Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934**

for the quarterly period ended June 30, 2010 or

¨ **Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934**

for the transition period from _______ to _______

Commission File Number: 1-9761

ARTHUR J. GALLAGHER & CO.

(Exact name of registrant as specified in its charter)

DELAWARE	**36-2151613**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

Two Pierce Place, Itasca, Illinois 60143-3141

(Address of principal executive offices) (Zip code)

(630) 773-3800

(Registrant s telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES x NO ¨

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO x

The number of outstanding shares of the registrant s Common Stock, $1.00 par value, as of June 30, 2010 was 105,203,000.

Table of Contents

Arthur J. Gallagher & Co.

Index

Table of Contents

Part I Financial Information

Item 1. Financial Statements (Unaudited)

Arthur J. Gallagher & Co.

Consolidated Statement of Earnings

(Unaudited-in millions, except per share data)

	Three-month period ended June 30, 2010	Three-month period ended June 30, 2009	Six-month period ended June 30, 2010	Six-month period ended June 30, 2009
Commissions	$ 257.0	$ 249.7	$ 461.2	$ 447.7
Fees	179.4	186.9	344.4	353.5
Supplemental and contingent commissions	19.3	11.8	62.7	41.3
Investment income	2.1	1.7	3.5	3.2
Gains realized on books of business sales	0.6	3.3	1.5	9.4
Revenues from clean-coal activities	2.4		65.1	0.4
Other net revenues (loss)	(1.3)	0.2	3.5	(0.8)
Total revenues	459.5	453.6	941.9	854.7
Compensation	275.8	270.4	538.0	521.7
Operating	87.4	79.1	168.6	158.0
Cost of revenues from clean-coal activities			64.0	
Interest	8.7	7.0	17.3	14.3
Depreciation	8.0	7.5	15.7	15.2
Amortization	16.6	14.1	30.5	26.5
Change in estimated acquisition earnout payables	(0.9)	1.4	1.0	1.4
Total expenses	395.6	379.5	835.1	737.1
Earnings from continuing operations before income taxes	63.9	74.1	106.8	117.6
Provision for income taxes	22.0	30.3	35.7	45.5
Earnings from continuing operations	41.9	43.8	71.1	72.1
Discontinued operations:				
Earnings (loss) on discontinued operations before income taxes	3.0		3.0	(3.3)
Gain on disposal of operations				0.1
Provision (benefit) for income taxes	0.9		0.9	(1.3)
Earnings (loss) from discontinued operations	2.1		2.1	(1.9)
Net earnings	$ 44.0	$ 43.8	$ 73.2	$ 70.2
Basic net earnings (loss) per share:				
Earnings from continuing operations	$ 0.40	$ 0.44	$ 0.69	$ 0.73
Earnings (loss) from discontinued operations	0.02		0.02	(0.02)
Net earnings	$ 0.42	$ 0.44	$ 0.71	$ 0.71

Diluted net earnings (loss) per share:								
Earnings from continuing operations	$	0.40	$	0.44	$	0.69	$	0.73
Earnings (loss) from discontinued operations		0.02				0.02		(0.02)
Net earnings	$	0.42	$	0.44	$	0.71	$	0.71
Dividends declared per common share	$	0.32	$	0.32	$	0.64	$	0.64

See notes to consolidated financial statements.

Table of Contents

Arthur J. Gallagher & Co.

Consolidated Balance Sheet

(In millions)

	June 30, 2010 (Unaudited)	December 31, 2009
Cash and cash equivalents	$ 230.0	$ 205.9
Restricted cash	566.0	522.6
Premiums and fees receivable	916.0	693.7
Other current assets	111.6	117.8
Total current assets	1,823.6	1,540.0
Fixed assets - net	79.0	80.7
Deferred income taxes	255.4	271.1
Other noncurrent assets	186.4	177.8
Goodwill - net	780.4	742.3
Amortizable intangible assets - net	431.0	438.4
Total assets	$ 3,555.8	$ 3,250.3
Premiums payable to insurance and reinsurance companies	$ 1,414.4	$ 1,166.5
Accrued compensation and other accrued liabilities	188.5	214.7
Unearned fees	43.7	41.5
Other current liabilities	43.3	51.7
Corporate related borrowings - current		
Total current liabilities	1,689.9	1,474.4
Corporate related borrowings - noncurrent	550.0	550.0
Other noncurrent liabilities	350.5	333.0
Total liabilities	2,590.4	2,357.4
Stockholders equity:		
Common stock - issued and outstanding 105.2 shares in 2010 and 102.5 shares in 2009	105.2	102.5
Capital in excess of par value	417.2	349.1
Retained earnings	456.3	450.3
Accumulated other comprehensive loss	(13.3)	(9.0)
Total stockholders equity	965.4	892.9
Total liabilities and stockholders equity	$ 3,555.8	$ 3,250.3

See notes to consolidated financial statements.

Table of Contents

Arthur J. Gallagher & Co.

Consolidated Statement of Cash Flows

(Unaudited - in millions)

	Six-month period ended June 30, 2010	2009
Cash flows from operating activities:		
Earnings from continuing operations	$ 71.1	$ 72.1
Adjustments to reconcile earnings from continuing operations to net cash provided by operating activities:		
Net (gain) loss on investments	(3.3)	0.9
Depreciation and amortization	46.2	41.7
Change in estimated acquisition earnout payables	1.0	1.4
Amortization of deferred compensation and restricted stock	3.3	3.1
Stock-based and other noncash compensation expense	3.9	3.9
Net change in restricted cash	(34.3)	(66.7)
Net change in premiums receivable	(196.9)	(279.7)
Net change in premiums payable	222.3	334.7
Net change in other current assets	3.4	10.0
Net change in accrued compensation and other accrued liabilities	(30.4)	(54.2)
Net change in fees receivable/unearned fees	(6.3)	(28.4)
Net change in income taxes payable	8.7	6.4
Net change in deferred income taxes	12.9	26.2
Net change in other noncurrent assets and liabilities	(11.0)	5.2
Net cash provided by operating activities of continuing operations	90.6	76.6
Earnings (loss) from discontinued operations	2.1	(1.9)
Noncash items related to discontinued operations	(3.1)	3.0
Net gain on disposal of discontinued operations		(0.1)
Net cash provided by operating activities	89.6	77.6
Cash flows from investing activities:		
Net additions to fixed assets	(13.0)	(13.5)
Cash paid for acquisitions, net of cash acquired	(25.0)	(31.9)
Net proceeds of investment transactions	13.2	0.3
Net cash used by investing activities	(24.8)	(45.1)
Cash flows from financing activities:		
Proceeds from issuance of common stock	23.1	4.5
Tax impact from issuance of common stock	2.4	(3.1)
Repurchases of common stock	(0.3)	(0.3)
Dividends paid	(65.9)	(62.9)
Borrowings on line of credit facility	48.0	105.0
Repayments on line of credit facility	(48.0)	(44.0)
Net cash used by financing activities	(40.7)	(0.8)
Net increase in cash and cash equivalents	24.1	31.7
Cash and cash equivalents at beginning of period	205.9	194.4

Cash and cash equivalents at end of period	$ 230.0	$ 226.1
Supplemental disclosures of cash flow information:		
Interest paid	$ 17.3	$ 14.3
Income taxes paid	12.8	15.4

See notes to consolidated financial statements.

Table of Contents

Arthur J. Gallagher & Co.

Consolidated Statement of Stockholders Equity

(Unaudited - in millions)

	Common Stock		Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Earnings (Loss)	Total
	Shares	Amount				
Balance at December 31, 2009	102.5	$ 102.5	$ 349.1	$ 450.3	$ (9.0)	$ 892.9
Net earnings				73.2		73.2
Net change in pension liability, net of taxes of $0.3 million					0.5	0.5
Foreign currency translation, net of taxes of $2.9 million					(4.8)	(4.8)
Comprehensive earnings						68.9
Compensation expense related to stock option plan grants			3.5			3.5
Tax expense from issuance of common stock			2.4			2.4
Common stock issued in:						
Fifteen purchase transactions	1.5	1.5	36.9			38.4
Stock option plans	1.0	1.0	18.1			19.1
Employee stock purchase plan	0.2	0.2	3.8			4.0
Deferred compensation and restricted stock			3.3			3.3
Other compensation expense			0.4			0.4
Common stock repurchases			(0.3)			(0.3)
Cash dividends declared on common stock				(67.2)		(67.2)
Balance at June 30, 2010	105.2	$ 105.2	$ 417.2	$ 456.3	$ (13.3)	$ 965.4

See notes to consolidated financial statements.

Table of Contents

Notes to June 30, 2010 Consolidated Financial Statements (Unaudited)

1. Nature of Operations and Basis of Presentation

Arthur J. Gallagher & Co. (Gallagher) provides insurance brokerage and risk management services to a wide variety of commercial, industrial, institutional and governmental organizations through two operating segments. Commission and fee revenue generated by the Brokerage Segment is primarily related to the negotiation and placement of insurance for Gallagher s clients. Fee revenue generated by the Risk Management Segment is primarily related to claims management, information management, risk control services and appraisals in the property/casualty (P/C) market. Investment income and other revenue is generated from Gallagher s investment portfolio, which includes invested cash and fiduciary funds, as well as tax-advantaged, clean-energy and other investments. Gallagher is headquartered in Itasca, Illinois, has operations in fifteen countries and does business in more than 100 countries globally through a network of correspondent brokers and consultants.

The accompanying unaudited consolidated financial statements have been prepared by Gallagher pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in annual financial statements have been omitted pursuant to such rules and regulations. Gallagher believes the disclosures are adequate to make the information presented not misleading. The unaudited consolidated financial statements included herein are, in the opinion of management, prepared on a basis consistent with the audited consolidated financial statements for the year ended December 31, 2009 and include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the information set forth. The quarterly results of operations are not necessarily indicative of results of operations for subsequent quarters or the full year. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in Gallagher s Annual Report on Form 10-K for the year ended December 31, 2009. Certain reclassifications have been made to the amounts reported herein related to prior year amounts in order to conform them to the current year presentation.

In the preparation of Gallagher s consolidated financial statements as of June 30, 2010, management evaluated all material subsequent events or transactions that occurred after the balance sheet date, through the date on which the financial statements were issued, for potential recognition in its consolidated financial statements and/or disclosure in the notes thereto.

2. Effect of New Accounting Pronouncements

Revenue Arrangements with Multiple Deliverables

In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2009-13, Multiple Deliverable Revenue Arrangements (ASU 2009-13). ASU 2009-13 updates the existing multiple-element revenue arrangements guidance currently included in Accounting Standards Codification (ASC) 605-25.

The revised guidance provides for two significant changes to the existing multiple element revenue arrangements guidance. The first relates to the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting. This change is significant as it will likely result in the requirement to separate more deliverables within an arrangement, ultimately leading to changes in revenue deferral.

The second change modifies the manner in which the transaction consideration is allocated across the separately identified deliverables. Together, these items may cause a change in the recognition of revenue for multiple-element arrangements from previous guidance. ASU 2009-13 also significantly expands the disclosures required for multiple-element revenue arrangements.

The revised multiple-element revenue arrangements guidance will be effective for the first annual reporting period beginning on or after June 15, 2010, and may be applied retrospectively for all periods presented or prospectively to arrangements entered into or materially modified after the adoption date. Early adoption is permitted provided that the revised guidance is retroactively applied to the beginning of the year of adoption. If the guidance is adopted prospectively, certain transitional disclosures are required for each reporting period in the initial year of adoption. Gallagher is currently evaluating the impact that the adoption of ASU 2009-13 could have, if any, on its consolidated financial statements and notes thereto. Gallagher has not yet determined whether it will elect to early adopt ASU 2009-13.

Table of Contents

Consolidation of Variable Interest Entities

In June 2009, the FASB issued an amendment to the consolidation rules for variable interest entities (VIEs), which (i) addresses the effects of eliminating the qualifying special-purpose entity concept from existing guidance and (ii) responds to concerns about the application of certain key provisions in existing guidance, including concerns over the transparency of disclosures related to an enterprise s involvement with VIEs.

These amendments are applicable to all enterprises and to all entities with which those enterprises are involved, regardless of when that involvement arose. Therefore, upon adoption of these amendments, all enterprises must reconsider the conclusions previously reached for the consolidation of a VIE. These amendments, among other things:

Amended certain guidance for determining whether an entity is a VIE, which may change an enterprise s assessment of which entities with which it is involved are VIEs.

Require a qualitative rather than a quantitative analysis to determine the primary beneficiary of a VIE.

Amended existing considerations of related party relationships in the determination of the primary beneficiary of a VIE by providing, among other things, an exception with respect to de facto agency relationships in certain circumstances.

Require continuous assessments of whether an enterprise is the primary beneficiary of a VIE.

Require enhanced disclosures about an enterprise s involvement with a VIE.

These amendments are effective as of the beginning of an enterprise s first annual reporting period that began after November 15, 2009 and for interim periods within that first annual reporting period. Thus, these amendments were effective for Gallagher beginning on January 1, 2010. The adoption of these amendments did not have any impact on Gallagher s consolidated financial statements or notes thereto.

3. Investments

The following is a summary of Gallagher s investments reported in other current and non-current assets in the accompanying consolidated balance sheet and the related funding commitments (in millions):

	June 30, 2010		December 31, 2009
	Assets	Funding Commitments	Assets
Clean-coal related ventures	$ 21.6	$	$ 29.8
Biomass energy ventures	8.5		8.5
Venture capital funds and other	7.2	1.3	7.4
Total investments	$ 37.3	$ 1.3	$ 45.7

Clean-Coal Related Ventures

Gallagher owns portions of various clean-coal production facilities and two early-stage clean-coal ventures, all of which have been deemed to be VIEs.

Eight Clean-Coal Facilities - Gallagher incurred capital expenditures totaling $31.4 million to build eight commercial clean-coal production facilities, and placed each into service in December 2009 at several coal-fired power plants. These facilities apply certain chemicals and technologies (licensed from Chem-Mod, LLC (Chem-Mod) as discussed below) to coal feedstock which, when mixed, reduce harmful emissions. In first quarter 2010, Gallagher sold portions of its ownership in six facilities, which reduced its net investment in the facilities to $22.3 million, and recognized a $4.8 million net pretax gain on the sales. Gallagher is currently seeking other utilities to purchase the coal produced by the two remaining facilities and additional partners to invest in these facilities.

Table of Contents

For the first two months of 2010, Gallagher was required to consolidate the operating results of these facilities because of its majority ownership position. Effective March 1, 2010, Gallagher sold a portion of its ownership interests in six of these facilities. As part of the sales of the interests in the six facilities, all owners must now consent to actions that would denote control, which eliminated the requirement for Gallagher to consolidate these facilities. These facilities are now accounted for using equity method accounting.

Chem-Mod Clean-Coal Venture - At June 30, 2010, Gallagher held a 42% interest in Chem-Mod s U.S. and Canadian operations and 20% of its other international operations. At June 30, 2010, Gallagher s carrying value of its investment in these Chem-Mod operations was zero. Chem-Mod, a multi-pollutant reduction venture, possesses rights, information and technologies for the reduction of unwanted emissions created during the combustion of coal. Chem-Mod has developed and is the exclusive licensee of proprietary emissions technologies it refers to as The Chem-Mod Solution, which uses a dual injection sorbent system to reduce mercury, sulfur dioxide and other toxic emissions at coal-fired power plants. Gallagher also believes that the application of The Chem-Mod Solution will qualify for refined coal tax credits under Internal Revenue Code Section 45 (IRC Section 45).

Chem-Mod has been determined to be a VIE. Gallagher is deemed to be the primary beneficiary based on the level of control it exerts on the operations of Chem-Mod, and therefore was required to consolidate this investment into its consolidated financial statements beginning in third quarter 2008. At June 30, 2010, total assets and total liabilities of this investment that were included in Gallagher s consolidated balance sheet were each less than $0.9 million. Gallagher is under no obligation to fund Chem-Mod s operations in the future and Chem-Mod has no debt that is recourse to Gallagher.

C-Quest Clean-Coal Venture - On April 15, 2010, Gallagher purchased an additional 3% interest in the global operations of C-Quest Technology LLC (C-Quest) for $1.5 million, which was written-off under equity method accounting. At June 30, 2010, Gallagher held an 8% interest in C-Quest s global operations and its carrying value in C-Quest was zero. Gallagher also has options to acquire an additional 19% interest in C-Quest s global operations (total price $9.5 million) at any time on or prior to August 1, 2013. C-Quest possesses rights, information and technology for the reduction of carbon dioxide emissions created by burning fossil fuels. C-Quest is deemed to be a VIE, but due to Gallagher s lack of control over the operation of C-Quest, Gallagher is not required to consolidate this investment.

Biomass Energy Ventures

Gallagher has made investments in various biomass energy ventures. At June 30, 2010, Gallagher s remaining investment of $8.5 million consisted of a 13.4% equity interest in a biomass company and related partnerships which own the rights to biogas from landfills and the wells, infrastructure and a pipeline to capture, distribute and sell biogas.

Venture Capital Funds and Other

At June 30, 2010, Gallagher s remaining investment of $7.2 million consisted of (i) four venture capital funds totaling $6.2 million, (ii) a 20% interest in an investment management company totaling $1.0 million, (iii) twelve certified low-income housing developments with zero carrying value, and (iv) two real estate entities with zero carrying value. Fourteen of the nineteen ventures have been determined to be VIEs, but are not required to be consolidated. At June 30, 2010, total assets and total debt of these fourteen ventures were approximately $63.0 million and $19.0 million, respectively. Gallagher s maximum exposure to a potential loss related to these investments was zero at June 30, 2010, which equaled the net aggregate carrying value of these ventures.

Table of Contents

4. Business Combinations

During the six-month period ended June 30, 2010, Gallagher acquired policy renewal rights and substantially all of the net assets of the following brokerage firms in exchange for Gallagher common stock and/or cash (in millions except share data):

Name and Effective Date of Acquisition	Common Shares Issued (000s)	Common Share Value	Cash Paid	Accrued Liability	Escrow Deposited	Recorded Earnout Payable	Total Recorded Purchase Price	Maximum Potential Earnout Payable
Securitas Re (SRE) February 12, 2010		$	$ 1.0	$ 0.3	$	$	$ 1.3	$
Winn & Company Insurance Brokers, Inc. (WIB) March 1, 2010	121	2.7	1.0		0.4	1.0	5.1	2.3
Policy renewal rights from FirstCity Partnership Ltd. (FCP) April 1, 2010	456	11.8	12.7			2.9	27.4	5.6
Risk & Reward Group (RRG) May 28, 2010			5.9			1.7	7.6	4.7
Bowen, Miclette, Britt & Merry of Arkansas, Inc. May 1, 2010	52	1.2			0.1	0.1	1.4	0.3
Joseph James & Associates (JJA) June 1, 2010	152	3.8	1.1		0.1	2.2	7.2	5.0
Two other acquisitionscompleted in first and second quarter	49	1.1	0.3		0.1	0.9	2.4	1.2
	830	$ 20.6	$ 22.0	$ 0.3	$ 0.7	$ 8.8	$ 52.4	$ 19.1

Common shares issued in connection with acquisitions are valued at closing market prices as of the effective date of the applicable acquisition. Escrow deposits that are returned to Gallagher as a result of adjustments to net assets acquired are recorded as reductions of goodwill when the escrows are settled. The maximum potential earnout payables disclosed in the foregoing table represent the maximum amount of additional consideration that could be paid pursuant to the terms of the respective purchase agreement related to each applicable acquisition. The amounts recorded as earnout payables are primarily based upon the future operating results of the acquired entities over a two- to three-year period subsequent to the acquisition date, are measured at fair value as of the acquisition date and are included on that basis in the recorded purchase price consideration in the foregoing table. Subsequent changes in these estimated earnout obligations, including the accretion of discount, will be recorded in the consolidated statement of earnings when incurred.

The fair value of these earnout obligations is based on the present value of the expected future payments to be made to the sellers of the acquired entities in accordance with the provisions outlined in the respective purchase agreements. In determining fair value, the acquired entity s future performance was estimated using financial projections developed by management for the acquired entity and market participant assumptions that were derived for revenue growth and/or profitability. The future payments are estimated using the earnout formula and performance targets specified in each purchase agreement and these financial projections. These payments were then discounted to present value using a risk-adjusted rate that takes into consideration market based rates of return which reflect the ability of the acquired entity to achieve the forecast. During the three-month periods ended June 30, 2010 and 2009, Gallagher recognized $1.5 million and $1.4 million, respectively, of expense in its consolidated statement of earnings related to the accretion of the discount recorded for earnout obligations

Table of Contents

related to its 2009 and 2010 acquisitions. During the six-month periods ended June 30, 2010 and 2009, Gallagher recognized $2.9 million and $1.4 million, respectively, of expense in its consolidated statement of earnings related to the accretion of the discount recorded for earnout obligations related to its 2009 and 2010 acquisitions. In addition, Gallagher recognized $2.5 million and $2.0 million of income during the three-month and six-month periods ended June 30, 2010, respectively, related to net adjustments in the estimated fair market values of earnout obligations related to four 2009 acquisitions. The aggregate amount of maximum earnout obligations related to the 2009 and 2010 acquisitions was $160.4 million, of which $70.5 million was recorded in the consolidated balance sheet as of June 30, 2010 based on the estimated fair value of the expected future payments to be made.

For all acquisitions made prior to 2009, potential earnout obligations were not included in the purchase price that was recorded for each applicable acquisition at its acquisition date because such obligations were not fixed and determinable. Future payments made under these arrangements, if any, will generally be recorded as additional goodwill when the earnouts are settled. The aggregate amount of maximum unrecorded earnout payables outstanding as of June 30, 2010 was $207.6 million related to acquisitions made by Gallagher during the period from 2006 to 2008.

The following is a summary of the estimated fair values of the net assets acquired at the date of each acquisition based on preliminary purchase price allocations (in millions):

	SRE	WIB	FCP	RRG	JJA	Three Other Acquisitions	Total
Current assets	$ 0.7	$ 0.7	$ 28.0	$ 2.0	$ 0.1	$ 2.4	$ 33.9
Fixed assets		0.4	0.5				0.9
Noncurrent assets			2.9				2.9
Goodwill	0.3	2.5	11.1	5.4	4.4	2.5	26.2
Expiration lists	1.0	2.2	10.0	2.9	2.8	1.5	20.4
Non-compete agreements		0.1				0.1	