PROASSURANCE CORP
Form 10-Q
May 05, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

þ Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2009 or __________

o Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from __________ to __________

Commission file number 0-16533

ProAssurance Corporation
(Exact Name of Registrant as Specified in Its Charter)

Delaware	63-1261433
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)
100 Brookwood Place, Birmingham, AL	35209
(Address of Principal Executive Offices)	(Zip Code)

(205) 877-4400

(Registrant s Telephone Number, Including Area Code)

(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 o

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 o No x

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

As of April 24, 2009, there were 33,083,968 shares of the registrant s common stock outstanding.

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FORWARD-LOOKING STATEMENTS

Any statements in this Form 10Q that are not historical facts are specifically identified as forward-looking statements. These statements are based upon our estimates and anticipation of future events and are subject to certain risks and uncertainties that could cause actual results to vary materially from the expected results described in the forward-looking statements. Forward-looking statements are identified by words such as, but not limited to, anticipate , believe , estimate , expect , hope , hopeful , intend , may , optimistic , preliminary , potential , project analogous expressions. There are numerous factors that could cause our actual results to differ materially from those in the forward-looking statements. Thus, sentences and phrases that we use to convey our view of future events and trends are expressly designated as forward-looking statements as are sections of this Form 10Q that are identified as giving our outlook on future business.

Forward-looking statements relating to our business include among other things: statements concerning liquidity and capital requirements, investment valuation and performance, return on equity, financial ratios, net income, premiums, losses and loss reserves, premium rates and retention of current business, competition and market conditions, the expansion of product lines, the development or acquisition of business in new geographical areas, the availability of acceptable reinsurance, actions by regulators and rating agencies, court actions, legislative actions, payment or performance of obligations under indebtedness, payment of dividends, and other matters.

These forward-looking statements are subject to significant risks, assumptions and uncertainties, including, among other things, the following factors that could affect the actual outcome of future events:

- general economic conditions, either nationally or in our market areas, that are different than anticipated;
- regulatory, legislative and judicial actions or decisions could affect our business plans or operations;
- the enactment or repeal of tort reforms;
- formation of state-sponsored malpractice insurance entities that could remove some physicians from the private insurance market;
- the impact of deflation or inflation;
- changes in the interest rate environment;
- the effect that changes in laws or government regulations affecting the U.S. economy or financial institutions, including the Emergency Economic Stabilization Act of 2008 and the American Recovery and Reinvestment Act of 2009, may have on the U.S. economy and our business;
- performance of financial markets affecting the fair value of our investments or making it difficult to determine the value of our investments;
- changes in accounting policies and practices that may be adopted by our regulatory agencies and the Financial Accounting Standards Board, or the Securities and Exchange Commission;
- changes in laws or government regulations affecting medical professional liability insurance or the financial community;
- the effects of changes in the health care delivery system;
- uncertainties inherent in the estimate of loss and loss adjustment expense reserves and reinsurance, and changes in the availability, cost, quality, or collectability of insurance/reinsurance;

the results of litigation, including pre-or-post-trial motions, trials and/or appeals we undertake;

bad faith litigation which may arise from our handling of any particular claim, including failure to settle;

loss of independent agents;

changes in our organization, compensation and benefit plans;

our ability to retain and recruit senior management;

our ability to purchase reinsurance and collect payments from our reinsurers;

increases in guaranty fund assessments;

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our ability to achieve continued growth through expansion into other states or through acquisitions or business combinations;

changes to the ratings assigned by rating agencies to our insurance subsidiaries, individually or as a group;

changes in competition among insurance providers and related pricing weaknesses in our markets; and

the expected benefits from completed and proposed acquisitions may not be achieved or may be delayed longer than expected due to business disruption, loss of customers and employees, increased operating costs or inability to achieve cost savings, and assumption of greater than expected liabilities, among other reasons.

Our results may differ materially from those we expect and discuss in any forward-looking statements. The principal risk factors that may cause these differences are described in Item 1A, Risk Factors in our annual report on Form 10K and other documents we file with the Securities and Exchange Commission, such as our current reports on Form 8-K, and our regular reports on Forms 10-Q and 10-K.

We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made, and advise readers that the factors listed above could affect our financial performance and could cause actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements. Except as required by law or regulations, we do not undertake and specifically decline any obligation to publicly release the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

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ProAssurance Corporation and Subsidiaries
Condensed Consolidated Balance Sheets

(In thousands, except per share data)	March 31 2009	December 31 2008
Assets		
Investments		
Fixed maturities, available for sale, at fair value	**$ 3,039,373**	$ 2,961,568
Equity securities, available for sale, at fair value	**4,793**	6,981
Equity securities, trading, at fair value	**11,533**	11,852
Short-term investments	**365,011**	441,996
Business owned life insurance	**63,862**	63,440
Investment in unconsolidated subsidiaries	**45,229**	44,522
Other investments	**44,270**	45,583
Total Investments	**3,574,071**	3,575,942
Cash and cash equivalents	**23,132**	3,459
Premiums receivable	**99,537**	86,137
Receivable from reinsurers on paid losses and loss adjustment expenses	**20,872**	17,826
Receivable from reinsurers on unpaid losses and loss adjustment expenses	**268,727**	268,356
Prepaid reinsurance premiums	**14,703**	13,009
Deferred policy acquisition costs	**23,282**	19,505
Deferred taxes	**124,105**	138,034
Real estate, net	**23,307**	23,496
Goodwill	**90,250**	72,213
Other assets	**60,081**	62,961
Total Assets	**$ 4,322,067**	$ 4,280,938
Liabilities and Stockholders Equity		
Liabilities		
Policy liabilities and accruals		
Reserve for losses and loss adjustment expenses	**$ 2,372,788**	$ 2,379,468
Unearned premiums	**227,286**	185,756
Reinsurance premiums payable	**128,801**	127,877
Total Policy Liabilities	**2,728,875**	2,693,101
Other liabilities	**95,701**	129,322
Long-term debt	**35,427**	34,930
Total Liabilities	**2,860,003**	2,857,353
Stockholders Equity		
Common stock, par value $0.01 per share 100,000,000 shares authorized, 34,190,201 and 34,109,196 shares issued, respectively	**342**	341
Additional paid-in capital	**520,364**	518,687

Accumulated other comprehensive income (loss), net of deferred tax expense (benefit) of $(7,432) and $(19,328) respectively	**(13,805)**	(35,898)
Retained earnings	**999,257**	970,891
	1,506,158	1,454,021
Treasury stock, at cost, 1,106,233 shares and 763,316 shares, respectively	**(44,094)**	(30,436)
Total Stockholders Equity	**1,462,064**	1,423,585
Total Liabilities and Stockholders Equity	**$ 4,322,067**	$ 4,280,938

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ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Changes in Capital (Unaudited)

(In thousands)	Total	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Other Capital Accounts
Balance at December 31, 2008	**$ 1,423,585**	**$ (35,898)**	**$ 970,891**	**$ 488,592**
Net income	**28,366**		**28,366**	**--**
Change in net unrealized gains (losses) on investments, after tax, net of reclassification adjustments	**22,093**	**22,093**		**--**
Purchase of treasury stock	**(18,642)**			**(18,642)**
Treasury shares issued in acquisition (see Note 3)	**5,161**			**5,161**
Common shares issued as compensation and net effect of stock options exercised	**188**			**188**
Share-based compensation	**1,313**			**1,313**
Balance at March 31, 2009	**$ 1,462,064**	**$ (13,805)**	**$ 999,257**	**$ 476,612**

(In thousands)	Total	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Other Capital Accounts
Balance at December 31, 2007	$ 1,255,070	$ 9,902	$ 793,166	$ 452,002
Net income	35,868		35,868	
Change in net unrealized gains (losses) on investments, after tax, net of reclassification adjustments	2,659	2,659		
Purchase of treasury stock	(23,436)			(23,436)
Common shares issued as compensation and net effect of stock options exercised	3,254			3,254
Share-based compensation	2,440			2,440
Balance at March 31, 2008	$ 1,275,855	$ 12,561	$ 829,034	$ 434,260

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ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Income (Unaudited)

(In thousands, except per share data)	Three Months Ended March 31 2009	2008
Revenues		
Gross premiums written	**$ 154,544**	$ 160,266
Net premiums written	**$ 142,387**	$ 148,415
Premiums earned	**$ 115,553**	$ 132,018
Premiums ceded	**(11,662)**	(11,441)
Net premiums earned	**103,891**	120,577
Net investment income	**34,569**	41,059
Equity in earnings (loss) of unconsolidated subsidiaries	**(1,428)**	(1,946)
Net realized investment gains (losses)	**(7,537)**	(1,426)
Other income	**1,474**	1,362
Total revenues	**130,969**	159,626
Expenses		
Losses and loss adjustment expenses	**76,707**	90,579
Reinsurance recoveries	**(7,590)**	(8,897)
Net losses and loss adjustment expenses	**69,117**	81,682
Underwriting, acquisition and insurance expenses	**23,979**	26,243
Interest expense	**627**	2,422
Total expenses	**93,723**	110,347
Income before income taxes	**37,246**	49,279
Provision for income taxes		
Current expense (benefit)	**6,082**	5,365
Deferred expense (benefit)	**2,798**	8,046
	8,880	13,411
Net income	**$ 28,366**	$ 35,868
Earnings per share:		
Basic	**$ 0.85**	$ 1.11

Diluted	**$ 0.84**	$ 1.04
Weighted average number of common shares outstanding:		
Basic	**33,367**	32,182
Diluted	**33,609**	35,068

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ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income
(Unaudited)

(In thousands)	Three Months Ended March 31 **2009**	2008
Comprehensive income:		
Net income	**$ 28,366**	$ 35,868
Decrease in net unrealized losses on investments, after tax, net of reclassification adjustments	**22,093**	2,659
Comprehensive income	**$ 50,459**	$ 38,527

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ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

(In thousands)	Three Months Ended March 31 2009	2008
Operating Activities		
Net income	**$ 28,366**	$ 35,868
Depreciation and amortization	**4,052**	3,756
Net realized investment (gains) losses	**7,537**	1,426
Share-based compensation	**1,314**	2,440
Deferred income taxes	**2,798**	8,046
Changes in assets and liabilities, net of the effects of acquisitions:		
Premiums receivable	**(13,603)**	(7,293)
Reserve for losses and loss adjustment expenses	**(12,496)**	(4,304)
Unearned premiums	**38,959**	27,994
Reinsurance related assets and liabilities	**(2,284)**	5,257
Other liabilities	**(46,393)**	(20,130)
Other	**(218)**	8,265
Net cash provided by operating activities	**8,032**	61,325
Investing Activities		
Purchases of:		
Fixed maturities available for sale	**(182,191)**	(276,176)
Equity securities available for sale	**(38)**	(2,346)
Equity securities trading	**(1,478)**	(2,288)
Other investments	**(106)**	(277)
Cash invested in unconsolidated subsidiaries	**(2,135)**	(20,960)
Proceeds from sale or maturities of:		
Fixed maturities available for sale	**137,831**	282,155
Equity securities available for sale	**333**	196
Equity securities trading	**144**	463
Other investments	**697**	1,886
Net (increase) decrease in short-term investments	**81,872**	(54,119)
Cash paid for acquisitions, net of cash received	**(3,900)**	
Other	**1,931**	4,144
Net cash provided (used) by investing activities	**32,960**	(67,322)
Financing Activities		
Repurchase of treasury stock	**(18,642)**	(23,436)
Book overdraft	**(2,677)**	13,501
Other		24
Net cash provided (used) by financing activities	**(21,319)**	(9,911)

Increase (decrease) in cash and cash equivalents	**19,673**	(15,908)
Cash and cash equivalents at beginning of period	**3,459**	30,274
Cash and cash equivalents at end of period	**$ 23,132**	$ 14,366
Significant Non-cash Transactions:		
Treasury stock issued in acquisition	**$ 5,161**	$

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ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2009

1. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of ProAssurance Corporation and its consolidated subsidiaries (ProAssurance). The financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation, consisting of normal recurring adjustments, have been included. Operating results for the three months ended March 31, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009. The accompanying Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes contained in ProAssurance s December 31, 2008 report on Form 10-K.

Certain reclassifications have been made in the prior period consolidated financial statements to conform to the current period presentation.

Accounting Changes

FASB Staff Position (FSP) EITF 99-20-1, *Amendments to the Impairment Guidance of EITF Issue No.99-20,* was issued in January 2009 to amend the impairment guidance in EITF Issue No. 99-20, *Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets*. EITF 99-20 specifies that an impairment is considered other-than-temporary if, based on an estimate of cash flows that a market participant would use in determining the current fair value, there has been an adverse change in those estimated cash flows. FSP EITF 99-20-1 alters this guidance by specifying that an impairment be considered other-than-temporary if it is probable there has been an adverse change in the holder s estimated cash flows from those previously projected. ProAssurance adopted FSP EITF 99-20-1 as of December 31, 2008 and considered the guidance provided therein in its impairment evaluations performed as of December 31, 2008 and March 31, 2009. There was no material effect from adoption.

In May 2008 the FASB issued FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement),* which alters the accounting for Convertible Debentures. FSP APB 14-1 requires issuers to account for convertible debt securities that allow for either mandatory or optional cash settlement (including partial cash settlement) by separating the liability and equity components in a manner that reflects the issuer s nonconvertible debt borrowing rate at the time of issuance and requires recognition of additional (non-cash) interest expense in subsequent periods based on the nonconvertible rate. Additionally, FSP APB 14-1 requires that when such debt instruments are repaid or converted any consideration transferred at settlement is to be allocated between the extinguishment of the liability component and the reacquisition of the equity component. FSP APB 14-1 is applicable to the Convertible Debentures which ProAssurance converted in July 2008. ProAssurance adopted FSP APB 14-1 on its effective date January 1, 2009. The adoption of FSP APB 14-1 has no effect on 2009 operating results because no convertible debt has been outstanding during 2009. The cumulative effect of adoption, which would be an increase to additional paid-in capital of $65,000 and an offsetting decrease to retained earnings of the same amount, has not been recorded because the effect is immaterial and would not change total stockholders equity.

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ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2009

1. Basis of Presentation (continued)

In December 2007 the FASB issued SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements*. SFAS 160 amends Accounting Research Bulletin 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. The Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. ProAssurance adopted SFAS 160 on its effective date, January 1, 2009. Adoption did not have a significant effect on ProAssurance s results of operations or financial position.

In December 2007 the FASB issued SFAS 141 (Revised December 2007) *Business Combinations.* SFAS 141(R) replaces FASB Statement No. 141, *Business Combinations,* but retains the fundamental requirement in SFAS 141 that the acquisition method (referred to as the *purchase* method in SFAS 141) of accounting be used for all business combinations. SFAS 141(R) provides new or additional guidance with respect to business combinations including: defining the acquirer in a transaction, the valuation of assets and liabilities when noncontrolling interests exist, the treatment of contingent consideration, the treatment of costs incurred to effect the acquisition, the treatment of reorganization costs, and the valuation of assets and liabilities when the purchase price is below the net fair value of assets acquired. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. ProAssurance adopted SFAS 141(R) as of its effective date, January 1, 2009. ProAssurance accounted for its acquisitions of Mid-Continent General Agency, Inc. (Mid-Continent) and Georgia Lawyers Insurance Company (Georgia Lawyers) during the first quarter of 2009 in accordance with SFAS 141(R).

Recent Accounting Developments

On April 9, 2009 the FASB issued three related FSPs:

(1) FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*

This FSP clarifies factors to be considered in determining whether there has been a significant decrease in market activity for an asset in relation to normal activity. The FSP provides additional guidance on when the use of multiple (or different) valuation techniques may be warranted and considerations for determining the weight that should be applied to the various techniques. The FSP also establishes a requirement that conclusions about whether transactions are orderly be based on the weight of the evidence. Entities are required to disclose any changes to valuation techniques (and related inputs) that result from a conclusion that markets are not orderly and to disclose the effect of the change, if practicable.

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ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2009

1. Basis of Presentation (continued)

(2) FSP FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*

This FSP replaces existing guidance that requires an impairment of a debt security be considered as other-than-temporary unless management is able to assert both the intent and the ability to hold the impaired security until recovery of value. The revised guidance establishes new criteria that must be met to avoid classification of an impairment as other-than-temporary: an entity must assert it has no intent to sell the security and that it is more likely than not that the entity will not be required to sell the security before recovery of its anticipated amortized cost basis.

The FSP also establishes the concept of credit loss. Credit loss is defined in the FSP as the difference between the present value of the cash flows expected to be collected from a debt security and the amortized cost basis of the security. The FSP states that in instances in which a determination is made that a credit loss exists but the entity does not intend to sell the debt security and it is not more likely than not that the entity will be required to sell the debt security before the anticipated recovery of its remaining amortized cost basis an impairment is to be separated into (a) the amount of total impairment related to the credit loss and (b) the amount of total impairment related to all other factors. The credit loss component of the impairment is to be recognized in income of the current period. The non-credit component is to be recognized as a part of other comprehensive income. Transition provisions of the FSP require a cumulative effect adjustment to reclassify the noncredit component of a previously recognized other-than temporary impairment from retained earnings to accumulated other comprehensive income if an entity does not intend to sell and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis.

(3) FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*

This FSP amends FAS 107 to require publicly traded companies to provide disclosures about fair values of financial instruments for interim reporting periods as well as in annual financial statements. The FSP also amends APB 28 to require that fair value disclosures be included in any summarized financial information issued at interim reporting periods.

Each of these FSPs is effective for interim and annual periods ending after June 15, 2009 with early adoption for periods ending after March 15, 2009 permitted in specified groupings. ProAssurance has elected to adopt the FSPs on the effective date but has not yet completed its evaluation of the effects of adoption.

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ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2009

2. Fair Value Measurement

Fair value is defined by SFAS 157 as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS 157 establishes a three level hierarchy for valuing assets and liabilities based on how transparent (observable) the inputs are that are used to determine fair value, with the inputs considered most observable categorized as Level 1 and those that are the least observable categorized as Level 3. Hierarchy levels are defined by SFAS 157 as follows:

Level 1: quoted (unadjusted) market prices in active markets for identical assets and liabilities. For ProAssurance, Level 1 inputs are generally quotes for debt or equity securities actively traded in exchange or over-the-counter markets.

Level 2: market data obtained from sources independent of the reporting entity (observable inputs). For ProAssurance, Level 2 inputs generally include quoted prices in markets that are not active, quoted prices for similar assets/liabilities, and other observable inputs such as interest rates and yield curves that are generally available at commonly quoted intervals.

Level 3: the reporting entity s own assumptions about market participant assumptions based on the best information available in the circumstances (unobservable inputs). For ProAssurance, Level 3 inputs are used in situations where little or no Level 1 or 2 inputs are available or are inappropriate given the particular circumstances. Level 3 inputs include results from pricing models and discounted cash flow methodologies as well as adjustments to externally quoted prices that are based on management judgment or estimation.

The following tables present information about ProAssurance s assets measured at fair value on a recurring basis as of March 31, 2009, and indicate the fair value hierarchy of the valuation techniques utilized to determine such value. No liabilities are measured at fair value at March 31, 2009. For some assets, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. When this is the case, the asset is categorized in the table based on the lowest level input that is significant to the fair value measurement in its entirety. ProAssurance s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the assets being valued.

Assets measured at fair value on a recurring basis as of March 31, 2009 are as follows:

	March 31, 2009 Fair Value Measurements Using			Total Fair Value
(In thousands)	Level 1	Level 2	Level 3	
Assets:				
Fixed maturities, available for sale				
Government/Government agencies	$	$ 208,654		