SELECTIVE INSURANCE GROUP INC
Form 10-K
February 28, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

(Mark one)

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

For the fiscal year ended December 31, 2007

OR

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

For the transition period from __________ to __________.

Commission file number 0-8641

SELECTIVE INSURANCE GROUP, INC.

(Exact name of registrant as specified in its charter)

New Jersey	22-2168890
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
40 Wantage Avenue, Branchville, New Jersey	07890
(Address of Principal Executive Office)	(Zip Code)

Registrant s telephone number, including area code: (973) 948-3000

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

Title of Each Class	Name of Each Exchange on Which Registered
7.5% Junior Subordinated Notes due September 27, 2066	New York Stock Exchange
Common Stock, par value $2 per share	NASDAQ Global Select Market

Preferred Share Purchase Rights

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

þ Yes o No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

o Yes þ No

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, and (2) has been subject to such filing requirements for the past 90 days.

þ Yes o No

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

o

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o (Do not check if a smaller reporting company) Smaller reporting company o

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

o Yes þ No

The aggregate market value of the voting Common stock held by non-affiliates of the registrant, based on the closing price on the NASDAQ Global Select Market, was $1,393,617,821 on June 30, 2007.

As of February 15, 2008, the registrant had outstanding 53,869,967 shares of Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive Proxy Statement for the 2008 Annual Meeting of Stockholders to be held on April 24, 2008 are incorporated by reference into Part III of this report.

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Exhibit 99.1

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PART I

Item 1. Business.

Overview

Selective Insurance Group, Inc., through its subsidiaries, (collectively known as Selective or the Company) offers property and casualty insurance products and diversified insurance services and products. Selective Insurance Group, Inc. was incorporated in New Jersey in 1977 and its main offices are located in Branchville, New Jersey. Selective Insurance Group, Inc. s Common Stock is publicly traded on the NASDAQ Global Select Market under the symbol, SIGI.

Selective classifies its business into three operating segments:

- Insurance Operations, which sells property and casualty insurance products and services primarily in 21 states in the Eastern and Midwestern United States;
- Investments; and
- Diversified Insurance Services, which provides human resource administration outsourcing products and services, and federal flood insurance administrative services.

Financial information about Selective s three operating segments is contained in this report in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8. Financial Statements and Supplementary Data, Note 12 to the consolidated financial statements, Segment Information.

Description of Operating Segment Products and Markets

Insurance Operations Segment

Selective s Insurance Operations sell property and casualty insurance policies, which are contracts to cover losses for specified risks in exchange for premiums. Property insurance generally covers the financial consequences of accidental loss to the insured s property. Property claims are generally reported and settled in a relatively short period of time. Casualty insurance generally covers the financial consequences of bodily injury and/or property damage to a third party as a result of the insured s negligent acts, omissions, or legal liabilities. Casualty claims often take years to be reported and settled.

Selective s Insurance Operations segment writes its property and casualty insurance products through seven insurance subsidiaries (Insurance Subsidiaries), which are listed on the following table together with their respective pooled financial strength ratings by A.M. Best Company, Inc. (A.M. Best), and state of domicile by which each is primarily regulated:

Insurance Subsidiaries	A.M. Best Rating[1]	Domiciliary State
Selective Insurance Company of America (SICA)	A+ (Superior)	New Jersey
Selective Way Insurance Company (SWIC)	A+ (Superior)	New Jersey
Selective Insurance Company of South Carolina (SICSC)	A+ (Superior)	South Carolina
Selective Insurance Company of the Southeast (SICSE)	A+ (Superior)	North Carolina
Selective Insurance Company of New York (SICNY)	A+ (Superior)	New York
Selective Insurance Company of New England (SICNE)	A+ (Superior)	Maine
Selective Auto Insurance Company of New Jersey (SAICNJ)	A+ (Superior)	New Jersey

[1] With regard to an A+ rating, A.M. Best uses its highest Financial Strength Rating of Secure, and a descriptor of Superior, which

it defines as, Assigned to companies that have, in our opinion, a superior ability to meet their ongoing obligations to policyholders. Only 10% of commercial and personal insurance companies carry an A+ or better rating from A.M. Best.

In 2007, A.M. Best, in its list of Top Property/Casualty Writers, ranked Selective the 46th largest property and casualty group in the United States based on the combined net premiums written (NPW) for 2006.

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Insurance Operations

Selective s Insurance Operations segment derives substantially all of its revenues from insurance policy premiums. The Insurance Subsidiaries predominantly write annual policies, of which the associated premiums are defined as NPW. NPW is recognized as revenue as net premiums earned (NPE) ratably over the term of the insurance policy. Expenses fall into three categories: (i) losses associated with claims and various loss expenses incurred for adjusting claims; (ii) expenses related to the issuance of insurance policies, such as agent commissions, premium taxes, and other underwriting expenses, including employee compensation and benefits; and (iii) policyholder dividends.

Selective s Insurance Subsidiaries are regulated by each of the states in which they do business. Each Insurance Subsidiary is required to file financial statements with such states, prepared in accordance with accounting principles prescribed by, or permitted by, such Insurance Subsidiary s state of domicile (Statutory Accounting Principles or SAP). SAP have been promulgated by the National Association of Insurance Commissioners (NAIC) and adopted by the various states. Selective evaluates the performance of our Insurance Subsidiaries in accordance with SAP. Incentive-based compensation to independent agents and employees is based on SAP results and our rating agencies use SAP information to evaluate our performance and for industry comparative purposes.

The underwriting performance of insurance companies is measured under SAP by four different ratios:

1) Loss and loss expense ratio, which is calculated by dividing incurred loss and loss expenses by NPE;

2) Underwriting expense ratio, which is calculated by dividing all expenses related to the issuance of insurance policies by NPW;

3) Dividend ratio, which is calculated by dividing policyholder dividends by NPE; and

4) Combined ratio, which is the sum of the loss and loss expense ratio, the underwriting expense ratio, and the dividend ratio.

A statutory combined ratio under 100% generally indicates an underwriting profit and a statutory combined ratio over 100% generally indicates an underwriting loss. The statutory combined ratio does not reflect investment income, federal income taxes, or other non-operating income or expense.

SAP differs in several ways from generally accepted accounting principles in the United States of America (GAAP), under which Selective is required to report our financial results to the United States Securities and Exchange Commission (SEC). The most notable differences impacting our reported net income are as follows:

Under SAP, underwriting expenses are recognized when incurred; whereas under GAAP, underwriting expenses are deferred and amortized over the life of the policy;

Under SAP, the underwriting expense ratio is calculated using NPW as the denominator; whereas NPE is used as the denominator under GAAP; and

Under SAP, the results of Selective s flood line of business are included in the Insurance Operations segment, whereas under GAAP, these results are included within the Diversified Insurance Services segment.

Selective primarily uses SAP information to monitor and manage its results of operations. Selective believes that providing SAP financial information for the Insurance Operations segment helps its investors, agents, and customers better evaluate the underwriting success of Selective s insurance business.

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The following table shows the statutory results of the Insurance Operations segment for the last three completed fiscal years:

	Year Ended December 31,		
(in thousands)	**2007**	2006	2005
Insurance Operations Results			
NPW	$ **1,562,728**	1,540,901	1,462,914
NPE	$ **1,525,163**	1,504,632	1,421,439
Losses and loss expenses incurred	**997,230**	958,741	902,557
Net underwriting expenses incurred	**494,944**	482,657	449,569
Policyholders dividends	**7,202**	5,927	5,688
Underwriting profit	$ **25,787**	57,307	63,625
Ratios:			
Losses and loss expense ratio	**65.4**%	63.7	63.5
Underwriting expense ratio	**31.6**%	31.3	30.7
Policyholders dividends ratio	**0.5**%	0.4	0.4
Combined ratio	**97.5**%	95.4	94.6
GAAP Combined ratio [1]	**98.9** %	96.1	95.1

[1] The GAAP Combined ratio excludes the flood line of business, which is included in the Diversified Insurance Services segment on a GAAP basis. The total Statutory Combined ratio excluding flood was 98.2% in 2007, 96.1% in 2006, and 95.3% in 2005.

Historically, Selective has produced a lower statutory combined ratio than the property and casualty insurance industry, and outperformed the industry average for the past 10-year period by 2.3 points. The table below sets forth a comparison of certain Company and industry statutory ratios:

	Simple Average of All Periods Presented	**2007**	2006	2005	2004	2003	2002	2001	2000	1999	1998
Selective Ratios: (1)											
Loss and loss expense	69.5%	**65.4**	63.7	63.5	65.3	70.3	72.3	74.3	75.7	74.4	70.2
Underwriting expense	31.1	**31.6**	31.3	30.7	30.3	30.7	30.3	31.5	31.7	30.5	32.2
Policyholders dividends	0.6	**0.5**	0.4	0.4	0.3	0.5	0.6	0.9	0.9	0.8	0.7
Statutory combined ratio	101.2	**97.5**	95.4	94.6	95.9	101.5	103.2	106.7	108.2	105.7	103.2
Growth (decline) in net premiums written	8.2	**1.4**	5.3	6.9	12.0	15.7	13.8	10.5	3.6	8.1	4.4
Industry Ratios: (1) (2)											
Loss and loss expense	76.3	**67.7**	65.3	75.3	73.5	75.0	81.5	88.4	81.5	78.8	76.2
Underwriting expense	26.3	**27.2**	26.2	25.4	24.9	24.6	25.1	26.5	27.4	27.9	27.7
Policyholders dividends	0.9	**0.6**	0.9	0.5	0.5	0.5	0.6	0.8	1.4	1.3	1.7
Statutory combined ratio	103.5	**95.6**	92.4	101.2	98.9	100.1	107.3	115.7	110.4	108.1	105.6
Growth in net premiums written	4.9	**(1.2)**	3.9	0.0	4.4	9.7	15.1	8.5	4.7	1.9	1.8
Selective Favorable (Unfavorable) to Industry:											
Statutory combined ratio	2.3	**(1.9)**	(3.0)	6.6	3.0	(1.4)	4.1	9.0	2.2	2.4	2.4
Growth (decline) in net premiums written	33	**2.6**	1.4	6.9	7.6	6.0	(1.3)	2.0	(1.1)	6.2	2.6

1. The ratios and percentages are based upon SAP prescribed or permitted by state insurance departments in the states in which each company is domiciled. Effective January 1, 2001, Selective adopted a codified set of statutory accounting principles, as

required by the NAIC. These principles were not retroactively applied, but would not have had a material effect on the ratios presented above.

2. Source: A.M. Best. The industry ratios for 2007 have been estimated by A.M. Best.

Lines of Business and Products

Selective s Insurance Operations segment includes commercial lines (Commercial Lines), which markets primarily to businesses and represents approximately 87% of Selective s NPW; and personal lines (Personal Lines), which markets primarily to individuals and represents approximately 13% of NPW.

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Commercial Lines

Commercial Lines underwrites general liability, commercial automobile, workers compensation, commercial property, business owners policy, and bond risks through traditional insurance and alternative risk management products.

Personal Lines

Personal Lines underwrites and issues insurance policies for personal automobile, homeowners, and other various risks.

Regional Geographic Market Focus

Selective s Insurance Operations segment primarily focuses its marketing efforts and sells its products and services in the Eastern and Midwestern regions of the United States. Although still concentrated in coastal eastern states, this geographic diversification lessens Selective s exposure to regulatory, competitive and catastrophic risk. The Insurance Operations segment does not conduct any business outside of the United States. The following table shows the principal states in which Selective writes insurance business and the percentage of Selective s total NPW that such state represents for the last three fiscal years.

	Year Ended December 31,		
Net Premiums Written	**2007**	2006	2005
New Jersey	**30.0**%	32.6	33.9
Pennsylvania	**14.1**	14.3	14.4
New York	**10.8**	11.1	11.2
Maryland	**7.6**	7.5	7.2
Virginia	**6.0**	5.9	5.6
Illinois	**4.4**	3.9	3.8
North Carolina	**4.0**	3.8	3.8
Georgia	**3.5**	3.2	3.1
Indiana	**3.5**	3.1	2.8
South Carolina	**2.8**	2.5	2.5
Michigan	**2.0**	1.9	1.8
Ohio	**1.8**	1.6	1.5
Connecticut	**1.7**	1.4	1.3
Rhode Island	**1.3**	1.3	1.2
Delaware	**1.2**	1.3	1.4
Wisconsin	**1.2**	1.1	1.1
Minnesota	**1.0**	1.1	1.1
Other states[1]	**3.1**	2.4	2.3
Total	**100.0**%	100.0	100.0

[1] Other states include, among others, Florida, Iowa, Kentucky, Missouri and Washington D.C.

Independent Insurance Agent Distribution Model

According to a study done by the Independent Insurance Agents and Brokers of America, in 2005, independent insurance agents and brokers wrote approximately 80% of commercial property and casualty insurance and approximately 36% of the personal lines insurance business in the United States. Independent agents are a significant force in overall insurance industry premium production, in large part because they represent more than one insurance company and, therefore, can provide insureds with a wider choice of commercial and personal property and casualty insurance products. As a result, Selective is committed to the independent agency distribution channel and focuses its primary strategy on building relationships with well-established, independent insurance agents, including efforts to assist in the hiring and training of producers. In addition, Selective carefully monitors each agent s profitability, growth, financial stability, staff, and mix of business against plans that are developed annually with the agent. In developing annual plans with its independent insurance agents, Selective s field personnel and management spend considerable time meeting with agencies to: (i) advise them on Company developments; (ii) receive feedback on products and services; (iii) help agents increase market share; and (iv) consolidate more of their business utilizing Selective s technology advantages.

As of December 31, 2007, Selective s Insurance Subsidiaries had entered into agency agreements with approximately 880 independent insurance agents having approximately 1,800 storefronts pursuant to these agreements. The agents are authorized to sell policies written by the Insurance Subsidiaries and are paid commissions pursuant to calculations and specific percentages stated in the agency agreement. Under the agency agreement, other than as provided by law, agents are not permitted to receive compensation for the business they place with Selective from any insured or applicant for insurance other than Selective. The agency agreement provides for commissions to be paid based on a percentage of the premium written. Selective and its agents also negotiate other compensation arrangements, including supplemental commissions, based on the volume and underwriting results of the business the agent writes with Selective.

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Technology and Field Model Business Strategy

Selective uses the service mark High Tech x High Touch = HT® to describe its business strategy for the Insurance Operations. High Tech signifies the advanced technology that Selective uses to make it easy for: (i) independent insurance agents to transact and process business with Selective; and (ii) customers to access real-time information, manage their accounts and pay their bills through an on-line customer portal that was established in September 2006. High Touch signifies the close relationships that Selective has with its independent insurance agents and customers as a result of its business model that places underwriters, claims representatives, technical or technology staff, and safety management representatives in the field near its agents and customers.

Technology

Selective seeks to transact as much of its business as possible through the use of technology and, in recent years, has made significant investments in state-of-the-art information technology platforms, integrated systems, Internet-based applications, and predictive modeling initiatives to: (i) provide its independent agents and customers with access to accurate business information; (ii) provide independent agents the ability to process business transactions from their offices and systems; and (iii) provide underwriters with targeted pricing tools to enhance profitability while growing the business. In 2007, Applied Systems Client Network presented Selective with the 2007 Commercial Lines Interface Carrier of the Year Award for promoting efficient communication between insurance carriers and independent agents. Applied Systems is a provider of automated solutions for property and casualty insurance agents. The award was given in recognition of Selective s excellent work to implement download and real-time interface technology with independent agents through its xSELerate® agency integration technology. Selective also received the 2007 Quantum Award from the AMS Users Group, another major provider of automated management solutions for agents, for creating technology that enables independent agents to make a quantum leap in productivity and profitability. This award was granted to Selective for increasing productivity and efficiency for its independent insurance agents through its xSELerate® agency integration technology. Additionally, Selective was recognized as a model carrier component by Celent, an IT consulting group, for its effective use of its xSELerate® technology.

Selective manages its information technology projects through a project management office (PMO). The PMO is staffed by certified individuals who apply methodologies to: (i) communicate project management standards; (ii) provide project management training and tools; (iii) review project status and cost; and (iv) provide non-technology project management consulting services to the rest of Selective. Selective s senior management meets monthly with the PMO to review all major projects and report on the status of other projects. Selective believes that the PMO is a factor in the success of its technology implementation and is a competitive advantage. Selective s technology operations are located in Branchville, New Jersey; Glastonbury, Connecticut; and Sarasota, Florida.

Field Strategy

To support its independent agents, Selective employs a field underwriting model and a field claims model that are supported by the home office in Branchville, New Jersey, and six regional branch offices (Region), which as of December 31, 2007 were as follows:

Region	Office Location
Great Lakes/Big River	Columbus, Ohio
Heartland	Carmel, Indiana
New Jersey	Hamilton, New Jersey
Northeast	Branchville, New Jersey
Mid-Atlantic	Allentown, Pennsylvania and Hunt Valley, Maryland
Southern	Charlotte, North Carolina

As of December 31, 2007, Selective s field force included:

- 98 Commercial Lines field underwriters, known as agency management specialists (AMSs). AMSs live and work in the geographic vicinity of Selective s appointed agents and generally work from offices in their homes. As a result of this close proximity and direct and regular interaction, AMSs are able to build strong relationships with agents.

- 11 Personal Lines territory managers that work with AMSs and independent agents to advance production. Territory managers build strong relationships with agents through direct and regular interaction, which better positions them to evaluate new business opportunities.

- 14 field technology employees. These employees work directly with agents, training and marketing Selective s technology systems like xSELerate® and SelectPLUS®. They also gather feedback from the agents to help improve Selective s technology to meet the needs of the agency force.

- 75 safety management specialists (SMSs). SMSs are located in the Regions and are responsible for surveying and assessing insured and prospective risks from a risk/safety standpoint, and for providing ongoing safety management services to certain insureds.

- 149 field claims adjusters, known as claim management specialists (CMSs). Like AMSs, CMSs live in the geographic vicinity of Selective s appointed agents and generally work from offices in their homes. CMSs, because of their geographic location, are able to conduct on-site inspections of losses and resolve claims faster, more accurately, and with higher levels of customer satisfaction. As a result, CMSs also obtain knowledge about potential exposures that they can share with AMSs.

Underwriting

Selective seeks to underwrite a variety of insurance risks and divides its markets into three segments:

- Small business accounts with premiums less than $25,000 represent 52% of total direct premium written. During 2007, 30% of new small business was written through Selective s Internet-based One & Done® system s automated underwriting templates;

- Middle market business accounts with premiums greater than $25,000 but less than $250,000 represent 42% of total direct premium written. This business, which cannot be written through the One & Done® system, is the primary focus of the AMSs; and,

- Large business accounts with annual premiums of approximately $250,000 or greater represent 6% of Selective s total direct premium written and are underwritten by a specialized commercial lines unit, Selective Risk Managers (SRM). Approximately 24% of the of the SRM premium includes alternative risk transfer mechanisms such as retrospective rating plans, self-insured group retention programs, or individual self-insured accounts.

Selective s underwriting process requires communication and interaction among:

- The independent agents and the AMSs, who identify product and market needs;

- Selective s strategic business units (SBUs), located in the home office, which are organized by customer and product type, and develop Selective s pricing and underwriting guidelines in conjunction with regions;

- The Regions, which work with the SBUs to establish annual premium and pricing goals; and

- The Actuarial Department, located in the home office, which assists in the determination of rate and pricing levels while also monitoring pricing and profitability.

Selective also has an underwriting service center (USC) located in Richmond, Virginia. The USC assists Selective s agents by servicing small to mid-sized business customers. During 2006, the USC became available to personal lines business customers of our New Jersey agents, with a rollout to Selective s remaining states during 2007. At the USC, Selective employees, who are licensed agents, respond to customer inquiries about insurance coverage, billing transactions, and other matters. The agent, as consideration for these services, receives a commission that is lower than the standard commission by approximately two points. Selective has found that the USC also provides additional opportunities to increase direct premiums written, as larger agencies seek insurance companies that have service center capabilities. Currently, the USC is servicing commercial lines net premiums written of $70 million and personal lines net premiums written of $33 million. The total $103 million serviced represents 7% of total net premiums written.

Selective believes that a distinct advantage of its field underwriting model is its ability to provide a wide range of front-line safety management services focused on improving the policyholder s safety and risk management programs, as expressed by its service mark Safety Management: Solutions for a safer workplace[SM] . Safety management services include: (i) risk evaluation and improvement surveys intended to evaluate potential exposures and provide solutions for mitigation; (ii) web-based safety management educational resources, including a large library of coverage-specific safety materials, videos and on-line courses, such as defensive driving and employee educational safety courses; (iii) thermographic infrared surveys aimed at identifying electrical hazards; and (iv) OSHA construction and general industry certification training. Risk improvement efforts for existing customers are designed to improve loss experience and policyholder retention through valuable ongoing consultative service. Selective s safety management goal is to partner with its policyholders to identify and eliminate potential loss exposures.

Selective analyzes its underwriting profitability by line of business, account, product, agency and other bases. Selective s goal is to continue to underwrite the risks that it understands well and that, in aggregate, are profitable.

Field Claims Management

Effective, fair, and timely claims management is one of the most important customer services that Selective provides and one of the critical factors in achieving underwriting profitability. Selective s claims practices emphasize the maintenance of timely and adequate claims reserves, and the cost-effective delivery of claims services by controlling losses and loss expenses. CMSs are primarily responsible for investigating and settling claims directly with policyholders and claimants. By promptly and personally investigating claims, CMSs are able to provide personal service and quickly resolve claims. CMSs also provide guidance on the handling of the claim until its final disposition. Selective also believes that by visiting the site of the claim, and meeting face-to-face with the insured or claimant, the settlement will be more accurate. In territories where there is insufficient claim volume to justify the placement of a CMS, or when a particular claim expertise is required, Selective uses independent adjusters to investigate and settle claims.

Selective has a centralized special investigations unit (SIU) that investigates potential insurance fraud and abuse, and supports efforts by regulatory bodies and trade associations to curtail the cost of fraud. The SIU adheres to uniform internal procedures to improve detection and takes action on potentially fraudulent claims. It is Selective s practice to notify the proper authorities of its findings. This practice sends a clear message that Selective will not tolerate fraudulent activity committed against it or its customers. The SIU also supervises anti-fraud training for CMSs and other employees, including AMSs.

Selective has a claims service center (CSC), co-located with the USC, in Richmond, Virginia. The CSC provides enhanced services to Selective s policyholders, including immediate claim review, 24 hours a day, seven days a week. The CSC is also designed to reduce the loss settlement time on first-party automobile claims and increase the usage of Selective s discounts at body shops, glass repair shops, and car rental agencies.

Net Loss and Loss Expense Reserves

Selective establishes loss and loss expense reserves that are estimates of amounts needed to pay claims and related expenses in the future for insured loss events that have already occurred. The process of estimating reserves involves a considerable degree of judgment by management and, as of any given date, is inherently uncertain. See Critical Accounting Policies and Estimates in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations in this Form 10-K for a full discussion regarding Selective s loss reserving process.

Selective s loss and loss expense reserve development over the proceeding 10 years is shown on the following table. Section I of the 10-year table shows the estimated liability that was recorded at the end of each of the indicated years for all current and prior accident year s unpaid loss and loss expenses. The liability represents the estimated amount of loss and loss expenses for claims that were unpaid at the balance sheet date, including incurred but not reported (IBNR) reserves. In accordance with GAAP, the liability for unpaid loss and loss expenses is recorded in the balance sheet gross of the effects of reinsurance with an estimate of reinsurance recoverables arising from reinsurance contracts reported separately as an asset. The net balance represents the estimated amount of unpaid loss and loss expenses outstanding as of the balance sheet date, reduced by estimates of amounts recoverable under reinsurance contracts.

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Section II shows the re-estimated amount of the previously recorded net liability as of the end of each succeeding year. Estimates of the liability for unpaid loss and loss expenses are increased or decreased as payments are made and more information regarding individual claims and trends, such as overall frequency and severity patterns, becomes known. Section III shows the cumulative amount of net loss and loss expenses paid relating to recorded liabilities as of the end of each succeeding year. Section IV shows the re-estimated gross liability and re-estimated reinsurance recoverables through December 31, 2007. Section V shows the cumulative net (deficiency)/redundancy representing the aggregate change in the liability from the original balance sheet dates and the re-estimated liability through December 31, 2007.

This table does not present accident or policy year development data. Conditions and trends that have affected development of the reserves in the past may not necessarily occur in the future. Accordingly, it may not be appropriate to extrapolate redundancies or deficiencies based on this table.

($ in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
I. Gross reserves for unpaid losses and loss expenses at December 31	$ 1,161.2	1,193.3	1,273.8	1,272.7	1,298.3	1,403.4	1,587.8	1,835.2	2,084.0	2,288.8	**2,542.5**
Reinsurance recoverable on unpaid losses and loss expenses at December 31	$ (124.2)	(140.5)	(192.0)	(160.9)	(166.5)	(160.4)	(184.6)	(218.8)	(218.2)	(199.7)	**(227.8)**
Net reserves for unpaid losses and loss expenses at December 31	$ 1,037.0	1,052.8	1,081.8	1,111.8	1,131.8	1,243.1	1,403.2	1,616.4	1,865.8	2,089.0	**2,314.7**
II. Net Reserves estimated as of:											
One year later	$ 1,034.5	1,044.2	1,080.7	1,125.5	1,151.7	1,258.1	1,408.1	1,621.5	1,858.5	**2,070.2**	
Two years later	1,024.8	1,035.9	1,088.2	1,152.7	1,175.8	1,276.3	1,452.3	1,637.3	**1,845.1**		
Three years later	1,014.0	1,033.3	1,115.6	1,181.9	1,210.7	1,344.6	1,491.1	**1,643.7**			
Four years later	998.1	1,040.3	1,134.4	1,220.2	1,290.2	1,371.5	**1,522.9**				
Five years later	997.9	1,049.9	1,156.0	1,278.3	1,306.8	**1,413.8**					
Six years later	1,003.6	1,058.6	1,194.6	1,287.5	**1,349.6**						
Seven years later	1,011.6	1,090.0	1,203.2	**1,325.5**							
Eight years later	1,038.0	1,101.1	**1,238.2**								
Nine years later	1,045.2	**1,135.4**									
	1,078.3										

Ten years later										
Cumulative net redundancy (deficiency)	$ **(41.3)**	**(82.6)**	**(156.5)**	**(213.7)**	**(217.8)**	**(170.8)**	**(119.7)**	**(27.3)**	**20.7**	**18.8**
III. Cumulative amount of net reserves paid through:										
One year later	$ 313.7	328.1	348.2	399.2	377.1	384.0	414.5	422.4	468.6	**469.4**
Two years later	531.1	537.5	600.3	649.1	627.3	653.3	691.4	729.5	**775.0**	
Three years later	665.5	703.8	767.5	815.3	807.2	836.3	903.7	**942.4**		
Four years later	760.8	797.1	870.8	930.9	926.9	966.2	**1,033.5**			
Five years later	812.2	856.1	933.6	1,002.4	1,003.3	**1,044.6**				
Six years later	849.7	892.2	974.6	1,046.3	**1,053.8**					
Seven years later	875.9	919.2	1,001.1	**1,081.7**						
Eight years later	894.7	937.1	**1,029.0**							
Nine years later	908.5	**956.7**								
Ten years later	**922.5**									
IV. Re-estimated gross liability	$ 1,338.6	1,399.8	1,519.0	1,574.5	1,613.2	1,654.3	1,782.6	1,912.0	2,121.8	2,303.1
Re-estimated reinsurance recoverable	$ (260.3)	(264.4)	(280.8)	(249.0)	(263.6)	(240.4)	(259.6)	(268.3)	(276.7)	(232.9)
Re-estimated net liability	$ 1,078.3	1,135.4	1,238.2	1,325.5	1,349.6	1,413.8	1,522.9	1,643.7	1,845.1	2070.2
V. Cumulative gross deficiency	$ (177.4)	(206.5)	(245.2)	(301.8)	(314.8)	(250.8)	(194.8)	(76.8)	(37.8)	(14.4)
Cumulative net redundancy (deficiency)	$ (41.3)	(82.6)	(156.5)	(213.7)	(217.8)	(170.8)	(119.7)	(27.3)	20.7	18.8

Note: Some amounts may not foot due to rounding.

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Selective experienced favorable prior year development in 2007 and 2006 of $18.8 million and $7.3 million, respectively. In 2005, prior year adverse development was $5.1 million. The following paragraphs provide information regarding the development in each of these calender years.

Selective experienced overall favorable development in its loss and loss expense reserves totaling $18.8 million in 2007, which was primarily driven as follows:

- The commercial automobile line of business experienced favorable prior year loss and loss expense reserve development of approximately $19 million, which was primarily driven by lower than expected severity in accident years 2004 through 2006.

- The personal automobile line of business experienced favorable prior year development of approximately $10 million, due to lower than expected loss emergence for accident years 2005 and prior partially offset by higher severity in accident year 2006.

- The workers compensation line of business experienced favorable prior year development of approximately $4 million reflecting the implementation of a series of improvement strategies for this line in recent accident years partially offset by an increase in the tail factor related to medical inflation and general development trends.

- The homeowners line of business experienced adverse prior year loss and loss expense reserve development of approximately $6 million driven by unfavorable trends in claims for groundwater contamination caused by the leakage of certain underground oil storage tanks.

- The personal umbrella line of business experienced adverse prior year loss and loss expense reserve development of approximately $4 million in 2007, which was due to the impact of several significant losses on this small line.

- The remaining lines of business, which collectively contributed approximately $4 million of adverse development, do not individually reflect any significant trends related to prior year development.

Selective s 2006 overall favorable loss and loss expense reserve development was driven by the following:

- The commercial automobile line of business experienced favorable prior year loss and loss expense reserve development of approximately $15 million, which was primarily driven by lower than expected severity in accident years 2004 and 2005.

- The workers compensation line of business experienced favorable prior year development of approximately $4 million, which was driven, in part, by savings realized from changing medical and pharmacy networks outside New Jersey and re-contracting our medical bill review services.

- The personal automobile line of business experienced favorable prior year development of approximately $9 million, due to lower than expected frequency.

- The general liability line of business experienced adverse prior year loss and loss expense reserve development of approximately $15 million in 2006, which was largely driven by our contractor completed operations business and an increase in reserves for legal expenses.

- The remaining lines of business, which collectively contributed approximately $6 million of adverse development, do not individually reflect significant prior year development.

During the course of 2005, Selective had analyzed certain negative trends in the workers compensation line of business and certain positive trends in the commercial automobile line of business. In the fourth quarter of 2005, Selective had accumulated sufficient evidence to change management s best estimate of loss reserves for these lines.

Accordingly, Selective took the following actions:

- Workers compensation reserves were increased by approximately $42 million to reflect rising medical cost trends that impacted accident years 2001 and prior.

- Commercial automobile reserves were decreased by approximately $48 million, primarily due to ongoing favorable severity trends in the 2002 through 2004 accident years.

- The general liability reserves adversely developed by approximately $14 million over the course of the year, which was driven mainly by our contractor completed operations business impacting accident years 2001 and prior, but partially offset by positive development in accident years 2002 through 2004.

The adverse judicial ruling by the New Jersey Supreme Court in the second quarter of 2005 that eliminated the application of the serious life impact standard to personal automobile bodily injury liability cases under the verbal tort threshold of the New Jersey Automobile Insurance Cost Reduction Act (AICRA) led to an increase in personal automobile reserves of approximately $10 million, of which $6 million represents adverse development from prior years.

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The cumulative loss and loss expense reserve net deficiencies seen in the years 1998 through 2003 are generally reflective of the soft market pricing in the industry during that time frame, which hit the lowest levels in 1999. The property and casualty insurance industry, as a whole, underestimated reserves and loss trends leading to intense pricing competition. Additionally, during 1999, Selective significantly increased gross and ceded reserves by $37.5 million for prior accident years related to unlimited medical claims under personal injury protection provisions of personal automobile policies ceded to the Unsatisfied Claim and Judgment Fund in the State of New Jersey. Approximately 18% of the cumulative gross deficiency for years 1998 and prior stems from this increase.

The following table reconciles losses and loss expense reserves under SAP and GAAP at December 31, as follows:

(in thousands)	**2007**	2006
Statutory losses and loss expense reserves [1]	$ **2,312,086**	2,084,012
Provision for uncollectible reinsurance	**2,750**	2,700
Pension adjustment	**72**	2,619
Other	**(162)**	(299)
GAAP losses and loss expense reserve net	**2,314,746**	2,089,032
Reinsurance recoverable on unpaid losses and loss expenses	**227,801**	199,738
GAAP losses and loss expense reserves gross	$ **2,542,547**	2,288,770

(1) Statutory losses and loss expense reserves are presented net of reinsurance recoverable on unpaid losses and loss expenses.

Environmental Reserves

Reserves established for liability insurance include exposure to environmental claims, both asbestos and non-asbestos. Selective s exposure to environmental liability is primarily due to: (i) policies written prior to the introduction of the absolute pollutions endorsement in the mid-1980 s; and (ii) underground storage tank leaks, mostly from New Jersey homeowners policies in recent years. Selective s asbestos and non-asbestos environmental claims have arisen primarily from insured exposures in municipal government, small non-manufacturing commercial risks, and homeowners policies. The emergence of these claims is slow and highly unpredictable.

Asbestos claims are claims presented to Selective in which bodily injury is alleged to have occurred as a result of exposure to asbestos and/or asbestos-containing products. During the past two decades, the insurance industry has experienced the emergence and development of an increasing number of asbestos claims. At December 31, 2007, asbestos claims constituted 89% of Selective s 2,448 environmental claims compared with 88% of Selective s 2,575 outstanding environmental claims at December 31, 2006.

Non-asbestos claims are pollution and environmental claims alleging bodily injury or property damage presented, or expected to be presented to Selective, other than asbestos claims. These claims primarily include landfills and leaking underground storage tanks. In past years, landfill claims have accounted for a significant portion of Selective s environmental claim unit s litigation costs. Over the past few years, Selective has been experiencing adverse development in its homeowners line of business as a result of unfavorable trends in claims for groundwater contamination caused by leakage of certain underground heating oil storage tanks in New Jersey.

Selective refers all environmental claims to its centralized and specialized environmental claim unit. Environmental reserves are evaluated on a case-by-case basis. As cases progress, the ability to assess potential liability often improves. Reserves are then adjusted accordingly. In addition, each case is reviewed in light of other factors affecting liability, including judicial interpretation of coverage issues.

IBNR reserve estimation for environmental claims is difficult because, in addition to other factors, there are significant uncertainties associated with critical assumptions in the estimation process, such as average clean-up costs, third-party costs, potentially responsible party shares, allocation of damages, insurer litigation costs, insurer coverage defenses and potential changes to state and federal statutes. Moreover, normal historically-based actuarial approaches are difficult to apply because past environmental claims are not indicative of future potential environmental claims. In addition, while models can be applied, such models can produce significantly different results with small changes in assumptions. As a result, management does not calculate a specific environmental loss range. Historically, Selective s environmental claims have been significantly less volatile and uncertain than other competitors in the commercial lines industry. In part, this is due to the fact that Selective is the primary insurance carrier on the majority of its environmental exposures, thus providing more certainty in its reserve position compared to the insurance marketplace.

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Reinsurance

In the ordinary course of their business, the Insurance Subsidiaries reinsure a portion of the risks that they underwrite in order to control exposure to losses and protect capital resources. Reinsurance also permits the Insurance Subsidiaries additional underwriting capacity by permitting them to accept larger risks and underwrite a greater number of risks without a corresponding increase in capital or surplus. For a premium paid by the Insurance Subsidiaries, reinsurers assume a portion of the losses ceded by the Insurance Subsidiaries. Selective uses traditional forms of reinsurance and does not use finite risk reinsurance. Amounts not reinsured are known as retention. The Insurance Subsidiaries use two types of reinsurance to control exposure to losses:

Treaty reinsurance, in which certain types of policies are automatically reinsured without the need for approval by the reinsurer of the individual risks covered; and

Facultative reinsurance, in which an individual insurance policy or a specific risk is reinsured with the prior approval of the reinsurer. Facultative reinsurance is primarily used for policies with limits greater than the limits available under the reinsurance treaties.

In addition to treaty and facultative reinsurance, the Insurance Subsidiaries are partially protected by the Terrorism Risk Insurance Act of 2002, which was modified and extended through December 31, 2014 via the Terrorism Risk Insurance Program Reauthorization Act of 2007. For further information regarding this legislation, see Item 1A. Risk Factors of this Form 10-K.

Reinsurance does not legally discharge an insurer from its liability for the full-face amount of its policies, but it does make the reinsurer liable to the insurer to the extent of the reinsurance ceded. Reinsurance carries counterparty credit risk, which may be mitigated in certain cases by collateral such as letters of credit, trust funds, or funds withheld by the Insurance Subsidiaries. Selective attempts to mitigate the credit risk related to reinsurance by pursuing relationships with companies rated A- or higher in most circumstances and/or requiring collateral to secure reinsurance obligations. In addition, Selective employs procedures to continuously review the quality of reinsurance recoverables and reserve for uncollectible reinsurance. Selective also may take actions, such as commutations, in cases of potential reinsurer default. Some of the Insurance Subsidiaries reinsurance contracts include provisions that give Selective a contractual right to terminate and/or commute the reinsurers portion of the liabilities based on deterioration of the reinsurer s rating or financial condition.

Reinsurance recoverable balances tend to fluctuate based on the underlying losses incurred by the Insurance Subsidiaries. If a severe catastrophic event occurs, reinsurance recoverable balances may increase significantly. The reinsurance recoverable balances on paid and unpaid claims were 22% of stockholders equity at December 31, 2007 compared to 19% at December 31, 2006. These balances, net of available collateral, were 18% of stockholders equity at December 31, 2007 compared to 15% at December 31, 2006. Federal or state sponsored pools, which Selective believes to have minimal default risk, represented approximately 44% at December 31, 2007 and 50% at December 31, 2006 of the uncollateralized reinsurance recoverable on paid and unpaid balance. The following are the five largest individual uncollateralized reinsurance recoverables on paid and unpaid balances:

		As of: 12/31/07		**As of: 12/31/06**	
($ in thousands)	**Ratings:**	**Unsecured Recoverable on Paidand**	**% of**	**Unsecured Recoverable on Paid and**	**% of**
Reinsurer Name	**A.M. Best**	**Unpaid**	**Total**	**Unpaid**	**Total**

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The table below summarizes the significant reinsurance treaties covering the Insurance Subsidiaries.

Treaty	Reinsurance Coverage	Terrorism Coverage
TRIA, Federal Statutory Program	See above for the description of TRIA. 85% of all TRIA certified losses above the retention. Selective s retention for 2008 is approximately $203 million. Current program covers both domestic and foreign terrorism. Terrorism acts related to the use of nuclear, biological, chemical or radioactive (NBCR) weapons are covered by TRIA provided that the Secretary of the Treasury certifies the event.	Current program is set to expire on December 31, 2014. For further information regarding this legislation and our risks concerning terrorism exposure, see Item 1A. Risk Factors of this Form 10-K.
Property Excess of Loss	$23 million above a $2 million retention in two layers. Losses other than TRIA certified losses are subject to the following reinstatements and annual aggregate limits: $8 million in excess of $2 million layer provides unlimited reinstatements, no annual aggregate limit; $15 million in excess of $10 million layer provides two reinstatements, $45 million in annual aggregate.	All NBCR losses are excluded regardless of whether or not they are certified under TRIA. For non-NBCR losses, the treaty distinguishes between acts certified under TRIA and those that are not. The treaty provides annual aggregate limits for TRIA certified (other than NBCR) acts of $24 million for the first layer and $22.5 million for the second layer. Non-certified terrorism losses (other than NBCR) are subject to the normal limits under the treaty.
Property Catastrophe Excess of Loss	95% of $310 million above $40 million retention in three layers: 95% of losses in excess of $40 million up to $100 million; 95% of losses in excess of $100 million up to $200 million; 95% of losses in excess of $200 million up to $350 million; and The treaty provides one reinstatement per layer, $589.0 million in annual aggregate limit, net of Selective s co-participation.	All nuclear, biological and chemical (NBC) losses are excluded regardless of whether or not they are certified under TRIA. TRIA losses related to foreign acts of terrorism are excluded from the treaty. Domestic terrorism is included regardless of whether it is certified under TRIA or not. Please see Item 1A. Risk Factors of this Form 10-K for further discussion regarding changes in TRIA.
Casualty Excess of Loss	Casualty Excess of Loss program is structured in two treaties: Workers compensation only working layer treaty and all inclusive Casualty treaty, which provides coverage for all casualty lines including Workers compensation. Workers compensation losses have per	All NBC losses are excluded. All other losses stemming from the acts of terrorism are subject to the following reinstatements and annual aggregate limits: Workers compensation only working

	occurrence coverage of $48 million in excess of $2 million retention and additional coverage of 75% of $40 million in excess of $50 million. All other casualty losses have per occurrence coverage of $45 million in excess of $5 million retention and additional coverage of 75% of $40 million in excess of $50 million. Losses other than TRIA certified losses are subject to the following reinstatements and annual aggregate limits: Workers compensation only working layer of $3 million in excess of $2 million layer provides five reinstatements, $18 million annual aggregate limit; Casualty treaty: $7 million in excess of $5 million layer provides three reinstatements, $28 million annual aggregate limit; $9 million in excess of $12 million layer provides two reinstatements, $27 million annual aggregate limit; $9 million in excess of $21 million layer provides one reinstatement, $18 million annual aggregate limit; and $20 million in excess of $30 million layer provides one reinstatement, $40 million annual aggregate limit. 75% of $40 million in excess of $50 million layer provides up to $30 million of coverage net of co-participation with one reinstatement, $60 million in net annual aggregate limit.	layer of $3 million in excess of $2 million layer provides two reinstatements for terrorism losses, $9 million annual aggregate limit; Casualty treaty: $7 million in excess of $5 million layer provides two reinstatements for terrorism losses, $21 million annual aggregate limit; $9 million in excess of $12 million layer provides two reinstatements for terrorism losses, $27 million annual aggregate limit; $9 million in excess of $21 million layer provides one reinstatement for terrorism losses, $18 million annual aggregate limit; $20 million in excess of $30 million layer provides one reinstatement for terrorism losses, $40 million annual aggregate limit; 75% of $40 million in excess of $50 million layer provides up to $30 million of coverage net of co-participation with one reinstatement for terrorism losses, $60 million in net annual aggregate limit; and
Flood	100% reinsurance by the federal government s National Flood Insurance Program Write Your Own program.	None.

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Reinsurance Pooling Agreement

The Insurance Subsidiaries are parties to an inter-company reinsurance pooling agreement (Pooling Agreement). The purpose of the Pooling Agreement is to:

- Pool or share proportionately the underwriting profit and loss results of property and casualty underwriting operations through reinsurance;
- Prevent any Insurance Subsidiary from suffering undue loss;
- Reduce administration expenses; and
- Permit all of the Insurance Subsidiaries to obtain a uniform rating from A.M. Best.

Under the Pooling Agreement, all of the Insurance Subsidiaries mutually reinsure all insurance risks written by them pursuant to the respective percentage set forth opposite each Insurance Subsidiary s name on the table below:

Insurance Subsidiary	**Respective Percentage**
SICA	49.5%
SWIC	21.0%
SICSC	9.0%
SICSE	7.0%
SICNY	7.0%
SAICNJ	6.0%
SICNE	0.5%

Insurance Regulation

General

Insurance companies are subject to supervision and regulation in the states in which they are domiciled and transact business. Such supervision and regulation relates to a variety of aspects of an insurance company s business and financial condition. The primary public purpose of such supervision and regulation is to protect the insurer s policyholders, not the insurer s shareholders. The extent of regulation varies, and generally is derived from state statutes that delegate regulatory, supervisory, and administrative authority to state insurance departments. Although the insurance industry is primarily regulated by individual states, federal initiatives can have an impact on the industry, such as the federal government s enactment and extension of TRIA, the enforcement of economic and trade sanctions by the Office of Foreign Assets Control, and the proposal for an optional federal charter that would allow companies to choose between state regulation and national regulatory structure that would eliminate the need to comply with 51 sets of different regulations.

The Financial Services Modernization Act of 1999, also known as the Gramm-Leach-Bliley Act (GLB), and related regulations govern, among other things, the privacy of consumer financial information. GLB limits disclosure by financial institutions of nonpublic personal information about individuals who obtain financial products or services for personal, family, or household purposes. GLB generally applies to disclosures to non-affiliated third parties, but not to disclosures to affiliates. Many states in which Selective operates have adopted laws that are at least as restrictive as GLB. Privacy of consumer financial information is an evolving area of regulation requiring continued monitoring to ensure continued compliance with GLB.

Selective cannot quantify the financial impact it would incur to satisfy revised or additional regulatory requirements that may be imposed in the future.

State Regulation

The regulatory authority of state insurance departments extends to such matters as insurer solvency standards, insurer and agent licensing, investment restrictions, payment of dividends and distributions, provisions for current losses and future liabilities, deposit of securities for the benefit of policyholders, restrictions on policy terminations, unfair trade practices, and approval of premium rates and policy forms. State insurance departments also conduct periodic examinations of the financial and business affairs of insurers and require insurers to file annual and other periodic reports relating to their financial condition. Regulatory agencies require that premium rates not be excessive, inadequate, or unfairly discriminatory. The Insurance Subsidiaries, consequently, must file all rates for commercial and personal insurance with the insurance department of each state in which they operate.

All states have enacted legislation that regulates insurance holding company systems. Each insurance company in a holding company system is required to register with certain insurance supervisory agencies and furnish information concerning the operations of companies within the holding company system that may materially affect the operations, management, or financial condition of the insurers. Pursuant to these laws, the respective departments may: (i) examine Selective and the Insurance Subsidiaries at any time; (ii) require disclosure or prior approval of material transactions of the Insurance Subsidiaries with any affiliate; and (iii) require prior approval or notice of certain transactions, such as dividends or distributions to Selective Insurance Group, Inc. (the Parent) from the Insurance Subsidiary domiciled in that state.

National Association of Insurance Commissioners (NAIC) Guidelines

The Insurance Subsidiaries are subject to statutory accounting principles and reporting formats established by the NAIC. The NAIC also promulgates model insurance laws and regulations relating to the financial and operational regulations of insurance companies, which includes the Insurance Regulatory Information System (IRIS). IRIS identifies 11 industry ratios and specifies usual values for each ratio. Departure from the usual values on four or more of the ratios can lead to inquiries from individual state insurance departments about certain aspects of the insurer s business. The Insurance Subsidiaries have consistently met the majority of the IRIS ratio tests.

NAIC model laws and regulations are not usually applicable unless enacted into law or promulgated into regulation by the individual states. The adoption of certain NAIC model laws and regulations is a key aspect of the NAIC Financial Regulations Standards and Accreditation Program, which also sets forth minimum staffing and resource levels for all state insurance departments. All of the Insurance Subsidiaries states of domicile, except New York, are accredited by the NAIC. Examinations conducted by, or along with, accredited states can be accepted by other states. The NAIC intends to create nationwide regulatory network of accredited states.

The NAIC model laws and regulations are also intended to enhance the regulation of insurer solvency. These model laws and regulations contain certain risk-based capital requirements for property and casualty insurance companies designed to assess capital adequacy and to raise the level of protection that statutory surplus provides for policyholders. Risk-based capital is measured by the four major areas of risk to which property and casualty insurers are exposed: (i) asset risk; (ii) credit risk; (iii) underwriting risk; and (iv) off-balance sheet risk. Insurers with total adjusted capital that is less than two times their Authorized Control Level, as calculated pursuant to the NAIC model laws and regulations, are subject to different levels of regulatory intervention and action. Based upon the unaudited 2007 statutory financial statements for the Insurance Subsidiaries, each Insurance Subsidiary s total adjusted capital substantially exceeded two times their Authorized Control Level.

Investments Segment

Selective s investment philosophy includes setting certain return and risk objectives for its equity and fixed maturity portfolios. The return objective of the equity portfolio is to meet or exceed a weighted-average benchmark of public equity indices. The primary return objective of the fixed maturity portfolio is to maximize after-tax investment yield and income while balancing certain risk objectives. The risk objectives for all portfolios are structured conservatively, focusing on: (i) asset diversification; (ii) investment quality; (iii) liquidity, particularly to meet the cash obligations of the insurance operations; (iv) consideration of taxes; and (v) preservation of capital. At December 31, 2007, Selective s investment portfolio consisted of $3,079.3 million (83%) of fixed maturity securities, $274.7 million (7%) of equity securities, $190.2 million (5%) of short-term investments, and $188.8 million (5%) of other investments.

Selective s fixed maturity portfolio is comprised primarily of highly rated securities, with almost 100% rated investment grade. The average rating of its fixed maturity securities is AA+ by Standard & Poor s (S&P), their second highest credit quality rating. Selective expects to continue to invest primarily in high quality, fixed maturity investments in order to reduce volatility of the portfolio and to maximize after-tax investment yield. For further information regarding Selective s interest rate sensitivity as well as other risks associated with its portfolio, see Item 7A. Quantitative and Qualitative Disclosures about Market Risk in this Form 10-K. The average duration of the fixed maturity portfolio, including short-term investments of $190.2 million at December 31, 2007 and $197.0 million at December 31, 2006, was 3.9 years at December 31, 2007 and 3.8 years at December 31, 2006.

Selective s Investments segment operations are based primarily in Parsippany, New Jersey, while certain segments of the portfolio are managed by external money managers. For additional information about investments, see the sections entitled, Investments, in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8. Financial Statements and Supplementary Data, Note 4 to the consolidated financial statements.

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Diversified Insurance Services Segment

Selective s Diversified Insurance Services segment provides fee-based revenues that are expected to contribute to earnings, increase operating cash flow, and help mitigate potential volatility in insurance operating results. The Diversified Insurance Services segment is complementary to Selective s business model by sharing a common marketing or distribution system and creating new opportunities for independent agents to bring value-added services and products to their customers. In December 2005, Selective divested itself of its 100% ownership interest in CHN Solutions (Alta Services, LLC and Consumer Health Network Plus, LLC), which had historically been reported as part of the Managed Care component of the Diversified Insurance Services segment. For more information concerning the results of the Diversified Insurance Services segment for the last three fiscal years ended December 31, refer to Note 15, Discontinued Operations in Item 8. Financial Statements and Supplementary Data on this Form 10-K. The Diversified Insurance Services operation currently has two major components: (i) human resource administration outsourcing; and (ii) flood insurance.

Human Resource Administration Outsourcing

Human resource administration outsourcing (HR Outsourcing) products and services are sold by Selective HR Solutions, Inc. and its subsidiaries (Selective HR), which are headquartered in Sarasota, Florida. Selective HR s customers are small businesses who generally have existing relationships with independent insurance agents. Selective HR leverages these relationships by using independent insurance agents as its distribution channel for its products and services in the states where it operates. As a Professional Employer Organization (PEO), Selective HR enters into agreements with clients that establish a three-party relationship under which Selective HR and the client are co-employers of the employees who work at the client s location (worksite employees). As of December 31, 2007, Selective HR had approximately 25,111 worksite employees, 39% of which are from the state of Florida.

Flood Insurance

Selective is a servicing carrier in the Write-Your-Own (WYO) Program of the United States government s National Flood Insurance Program (NFIP). The WYO Program operates within the context of the NFIP, and is subject to its rules and regulations. The NFIP is administered by the Federal Emergency Management Agency (FEMA), which is part of the Department of Homeland Security. The WYO Program is a cooperative undertaking of the insurance industry and FEMA. The WYO Program allows participating property and casualty insurance companies to write and service the Standard Flood Insurance Policy in their own names, while ceding all of the premiums collected on these policies to the federal government. The companies receive an expense allowance, or servicing fee, for policies written and claims processed under the program, while the federal government retains responsibility for all underwriting losses. Selective is servicing approximately 299,000 flood policies under the NFIP through over 5,900 independent agents in 50 states and the District of Columbia.

Diversified Insurance Services Regulation

The companies within the Diversified Insurance Services segment are subject to certain laws and regulations. In particular, as a co-employer for some of its clients, Selective HR is subject to federal, state, and local laws and regulations relating to labor, tax, employment, employee benefits, and immigration matters. By contracting with its clients and creating a co-employer relationship with the worksite employees, Selective HR may be assuming certain contractual and legal obligations and responsibilities of an employer and could incur liability for violations of such laws and regulations, even if it was not actually responsible for the conduct giving rise to such liability. Some states in which Selective HR operates have already passed licensing or registration requirements for PEOs. These laws and regulations vary from state to state but generally provide for the monitoring of the fiscal responsibility of PEOs. Currently, many of these laws and regulations do not specifically address the obligations and responsibilities of co-employers. There can be no assurance that Selective HR will be able to satisfy new or revised laws and regulations. The viability of the NFIP s reinsurance program under the WYO Program is an essential component of Selective s Diversified Insurance Services operations. In 2005, the destruction caused by the active hurricane season stressed the NFIP with excessive levels of flood losses. Selective continues to monitor developments with the NFIP regarding its ability to pay claims in the event of another large-scale disaster. Congress controls the federal agency s funding authority, which was exceeded after Hurricane Katrina, and is again nearing maximum capacity. Bills are pending in the House and Senate that could impact the NFIP. These bills contain substantial legislative changes and revisions to the NFIP and WYO Program, some of which may be favorable and some of which may be unfavorable for Selective. For additional information regarding regulation of flood insurance see Item 1A. Risk Factors of this Form 10-K.

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Competition

Selective faces significant competition in both the Insurance Operations and Diversified Insurance Services segments. Property and casualty insurance is highly competitive on the basis of both price and service, and is extensively regulated by state insurance departments. In 2007, Selective was ranked as the 46th largest property and casualty group in the United States based on the 2006 NPW, by A.M. Best in its list, Top Property/Casualty Writers. The Insurance Operations compete with regional insurers, such as Cincinnati Financial and Harleysville, and national insurance companies, such as Travelers, The Hartford, and Zurich. Selective also competes against direct writers of insurance coverage, including insurance offered through competitors internet websites. These writers offer coverage primarily in personal lines, such as GEICO and Progressive. Many of these competitors have greater financial and operating resources than Selective. Many of them also have more customers, which provide them with more information regarding their risks and, with the use of statistical and computer models, may give them greater ability to make pricing and underwriting decisions. Purchasers of property and casualty insurance products do not always differentiate between insurance carriers and differences in coverage. The more significant competitive factors for most of Selective s insurance products are financial ratings, safety management, price, coverage terms, claims service, and technology. In addition, Selective also faces competition within each insurance agency that sells its insurance products as most of the agencies represent more than one insurance company.

With regard to the Diversified Insurance Services segment, according to the most recent published information, Selective HR was ranked as the 11th largest Professional Employer Organization in a Staffing Industry Report published by Staffing Industry Analysts, Inc., based on 2005 gross revenue. Based on 2006 information, Selective s Flood line of business is the 7th largest WYO carrier for the NFIP based on information obtained from Statutory Annual Statements.

Please refer to Item 1A. Risk Factors, of this Form 10-K for a discussion of the factors that could impact Selective s ability to compete.

Seasonality

Selective s insurance business experiences modest seasonality with regard to premiums written. Due to the general timing of commercial policy renewals, premiums written are usually highest in January and July and lowest during the fourth quarter of the year. Although the writing of insurance policies experiences modest seasonality, the premiums related to these policies are earned consistently over the period of coverage. Losses and loss expenses incurred tend to remain consistent throughout the year, unless a catastrophe occurs from man-made or weather-related events such as hail, tornadoes, windstorms, hurricanes, and nor easters.

Customers

No one customer or independent agency accounts for 10% or more of Selective s total revenue or the revenue of any one of its business segments.

Employees

At December 31, 2007, Selective had approximately 2,200 employees, of which 2,000 worked in the Insurance Operations and Investments segments and 200 worked in the Diversified Insurance Services segment.

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Executive Officers of the Registrant

The following table sets forth biographical information about Selective s Chief Executive Officer, Executive Officers, and senior management, as of February 28, 2008:

Name, Age, Title	**Occupation And Background**
Gregory E. Murphy, 52 Chairman, President, and Chief Executive Officer	Chairman, President, and Chief Executive Officer of Selective, present position since May 2000 President, Chief Executive Officer, and Director of Selective, May 1999 to May 2000 President, Chief Operating Officer, and Director of Selective, 1997 to May 1999 Other senior executive, management, and operational positions at Selective, since 1980 Director, Newton Memorial Hospital Foundation, Inc., since 1999 Director, Insurance Information Institute Trustee, the American Institute for CPCU (AICPCU) and the Insurance Institute of America (IIA), since June 2001 Graduate of Boston College (B.S. Accounting) Harvard University (Advanced Management Program) Certified Public Accountant (New Jersey) (Inactive)
Jamie Ochiltree III, 55 Senior Executive Vice President, Insurance Operations	Present position since February 2004 (scheduled retirement in March 2008) Variety of executive positions, Selective, 1994 February 2004 Miami University (B.A. Zoology) Wharton School (Advanced Management Program)
Richard F. Connell, 62 Senior Executive Vice President and Chief Administrative Officer	Present position since October 2007 Senior Executive Vice President and Chief Information Officer, August 2000 October 2007 Executive Vice President and Chief Information Officer, August 2000 January 2006 Central Connecticut State University (B.S. Marketing)
Kerry A. Guthrie, 50 Executive Vice President and Chief Investment Officer	Present position since February 2005 Senior Vice President and Chief Investment Officer, Selective, August 2002 February 2005 Variety of investment positions, Selective, 1987 2002 Chartered Financial Analyst Certified Public Accountant (New Jersey) (Inactive) Member, New York Society of Security Analysts Siena College (B.S. Accounting) Fairleigh Dickinson University (M.B.A. Finance)