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OLD REPUBLIC INTERNATIONAL CORP

Form 10-Q

May 07, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

Quarterly report pursuant to section 13 or 15(d) of the Security Exchange Act of 1934
for the quarterly period ended: March 31, 2014 or

Transition report pursuant to section 13 or 15(d) of the Security Exchange Act of 1934
Commission File Number: 001-10607

OLD REPUBLIC INTERNATIONAL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

No. 36-2678171
(IRS Employer Identification No.)

307 North Michigan Avenue, Chicago,
Illinois
(Address of principal executive office)

60601
(Zip Code)

Registrant's telephone number, including area code: 312-346-8100

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 definitions of "accelerated filer", "large accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one).

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2). Yes: No:

Class

Shares Outstanding
March 31, 2014

Common Stock / \$1 par value

260,546,465

There are 46 pages in this report

OLD REPUBLIC INTERNATIONAL CORPORATION

Report on Form 10-Q / March 31, 2014

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Old Republic International Corporation and Subsidiaries
Consolidated Balance Sheets
(\$ in Millions, Except Share Data)

	(Unaudited) March 31, 2014	December 31, 2013
Assets		
Investments:		
Available for sale:		
Fixed maturity securities (at fair value) (amortized cost: \$8,255.9 and \$8,477.3)	\$8,554.6	\$8,712.3
Equity securities (at fair value) (cost: \$966.4 and \$632.0)	1,190.0	1,004.2
Short-term investments (at fair value which approximates cost)	1,291.5	1,124.8
Miscellaneous investments	21.9	21.6
Total	11,058.0	10,863.1
Other investments	5.9	5.3
Total investments	11,063.9	10,868.5
Other Assets:		
Cash	130.2	153.3
Securities and indebtedness of related parties	20.2	18.0
Accrued investment income	92.0	87.2
Accounts and notes receivable	1,288.0	1,190.5
Federal income tax recoverable: Current	9.2	114.7
Deferred	78.3	48.4
Prepaid federal income taxes	20.1	—
Reinsurance balances and funds held	179.4	189.2
Reinsurance recoverable: Paid losses	69.3	64.9
Policy and claim reserves	3,201.0	3,150.8
Deferred policy acquisition costs	204.6	192.6
Sundry assets	454.1	455.7
Total Other Assets	5,747.0	5,665.9
Total Assets	\$16,811.0	\$16,534.4
Liabilities, Preferred Stock, and Common Shareholders' Equity		
Liabilities:		
Losses, claims, and settlement expenses	\$9,498.0	\$9,433.5
Unearned premiums	1,575.7	1,487.8
Other policyholders' benefits and funds	207.1	207.8
Total policy liabilities and accruals	11,280.8	11,129.2
Commissions, expenses, fees, and taxes	376.9	409.8
Reinsurance balances and funds	508.0	441.9
Debt	566.2	569.2
Sundry liabilities	213.1	209.0
Commitments and contingent liabilities		
Total Liabilities	12,945.2	12,759.4
Preferred Stock (1)	—	—
Common Shareholders' Equity:		

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Common stock (1)	260.5	260.4
Additional paid-in capital	674.5	673.9
Retained earnings	2,632.8	2,485.3
Accumulated other comprehensive income (loss)	319.5	378.2
Unallocated ESSOP shares (at cost)	(21.6	) (23.0
Total Common Shareholders' Equity	3,865.8	3,775.0
Total Liabilities, Preferred Stock and Common Shareholders' Equity	\$16,811.0	\$16,534.4

At March 31, 2014 and December 31, 2013, there were 75,000,000 shares of \$0.01 par value preferred stock authorized, of which no shares were outstanding. As of the same dates, there were 500,000,000 shares of common (1) stock, \$1.00 par value, authorized, of which 260,546,465 and 260,462,217 were issued as of March 31, 2014 and December 31, 2013, respectively. At March 31, 2014 and December 31, 2013, there were 100,000,000 shares of Class B Common Stock, \$1.00 par value, authorized, of which no shares were issued.

See accompanying Notes to Consolidated Financial Statements.

Old Republic International Corporation and Subsidiaries
Consolidated Statements of Income (Unaudited)
(\$ in Millions, Except Share Data)

	Quarters Ended	
	March 31,	
	2014	2013
Revenues:		
Net premiums earned	\$1,057.2	\$1,060.2
Title, escrow, and other fees	75.4	105.4
Total premiums and fees	1,132.7	1,165.6
Net investment income	82.8	79.3
Other income	23.8	20.4
Total operating revenues	1,239.3	1,265.4
Realized investment gains (losses):		
From sales	191.2	4.5
From impairments	—	—
Total realized investment gains (losses)	191.2	4.5
Total revenues	1,430.6	1,269.9
Benefits, Claims and Expenses:		
Benefits, claims and settlement expenses	556.1	578.8
Dividends to policyholders	3.9	4.8
Underwriting, acquisition, and other expenses	567.8	595.9
Interest and other charges	5.7	5.8
Total expenses	1,133.6	1,185.4
Income (loss) before income taxes (credits)	296.9	84.5
Income Taxes (Credits):		
Current	106.0	(.8)
Deferred	(3.4)	29.1)
Total	102.5	28.3
Net Income (Loss)	\$194.4	\$56.2
Net Income (Loss) Per Share:		
Basic	\$.75	\$.22
Diluted	\$.67	\$.21
Average shares outstanding: Basic	257,933,928	256,279,364
Diluted	294,513,903	292,081,785
Dividends Per Common Share:		
Cash	\$.1825	\$.1800

See accompanying Notes to Consolidated Financial Statements.

Old Republic International Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income (Unaudited)
(\$ in Millions)

	Quarters Ended	
	March 31,	
	2014	2013
Net Income (Loss) As Reported	\$ 194.4	\$ 56.2
Other comprehensive income (loss):		
Unrealized gains (losses) on securities:		
Unrealized gains (losses) on securities before reclassifications	106.3	109.0
Amounts reclassified as realized investment gains from sales in the statements of income	(191.2	) (4.5
Pretax unrealized gains (losses) on securities	(84.9	) 104.5
Deferred income taxes (credits)	(29.7	) 36.6
Net unrealized gains (losses) on securities, net of tax	(55.1	) 67.9
Defined benefit pension plans:		
Net pension adjustment before reclassifications	—	—
Amounts reclassified as underwriting, acquisition, and other expenses in the statements of income	(.4	) 2.9
Net adjustment related to defined benefit pension plans	(.4	) 2.9
Deferred income taxes (credits)	(.1	) 1.0
Net adjustment related to defined benefit pension plans, net of tax	(.3	) 1.8
Foreign currency translation and other adjustments	(3.2	) (3.1
Net adjustments	(58.7	) 66.6
Comprehensive Income (Loss)	\$ 135.7	\$ 122.8

See accompanying Notes to Consolidated Financial Statements.

Old Republic International Corporation and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)
(\$ in Millions)

	Quarters Ended	
	March 31,	
	2014	2013
Cash flows from operating activities:		
Net income (loss)	\$ 194.4	\$ 56.2
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Deferred policy acquisition costs	(12.2)	(2.5)
Premiums and other receivables	(97.7)	(49.1)
Unpaid claims and related items	45.9	44.8
Unearned premiums and other policyholders' liabilities	56.7	39.4
Income taxes	101.9	46.4
Prepaid federal income taxes	(20.1)	—
Reinsurance balances and funds	71.5	28.2
Realized investment (gains) losses	(191.2)	(4.5)
Accounts payable, accrued expenses and other	(13.7)	(15.7)
Total	135.4	143.2
Cash flows from investing activities:		
Fixed maturity securities:		
Maturities and early calls	201.8	279.1
Sales	498.2	15.8
Sales of:		
Equity securities	179.7	—
Other - net	4.3	19.4
Purchases of:		
Fixed maturity securities	(482.0)	(441.7)
Equity securities	(334.3)	—
Other - net	(9.5)	(9.2)
Net decrease (increase) in short-term investments	(166.8)	64.9
Other - net	—	(.4)
Total	(108.5)	(72.1)
Cash flows from financing activities:		
Issuance of common shares	1.0	.5
Redemption of debentures and notes	(3.0)	(2.8)
Dividends on common shares	(46.9)	(46.0)
Other - net	(1.0)	(1.3)
Total	(50.0)	(49.7)
Increase (decrease) in cash	(23.1)	21.3
Cash, beginning of period	153.3	101.2
Cash, end of period	\$ 130.2	\$ 122.6
Supplemental cash flow information:		
Cash paid (received) during the period for: Interest	\$ 10.4	\$ 10.4

Income taxes	\$.6	\$(17.7)
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See accompanying Notes to Consolidated Financial Statements.

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OLD REPUBLIC INTERNATIONAL CORPORATION
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
 (\$ in Millions, Except Share Data)

1. Accounting Policies and Basis of Presentation:

The accompanying consolidated financial statements have been prepared in conformity with the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC") of accounting principles generally accepted in the United States of America ("GAAP"). These interim financial statements should be read in conjunction with these notes and those included in the Company's 2013 Annual Report on Form 10-K incorporated herein by reference.

Pertinent accounting and disclosure pronouncements issued from time to time by the FASB are adopted by the Company as they become effective. In 2013, Old Republic adopted guidance requiring additional disclosures of amounts reclassified out of accumulated other comprehensive income. Such requirements are reflected in the presentation of the Consolidated Statements of Comprehensive Income.

The financial accounting and reporting process relies on estimates and on the exercise of judgment. In the opinion of management all adjustments consisting only of normal recurring accruals necessary for a fair presentation of the results have been recorded for the interim periods. Amounts shown in the consolidated financial statements and applicable notes are stated (except as otherwise indicated and as to share data) in millions, which amounts may not add to totals shown due to truncation. Necessary reclassifications are made in prior periods' financial statements whenever appropriate to conform to the most current presentation.

2. Common Share Data:

Earnings Per Share - Consolidated basic earnings per share excludes the dilutive effect of common stock equivalents and is computed by dividing income (loss) available to common stockholders by the weighted-average number of common shares actually outstanding for the quarterly and year-to-date periods. Diluted earnings per share are similarly calculated with the inclusion of dilutive common stock equivalents. The following table provides a reconciliation of net income (loss) and the number of shares used in basic and diluted earnings per share calculations.

	Quarters Ended	
	March 31,	
	2014	2013
Numerator:		
Net income (loss)	\$194.4	\$56.2
Numerator for basic earnings per share - income (loss) available to common stockholders	194.4	56.2
Adjustment for interest expense incurred on assumed conversion of convertible notes	3.6	3.6
Numerator for diluted earnings per share - income (loss) available to common stockholders after assumed conversion of convertible notes	\$198.0	\$59.8
Denominator:		
Denominator for basic earnings per share - weighted-average shares (a)	257,933,928	256,279,364
Effect of dilutive securities - stock based compensation awards	1,089,795	364,986
Effect of dilutive securities - convertible senior notes	35,490,180	35,437,435

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Denominator for diluted earnings per share - adjusted weighted-average shares and assumed conversion of convertible notes (a)	294,513,903	292,081,785
Earnings per share: Basic	\$.75	\$.22
Diluted	\$.67	\$.21
Anti-dilutive common stock equivalents excluded from earning per share computations:		
Stock based compensation awards	6,750,559	12,066,638
Convertible senior notes	—	—
Total	6,750,559	12,066,638

(a) In calculating earnings per share, pertinent accounting rules require that common shares owned by the Company's Employee Savings and Stock Ownership Plan that are as yet unallocated to participants in the plan be excluded from the calculation. Such shares are issued and outstanding and have the same voting and other rights applicable to all other common shares.

3. Investments:

The Company may classify its invested assets in terms of those assets relative to which it either (1) has the positive intent and ability to hold until maturity, (2) has available for sale or (3) has the intention of trading. As of March 31, 2014 and December 31, 2013, substantially all the Company's invested assets were classified as "available for sale."

Fixed maturity securities classified as "available for sale" and other preferred and common stocks (equity securities) are included at fair value with changes in such values, net of deferred income taxes, reflected directly in shareholders' equity. Fair values for fixed maturity securities and equity securities are based on quoted market prices or estimates using values obtained from independent pricing services as applicable.

The Company reviews the status and fair value changes of each of its investments on at least a quarterly basis during the year, and estimates of other-than-temporary impairments ("OTTI") in the portfolio's value are evaluated and established at each quarterly balance sheet date. In reviewing investments for OTTI, the Company, in addition to a security's market price history, considers the totality of such factors as the issuer's operating results, financial condition and liquidity, its ability to access capital markets, credit rating trends, most current audit opinion, industry and securities markets conditions, and analyst expectations to reach its conclusions. Sudden fair value declines caused by such adverse developments as newly emerged or imminent bankruptcy filings, issuer default on significant obligations, or reports of financial accounting developments that bring into question the validity of previously reported earnings or financial condition, are recognized as realized losses as soon as credible publicly available information emerges to confirm such developments. Absent issuer-specific circumstances that would result in a contrary conclusion, any equity security with an unrealized investment loss amounting to a 20% or greater decline for a six month period is considered OTTI. In the event the Company's estimate of OTTI is insufficient at any point in time, future periods' net income (loss) would be adversely affected by the recognition of additional realized or impairment losses, but its financial position would not necessarily be affected adversely inasmuch as such losses, or a portion of them, could have been recognized previously as unrealized losses in shareholders' equity. The Company recognized no OTTI adjustments for the quarters ended March 31, 2014 and 2013.

The amortized cost and estimated fair values by type and contractual maturity of fixed maturity securities are shown in the following tables. Expected maturities will differ from contractual maturities since borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed Maturity Securities by Type:				
March 31, 2014:				
U.S. & Canadian Governments	\$1,140.8	\$35.1	\$5.7	\$1,170.3
Tax-exempt	129.8	2.8	.4	132.3
Corporate	6,985.1	295.5	28.7	7,251.8
	\$8,255.9	\$333.6	\$34.9	\$8,554.6
December 31, 2013:				
U.S. & Canadian Governments	\$1,133.0	\$36.7	\$8.7	\$1,161.1
Tax-exempt	168.1	3.7	.5	171.3
Corporate	7,176.0	268.1	64.3	7,379.8
	\$8,477.3	\$308.7	\$73.6	\$8,712.3
			Amortized Cost	Estimated Fair Value

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Fixed Maturity Securities Stratified by Contractual Maturity at March 31, 2014:

Due in one year or less	\$717.6	\$726.5
Due after one year through five years	3,732.1	3,937.7
Due after five years through ten years	3,609.7	3,686.8
Due after ten years	196.4	203.4
	\$8,255.9	\$8,554.6

A summary of the Company's equity securities follows:

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Equity Securities:				
March 31, 2014	\$966.4	\$224.1	\$.5	\$1,190.0
December 31, 2013	\$632.0	\$372.7	\$.5	\$1,004.2

The following table reflects the Company's gross unrealized losses and fair value, aggregated by category and length of time that individual securities have been in an unrealized loss position. Fair value and issuer's cost comparisons follow:

	12 Months or Less		Greater than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2014:						
Fixed Maturity Securities:						
U.S. & Canadian Governments	\$231.3	\$3.1	\$72.8	\$2.5	\$304.1	\$5.7
Tax-exempt	5.2	.1	3.3	.2	8.6	.4
Corporate	1,290.2	18.2	240.6	10.5	1,530.9	28.7
Subtotal	1,526.7	21.5	316.9	13.3	1,843.7	34.9
Equity Securities	41.5	.5	—	—	41.5	.5
Total	\$1,568.3	\$22.1	\$316.9	\$13.3	\$1,885.3	\$35.4