(16.7)	100.0	72.7	--	--	--	(9.1)				
Homeowners	63.5	67.6	13.5	15.7	(7.3)	(1.9)	77.4	68.6	25.3	16.2	(3.4)	(4.4)				
Other personal lines	60.9	65.4	--	--	(4.3)	7.7	72.2	72.0	4.2	1.2	(1.4)	9.8				
Total Encompass brand loss ratio	70.7	73.1	4.8	5.0	(3.7)	1.9	75.9	72.7	8.8	5.2	(0.1)	(0.2)				
Encompass brand expense ratio	31.0	27.2					28.4	27.1								
Encompass brand combined ratio	101.7	100.3					104.3	99.8								

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Allstate Protection loss ratio	70.5		69.7		5.9	6.2	(0.2)	(1.0)	72.2		72.6	8.6	8.8	(1.0)	(0.5)
Allstate Protection expense ratio	25.1		24.7						24.9		24.5				
Allstate Protection combined ratio	95.6		94.4						97.1		97.1				

(1) Ratios are calculated using the premiums earned for the respective line of business.

Standard auto loss ratio for the Allstate brand increased 0.1 points in both the third quarter and first nine months of 2010 compared to the same periods of 2009 due to higher claim frequency, partially offset by favorable reserve reestimates and lower catastrophe losses. In the third quarter and first nine months of 2010, claim frequencies in the bodily injury and physical damage coverages have increased compared to the same periods of

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2009, but remain within historical norms. Bodily injury and physical damage coverages severity results increased in line with historical Consumer Price Index (CPI) trends.

Non-standard auto loss ratio for the Allstate brand decreased 1.9 points in the third quarter of 2010 compared to the same period of 2009 due to higher favorable reserve reestimates and lower catastrophe losses, partially offset by higher claim frequencies. Non-standard auto loss ratio for the Allstate brand increased 0.1 points in the first nine months of 2010 compared to the same period of 2009 due to higher claim frequencies, partially offset by higher favorable reserve reestimates and lower catastrophe losses. Bodily injury and physical damage coverages severity results increased in line with historical CPI trends.

Homeowners loss ratio for the Allstate brand increased 5.1 points to 80.5 in the third quarter of 2010 from 75.4 in the third quarter of 2009, and decreased 1.0 points to 83.5 in the first nine months of 2010 from 84.5 in the first nine months of 2009. The increase in the third quarter of 2010 compared to the same period of 2009 was due to a \$70 million unfavorable prior year reserve reestimate related to a litigation settlement and higher catastrophe losses including prior year reserve reestimates for catastrophes, partially offset by average earned premiums increasing faster than loss costs. The decrease in the first nine months of 2010 compared to the same period of 2009 was due to average earned premiums increasing faster than loss costs and lower catastrophe losses including prior year reserve reestimates for catastrophes, partially offset by a \$70 million unfavorable prior year reserve reestimate related to a litigation settlement.

Expense ratio for Allstate Protection increased 0.4 points in both the third quarter and first nine months of 2010 compared to the same periods of 2009. Restructuring costs decreased 0.4 points and 0.2 points in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009, driven by costs associated with claim office consolidations and technology prioritization and efficiency efforts. Excluding restructuring, the expense ratio for Allstate Protection increased 0.8 points and 0.6 points in the third quarter and first nine months of 2010, respectively, compared to the same periods of 2009. Improved operational efficiencies were offset by increased investments in marketing and increases in the net costs of employee benefits.

The impact of specific costs and expenses on the expense ratio are included in the following table.

	Three months ended September 30,					
	Allstate brand		Encompass brand		Allstate Protection	
	2010	2009	2010	2009	2010	2009
Amortization of DAC	13.9	14.2	18.1	18.3	14.1	14.4
Other costs and expenses	10.8	9.9	11.6	8.6	10.9	9.8
Restructuring and related charges	0.1	0.5	1.3	0.3	0.1	0.5
Total expense ratio	24.8	24.6	31.0	27.2	25.1	24.7

	Nine months ended September 30,					
	Allstate brand		Encompass brand		Allstate Protection	
	2010	2009	2010	2009	2010	2009
Amortization of DAC	13.9	14.1	18.2	18.5	14.1	14.4
Other costs and expenses	10.7	9.8	9.4	8.3	10.6	9.7
Restructuring and related charges	0.1	0.5	0.8	0.3	0.2	0.4

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Total expense ratio	24.7	24.4	28.4	27.1	24.9	24.5
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Allstate Protection Reinsurance

Our catastrophe reinsurance program was designed, utilizing our risk management methodology, to address our exposure to catastrophes nationwide. Our program provides reinsurance protection for catastrophes including storms named or numbered by the National Weather Service, fires following earthquakes, earthquakes and wildfires, including California wildfires. These reinsurance agreements are part of our catastrophe management strategy, which is intended to provide our shareholders an acceptable return on the risks assumed in our property business, and to reduce variability of earnings while providing protection to our customers.

Our reinsurance program coordinates coverage under various agreements and comprises agreements that provide coverage for the occurrence of:

- certain qualifying catastrophes in specific states including New York, New Jersey, Connecticut, Rhode Island, Pennsylvania, and California for multiple perils (multi-peril). The California contracts that expire May 31, 2011 and May 31, 2012, provide coverage only for fires following earthquakes, and the California contract, expiring May 31, 2013, reinsures multiple perils, including earthquakes and fires following earthquakes, resulting in the classification of the California agreement as a multi-peril agreement;
- hurricane catastrophe losses in the states of Texas, Louisiana, Mississippi and Alabama (Gulf States) and Georgia, South Carolina, North Carolina, Virginia, Maryland and Delaware and the District of Columbia (Atlantic States);
- hurricane catastrophe losses in the state of Texas (Texas Hurricane); and for earthquakes and fires following earthquakes losses in the state of Kentucky (Kentucky); and
- the aggregate or sum of qualifying losses nationwide, excluding Florida, in excess of an annual retention associated with storms named or numbered by the National Weather Service, fires following earthquakes and California wildfires (aggregate excess).

During the second quarter of 2010, we placed reinsurance contracts for the state of Florida. The Florida component of the reinsurance program is designed separately from the other components of the program to address the distinct needs of our separately capitalized legal entities in that state. See The Allstate Corporation Form 10-Q for the quarterly period ended June 30, 2010 for additional details on our current Florida program.

We estimate that the total annualized cost of all catastrophe reinsurance programs for the year beginning June 1, 2010 will be approximately \$560 million or \$140 million per quarter compared to \$640 million annualized cost for the year beginning June 1, 2009. The total cost of our reinsurance programs during 2009 was \$158 million in the first quarter, \$156 million in the second quarter, \$162 million in the third quarter and \$153 million in the fourth quarter. The total cost of our property catastrophe reinsurance programs during the first, second and third quarter of

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2010 was \$151 million, \$152 million and \$142 million, respectively. We continue to attempt to capture our reinsurance cost in premium rates as allowed by state regulatory authorities.

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Reserve reestimates The tables below show Allstate Protection net reserves representing the estimated cost of outstanding claims as they were recorded at the beginning of years 2010 and 2009, and the effect of reestimates in each year.

(\$ in millions)	January 1 reserves	
	2010	2009
Auto	\$ 10,606	\$ 10,220
Homeowners	2,399	2,824
Other personal lines	2,145	2,207
Total Allstate Protection		