
**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 **March 31, 2010**

OR

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

For the transition period from _____ to _____

0-14697

(Commission file number)

HARLEYSVILLE GROUP INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

51-0241172

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

355 Maple Avenue, Harleysville, PA 19438-2297

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(215) 256-5000**

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 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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

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 .

At May 4, 2010, 27,550,253 shares of common stock of Harleysville Group Inc. were outstanding.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**INDEX**

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Item 1. Financial Statements

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	March 31, 2010	December 31, 2009
	(Unaudited)	
Assets		
Investments:		
Fixed maturities:		
Held to maturity, at amortized cost (fair value \$211,899 and \$213,838)	\$ 202,313	\$ 204,284
Available for sale, at fair value (amortized cost \$2,117,263 and \$2,036,993)	2,215,263	2,130,179
Equity securities, at fair value (cost \$137,781 and \$137,150)	195,946	186,395
Short-term investments, at cost, which approximates fair value	62,440	116,476
Other invested assets, at cost, which approximates fair value	2,300	2,480
Total investments	2,678,262	2,639,814
Cash	126	126
Receivables:		
Premiums	142,244	141,486
Reinsurance	219,889	226,781
Accrued investment income	25,733	26,058
Total receivables	387,866	394,325
Deferred policy acquisition costs	113,673	111,649
Prepaid reinsurance premiums	46,261	48,314
Property and equipment, net	13,448	13,579
Deferred income taxes	17,883	21,429
Other assets	45,631	72,750
Total assets	\$ 3,303,150	\$ 3,301,986
Liabilities and Shareholders' Equity		
Liabilities:		
Unpaid losses and loss settlement expenses (affiliate \$259,664 and \$257,562)	\$ 1,799,907	\$ 1,782,292
Unearned premiums (affiliate \$42,680 and \$44,275)	490,204	484,510
Accounts payable and accrued expenses	111,857	130,780
Due to affiliate	2,954	13,276
Debt (affiliate \$18,500 and \$18,500)	118,500	118,500
Total liabilities	2,523,422	2,529,358
Shareholders' equity:		
Preferred stock, \$1 par value, authorized 1,000,000 shares; none issued		
Common stock, \$1 par value, authorized 80,000,000 shares; issued 34,815,213 and 34,583,182 shares; outstanding 27,559,223 and 27,615,120 shares	34,815	34,583
Additional paid-in capital	253,185	245,636
Accumulated other comprehensive income	71,687	62,276
Retained earnings	639,613	640,593
Treasury stock, at cost, 7,255,990 and 6,968,062 shares	(219,572)	(210,460)
Total shareholders' equity	779,728	772,628
Total liabilities and shareholders' equity	\$ 3,303,150	\$ 3,301,986

See accompanying notes to consolidated financial statements.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

For the three months ended March 31, 2010 and 2009

(dollars in thousands, except per share data)

	<u>2010</u>	<u>2009</u>
Revenues:		
Premiums earned from affiliate (ceded to affiliate, \$186,454 and \$181,654)	\$ 209,083	\$ 218,023
Investment income, net of investment expense	25,883	26,389
Realized investment gains (losses), net:		
Total other-than-temporary impairment losses	—	(943)
Portion of loss recognized in other comprehensive income	—	—
Other realized investment gains, net	334	—
Total realized investment gains (losses), net	<u>334</u>	<u>(943)</u>
Other income (affiliate \$1,711 and \$1,806)	<u>3,657</u>	<u>3,425</u>
Total revenues	<u>238,957</u>	<u>246,894</u>
Losses and expenses:		
Losses and loss settlement expenses (ceded to affiliate, \$128,304 and \$120,368)	152,036	146,729
Amortization of deferred policy acquisition costs	53,034	54,097
Other underwriting expenses	21,484	20,726
Interest expense (affiliate \$32 and \$140)	1,514	1,622
Other expenses	<u>954</u>	<u>812</u>
Total expenses	<u>229,022</u>	<u>223,986</u>
Income before income taxes	9,935	22,908
Income taxes	<u>1,885</u>	<u>5,619</u>
Net income	<u>\$ 8,050</u>	<u>\$ 17,289</u>
Per common share:		
Basic net income	<u>\$.29</u>	<u>\$.61</u>
Diluted net income	<u>\$.29</u>	<u>\$.61</u>
Cash dividend	<u>\$.325</u>	<u>\$.30</u>

See accompanying notes to consolidated financial statements.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(Unaudited)
For the three months ended March 31, 2010
(dollars in thousands)

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income	Retained Earnings	Treasury Stock	Total
	Shares	Amount					
Balance at December 31, 2009	34,583,182	\$ 34,583	\$ 245,636	\$ 62,276	\$ 640,593	\$ (210,460)	\$ 772,628
Net income					8,050		8,050
Other comprehensive income, net of tax:							
Unrealized investment gains, net of reclassification adjustment				8,926			8,926
Defined benefit pension plans: Recognized net actuarial loss				485			485
Other comprehensive income							9,411
Comprehensive income							17,461
Issuance of common stock:							
Incentive plans	223,963	224	5,379				5,603
Dividend reinvestment plan	8,068	8	262				270
Tax benefit from stock compensation			485				485
Stock compensation			1,423				1,423
Purchase of treasury stock, 287,928 shares						(9,112)	(9,112)
Cash dividend paid					(9,030)		(9,030)
Balance at March 31, 2010	<u>34,815,213</u>	<u>\$ 34,815</u>	<u>\$ 253,185</u>	<u>\$ 71,687</u>	<u>\$ 639,613</u>	<u>\$ (219,572)</u>	<u>\$ 779,728</u>

See accompanying notes to consolidated financial statements.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
For the three months ended March 31, 2010 and 2009
(in thousands)

	<u>2010</u>	<u>2009</u>
Cash flows from operating activities:		
Net income	\$ 8,050	\$ 17,289
Adjustments to reconcile net income to net cash provided by operating activities:		
Change in receivables, unearned premiums and prepaid reinsurance balances	14,206	5,649
Change in affiliate balance	(10,322)	(15,020)
Increase in unpaid losses and loss settlement expenses	17,615	9,292
Deferred income taxes	(1,522)	(588)
Increase in deferred policy acquisition costs	(2,024)	(605)
Amortization and depreciation	2,268	1,618
Realized investment (gains) losses, net	(334)	943
Other, net	<u>(13,157)</u>	<u>(6,900)</u>
Net cash provided by operating activities	<u>14,780</u>	<u>11,678</u>
Cash flows from investing activities:		
Fixed maturity investments:		
Purchases	(164,723)	(123,312)
Sales or maturities	108,209	64,188
Equity securities:		
Purchases	(631)	(38,158)
Other invested assets:		
Maturities	180	86
Net sales of short-term investments	54,036	96,024
Purchase of property and equipment, net	<u>(67)</u>	<u>(844)</u>
Net cash used by investing activities	<u>(2,996)</u>	<u>(2,016)</u>
Cash flows from financing activities:		
Issuance of common stock	5,873	3,354
Purchase of treasury stock	(9,112)	(4,834)
Dividends paid (to affiliate, \$4,721 and \$4,357)	(9,030)	(8,476)
Excess tax benefits from share-based payment arrangements	<u>485</u>	<u>294</u>
Net cash used by financing activities	<u>(11,784)</u>	<u>(9,662)</u>
Change in cash	-	-
Cash at beginning of period	<u>126</u>	<u>146</u>
Cash at end of period	<u>\$ 126</u>	<u>\$ 146</u>

See accompanying notes to consolidated financial statements.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1 – Basis of Presentation

The financial information for the interim periods included herein is unaudited; however, such information reflects all adjustments which are, in the opinion of management, necessary to a fair presentation of the financial position, results of operations, and cash flows for the interim periods. The results of operations for interim periods are not necessarily indicative of results to be expected for the full year.

These financial statements should be read in conjunction with the financial statements and notes for the year ended December 31, 2009 included in the Company's 2009 Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission (SEC).

The affiliate transaction disclosures on the face of the financial statements are in regards to transactions with Harleysville Mutual Insurance Company (the Mutual Company). The Mutual Company owns approximately 53% of the outstanding common stock of Harleysville Group Inc. As used herein, "Harleysville Group" refers to Harleysville Group Inc. and its subsidiaries and the "Company" refers to Harleysville Group Inc.

2 – Share-Based Payments

Harleysville Group has several share-based compensation plans. Harleysville Group measures compensation expense associated with the plans based on the grant-date fair value of the awards.

Harleysville Group Inc. has the following share-based compensation plans:

- The Amended and Restated Equity Incentive Plan (EIP) provides for awards to key employees in the form of stock options, stock appreciation rights (SARs), restricted stock, restricted stock units or any combination of the above.
- The Employee Stock Purchase Plan provides that a participant may elect to have up to 15% of base pay withheld to purchase shares. The purchase price of the stock is 85% of the lower of the beginning-of-the-subscription period or end-of-the-subscription-period fair market value. There are two subscription periods during each year.
- The Directors' Equity Compensation Plan provides for the grant of equity-based awards to non-employee directors of Harleysville Group Inc. and the Mutual Company. These awards can be in the form of stock options, deferred stock units or restricted stock.

The compensation expense for the various share-based compensation plans that has been charged against income before income taxes was \$1,423,000 and \$1,376,000 for the three months ended March 31, 2010 and 2009, respectively, with a corresponding income tax benefit of \$470,000 and \$450,000, respectively.

During the first quarter of 2010, 511,790 stock options were granted at a Black Scholes value of \$6.84 per option. These options vest 33 1/3% per year over a three year period. Restricted stock unit grants of 99,060 units were also made during the first quarter of 2010 and 39,485 of these units include performance conditions. The weighted average fair value of the restricted stock unit grants was \$33.94 per share. These awards vest over three years.

During the first quarter of 2009, 533,790 stock options were granted at a Black Scholes value of \$5.67 per option. These options vest 33 1/3% per year over a three year period. Restricted stock grants of 77,917 shares and restricted stock unit grants of 27,270 units were also made during the first quarter of 2009. The weighted average fair value of the restricted stock grants was \$29.19 per share. The weighted average fair value of the grant of restricted stock units was \$34.21 per unit. These awards vest over three years. All of the restricted stock units awarded and 15,065 of the restricted stock shares awarded include performance conditions.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

As of March 31, 2010, the Company's total unrecognized compensation cost related to nonvested share-based compensation arrangements and the weighted average period over which the compensation cost is expected to be recognized is as follows:

	<u>Unrecognized Compensation Cost</u> (in thousands)	<u>Weighted Average Period of Recognition</u> (in years)
Equity incentive plan awards	\$ 10,173	2.2
Employee stock purchase plan	\$ 81	0.3

3 – Investments

Fair value accounting guidance defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements.

Fair value measurements are determined under a three-level hierarchy which gives the highest priority to quoted prices in active markets and the lowest priority to unobservable inputs which are based on the Company's own assumptions. The three levels of the hierarchy are as follows:

Level 1 - Unadjusted quoted market prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 - Inputs other than Level 1 that are based on observable market data. These include quoted prices for similar assets in active markets, quoted prices for identical assets in inactive markets, inputs other than quoted prices that are observable for the asset or liability and inputs that are derived from or corroborated by observable market data.

Level 3 - Inputs that are unobservable, reflecting the Company's own assumptions.

For investments that have quoted market prices in active markets, the Company uses the quoted market price as fair value and includes these investments in Level 1 of the fair value hierarchy. The Company classifies U.S. Treasury securities and publicly traded equity mutual funds as Level 1. When quoted market prices in active markets are not available, the Company relies on a pricing service to estimate fair value. The Company classifies its fixed maturity securities other than U.S. Treasury securities and private placements as Level 2. Private placement fixed maturity securities, non-publicly traded equity securities and investments in receivership are classified as Level 3. The fair value of the investments in receivership is based on cash flow analysis and other valuation techniques.

The Company utilizes a nationally recognized independent pricing service to obtain fair value estimates for its fixed maturity holdings because of the detailed process it uses in arriving at a fair value estimate. For fixed maturity securities that have quoted prices in active markets, market quotations are provided. For fixed maturity securities that do not trade on a daily basis, the independent pricing service prepares estimates of fair value using a wide array of observable inputs including relevant market information, benchmark curves, benchmarking of like securities, sector groupings and matrix pricing. The observable market inputs that our independent pricing service utilizes include, listed in approximate order of priority: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data including market research publications. Additionally, the independent pricing service uses an Option Adjusted Spread model to develop prepayment and interest rate scenarios.

When the independent pricing service provides a fair value estimate, the Company uses that estimate. At March 31, 2010, the independent pricing service provided a fair value estimate for all of the investments classified as level 1 investments within the fair value hierarchy and approximately 99% of the investments classified as level 2 estimates within the fair value hierarchy. The fair value of all level 2 securities is based on observable market inputs.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

In instances when the independent pricing service is unable to provide a fair value estimate, the Company attempts to obtain a non-binding fair value estimate from a number of broker/dealers and reviews any fair value estimate reported by an independent business news service. In instances where only one broker/dealer provides a fair value estimate for a fixed maturity security, the Company uses that estimate. In instances where the Company is able to obtain fair value estimates from more than one broker/dealer, the Company generally uses the lowest or next to lowest fair value estimate. In instances where neither the independent pricing service nor a broker/dealer is able to provide a fair value estimate, the fair value is based on cash flow analysis and other valuation techniques which utilize significant unobservable inputs and the Company classifies the fixed maturity investment as a level 3 investment. Level 3 investments represent less than 1% of the Company's total investment portfolio.

Quotes obtained from third parties are non-binding. The third parties from whom quotes are obtained are knowledgeable market participants that have a detailed understanding of the sector, the security type and the issuer. The non-binding quotes are fair value estimates based on observable market data utilized by these market participants. The Company does not adjust quotes or prices obtained from third parties.

Management reviews, on an ongoing basis, the reasonableness of the methodologies employed by the independent pricing service. As part of the monthly review process, management examines the prices obtained from the independent pricing service. This process routinely involves reviewing any available recent transaction activity reported via various investment research tools. Additionally, the Company tracks changes in credit ratings of all fixed maturity securities on a monthly basis and performs a more in-depth, quarterly evaluation of fixed income securities that are rated below single A by Moody's and/or S&P. If as a result of its review, management does not believe that a price received with respect to any particular security is a reasonable estimate of the fair value of the security, it will discuss this with the independent pricing service to resolve the discrepancy. Management then determines the appropriate level of classification of each investment within the fair value hierarchy based on its evaluation of the inputs used in determining the fair value.

The following is a summary of the fair value measurements of applicable Company assets by level within the fair value hierarchy as of March 31, 2010 and December 31, 2009. These assets are measured at fair value on a recurring basis. There were no transfers to or from Levels 1 and 2 of the fair value hierarchy in the first quarter of 2010. The Company's policy is to recognize transfers between levels as of the end of the reporting period.

	Fair Value Measurements at Reporting Date Using			
	March 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in thousands)		
Fixed maturities available for sale:				
U.S. Treasury securities	\$ 120,264	\$ 120,264		
Obligations of U.S. government corporations and agencies	21,836		\$ 21,836	
Obligations of states and political subdivisions	1,207,279		1,207,279	
Corporate securities	464,419		464,319	\$ 100
Mortgage-backed securities	401,465		401,465	
Total available for sale	2,215,263	120,264	2,094,899	100
Equity securities:				
Global fund	40,819	40,819		
Total stock market index fund	155,121	155,121		
Other	6			6
Total equity securities	195,946	195,940		6
Total	\$ 2,411,209	\$ 316,204	\$2,094,899	\$ 106

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

	Fair Value Measurements at Reporting Date Using			
	December 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Fixed maturities available for sale:				
U.S. Treasury securities	\$ 110,228	\$ 110,228		
Obligations of U.S. government corporations and agencies	25,449		\$ 25,449	
Obligations of states and political subdivisions	1,074,458		1,074,458	
Corporate securities	516,611		516,511	\$ 100
Mortgage-backed securities	403,433		403,433	
Total available for sale	2,130,179	110,228	2,019,851	100
Equity securities:				
Global fund	40,093	40,093		
Total stock market index fund	146,296	146,296		
Other	6			6
Total equity securities	186,395	186,389		6
Total	\$ 2,316,574	\$ 296,617	\$ 2,019,851	\$ 106

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)		
	For the three months ended March 31, 2010		
	Fixed Maturities Available for Sale	Equity Securities	Total
	(in thousands)		
Balance at January 1, 2010	\$ 100	\$ 6	\$ 106
Balance at March 31, 2010	\$ 100	\$ 6	\$ 106

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

Fair Value Measurements Using Significant Unobservable Inputs (Level 3)			
For the three months ended March 31, 2009			
	Fixed Maturities Available for Sale	Equity Securities	Total
		(in thousands)	
Balance at January 1, 2009	\$ 3,116	\$ 6	\$ 3,122
Total losses (realized/unrealized)			
Included in earnings	(101)		(101)
Settlements	(165)		(165)
Balance at March 31, 2009	<u>\$ 2,850</u>	<u>\$ 6</u>	<u>\$ 2,856</u>

The amount of total losses for the period included in earnings (realized investment losses, net) attributable to the change in unrealized losses relating to assets still held at March 31, 2009

\$ (101)

The other invested assets on the balance sheet are carried at cost and are tested for impairment on a quarterly basis. During the first quarter of 2009, the security was written down to fair value and an impairment charge of \$299,000 was included in earnings for the period. Fair value is determined based on cash flow analysis and other valuation techniques, based on unobservable inputs (Level 3).

The amortized cost and estimated fair value of investments in fixed maturity and equity securities are as follows:

March 31, 2010				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
		(in thousands)		
Held to maturity:				
Obligations of U.S. government corporations and agencies	\$ 458	\$ 7		\$ 465
Obligations of states and political subdivisions	117,537	4,543		122,080
Corporate securities	84,318	5,036		89,354
Total held to maturity	<u>202,313</u>	<u>9,586</u>		<u>211,899</u>
Available for sale:				
U.S. Treasury securities	118,807	1,586	\$ (129)	120,264
Obligations of U.S. government corporations and agencies	20,791	1,121	(76)	21,836
Obligations of states and political subdivisions	1,167,261	42,959	(2,941)	1,207,279
Corporate securities	435,362	29,275	(218)	464,419
Mortgage-backed securities	375,042	26,474	(51)	401,465
Total available for sale	<u>2,117,263</u>	<u>101,415</u>	<u>(3,415)</u>	<u>2,215,263</u>
Total fixed maturities	<u>\$ 2,319,576</u>	<u>\$ 111,001</u>	<u>\$ (3,415)</u>	<u>\$ 2,427,162</u>
Total equity securities	<u>\$ 137,781</u>	<u>\$ 58,167</u>	<u>\$ (2)</u>	<u>\$ 195,946</u>

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

	December 31, 2009			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
	(in thousands)			
Held to maturity:				
Obligations of U.S. government corporations and agencies	\$ 459	\$ 8		\$ 467
Obligations of states and political subdivisions	119,430	5,012	\$ (12)	124,430
Corporate securities	<u>84,395</u>	<u>4,594</u>	<u>(48)</u>	<u>88,941</u>
Total held to maturity	<u>204,284</u>	<u>9,614</u>	<u>(60)</u>	<u>213,838</u>
Available for sale:				
U.S. Treasury securities	109,195	1,495	(462)	110,228
Obligations of U.S. government corporations and agencies	24,295	1,214	(60)	25,449
Obligations of states and political subdivisions	1,030,968	45,425	(1,935)	1,074,458
Corporate securities	491,782	25,591	(762)	516,611
Mortgage-backed securities	<u>380,753</u>	<u>22,691</u>	<u>(11)</u>	<u>403,433</u>
Total available for sale	<u>2,036,993</u>	<u>96,416</u>	<u>(3,230)</u>	<u>2,130,179</u>
Total fixed maturities	<u>\$ 2,241,277</u>	<u>\$ 106,030</u>	<u>\$ (3,290)</u>	<u>\$ 2,344,017</u>
Total equity securities	<u>\$ 137,150</u>	<u>\$ 49,256</u>	<u>\$ (11)</u>	<u>\$ 186,395</u>

The amortized cost and estimated fair value of fixed maturity securities at March 31, 2010 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
	(in thousands)	
Held to maturity:		
Due through December 31, 2011	\$ 53,763	\$ 55,005
Due 2012 through 2015	130,162	137,638
Due 2016 through 2020	8,040	8,348
Due after 2020	<u>10,348</u>	<u>10,908</u>
	<u>202,313</u>	<u>211,899</u>
Available for sale:		
Due through December 31, 2011	226,191	233,191
Due 2012 through 2015	474,680	500,672
Due 2016 through 2020	623,956	649,971
Due after 2020	<u>417,394</u>	<u>429,964</u>
	<u>1,742,221</u>	<u>1,813,798</u>
Mortgage-backed securities	<u>375,042</u>	<u>401,465</u>
	<u>2,117,263</u>	<u>2,215,263</u>
Total fixed maturities	<u>\$ 2,319,576</u>	<u>\$ 2,427,162</u>

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

Realized gross gains (losses) from investments were as follows:

	For the three months ended March 31,	
	2010	2009
	(in thousands)	
Fixed maturity securities:		
Available for sale:		
Gross gains	\$ 334	
Other than temporary impairment losses		\$ (644)
Other invested assets:		
Other than temporary impairment losses		(299)
Net realized investment gains (losses)	\$ 334	\$ (943)

Harleysville Group held securities with unrealized losses at March 31, 2010 and December 31, 2009 as follows:

	March 31, 2010			
	Fair Value	Unrealized Loss	Length of Unrealized Loss	
			Less Than 12 Months	Over 12 Months
	(in thousands)			
Fixed maturities:				
U.S. Treasury securities	\$ 34,537	\$ 129	\$ 129	
Obligations of U.S. government corporations and agencies	1,414	76	76	
Obligations of states and political subdivisions	232,199	2,941	2,941	
Corporate securities	17,250	218	52	\$ 166
Mortgage-backed securities	2,934	51	51	
Total fixed maturities	288,334	3,415	3,249	166
Equity mutual funds	629	2	2	
Total temporarily impaired securities	\$ 288,963	\$ 3,417	\$ 3,251	\$ 166

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

	December 31, 2009			
	Fair Value	Unrealized Loss	Length of Unrealized Loss	
			Less Than	Over 12
			12 Months	Months
			(in thousands)	
Fixed maturities:				
U.S. Treasury securities	\$ 76,791	\$ 462	\$ 462	
Obligations of U.S. government corporations and agencies	1,429	60	60	
Obligations of states and political subdivisions	115,997	1,947	1,947	
Corporate securities	27,450	810	22	\$ 788
Mortgage-backed securities	2,973	11	11	
Total fixed maturities	<u>224,640</u>	<u>3,290</u>	<u>2,502</u>	<u>788</u>
Equity mutual funds	944	11	11	
Total temporarily impaired securities	<u>\$ 225,584</u>	<u>\$ 3,301</u>	<u>\$ 2,513</u>	<u>\$ 788</u>

All of the fixed maturity securities with an unrealized loss at March 31, 2010 are classified as available for sale and are carried at fair value on the balance sheet.

The fixed maturity investments with continuous unrealized losses for less than twelve months were primarily due to changes in interest rates, especially tax-exempt rates, rather than a decline in credit quality. There are \$8,800,000 in fixed maturity securities, at fair value, that at March 31, 2010, have been below amortized cost for over twelve months. The \$166,000 of unrealized losses on such securities relates to securities which carry an investment grade debt rating where the unrealized loss was primarily due to a widening of credit spreads, primarily on securities of financial institutions. Per the Company's current policy, a fixed maturity security is other than temporarily impaired if the present value of the cash flows expected to be collected is less than the amortized cost of the security or where the security's fair value is below cost and the Company intends to sell, or more likely than not will be required to sell, the security before recovery of its value. The Company believes, based on its analysis, that these securities are not other than temporarily impaired. However, depending on developments involving both the issuers and worsening economic conditions, these investments may be written down in the income statement in the future.

There were no impairment charges in the three months ended March 31, 2010. There were impairment charges of \$943,000 in the three months ended March 31, 2009. The 2009 impairment charge consisted of \$644,000 on fixed income securities and \$299,000 on other invested assets.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**(Unaudited)****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(Continued)**

4 – Earnings Per Share

The computation of basic and diluted earnings per share is as follows:

	For the three months ended March 31,	
	<u>2010</u>	<u>2009</u>
	(in thousands, except per share data)	
Numerator for basic and diluted earnings per share:		
Net income	\$ 8,050	\$ 17,289
Denominator for basic earnings per share--weighted average shares outstanding	27,709,496	28,292,198
Effect of stock incentive plans	<u>206,983</u>	<u>170,688</u>
Denominator for diluted earnings per share	<u>27,916,479</u>	<u>28,462,886</u>
Basic earnings per share	<u>\$.29</u>	<u>\$.61</u>
Diluted earnings per share	<u>\$.29</u>	<u>\$.61</u>

The following options to purchase shares of common stock were not included in the computation of diluted earnings per share because the exercise price of the options was greater than the average market price:

	For the three months ended March 31,	
	<u>2010</u>	<u>2009</u>
	(in thousands)	
Number of options	<u>777</u>	<u>579</u>

5 – Reinsurance

Premiums earned are net of amounts ceded of \$30,009,000 and \$25,689,000 for the three months ended March 31, 2010 and 2009, respectively. Losses and loss settlement expenses are net of amounts ceded of \$11,470,000 and \$11,966,000 for the three months ended March 31, 2010 and 2009, respectively. Such amounts ceded do not include the reinsurance transactions with the Mutual Company under the pooling arrangement (described below) which are reflected on the face of the income statements, but do include reinsurance with unaffiliated reinsurers.

Pursuant to the terms of the reinsurance pooling agreement with the Mutual Company, each of the insurance subsidiaries of Harleysville Group Inc. and Harleysville Pennland Insurance Company (Pennland), a subsidiary of the Mutual Company, cede premiums, losses and underwriting expenses on all of their respective business to the Mutual Company which, in turn, retrocedes to such subsidiaries and Pennland a specified portion of premiums, losses and underwriting expenses of the Mutual Company and such subsidiaries and Pennland. Because this agreement does not relieve Harleysville Group Inc.'s insurance subsidiaries of primary liability as originating insurers, there is a concentration of credit risk arising from business ceded to the Mutual Company. However, the reinsurance pooling agreement provides for the right of offset. The Mutual Company has an A. M. Best rating of "A" (Excellent). Effective January 1, 2010, the pooling agreement was amended to exclude reinsurance premiums, losses, loss settlement expenses and underwriting expenses voluntarily assumed by the Mutual Company.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

6 – Cash Flows

There were no cash tax payments in the first quarter of 2010 or 2009. Cash interest payments of \$2,908,000 and \$3,015,000 were made in the first quarter of 2010 and 2009, respectively.

7 – Segment Information

The performance of the personal lines and commercial lines is evaluated based upon underwriting results as determined under statutory accounting practices (SAP).

Financial data by segment is as follows:

	For the three months ended March 31,	
	2010	2009
	(in thousands)	
Revenues:		
Premiums earned:		
Commercial lines	\$ 164,633	\$ 177,678
Personal lines	44,450	40,345
Total premiums earned	209,083	218,023
Net investment income	25,883	26,389
Realized investment gains (losses)	334	(943)
Other	3,657	3,425
Total revenues	<u>\$ 238,957</u>	<u>\$ 246,894</u>
Income before income taxes:		
Underwriting income (loss):		
Commercial lines	\$ (10,651)	\$ (4,876)
Personal lines	(8,365)	1,055
SAP underwriting loss	(19,016)	(3,821)
GAAP adjustments	1,545	292
GAAP underwriting loss	(17,471)	(3,529)
Net investment income	25,883	26,389
Realized investment gains (losses)	334	(943)
Other	1,189	991
Income before income taxes	<u>\$ 9,935</u>	<u>\$ 22,908</u>

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

8 – Comprehensive Income

Comprehensive income for the three months ended March 31, 2010 and 2009 consisted of the following:

	For the three months ended March 31,	
	<u>2010</u>	<u>2009</u>
	(in thousands)	
Net income	\$ 8,050	\$ 17,289
Other comprehensive income:		
Unrealized gains on securities:		
Unrealized investment holding gains arising during period, net of taxes of \$4,923 and \$4,905	9,143	9,110
Less:		
Reclassification adjustment for (gains) losses included in net income, net of taxes of \$(117) and \$330	<u>(217)</u>	<u>613</u>
Net unrealized investment gains	<u>8,926</u>	<u>9,723</u>
Defined benefit pension plans:		
Recognized net actuarial loss, net of taxes of \$261 and \$159	<u>485</u>	<u>296</u>
Other comprehensive income	<u>9,411</u>	<u>10,019</u>
Comprehensive income	<u>\$ 17,461</u>	<u>\$ 27,308</u>

Accumulated other comprehensive income (loss) at March 31, 2010 and December 31, 2009 consisted of the following amounts (which are net of tax):

	<u>March 31,</u>	<u>December 31,</u>
	2010	2009
	(in thousands)	
Unrealized investment gains	\$ 101,507	\$ 92,581
Defined benefit pension plan - net actuarial loss	<u>(29,820)</u>	<u>(30,305)</u>
Accumulated other comprehensive income	<u>\$ 71,687</u>	<u>\$ 62,276</u>

9 – Pension

Harleysville Group Inc. has a frozen pension plan that covers employees hired before January 1, 2006. The net periodic pension cost for the plan, including the Mutual Company, consists of the following components:

	For the three months ended March 31,	
	<u>2010</u>	<u>2009</u>
	(in thousands)	
Components of net periodic pension cost:		
Interest cost	\$ 2,966	\$ 2,871
Expected return on plan assets	(3,012)	(2,980)
Recognized net actuarial loss	<u>1,057</u>	<u>639</u>
Net periodic pension cost:		
Entire plan	<u>\$ 1,011</u>	<u>\$ 530</u>
Harleysville Group portion	<u>\$ 713</u>	<u>\$ 377</u>

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

Harleysville Group's expected portion of the 2010 contribution to the pension plan is \$6,720,000. Contributions of \$1,682,000 were made in the quarter ended March 31, 2010.

10 – Borrowings

Debt is as follows:

	March 31, 2010	December 31, 2009
	(in thousands)	
Notes, 5.75%, due 2013	\$ 100,000	\$ 100,000
Demand term-loan payable to the Mutual Company, LIBOR plus 0.45%, due 2012	18,500	18,500
Total debt	\$ 118,500	\$ 118,500

The fair value of the notes was \$100,622,000 and \$99,975,000 at March 31, 2010 and December 31, 2009, respectively, based on quoted market prices for the same or similar debt. The carrying value of the remaining debt approximates fair value.

11 – Shareholders' Equity

Various states have adopted the National Association of Insurance Commissioners (NAIC) risk-based capital (RBC) standards that require insurance companies to calculate and report statutory capital and surplus needs based on a formula measuring underwriting, investment and other business risks inherent in an individual company's operations. These RBC standards have not affected the operations of Harleysville Group since each of the Company's insurance subsidiaries has statutory capital and surplus in excess of RBC requirements.

These RBC standards require the calculation of a ratio of total adjusted capital to Authorized Control Level. Insurers with a ratio below 200% are subject to different levels of regulatory intervention and action. Based upon their 2009 statutory financial statements, the ratio of total adjusted capital to the Authorized Control Level for the Company's eight insurance subsidiaries at December 31, 2009 ranged from 471% to 696%.

12 – Income Taxes

As of March 31, 2010, Harleysville Group had no material unrecognized tax benefits or accrued interest and penalties. The Company's policy is to account for interest as a component of interest expense and penalties as a component of other expense. Federal tax years 2006 through 2009 were open for examination as of March 31, 2010.

13 – New Accounting Standards

In June 2009, the Financial Accounting Standards Board (FASB) issued guidance which replaces the quantitative-based risks and rewards calculation for determining whether an enterprise is the primary beneficiary in a variable interest entity with an approach that is primarily qualitative, and requires ongoing assessments of whether an enterprise is the primary beneficiary of a variable interest entity. The guidance, which is effective for financial statements issued for fiscal years beginning after November 15, 2009, also requires additional disclosures about an enterprise's involvement in variable interest entities. The adoption of this guidance did not have a material impact on the Company's results of operations or financial position.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

In January 2010, the FASB issued Accounting Standards Update (ASU) 2010-06, “Fair Value Measurements and Disclosures.” ASU 2010-06 applies to all entities that are required to make disclosures about recurring or non-recurring fair value measurements. ASU 2010-06 provides guidance on additional disclosures on any significant transfers in and out of Level 1 and Level 2 and a description of the transfer. ASU 2010-06 also requires separate disclosures of the activity in the Level 3 category related to any purchases, sales, issuances and settlements on a gross basis. The effective date of the new disclosures relating to the existing disclosures regarding Level 1 and Level 2 categories is for interim and annual periods beginning after December 15, 2009. The effective date of the disclosures regarding purchases, sales, issuances and settlements to the Level 3 category is for interim and annual periods beginning after December 15, 2010. The portion of ASU 2010-06 that has been adopted did not have a material impact on the Company’s results of operations or financial position as it focuses on additional disclosures. The portion of ASU 2010-06 that has not yet been adopted is not expected to have a material impact on the Company’s results of operations or financial position.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

Item 2.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Certain of the statements contained herein (other than statements of historical facts) are forward looking statements. Such forward looking statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and include estimates and assumptions related to economic, competitive, legislative and regulatory developments. These forward-looking statements are subject to change and uncertainty which are, in many instances, beyond the Company's control and have been made based upon management's expectations and beliefs concerning future developments and their potential effect on Harleysville Group. There can be no assurance that future developments will be in accordance with management's expectations or that the effect of future developments on Harleysville Group will be those anticipated by management. Actual financial results, including premium levels and underwriting results, could differ materially from those anticipated by Harleysville Group depending on the outcome of certain factors, which may include changes in property and casualty loss trends and reserves; the insurance product pricing environment; changes in applicable law; government regulation and changes therein that may impede the ability to charge adequate rates; performance of and instability in the financial markets; investment losses; fluctuations in interest rates; significant catastrophe events in the geographic regions where we do business; decreased demand for property and casualty insurance; availability and price of reinsurance; the A.M. Best group rating of Harleysville Group; and the status of labor markets in which the Company operates.

Overview

The Company's net income is primarily determined by three elements:

- net premium income
- investment income and realized investment gains (losses)
- amounts paid or reserved to settle insured claims

Variations in premium income are subject to a number of factors, including:

- limitations on premium rates arising from the competitive market place or regulation
- limitations on available business arising from a need to maintain the quality of underwritten risks
- the Company's ability to maintain its A ("excellent") group rating by A.M. Best
- the ability of the Company to maintain a reputation for efficiency and fairness in claims administration

Variations in investment income and realized investment gains (losses) are subject to a number of factors, including:

- general interest rate levels and financial market conditions
- specific adverse events affecting the issuers of debt obligations held by the Company
- changes in the prices of debt and equity securities generally and those held by the Company specifically

Loss and loss settlement expenses are affected by a number of factors, including:

- the quality of the risks underwritten by the Company
- the nature and severity of catastrophic losses
- the availability, cost and terms of reinsurance
- underlying settlement costs, including medical and legal costs

The Company seeks to manage each of the foregoing to the extent within its control. Many of the foregoing factors are partially, or entirely, outside of the control of the Company.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**Management's Discussion and Analysis of Financial Condition
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(Continued)

Critical Accounting Policies and Estimates

The consolidated financial statements are prepared in conformity with U.S. generally accepted accounting principles, which require Harleysville Group to make estimates and assumptions (see Note 1 of the Notes to Consolidated Financial Statements for the year ended December 31, 2009 included in the Company's 2009 Annual Report on Form 10-K filed with the SEC). Harleysville Group believes that of its significant accounting policies, the following may involve a higher degree of judgment and estimation. The judgments, or the methodology on which the judgments are made, are reviewed quarterly with the Audit Committee.

Liability for Losses and Loss Settlement Expenses. The liability for losses and loss settlement expenses represents estimates of the ultimate unpaid cost of all losses incurred, including losses for claims which have not yet been reported to Harleysville Group. The amount of loss reserves for reported claims is based primarily upon a case-by-case evaluation of the type of risk involved, knowledge of the circumstances surrounding each claim and the insurance policy provisions relating to the type of loss. The amounts of loss reserves for unreported claims and loss settlement expense reserves are determined utilizing historical information by line of insurance as adjusted to current conditions. Inflation is implicitly provided for in the reserving function through analysis of costs, trends and reviews of historical reserving results. Estimates of the liabilities are reviewed and updated on a regular basis using the most recent information on reported claims and a variety of actuarial techniques. It is expected that such estimates will be more or less than the amounts ultimately paid when the claims are settled. Changes in these estimates are reflected in current operations.

Investments. Generally, unrealized investment gains or losses on investments carried at fair value, net of applicable income taxes, are reflected directly in shareholders' equity as a component of comprehensive income and, accordingly, have no effect on net income. However, if the fair value of an investment in equity securities declines below its cost and that decline is deemed other than temporary, the amount of the decline below cost is currently charged to earnings. Per the Company's current policy, a fixed maturity security is other than temporarily impaired if the present value of the cash flows expected to be collected is less than the amortized cost of the security or where the security's fair value is below cost and the Company intends to sell, or more likely than not will be required to sell, the security before recovery of its value. If the Company does not intend to sell, or more likely than not will not be required to sell, a fixed maturity security whose fair value has declined below its cost, the amount of the decline below cost due to credit-related reasons is charged to earnings and the remaining difference is included in comprehensive income. Harleysville Group monitors its investment portfolio and at least quarterly reviews investments that have experienced a decline in fair value below cost to evaluate whether the decline is other than temporary. Such evaluations consider, among other things, the magnitude and reasons for a decline, the prospects for the fair value to recover in the near term and Harleysville Group's intent to retain the investment for a period of time sufficient to allow for a recovery in value. Future adverse investment market conditions, or poor operating results of underlying investments, could result in an impairment charge in the future.

The severe downturn in the public debt and equity markets in recent years, reflecting uncertainties associated with the mortgage crisis, worsening economic conditions, widening of credit spreads, bankruptcies and government intervention in large financial institutions, has resulted in significant realized and unrealized losses in our investment portfolio in the past. Depending on market conditions going forward, we could incur additional realized and unrealized losses in future periods.

The fair value of equity securities is based on the closing market value. The fair value of mutual fund holdings is based on the closing net asset value reported by the fund. The fair value of fixed maturities is based upon data supplied by an independent pricing service. It can be difficult to determine the fair value of non-traded securities, but Harleysville Group does not own a material amount of non-traded securities.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**Management's Discussion and Analysis of Financial Condition
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(Continued)

Policy Acquisition Costs. Policy acquisition costs, such as commissions, premium taxes and certain other underwriting and agency expenses that vary with and are primarily related to the production of business, are deferred and amortized over the effective period of the related insurance policies and in proportion to the premiums earned. The method followed in computing deferred policy acquisition costs limits the amount of such deferred costs to their estimated realizable value. The estimation of net realizable value takes into account the premium to be earned, related investment income over the claim paying period, expected losses and loss settlement expenses, and certain other costs expected to be incurred as the premium is earned. Future changes in estimates, the most significant of which is expected losses and loss settlement expenses, may require adjustments to deferred policy acquisition costs. If the estimation of net realizable value indicates that the deferred acquisition costs are not recoverable, they would be written off and further analyses would be performed to determine if an additional liability would need to be accrued.

Contingencies. Besides claims related to its insurance products, Harleysville Group is subject to proceedings, lawsuits and claims in the normal course of business. Harleysville Group assesses the likelihood of any adverse outcomes to these matters as well as potential ranges of probable losses. There can be no assurance that actual outcomes will be consistent with those assessments.

The application of certain of these critical accounting policies to the periods ended March 31, 2010 and 2009 is discussed in greater detail below.

Results of Operations

The Company's property and casualty subsidiaries participate in a pooling agreement with the Mutual Company and its property and casualty insurance subsidiary, Harleysville Pennland Insurance Company (Pennland), whereby such subsidiaries and Pennland cede to the Mutual Company all of their insurance business and assume from the Mutual Company an amount equal to their participation in the pooling agreement. All losses and loss settlement expenses and other underwriting expenses are prorated among the parties on the basis of participation in the pooling agreement. The pooling agreement provides for the allocation of premiums, losses and loss settlement expenses and underwriting expenses between Harleysville Group and the Mutual Company. Harleysville Group is not liable for any losses incurred by its subsidiaries, Harleysville Preferred Insurance Company and Harleysville Insurance Company of New Jersey, and the Mutual Company prior to January 1, 1986, the date the pooling agreement became effective. Harleysville Group's participation in the pool has been 80% since January 1, 2008. Effective January 1, 2010, the pooling agreement was amended to exclude reinsurance premiums, losses, loss settlement expenses and underwriting expenses voluntarily assumed by the Mutual Company.

Effective January 1, 2010, the management agreement under which the Company provides certain management services to the Mutual Company was amended to include voluntary assumed reinsurance business written by the Mutual Company.

Premiums earned decreased \$8.9 million, or 4.1%, during the three months ended March 31, 2010 as compared to the three months ended March 31, 2009, primarily due to a decrease of \$13.0 million in premiums earned for commercial lines, partially offset by an increase of \$4.1 million in premiums earned for personal lines. The decrease in premiums earned for commercial lines was 7.3%, primarily due to lower average premiums and lower exposures and a decline in assumed earned premiums from involuntary markets. The increase in premiums earned for personal lines was 10.2%, primarily due to an increase in new business writings and higher average premiums.

Investment income decreased \$0.5 million for the three months ended March 31, 2010 primarily due to a lower investment yield on fixed income securities and short-term investments and a greater percentage of fixed income securities invested in tax-exempt securities.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

**Management's Discussion and Analysis of Financial Condition
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(Continued)

Net realized investment gains (losses) increased \$1.3 million for the three months ended March 31, 2010 compared to the three months ended March 31, 2009, primarily due to impairment charges of \$0.9 million in the three months ended March 31, 2009, as the decline in the investments below cost was deemed to be other than temporary. There were no impairment charges in the three months ended March 31, 2010.

Harleysville Group held securities with unrealized losses at March 31, 2010 as follows:

	<u>Fair Value</u>	<u>Unrealized Loss</u>	<u>Length of Unrealized Loss</u>	
			<u>Less Than 12 Months</u>	<u>Over 12 Months</u>
			(in thousands)	
Fixed maturities:				
U.S. Treasury securities	\$ 34,537	\$ 129	\$ 129	
Obligations of U.S. government corporations and agencies	1,414	76	76	
Obligations of states and political subdivisions	232,199	2,941	2,941	
Corporate securities	17,250	218	52	\$ 166
Mortgage-backed securities	<u>2,934</u>	<u>51</u>	<u>51</u>	
Total fixed maturities	<u>288,334</u>	<u>3,415</u>	<u>3,249</u>	<u>166</u>
Equity mutual funds	<u>629</u>	<u>2</u>	<u>2</u>	
Total temporarily impaired securities	<u>\$ 288,963</u>	<u>\$ 3,417</u>	<u>\$ 3,251</u>	<u>\$ 166</u>

All of the fixed maturity securities with an unrealized loss at March 31, 2010 are classified as available for sale and are carried at fair value on the balance sheet.

The fixed maturity investments with continuous unrealized losses for less than twelve months were primarily due to changes in interest rates, especially tax-exempt rates, rather than a decline in credit quality. There are \$8.8 million in fixed maturity securities, at fair value, that at March 31, 2010, have been below amortized cost for over twelve months. The \$0.2 million of unrealized losses on such securities relates to securities which carry an investment grade debt rating where the unrealized loss was primarily due to a widening of credit spreads, primarily on securities of financial institutions. Per the Company's current policy, a fixed maturity security is other than temporarily impaired if the present value of the cash flows expected to be collected is less than the amortized cost of the security or where the security's fair value is below cost and the Company intends to sell, or more likely than not will be required to sell, the security before recovery of its value. The Company believes, based on its analysis, that these securities are not other than temporarily impaired. However, depending on developments involving both the issuers and worsening economic conditions, these investments may be written down in the income statement in the future.

In the first quarter of 2010, Harleysville Group had income before income taxes of \$9.9 million, compared to \$22.9 million in the first quarter of 2009. The decrease in income before income taxes of \$13.0 million for the three months ended March 31, 2010, as compared to the same period in 2009, was primarily due to a greater underwriting loss in the 2010 period compared to the 2009 period. The greater underwriting loss in 2010 was primarily due to greater catastrophe losses. Net catastrophe losses increased to \$21.0 million for the three months ended March 31, 2010 from \$1.7 million for the three months ended March 31, 2009. The increase of \$19.3 million for the three months ended March 31, 2010 was due to a greater number of and more severe catastrophes in the 2010 period than in the comparable period in 2009.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

**Management's Discussion and Analysis of Financial Condition
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An insurance company's statutory combined ratio is a standard measure of underwriting profitability. This ratio is the sum of (1) the ratio of incurred losses and loss settlement expenses to net earned premium; (2) the ratio of expenses incurred for commissions, premium taxes, administrative and other underwriting expenses to net written premium; and (3) the ratio of dividends to policyholders to net earned premium. The combined ratio does not reflect investment income, federal income taxes or other non-operating income or expense. A ratio of less than 100 percent generally indicates underwriting profitability. Harleysville Group's statutory combined ratio for the three months ended March 31, 2010 was 107.8%, compared to 101.9% for the three months ended March 31, 2009. Such increase was primarily due to greater catastrophe losses, which added 10.0% points to the combined ratio in the 2010 period compared to 0.8 points in the 2009 period.

The statutory combined ratios by line of business for the three months ended March 31, 2010 and March 31, 2009 are shown below:

	For the three months ended March 31,	
	2010	2009
Commercial:		
Automobile	98.3%	89.2%
Workers compensation	107.7%	107.7%
Commercial multi-peril	110.7%	107.8%
Other commercial	93.1%	107.6%
Total commercial	104.7%	102.6%
Personal:		
Automobile	101.1%	107.0%
Homeowners	148.7%	94.5%
Other personal	60.4%	77.7%
Total personal	119.3%	98.9%
Total personal and commercial	107.8%	101.9%

The commercial lines statutory combined ratio increased to 104.7% for the three months ended March 31, 2010 from 102.6% for the three months ended March 31, 2009. The increase is primarily due to higher catastrophe losses affecting property coverages in the three months ended March 31, 2010. Catastrophe losses in the commercial lines represented 6.2 points of the combined ratio in the three months ended March 31, 2010 compared to 0.7 points in the three months ended March 31, 2009. The higher than average catastrophe experience relates to a series of severe winter storms that impacted the mid-Atlantic, northeast and southeast regions of the country.

The personal lines statutory combined ratio increased to 119.3% for the three months ended March 31, 2010 from 98.9% for the three months ended March 31, 2009. The increase is primarily due to higher catastrophe losses affecting property coverages in the three months ended March 31, 2010. Catastrophe losses in the personal lines represented 24.2 points of the combined ratio in the three months ended March 31, 2010 compared to 1.3 points in the three months ended March 31, 2009. The higher than average catastrophe experience relates to a series of severe winter storms that impacted the mid-Atlantic, northeast and southeast regions of the country.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

**Management's Discussion and Analysis of Financial Condition
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(Continued)

The following table presents the liability for unpaid losses and loss settlement expenses by major line of business:

	<u>March 31,</u> <u>2010</u>	<u>December 31,</u> <u>2009</u>
	(in thousands)	
Commercial:		
Automobile	\$ 303,384	\$ 302,378
Workers compensation	375,747	376,522
Commercial multi-peril	636,162	623,946
Other commercial	<u>141,739</u>	<u>139,612</u>
Total commercial	<u>1,457,032</u>	<u>1,442,458</u>
Personal:		
Automobile	77,244	77,234
Homeowners	45,533	35,406
Other personal	<u>3,646</u>	<u>4,066</u>
Total personal	<u>126,423</u>	<u>116,706</u>
Total personal and commercial	1,583,455	1,559,164
Plus reinsurance recoverables	<u>216,452</u>	<u>223,128</u>
Total liability	<u>\$ 1,799,907</u>	<u>\$ 1,782,292</u>

The following table presents the increase (decrease) in the estimated ultimate loss and loss settlement expenses attributable to insured events of prior years for the three months ended March 31, 2010 by line of business:

	<u>Accident Years</u>			
	<u>Total</u>	<u>2009</u>	<u>2008</u>	<u>2007 and</u> <u>Prior Years</u>
	(in thousands)			
Commercial:				
Automobile	\$ (2,441)	\$ 447	\$ (24)	\$ (2,864)
Workers compensation	(1,459)	37	20	(1,516)
Commercial multi-peril	(4,987)	(1,380)	(395)	(3,212)
Other commercial	<u>(1,035)</u>	<u>278</u>	<u>(13)</u>	<u>(1,300)</u>
Total commercial	<u>(9,922)</u>	<u>(618)</u>	<u>(412)</u>	<u>(8,892)</u>
Personal:				
Automobile	(1,446)	(274)	(69)	(1,103)
Homeowners	(300)	(461)	12	149
Other personal	<u>(310)</u>	<u>(141)</u>	<u>16</u>	<u>(185)</u>
Total personal	<u>(2,056)</u>	<u>(876)</u>	<u>(41)</u>	<u>(1,139)</u>
Total net development	<u>\$ (11,978)</u>	<u>\$ (1,494)</u>	<u>\$ (453)</u>	<u>\$ (10,031)</u>

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

**Management's Discussion and Analysis of Financial Condition
and Results of Operations**

(Continued)

There was \$12.0 million of net favorable development in the provision for insured events of prior years for the three months ended March 31, 2010, of which \$9.9 million was in commercial lines and \$2.1 million was in personal lines. The favorable development primarily related to the 2004 through 2006 accident years as a result of lower than expected claim severity experienced broadly across all lines of business, particularly commercial multiperil, commercial and personal automobile, and workers compensation.

There was \$10.2 million of net favorable development in the provision for insured events of prior years for the three months ended March 31, 2009, of which \$9.4 million was in commercial lines and \$0.8 million was in personal lines. The favorable development primarily related to the 2003 through 2006 accident years as a result of lower than expected claim severity experienced in the commercial automobile, commercial multi-peril and workers compensation lines of business.

The following table presents workers compensation claim count information for the total pooled business in which Harleysville Group participates and related payment amounts which are Harleysville Group's pooling share of the total pooled amounts:

	<u>For the three months ended March 31, 2010</u>	<u>For the year ended December 31, 2009</u>
	(dollars in thousands)	
Number of claims pending, beginning of period	4,743	5,367
Number of claims reported	1,497	6,674
Number of claims settled or dismissed	<u>(1,519)</u>	<u>(7,298)</u>
Number of claims pending, end of period	<u>4,721</u>	<u>4,743</u>
Losses paid	\$ 12,448	\$ 62,956
Loss settlement expenses paid	\$ 3,637	\$ 14,141

Workers compensation losses primarily consist of indemnity and medical costs for injured workers.

Harleysville Group records the actuarial best estimate of the ultimate unpaid losses and loss settlement expenses incurred. The estimate represents the actuarially determined expected amount of future payments on all loss and loss settlement expenses incurred on or before March 31, 2010. Actuarial loss reserving techniques and assumptions, which rely on historical information as adjusted to reflect current conditions, have been consistently applied, after including consideration of recent case reserve activity, during the periods presented. Changes in the estimate of the liability for unpaid losses and loss settlement expenses reflect actual payments and evaluations of new information and data since the last reporting date. These changes correlate with actuarial trends.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

**Management's Discussion and Analysis of Financial Condition
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(Continued)

The following table presents the liability for unpaid losses and loss settlement expenses (LAE) by case and incurred but not reported (IBNR) reserves by line of business as of March 31, 2010:

	<u>Case</u>	<u>IBNR</u>	<u>LAE Liability</u> (in thousands)	<u>IBNR</u> (<u>Incl. LAE</u>)	<u>Total</u> <u>Liability</u>
Commercial:					
Automobile	\$ 109,955	\$ 141,476	\$ 51,953	\$ 193,429	\$ 303,384
Workers compensation	162,873	160,587	52,287	212,874	375,747
Commercial multi-peril	176,320	293,185	166,657	459,842	636,162
Other commercial	<u>34,985</u>	<u>75,777</u>	<u>30,977</u>	<u>106,754</u>	<u>141,739</u>
Total commercial	<u>484,133</u>	<u>671,025</u>	<u>301,874</u>	<u>972,899</u>	<u>1,457,032</u>
Personal:					
Automobile	34,604	29,104	13,536	42,640	77,244
Homeowners	13,125	25,009	7,399	32,408	45,533
Other personal	<u>1,650</u>	<u>1,435</u>	<u>561</u>	<u>1,996</u>	<u>3,646</u>
Total personal	<u>49,379</u>	<u>55,548</u>	<u>21,496</u>	<u>77,044</u>	<u>126,423</u>
Total net liability	<u>533,512</u>	<u>726,573</u>	<u>323,370</u>	<u>1,049,943</u>	<u>1,583,455</u>
Reinsurance recoverables	<u>141,264</u>	<u>74,996</u>	<u>192</u>	<u>75,188</u>	<u>216,452</u>
Total gross liability	<u>\$ 674,776</u>	<u>\$ 801,569</u>	<u>\$ 323,562</u>	<u>\$ 1,125,131</u>	<u>\$ 1,799,907</u>

Reinsurance receivables were \$219.9 million and \$226.8 million at March 31, 2010 and December 31, 2009, respectively. Of these amounts, \$102.0 million and \$107.4 million, respectively, or 46% and 47%, respectively, of the receivables were due from governmental bodies, regulatory agencies or quasi-governmental pools and reinsurance facilities where Harleysville Group believes there is limited credit risk. The remainder of the reinsurance receivables are principally due from reinsurers rated A- or higher by A.M. Best. Ceded reinsurance contracts do not relieve Harleysville Group's primary obligation to its policyholders. Consequently, an exposure exists with respect to reinsurance recoverables to the extent that any reinsurer is unable to meet its obligation or disputes the liabilities assumed under the reinsurance contract. From time to time, Harleysville Group may encounter such disputes with its reinsurers. In addition, the creditworthiness of our reinsurers could deteriorate in the future due to adverse events affecting the reinsurance industry, such as a large number of major catastrophes.

Effective January 1, 2010, the Company's subsidiaries and the Mutual Company and its wholly owned subsidiaries increased their retention for commercial lines coverages on their casualty excess of loss treaty affording recovery to \$47.5 million above a retention of \$2.5 million for each loss occurrence by retaining a 30% participation on losses of \$2.5 million in excess of \$2.5 million. Accordingly, Harleysville Group's current pooling share for each loss occurrence subject to this treaty would be up to \$37.4 million above a retention of \$2.0 million for commercial lines.

Because of the nature of insurance claims, there are uncertainties inherent in the estimates of ultimate losses. Harleysville Group's reorganization of its claims operation in recent years has resulted in new people and processes involved in settling claims. As a result, more recent statistical data reflects different patterns than in the past and gives rise to uncertainty as to the pattern of future loss settlements. There are uncertainties regarding future

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**Management's Discussion and Analysis of Financial Condition
and Results of Operations**

(Continued)

loss cost trends particularly related to medical treatments and automobile repair. Court decisions, regulatory changes and economic conditions can affect the ultimate cost of claims that occurred in the past. Accordingly, the ultimate liability for unpaid losses and loss settlement expenses will likely differ from the amount recorded at March 31, 2010.

The property and casualty industry has had substantial aggregate loss experience from claims related to asbestos-related illnesses, environmental remediation, product liability, mold, and other uncertain exposures. Harleysville Group has not experienced significant losses from such claims.

The income tax expense for the three month periods ended March 31, 2010 and 2009 includes a tax benefit of \$3.2 million and \$2.4 million, respectively, related to tax-exempt investment income.

Liquidity and Capital Resources

Operating activities provided \$14.8 million and \$11.7 million of net cash for the three months ended March 31, 2010 and 2009, respectively. The increase of \$3.1 million primarily is due to the change in the affiliate balance.

Investing activities used \$3.0 million and \$2.0 million of net cash for the three months ended March 31, 2010 and 2009, respectively. The change is primarily due to higher net purchases of investments in the 2010 period due to the increase in cash provided by operating activities, partially offset by the increase in cash used by financing activities.

Financing activities used \$11.8 million and \$9.7 million of net cash for the three months ended March 31, 2010 and 2009, respectively. The change is primarily due to an increase in the purchase of treasury stock in 2010.

Harleysville Group's investment strategy is designed to complement and support the insurance operations. Harleysville Group considers projected cash flow (premiums, investment income, reinsurance programs, liability payout patterns, general expenses, large seasonal obligations, intercompany transfers, etc.) to assure that sufficient liquidity exists within Harleysville Group and the Mutual Company. Maintaining a regular maturity schedule in readily marketable securities is an essential part of addressing liquidity. This regular maturity schedule is maintained in all interest rate environments. After-tax yield will be maximized consistent with safety and liquidity considerations by investment in taxable or tax-exempt securities, depending on Harleysville Group's tax position.

Harleysville Group Inc. had \$25.4 million of cash and marketable securities at March 31, 2010 which is available for general corporate purposes including dividends, debt service, capital contributions to subsidiaries, acquisitions and the repurchase of stock. On February 19, 2009, the Board of Directors authorized the Company to repurchase up to 800,000 shares of its outstanding common stock over a two year period in the open market or in privately negotiated transactions. Additionally, the Board authorized the Company to make purchases under the terms of a Rule 10b5-1 trading plan, which allows the Company to purchase its shares at times when it ordinarily would not be in the market because of self-imposed trading blackout periods, such as the time preceding its quarterly earnings releases, or because its officers are in possession of material, non-public information. The Company repurchased shares in open market transactions from the public float, and did not repurchase shares from the Mutual Company. This program was completed on June 15, 2009. On July 30, 2009 the Board of Directors authorized the Company to repurchase up to an additional 800,000 shares of its outstanding common stock over a two year period under terms similar to the repurchase authorization of February 19, 2009. The Company currently intends to repurchase shares in open market transactions from the public float, and not repurchase shares from the Mutual Company. As of May 4, 2010, the Company had repurchased 374,096 shares under this authorization, leaving 425,904 shares authorized to be repurchased. Harleysville Group has no other material commitments for capital expenditures as of March 31, 2010.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**Management's Discussion and Analysis of Financial Condition
and Results of Operations**

(Continued)

As a holding company, the Company's principal source of cash for the payment of dividends is dividends from its insurance subsidiaries. The Company's insurance subsidiaries are subject to state laws that restrict their ability to pay dividends. The Company's insurance subsidiaries paid dividends of \$12.1 million to the Company in the first quarter of 2010. These dividends had been declared in 2009.

The timing of future cash payments associated with unpaid losses and loss settlement expenses and contractual obligations pursuant to debt agreements is not expected to be materially different from that disclosed in the Company's Annual Report on Form 10-K for fiscal year 2009.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**Item 3.****Quantitative and Qualitative Disclosure
about Market Risk**

Harleysville Group's market risk generally represents the risk of gain or loss that may result from the potential change in the fair value of Harleysville Group's investment portfolio as a result of fluctuations in prices and interest rates. Harleysville Group attempts to manage its interest rate risk by maintaining an appropriate relationship between the average duration of the investment portfolio and the approximate duration of its liabilities. Changes to Harleysville Group's market risk since December 31, 2009 are reflected within Management's Discussion and Analysis of Financial Condition and Results of Operations and within the financial statements contained within this Form 10-Q.

Harleysville Group has maintained approximately the same duration of its investment portfolio to its liabilities from December 31, 2009 to March 31, 2010.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**Item 4.****Controls and Procedures**

- (a) *Evaluation of disclosure controls and procedures.* Our management, under the supervision and with the participation of the chief executive officer and the chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures as required by Rule 14a-15(b) or Rule 15d-15(b) of the Securities Exchange Act of 1934, as amended, as of March 31, 2010, which is the end of the period covered by this quarterly report on Form 10-Q. Based on that evaluation, the chief executive officer and chief financial officer have concluded that these disclosure controls and procedures are effective to provide that (a) material information relating to us, including our consolidated subsidiaries, is made known to these officers by other employees of us and our consolidated subsidiaries, particularly material information related to the first quarter of 2010, for which this periodic report is being prepared; and (b) this information is recorded, processed, summarized, evaluated and reported, as applicable, within the time periods specified in the rules and forms of the SEC.
- (b) *Change in internal control over financial reporting.* There was no change in the Company's internal control over financial reporting that occurred during the first quarter of 2010 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES

PART II. OTHER INFORMATION

ITEM 1A. Risk Factors

The business, results of operations and financial condition, and therefore the value of Harleysville Group's securities, are subject to a number of risks. Some of those risks are set forth in the Company's annual report on Form 10-K for fiscal year 2009, filed with the SEC on March 5, 2010. There has been no material change from risk factors as previously disclosed in the Company's annual report for fiscal year 2009.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities ⁽¹⁾

Period	Total Number of Shares Purchased ⁽²⁾	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
January 1 - January 31, 2010	190,609	\$31.66	190,609	539,238
February 1 - February 28, 2010	115,309	\$32.15	97,319	441,919
March 1 - March 31, 2010	—	—	—	—

(1) On February 19, 2009, the Board of Directors authorized the Company to repurchase up to 800,000 shares of its outstanding common stock over a two year period in the open market or in privately negotiated transactions. Additionally, the Board authorized the Company to make purchases under the terms of a Rule 10b5-1 trading plan, which allows the Company to purchase its shares at times when it ordinarily would not be in the market because of self-imposed trading blackout periods, such as the time preceding its quarterly earnings releases, or because its officers are in possession of material, non-public information. The Company repurchased shares in open market transactions from the public float, and did not repurchase shares from the Mutual Company. This program was completed on June 15, 2009. On July 30, 2009 the Board of Directors authorized the Company to repurchase up to an additional 800,000 shares of its outstanding common stock over a two year period under terms similar to the repurchase authorization of February 19, 2009. The Company currently intends to repurchase shares in open market transactions from the public float, and not repurchase shares from the Mutual Company. As of May 4, 2010, the Company had repurchased 374,096 shares under this authorization, leaving 425,904 shares authorized to be repurchased. Harleysville Group has no other material commitments for capital expenditures as of March 31, 2010.

(2) Represents the total number of shares repurchased during the period, of which 305,918 of these shares were settled for cash on or before March 31, 2010.

In accordance with the terms of its Equity Incentive Plan, the Company acquired the following shares from employees in connection with stock option exercises and the vesting of restricted stock. The stock was received in payment of the exercise price of the stock options and in satisfaction of withholding taxes due upon exercise or vesting.

February: 17,990 shares

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**PART II. OTHER INFORMATION**

(Continued)

ITEM 6. a. Exhibits

- 10.1 Harleysville Group Inc. Amended and Restated Equity Incentive Plan (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K dated April 28, 2010 and filed with the SEC on May 4, 2010).
- 10.2* Harleysville Group Inc. Amended and Restated Employee Stock Purchase Plan, as amended by the Board of Directors April 28, 2010.
- 31.1* Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2* Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1* Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2* Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

*Filed herewith.

HARLEYSVILLE GROUP INC. AND SUBSIDIARIES**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Harleysville Group Inc.

Date: May 7, 2010

By: /s/ ARTHUR E. CHANDLER

Arthur E. Chandler
Senior Vice President and
Chief Financial Officer
(principal financial officer)

HARLEYSVILLE GROUP INC.**AMENDED AND RESTATED EMPLOYEE STOCK PURCHASE PLAN**

Amended and Restated by the Board of Directors April 28, 2010

I. PURPOSE

The Harleysville Group Inc. Amended and Restated Employee Stock Purchase Plan (the "Plan") is established by the Harleysville Group Inc. (the "Company") for the benefit of the eligible employees of the Company, its parent and their respective subsidiaries. The purpose of the Plan is to provide each eligible employee with an opportunity to acquire or increase a proprietary interest in the Company. The Plan is intended to meet the requirements of Section 423 of the Internal Revenue Code of 1986, as amended (the "Code"). As used herein, the terms "parent" and "subsidiary" shall have the same meaning as in Section 425 of the Code.

II. DEFINITIONS

1. "Company" means Harleysville Group Inc., a Delaware corporation, and any successor in a reorganization or similar transaction.
2. "Base Pay" means the regular compensation paid to a Participant with respect to the Enrollment Period. Base Pay shall not include overtime, bonuses, or other items which are not considered to be regular earnings by the Company.
3. "Board" means the Board of Directors of the Company.
4. "Code" means the Internal Revenue Code of 1986, as amended.
5. "Committee" means the Committee of at least three officers appointed by the Board.
6. "Common Stock" means the common stock of the Company, par value of \$1.00 per share, and may be either stock previously authorized but unissued, or stock reacquired by the Company.
7. "Disability" means the inability of a Participant to perform the services normally rendered due to any physical or mental impairment that can be expected to be of either permanent or indefinite duration, as determined by the Company on the basis of appropriate medical evidence, and that results in the Participant's cessation of active employment with the Company.
8. "Enrollment Period" means the January 1-14 or July 1-14 immediately preceding a subscription period.
9. "Fair Market Value" means the closing sale price of a share of Common Stock on a given date (as described in this Plan) on the principal securities exchange on which the Company's Common Stock is listed or traded.

10. "Participant" means an eligible employee of the Company, its parent or any of their respective subsidiaries who files an enrollment card.
11. "Plan" means this Amended and Restated Employee Stock Purchase Plan.
12. "Retirement" means cessation of a Participant's employment in accordance with the then-current retirement eligibility standards of the Company, its parent or the relevant subsidiary, which may include early retirement or normal retirement.
13. "Share Purchase Limit" means, for each Subscription Period, a maximum of 1,000 shares of Common Stock, subject to adjustment as set forth in Section III.D.
14. "Subscription Period" means the period from January 15 through July 14 or from July 15 through January 14.
15. "Subscription Price" has the meaning set forth in Article VI.
16. "Termination of Employment" means a cessation of the Participant's employment with the Company, its parent or any affiliates for any reason other than Retirement, death or disability.

III. PLAN ADMINISTRATION

- A. ADMINISTRATION: The Plan shall be administered by the Committee. Subject to the express provisions of the Plan, the Committee shall have full and exclusive authority:

- (1) to interpret the Plan;
- (2) to prescribe, amend and rescind rules and regulations relating to the Plan; and
- (3) to make all other determinations deemed necessary or advisable in the implementation and administration of the Plan as permitted by federal and state laws and regulations, or by rules and regulations of a national securities exchange or the Nasdaq Stock Market.

All determinations of the Committee in the administration of the Plan, as described herein, shall be final and conclusive and binding upon all persons including, without limitation, the Company, its stockholders, Participants, and any persons having any interest under the Plan.

- B. MAXIMUM NUMBER OF SHARES AVAILABLE:

- (1) Subject to adjustment as specified in Section III.D. below, the aggregate number of shares of common stock that may be issued under the Plan is 3,150,000 shares, representing 1,000,000 shares previously approved in 1995, 650,000 approved in 2003, and 1,500,000 shares approved in 2008. Such shares that are issued may be authorized and unissued shares or treasury shares. Except as provided herein, any shares subject to an award which for any reason are not issued shall again be available under the Plan.

C. ELIGIBILITY; SHARE PURCHASE LIMITATIONS; EFFECT OF HARDSHIP WITHDRAWAL:

(1) All regular full-time employees and regular part-time employees who work at least twenty (20) hours or more a week for the Company, its parent, or any of their respective subsidiaries which have been designated by the Board as participating in the Plan (including subsidiaries which are so designated after the stockholders have approved the Plan) are eligible to participate in the Plan.

(2) A person who is otherwise eligible to participate shall not be granted any right to purchase stock under the Plan to the extent (i) it would, if exercised, cause the person to own shares of stock (including shares which would be owned if all outstanding options to purchase stock owned by such person were exercised) which possess five percent (5%) or more of the total combined voting power or value of all classes of stock of the Company, its parent or any of their respective subsidiaries; (ii) it would, if exercised, cause the person to have the right to acquire through the Plan shares of Common Stock in excess of the Share Purchase Limit, or (iii) it causes such person to have purchase rights under the Plan (and all other stock purchase plans of the Company, its parent or any subsidiary, which meet the requirements of Section 423 of the Code) which accrue at a rate which exceeds \$25,000 of Fair Market Value of stock of the Company, its parent or any subsidiary (determined at the time the right to purchase stock under this Plan is granted) for each calendar year in which such right is outstanding. For this purpose a right to purchase stock accrues when it first becomes exercisable during the calendar year (but the rate of accrual for any calendar year can in no event exceed \$25,000 of the Fair Market Value of the stock subject to the right) and the number of shares of stock under one right may not be carried over to any other right.

(3) If an employee obtains a hardship withdrawal under the Company's Retirement Savings Plus Plan or any similar plan maintained by the Company, its parent, or a subsidiary, then said employee may not, for the six (6) month period following the hardship withdrawal, make any contributions for purchase of stock under the Plan. In such case, such employee will be deemed to have withdrawn his or her contribution for the current Subscription Period and will have such contributions returned to him or her. The employee is further not entitled to re-subscribe to the Plan until the beginning of the first Subscription Period following the completion of the six (6) month period.

D. ADJUSTMENTS: In the event of stock dividends, stock splits, re capitalizations, mergers, consolidations, combinations, exchanges of shares, spin-offs, liquidations, reclassifications or other similar changes in the capitalization of the Company, such automatic substitution or adjustment shall be made in the Share Purchase Limit, the maximum aggregate number of shares which may be issued under this Plan, the maximum number of shares that can be purchased in any calendar year or Subscription Period and the Subscription Price for such shares, as the Board determines shall

cause an equitable adjustment under this Plan, in proportion to the effect of such change to the Common Stock generally. In the event of a change in the Common Stock as presently constituted, which change is limited to a change of all of the authorized shares with par value into the same number of shares with a different par value or without par value, the shares resulting from any such change shall be deemed to be the Common Stock within the meaning of this Plan.

IV. ENROLLMENT AND ENROLLMENT PERIODS

Enrollment will take place in the Enrollment Periods. Any employee who is eligible to participate and desires to subscribe for the purchase of shares of Common Stock for the following Subscription Period must file a subscription agreement with the Company's Payroll unit during the applicable Enrollment Period. Once enrolled, a Participant Employee will continue to participate in the Plan for each succeeding Subscription Period until he or she terminates his or her participation or ceases to be an eligible employee. If a Participant desires to change his or her rate of contribution, he or she may do so effective for the next Subscription Period by filing a new subscription agreement during the applicable Enrollment Period.

V. DURATION OF OFFER AND SUBSCRIPTION PERIODS

The Effective Date of this Plan shall be the first day of the Subscription Period following approval of this Plan by the Company's stockholders; provided, that the applicable Enrollment Period may occur prior to such date in accordance with this Plan. No Subscription Period shall commence on or after the tenth anniversary of the Effective Date, but a Subscription Period started prior to such date may extend until completion of such final Subscription Period. Thereafter, this Plan shall terminate.

VI. SUBSCRIPTION PRICE

The "Subscription Price" for each share of Common Stock shall be the lesser of eighty-five percent (85%) of the Fair Market Value of such Common Stock on the last trading day before the first day of the Subscription Period or eighty-five percent (85%) of the Fair Market Value of such share on the last trading day of the Subscription Period, but in no event less than \$1.00 per share, the par value of a share of Common Stock.

VII. AMOUNT OF CONTRIBUTION AND METHOD OF PAYMENT

Except as otherwise provided herein, the Subscription Price shall be paid by a Participant by means of the use of funds credited to such Participant's Plan account during the Subscription Period through payroll deductions. The minimum deduction shall be no less than the lesser of one percent (1%) of the Participant's Base Pay or \$3.00 bi-weekly and the maximum deduction shall be no more than fifteen percent (15%) of such Base Pay. Payroll deductions shall commence with the first pay issued during the Subscription Period and shall continue with each pay throughout the entire Subscription Period except for pay periods for which the Participant receives no compensation (i.e., uncompensated personal leave, leave of absence, etc.).

VIII. PURCHASE OF SHARES

The Company will maintain on its books a "Plan Account" in the name of each Participant. At the close of each pay period, the amount deducted from the Participant's Base Pay will be credited to the Participant's Plan Account. As of the last day of each Subscription Period, the amount then in the Participant's Plan Account will be divided by the Subscription Price for such Subscription Period and the Participant's Plan Account will be credited with the number of whole and fractional shares of Common Stock that results, subject to the limitations set forth in Section III.C(2). Shares will be issued in a book entry form with the Company's stock transfer agent. A Participant will receive a statement of account in a timely fashion from the transfer agent following the end of each Subscription Period. In the event the number of shares subscribed for any Subscription Period exceeds the number of shares available for sale under the Plan for such period, the available shares shall be allocated among the Participants in proportion to their Plan Account balances.

IX. WITHDRAWAL FROM THE PLAN

A Participant may withdraw from the Plan at any time. At the time of withdrawal the amount credited to the Participant's Plan Account will be refunded in cash without interest.

X. SEPARATION FROM EMPLOYMENT

Separation from employment for any reason including death, disability, Retirement or Termination of Employment shall be treated as an automatic withdrawal as set forth in Section IX, except that if separation occurs within three months prior to a purchase date, such Participant may continue to participate during that Subscription Period although no further contributions may be made. A transfer among the Company, its parent or their respective designated subsidiaries shall not be treated as a separation from employment.

XI. ASSIGNMENT

No Participant may assign his or her subscription or rights to subscribe to any other person and any attempted assignment shall be void.

XII. AMENDMENT OR DISCONTINUANCE OF THE PLAN

The Board shall have the right to amend, modify or terminate the Plan at any time without notice provided that no Participant's existing rights are adversely affected thereby and provided further that without the approval of the holders of a majority of the issued and outstanding shares of Common Stock no such amendment shall increase the total number of shares subject to the Plan, change the formula by which the price at which the shares shall be purchased is determined, change the class of employees eligible to participate in the Plan, materially increase the benefits accruing to Participants under the Plan, or make any other action effective that requires stockholder approval as required by federal or state laws or regulations or by rules and regulations of a national securities exchange or Nasdaq without seeking and receiving such stockholder approval.

XIII. TRANSFERABILITY

Neither payroll deductions credited to a Participant's Plan Account nor any rights with regard to any rights to purchase shares of Common Stock under this Plan may be assigned, transferred, pledged or otherwise disposed of in any way (other than by the laws of descent and distribution or as provided in Section XIII hereof) by the Participant. Any such attempt at assignment, transfer, pledge or other disposition shall be without effect.

XIV. NOTICE OF DISQUALIFYING DISPOSITION

If the Participant makes a disposition, within the meaning of Section 424(c) of the Code of any shares of Common Stock issued to Participant under this Plan, and such disposition occurs within the two-year period commencing on the day after the beginning of a Subscription Period or within the one-year period commencing on the day after the purchase of such Shares, the Participant shall, within ten (10) days of such disposition, notify the Company thereof in writing.

XV. MISCELLANEOUS PROVISIONS

A. GOVERNMENT AND OTHER REGULATIONS: The obligation of the Company to issue stock under the Plan shall be subject to all applicable laws, rules and regulations, and to such approvals by any government agencies as may be required.

B. OTHER COMPENSATION PLANS AND PROGRAMS: The Plan shall not be deemed to preclude the implementation by the Company, Parent or its subsidiaries of other compensation plans or programs which may be in effect from time to time. Participation in this Plan shall not affect an employee's eligibility to participate in any other benefit or incentive plan of the Company, its Parent or its subsidiaries except as provided in such other plan. Any purchases made pursuant to this Plan shall not be used in determining the benefits provided under any other plan of the Company, Parent or its subsidiaries unless specifically provided in such other plan.

C. CONSTRUCTION OF PLAN: The interpretation of the Plan and the application of any rules implemented hereunder shall be determined in accordance with the laws of the Commonwealth of Pennsylvania.

D. PRONOUNS, SINGULAR AND PLURAL: The masculine may be read as feminine, the singular as plural, and the plural as singular as necessary to give effect to the Plan.

E. LIMITATION OF RIGHTS:

(1) No Right to Continue as an Employee: Neither the Plan, nor the granting of a right to participate nor any other action taken pursuant to the Plan, shall constitute or be evidence of any agreement or understanding, express or implied, that the Participant has a right to continue as an employee of the Company, its parent or any of their respective subsidiaries for any period of time, or at any particular rate of compensation.

(2) No Stockholder's Rights: A Participant shall have no rights as a stockholder with respect to the shares issued hereunder

until the end of a Subscription Period in which a Participant is enrolled, and no adjustment will be made for dividends or other rights for which the record date is prior to the date such shares are issued.

F. STOCKHOLDER APPROVAL: The adoption of this Plan was subject to stockholder approval, which was obtained. The Company shall obtain the further approval of its stockholders for any amendment to this Plan if such approval is required by law or the rules of any applicable stock exchange.

TO RECORD THE ADOPTION OF THIS PLAN, THE COMPANY HAS CAUSED ITS AUTHORIZED OFFICERS TO AFFIX THE CORPORATE NAME AND SEAL HERETO THIS 28th DAY OF APRIL, 2010.

HARLEYSVILLE GROUP INC.

BY: /s/ Michael L. Browne
Michael L. Browne, President & CEO

ATTEST:

/s/ Robert A. Kauffman
Robert A. Kauffman, Secretary

**CERTIFICATION PURSUANT TO THE SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Michael L. Browne, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Harleysville Group Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 7, 2010

/s/ MICHAEL L. BROWNE

Michael L. Browne

President and Chief Executive Officer

**CERTIFICATION PURSUANT TO THE SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Arthur E. Chandler, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Harleysville Group Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 7, 2010

/s/ ARTHUR E. CHANDLER

Arthur E. Chandler

Senior Vice President and Chief Financial Officer

HARLEYSVILLE GROUP INC.
CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Harleysville Group Inc. (the "Company") on Form 10-Q for the period ended March 31, 2010, as filed with the U.S. Securities and Exchange Commission on the date hereof (the "Report"), I, Michael L. Browne, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that based on my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 7, 2010

/s/ MICHAEL L. BROWNE

Michael L. Browne

President and Chief Executive Officer

HARLEYSVILLE GROUP INC.
CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Harleysville Group Inc. (the "Company") on Form 10-Q for the period ended March 31, 2010, as filed with the U.S. Securities and Exchange Commission on the date hereof (the "Report"), I, Arthur E. Chandler, Senior Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that based on my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 7, 2010

/s/ ARTHUR E. CHANDLER

Arthur E. Chandler

Senior Vice President and Chief Financial Officer