Global Indemnity plc
Form 10-Q
November 06, 2013
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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 September 30, 2013

OR

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

For the Transition Period from __________ to __________

001-34809

Commission File Number

GLOBAL INDEMNITY PLC

(Exact name of registrant as specified in its charter)

Ireland	**98-0664891**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

25/28 NORTH WALL QUAY

DUBLIN 1

IRELAND

(Address of principal executive office, including zip code)

353 (0) 1 649 2000

(Registrant s telephone number, including area code)

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 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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.:

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	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

As of October 31, 2013, the registrant had outstanding 13,132,133 A Ordinary Shares and 12,061,370 B Ordinary Shares.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

GLOBAL INDEMNITY PLC

Consolidated Balance Sheets

(In thousands, except share amounts)

	(Unaudited) September 30, 2013	December 31, 2012
ASSETS		
Fixed maturities:		
Available for sale, at fair value (amortized cost: $1,175,002 and $1,187,094)	$ 1,196,275	$ 1,229,322
Equity securities:		
Available for sale, at fair value (cost: $175,125 and $167,179)	233,415	197,075
Other invested assets:		
Available for sale, at fair value (cost: $3,065 and $3,049)	3,269	3,132
Total investments	1,432,959	1,429,529
Cash and cash equivalents	115,953	104,460
Premiums receivable, net	40,132	37,752
Reinsurance receivables, net	221,751	241,827
Funds held by ceding insurers	30,825	7,410
Federal income taxes receivable	3,830	6,844
Deferred federal income taxes	6,338	10,824
Deferred acquisition costs	24,178	18,265
Intangible assets	18,078	18,343
Goodwill	4,820	4,820
Prepaid reinsurance premiums	5,227	5,945
Other assets	14,339	17,684
Total assets	$ 1,918,430	$ 1,903,703
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Unpaid losses and loss adjustment expenses	$ 823,063	$ 879,114
Unearned premiums	128,113	94,114
Ceded balances payable	5,093	4,201
Contingent commissions	9,652	9,911
Payable for securities purchased	4,882	2,634
Margin borrowing facility	65,009	
Notes and debentures payable	20,619	84,929

Other liabilities		23,096		22,182
Total liabilities		1,079,527		1,097,085
Commitments and contingencies (Note 11)				
Shareholders equity:				
Ordinary shares, $0.0001 par value, 900,000,000 ordinary shares authorized; A ordinary shares issued: 16,190,894 and 16,087,939, respectively; A ordinary shares outstanding: 13,132,133 and 13,030,938, respectively; B ordinary shares issued and outstanding: 12,061,370 and 12,061,370, respectively		3		3
Additional paid-in capital		515,545		512,304
Accumulated other comprehensive income, net of taxes		54,456		53,350
Retained earnings		370,148		342,171
A ordinary shares in treasury, at cost: 3,058,761 and 3,057,001 shares, respectively		(101,249)		(101,210)
Total shareholders equity		838,903		806,618
Total liabilities and shareholders equity	$	1,918,430	$	1,903,703

See accompanying notes to consolidated financial statements.

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GLOBAL INDEMNITY PLC

Consolidated Statements of Operations

(In thousands, except shares and per share data)

	(Unaudited) Quarters Ended September 30, 2013	(Unaudited) Quarters Ended September 30, 2012	(Unaudited) Nine Months Ended September 30, 2013	(Unaudited) Nine Months Ended September 30, 2012
Revenues:				
Gross premiums written	$ 68,785	$ 56,949	$ 227,969	$ 182,339
Net premiums written	$ 64,030	$ 51,455	$ 213,854	$ 162,871
Net premiums earned	$ 64,469	$ 55,329	$ 179,136	$ 177,658
Net investment income	8,486	14,777	28,285	37,265
Net realized investment gains:				
Other than temporary impairment losses on investments	(177)	(189)	(1,230)	(3,808)
Other than temporary impairment losses on investments recognized in other comprehensive income				541
Other net realized investment gains	1,818	3,400	11,434	10,180
Total net realized investment gains	1,641	3,211	10,204	6,913
Other income (loss)	183	101	484	(291)
Total revenues	74,779	73,418	218,109	221,545
Losses and Expenses:				
Net losses and loss adjustment expenses	35,483	35,407	102,195	113,574
Acquisition costs and other underwriting expenses	28,028	23,223	76,977	70,150
Corporate and other operating expenses	2,627	2,039	7,444	6,863
Interest expense	3,585	1,265	5,939	4,213
Income before income taxes	5,056	11,484	25,554	26,745
Income tax expense (benefit)	(1,892)	1,571	(2,423)	(3,634)
Net income	$ 6,948	$ 9,913	$ 27,977	$ 30,379
Per share data:				
Net income				
Basic	$ 0.28	$ 0.39	$ 1.12	$ 1.11

Diluted	$	0.28	$	0.39	$	1.11	$	1.11
Weighted-average number of shares outstanding								
Basic		25,082,237		25,391,885		25,065,725		27,263,275
Diluted		25,189,072		25,412,586		25,150,920		27,280,612

See accompanying notes to consolidated financial statements.

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GLOBAL INDEMNITY PLC

Consolidated Statements of Comprehensive Income

(In thousands)

	(Unaudited) Quarters Ended September 30,		(Unaudited) Nine Months Ended September 30,	
	2013	**2012**	**2013**	**2012**
Net income	$ 6,948	$ 9,913	$ 27,977	$ 30,379
Other comprehensive income, net of taxes:				
Unrealized holding gains	7,732	9,419	7,578	22,494
Portion of other-than-temporary impairment losses recognized in other comprehensive income	12	1	8	(538)
Recognition of previously unrealized holding gains	(1,004)	(2,292)	(6,656)	(5,523)
Unrealized foreign currency translation gains	142	98	176	60
Other comprehensive income, net of taxes	6,882	7,226	1,106	16,493
Comprehensive income, net of taxes	$ 13,830	$ 17,139	$ 29,083	$ 46,872

See accompanying notes to consolidated financial statements.

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GLOBAL INDEMNITY PLC

Consolidated Statements of Changes in Shareholders Equity

(In thousands, except share amounts)

	(Unaudited) Nine Months Ended September 30, 2013		Year Ended December 31, 2012	
Number of A ordinary shares issued:				
Number at beginning of period		16,087,939		21,429,683
Ordinary shares issued under share incentive plans		74,400		29,675
Ordinary shares issued to directors		28,555		
Ordinary shares retired				(5,371,419)
Number at end of period		16,190,894		16,087,939
Number of B ordinary shares issued:				
Number at beginning and end of period		12,061,370		12,061,370
Par value of A ordinary shares:				
Balance at beginning and end of period	$	2	$	2
Par value of B ordinary shares:				
Balance at beginning and end of period	$	1	$	1
Additional paid-in capital:				
Balance at beginning of period	$	512,304	$	621,917
Share compensation plans		3,241		2,582
A ordinary shares retired				(112,195)
Balance at end of period	$	515,545	$	512,304
Accumulated other comprehensive income, net of deferred income tax:				
Balance at beginning of period	$	53,350	$	40,174
Other comprehensive income:				
Change in unrealized holding gains		922		13,218
Change in other than temporary impairment losses recognized in other comprehensive income		8		(14)
Unrealized foreign currency translation gains (losses)		176		(28)
Other comprehensive income		1,106		13,176

Balance at end of period	$	54,456	$	53,350
Retained earnings:				
Balance at beginning of period	$	342,171	$	307,414
Net income		27,977		34,757
Balance at end of period	$	370,148	$	342,171
Number of Treasury Shares:				
Number at beginning of period		3,057,001		4,619,005
A ordinary shares purchased		1,760		3,809,415
A ordinary shares retired				(5,371,419)
Number at end of period		3,058,761		3,057,001
Treasury Shares, at cost:				
Balance at beginning of period	$	(101,210)	$	(130,444)
A ordinary shares purchased, at cost		(39)		(82,961)
A ordinary shares retired				112,195
Balance at end of period	$	(101,249)	$	(101,210)
Total shareholders equity	$	838,903	$	806,618

See accompanying notes to consolidated financial statements.

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GLOBAL INDEMNITY PLC

Consolidated Statements of Cash Flows

(In thousands)

	(Unaudited) Nine Months Ended September 30, 2013	2012
Cash flows from operating activities:		
Net income	$ 27,977	$ 30,379
Adjustments to reconcile net income to net cash used for operating activities:		
Amortization of trust preferred securities issuance costs	77	47
Amortization and depreciation	578	1,341
Restricted stock and stock option expense	3,241	1,878
Deferred federal income taxes	(1,697)	2,520
Amortization of bond premium and discount, net	4,800	5,250
Net realized investment gains	(10,204)	(6,913)
Changes in:		
Premiums receivable, net	(2,380)	5,364
Reinsurance receivables, net	20,076	13,993
Funds held by ceding insurers	(23,415)	41
Unpaid losses and loss adjustment expenses	(56,051)	(47,599)
Unearned premiums	33,999	(14,954)
Ceded balances payable	892	(5,837)
Other assets and liabilities, net	3,598	(7,697)
Contingent commissions	(259)	370
Federal income tax receivable/payable	3,014	(6,377)
Deferred acquisition costs, net	(5,913)	2,126
Prepaid reinsurance premiums	718	165
Net cash used for operating activities	(949)	(25,903)
Cash flows from investing activities:		
Proceeds from sale of fixed maturities	240,658	380,713
Proceeds from sale of equity securities	55,174	40,299
Proceeds from maturity of fixed maturities	126,564	46,620
Proceeds from sale of other invested assets		1,114
Purchases of fixed maturities	(357,494)	(366,706)
Purchases of equity securities	(53,104)	(45,041)
Purchases of other invested assets	(16)	(13)
Net cash provided by investing activities	11,782	56,986

Cash flows from financing activities:

Borrowings under margin borrowing facility		65,009		
Purchase of A ordinary shares		(39)		(80,382)
Retirement of junior subordinated debentures		(10,310)		
Principal payments of term debt		(54,000)		(18,071)
Net cash provided by (used for) financing activities		660		(98,453)
Net change in cash and cash equivalents		11,493		(67,370)
Cash and cash equivalents at beginning of period		104,460		175,860
Cash and cash equivalents at end of period	$	115,953	$	108,490

See accompanying notes to consolidated financial statements.

GLOBAL INDEMNITY PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Principles of Consolidation and Basis of Presentation

Global Indemnity plc (Global Indemnity or the Company) was incorporated on March 9, 2010 and is domiciled in Ireland. Global Indemnity replaced the Company s predecessor, United America Indemnity, Ltd., as the ultimate parent company as a result of a re-domestication transaction. United America Indemnity, Ltd. was incorporated on August 26, 2003, and is domiciled in the Cayman Islands. United America Indemnity, Ltd. is now a subsidiary of the Company. The Company s A ordinary shares are publicly traded on the NASDAQ Global Select Market under the trading symbol GBLI.

The Company manages its business through two business segments: Insurance Operations, which includes the operations of United National Insurance Company, Diamond State Insurance Company, United National Casualty Insurance Company, United National Specialty Insurance Company, Penn-America Insurance Company, Penn-Star Insurance Company, Penn-Patriot Insurance Company, American Insurance Adjustment Agency, Inc., Collectibles Insurance Services, LLC, Global Indemnity Insurance Agency, LLC, and J.H. Ferguson & Associates, LLC, and Reinsurance Operations, which includes the operations of Wind River Reinsurance Company, Ltd. (Wind River Reinsurance)

The interim consolidated financial statements are unaudited, but have been prepared in conformity with United States of America generally accepted accounting principles (GAAP), which differs in certain respects from those principles followed in reports to insurance regulatory authorities. The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The unaudited consolidated financial statements include all adjustments that are, in the opinion of management, of a normal recurring nature and are necessary for a fair statement of results for the interim periods. Results of operations for the quarters and nine months ended September 30, 2013 and 2012 are not necessarily indicative of the results of a full year. The accompanying notes to the unaudited consolidated financial statements should be read in conjunction with the notes to the consolidated financial statements contained in the Company s 2012 Annual Report on Form 10-K.

The consolidated financial statements include the accounts of Global Indemnity and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

The Company s wholly owned business trust subsidiaries, United National Group Capital Trust I (UNG Trust I) and United National Group Capital Statutory Trust II (UNG Trust II), are not consolidated pursuant to the Financial Accounting Standards Board (FASB) Accounting Standards Codification. The Company s business trust subsidiary, UNG Trust I, issued $10.0 million in floating rate capital securities (Trust Preferred Securities) and $0.3 million of floating rate common securities. On September 30, 2013, The Company repaid the entire outstanding principal due on its UNG Trust I junior subordinated notes. UNG Trust I was cancelled on October 4, 2013. The Company s business trust subsidiary, UNG Trust II, issued $20.0 million in Trust Preferred Securities and $0.6 million of floating rate common securities. The sole assets of UNG Trust II are $20.6 million of junior subordinated debentures issued by the Company, which have the same terms with respect to maturity, payments, and distributions as the Trust Preferred Securities and the floating rate common securities.

2. Premium Deficiency

The Company recognizes a premium deficiency if the sum of expected loss and loss adjustment expenses and unamortized acquisition costs exceeds related unearned premium after consideration of investment income. This evaluation is done at a product line level in Insurance Operations and at a treaty level in Reinsurance Operations. Any future expected loss on the related unearned premium is recorded first by impairing the unamortized acquisition costs on the related unearned premium followed by an increase to loss and loss adjustment expense reserves on additional expected loss in excess of unamortized acquisition costs.

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GLOBAL INDEMNITY PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - *(Continued)*

(Unaudited)

During the quarter and nine months ended September 30, 2013, the Company incurred a pre-tax premium deficiency charge of $1.7 million related to its commercial automobile lines. As a result of these charges, the Company reduced deferred acquisition costs during the quarter and nine months ended September 30, 2013 by $1.7 million. The Company did not incur a premium deficiency charge during the quarter and nine months ended September 30, 2012.

This charge of $1.7 million was recorded to acquisition cost and other underwriting expenses within the Company s U.S. Insurance Operations during the quarter and nine months ended September 30, 2013. The Company s Reinsurance Operations did not incur a premium deficiency charge during the quarter and nine months ended September 30, 2013.

3. Profit Enhancement Initiative

In 2010 and 2011, the Company committed to a Profit Enhancement Initiative in response to the continuing impact of the domestic recession and the competitive landscape within the excess and surplus lines market. The total cost of this initiative was recorded in the Company s statements of operations during those years. All action items related to this initiative were completed by December 31, 2011.

For further disclosure regarding the Profit Enhancement Initiative, please see Note 5 of the notes to the consolidated financial statements in Item 8 of Part II of the Company s 2012 Annual Report on Form 10-K.

The following table summarizes charges incurred by expense type and the remaining liability as of September 30, 2013 and December 31, 2012:

(Dollars in thousands)	**Employee Termination**	**Operating Leases**	**Total**
Liability at January 1, 2012	$ 785	$ 1,828	$ 2,613
Cash payments	(773)	(690)	(1,463)
Non-cash adjustments		(267)	(267)
Liability at December 31, 2012	$ 12	$ 871	$ 883
Cash payments	(12)	(402)	(414)
Non-cash adjustments		(108)	(108)
Liability at September 30, 2013	$	$ 361	$ 361

There was a reduction in expense of $0.0 million and $0.1 million, respectively, related to the Profit Enhancement Initiative resulting from a revision of expected sub-lease income included in the statement of operations within the Acquisition costs and other underwriting expenses line item for the quarter and nine months ended September 30, 2013.

There was a reduction in expense of $0.18 million related to the Profit Enhancement Initiative resulting from a revision of expected sub-lease income included in the statement of operations within the Acquisition costs and other underwriting expenses line item for the quarter and nine months ended September 30, 2012.

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GLOBAL INDEMNITY PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - *(Continued)*

(Unaudited)

4. Investments

The amortized cost and estimated fair value of investments were as follows as of September 30, 2013 and December 31, 2012:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Other than temporary impairments recognized in AOCI (1)
As of September 30, 2013					
Fixed maturities:					
U.S. treasury and agency obligations	$ 88,429	$ 4,436	$ (120)	$ 92,745	$
Obligations of states and political subdivisions	186,952	4,820	(1,746)	190,026	
Mortgage-backed securities	242,874	4,879	(2,213)	245,540	(5)
Asset-backed securities	133,137	1,290	(319)	134,108	(20)
Commercial mortgage-backed securities	53,957	2	(795)	53,164	
Corporate bonds and loans	414,265	10,251	(675)	423,841	
Foreign corporate bonds	55,388	1,463		56,851	
Total fixed maturities	1,175,002	27,141	(5,868)	1,196,275	(25)
Common stock	175,125	58,824	(534)	233,415	
Other invested assets	3,065	204		3,269	
Total	$ 1,353,192	$ 86,169	$ (6,402)	$ 1,432,959	$ (25)

(1) Represents the total amount of other than temporary impairment losses relating to factors other than credit losses recognized in accumulated other comprehensive income (AOCI).

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Other than temporary impairments recognized

					in AOCI (2)
As of December 31, 2012					
Fixed maturities:					
U.S. treasury and agency obligations	$ 102,186	$ 6,559	$ (1)	$ 108,744	$
Obligations of states and political subdivisions	194,326	6,883	(132)	201,077	
Mortgage-backed securities	247,639	8,492	(189)	255,942	(8)
Asset-backed securities	111,289	2,071	(9)	113,351	(24)
Commercial mortgage-backed securities	8,070	60	(13)	8,117	
Corporate bonds and loans	469,860	16,739	(428)	486,171	
Foreign corporate bonds	53,724	2,196		55,920	
Total fixed maturities	1,187,094	43,000	(772)	1,229,322	(32)
Common stock	167,179	32,847	(2,951)	197,075	
Other invested assets	3,049	83		3,132	
Total	$ 1,357,322	$ 75,930	$ (3,723)	$ 1,429,529	$ (32)

(2) Represents the total amount of other than temporary impairment losses relating to factors other than credit losses recognized in accumulated other comprehensive income (AOCI).

Excluding U.S. treasuries and agency bonds, the Company did not hold any debt or equity investments in a single issuer that was in excess of 4% and 3% of shareholders equity at September 30, 2013 and December 31, 2012, respectively.

The amortized cost and estimated fair value of the Company s fixed maturities portfolio classified as available for sale at September 30, 2013, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Dollars in thousands)	Amortized Cost	Fair Value
Due in one year or less	$ 145,935	$ 149,886
Due after one year through five years	486,326	497,325
Due after five years through ten years	88,913	92,001
Due after ten years through fifteen years	8,654	8,808
Due after fifteen years	15,206	15,443
Mortgage-backed securities	242,874	245,540
Asset-backed securities	133,137	134,108
Commercial mortgage-backed securities	53,957	53,164
Total	$ 1,175,002	$ 1,196,275

GLOBAL INDEMNITY PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - *(Continued)*

(Unaudited)

The following table contains an analysis of the Company s securities with gross unrealized losses, categorized by the period that the securities were in a continuous loss position as of September 30, 2013:

	Less than 12 months		12 months or longer (1)		Total	
(Dollars in thousands)	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fixed maturities:						
U.S. treasury and agency obligations	$ 6,288	$ (120)	$	$	$ 6,288	$ (120)
Obligations of states and political subdivisions	60,779	(1,684)	6,034	(62)	66,813	(1,746)
Mortgage-backed securities	112,117	(2,212)	3	(1)	112,120	(2,213)
Asset-backed securities	47,439	(318)	3	(1)	47,442	(319)
Commercial mortgage-backed securities	52,587	(795)			52,587	(795)
Corporate bonds and loans	55,317	(615)	1,362	(60)	56,679	(675)
Total fixed maturities	334,527	(5,744)	7,402	(124)	341,929	(5,868)
Common stock	7,517	(331)	1,520	(203)	9,037	(534)
Total	$ 342,044	$ (6,075)	$ 8,922	$ (327)	$ 350,966	$ (6,402)

(1) Fixed maturities in a gross unrealized loss position for twelve months or longer are primarily comprised of non-credit losses on investment grade securities where management does not intend to sell, and it is more likely than not that the Company will not be forced to sell the security before recovery. The Company has analyzed these securities and has determined that they are not other than temporarily impaired.

The following table contains an analysis of the Company s securities with gross unrealized losses, categorized by the period that the securities were in a continuous loss position as of December 31, 2012:

	Less than 12 months		12 months or longer (2)		Total	
(Dollars in thousands)	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fixed maturities:						
U.S. treasury and agency obligations	$ 2,002	$ (1)	$	$	$ 2,002	$ (1)

Obligations of states and political subdivisions	33,204	(132)			33,204	(132)
Mortgage-backed securities	33,635	(172)	640	(17)	34,275	(189)
Asset-backed securities	5,722	(3)	4,763	(6)	10,485	(9)
Commercial mortgage-backed securities	2,839	(13)			2,839	(13)
Corporate bonds and loans	8,202	(274)	3,308	(154)	11,510	(428)
Total fixed maturities	85,604	(595)	8,711	(177)	94,315	(772)
Common stock	30,153	(2,284)	3,950	(667)	34,103	(2,951)
Total	$ 115,757	$ (2,879)	$ 12,661	$ (844)	$ 128,418	$ (3,723)

(2) Fixed maturities in a gross unrealized loss position for twelve months or longer are primarily comprised of non-credit losses on investment grade securities where management does not intend to sell, and it is more likely than not that the Company will not be forced to sell the security before recovery. The Company has analyzed these securities and has determined that they are not other than temporarily impaired.

The Company regularly performs various analytical valuation procedures with respect to its investments, including reviewing each fixed maturity security in an unrealized loss position to assess whether the security is a candidate for credit loss. Specifically, the Company considers credit rating, market price, and issuer specific financial information, among other factors, to assess the likelihood of collection of all principal and interest as contractually due. Securities for which the Company determines that a credit loss is likely are subjected to further analysis through discounted cash flow testing to estimate the credit loss to be recognized in earnings, if any. The specific methodologies and significant assumptions used by asset class are discussed below. Upon identification of such securities and periodically thereafter, a detailed review is performed to determine whether the decline is considered other than temporary. This review includes an analysis of several factors, including but not limited to, the credit ratings and cash flows of the securities and the magnitude and length of time that the fair value of such securities is below cost.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - *(Continued)*

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For fixed maturities, the factors considered in reaching the conclusion that a decline below cost is other than temporary include, among others, whether:

(1) the issuer is in financial distress;

(2) the investment is secured;

(3) a significant credit rating action occurred;

(4) scheduled interest payments were delayed or missed;

(5) changes in laws or regulations have affected an issuer or industry;

(6) the investment has an unrealized loss and was identified by the Company s investment manager as an investment to be sold before recovery or maturity; and

(7) the investment failed cash flow projection testing to determine if anticipated principal and interest payments will be realized.

According to accounting guidance, for debt securities in an unrealized loss position, the Company is required to assess whether it has the intent to sell the debt security or more likely than not will be required to sell the debt security before the anticipated recovery. If either of these conditions is met the Company must recognize an other than temporary impairment with the entire unrealized loss being recorded through earnings. For debt securities in an unrealized loss position not meeting these conditions, the Company assesses whether the impairment of a security is other than temporary. If the impairment is deemed to be other than temporary, the Company must separate the other than temporary impairment into two components: the amount representing the credit loss and the amount related to all other factors, such as changes in interest rates. The credit loss represents the portion of the amortized book value in excess of the net present value of the projected future cash flows discounted at the effective interest rate implicit in the debt security prior to impairment. The credit loss component of the other than temporary impairment is recorded through earnings, whereas the amount relating to factors other than credit losses are recorded in other comprehensive income, net of taxes.

For equity securities, management carefully reviews all securities with unrealized losses to determine if a security should be impaired with a focus on securities that have either:

(1) persisted with unrealized losses for more than twelve consecutive months or

(2) the value of the investment has been 20% or more below cost for six continuous months or more.

The amount of any write-down, including those that are deemed to be other than temporary, is included in earnings as a realized loss in the period in which the impairment arose.

The following is a description, by asset type, of the methodology and significant inputs that the Company used to measure the amount of credit loss recognized in earnings, if any:

U.S. treasury and agency obligations As of September 30, 2013, gross unrealized losses related to U.S. treasury and agency obligations were $0.120 million. All unrealized losses have been in an unrealized loss position for less than twelve months. All of these securities are rated AA+. The Company s investment manager conducts extensive macroeconomic and market analysis which are driven by moderate interest rate anticipation, yield curve management, and security selection.

Obligations of states and political subdivisions As of September 30, 2013, gross unrealized losses related to obligations of states and political subdivisions were $1.746 million. Of this amount, $0.062 million have been in an unrealized loss position for twelve months or greater. All of these securities are rated A or higher. The Company s investment manager considers all factors that influence performance of the municipal bond market, including investor expectations, supply and demand patterns, and current versus historical yield and spread relationships. The manager relies on the output of its fixed income credit analysts, including dedicated municipal bond analysts. The dedicated municipal analysts perform extensive in-house fundamental analysis on each issuer, regardless of their rating by the major agencies.

Mortgage-backed securities (MBS) As of September 30, 2013, gross unrealized losses related to mortgage-backed securities were $2.213 million. Of this amount, $0.001 million have been in an unrealized loss position for twelve months or greater. All of these securities are rated AA+. The Company s investment manager models each

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mortgage-backed security to project principal losses under downside, base, and upside scenarios for the economy and home prices. The primary assumption that drives the security and loan level modeling is the Home Price Index (HPI) projection. The Company s investment manager first projects HPI at the national level, then at the zip code level based on the historical relationship between the individual zip code HPI and the national HPI, using inputs from its macroeconomic team, mortgage portfolio management team, and structured analyst team. The model utilizes loan level data and borrower characteristics including FICO score, geographic location, original and current loan size, loan age, mortgage rate and type (fixed rate / interest-only / adjustable rate mortgage), issuer / originator, residential type (owner occupied / investor property), dwelling type (single family / multi-family), loan purpose, level of documentation, and delinquency status as inputs. The model also includes the explicit treatment of silent second liens, utilization of loan modification history, and the application of roll rate adjustments.

Asset-backed securities (ABS) - As of September 30, 2013, gross unrealized losses related to asset-backed securities were $0.319 million. Of this amount, $0.001 million have been in an unrealized loss position for twelve months or greater. All of these securities are rated A. The weighted average credit enhancement for the Company s asset-backed portfolio is 26.0. This represents the percentage of pool losses that can occur before an asset-backed security will incur its first dollar of principle losses. The Company s investment manager analyzes every ABS transaction on a stand-alone basis. This analysis involves a thorough review of the collateral, prepayment, and structural risk in each transaction. Additionally, their analysis includes an in-depth credit analysis of the originator and servicer of the collateral. The Company s investment manager projects an expected loss for a deal given a set of assumptions specific to the asset type. These assumptions are used to calculate at what level of losses that the deal will incur a dollar of loss. The major assumptions used to calculate this ratio are loss severities, recovery lags, and no advances on principal and interest.

Commercial mortgage-backed securities (CMBS) - As of September 30, 2013, gross unrealized losses related to CMBS were $0.795 million. All unrealized losses have been in an unrealized loss position for less than twelve months. The weighted average credit enhancement for the Company s CMBS portfolio is 32.2. This represents the percentage of pool losses that can occur before a mortgage-backed security will incur its first dollar of principle losses. For the Company s CMBS portfolio, a loan level analysis is utilized where every underlying CMBS loan is re-underwritten based on the Company s investment manager s internally generated set of assumptions that reflect their expectation for the future path of the economy. In the analysis, the focus is centered on stressing the significant variables that influence commercial loan defaults and collateral losses in CMBS deals. These variables include: (1) occupancies are projected to drop; (2) capitalization rates vary by property type and are forecasted to return to more normalized levels as the capital markets repair and capital begins to flow again; and (3) property value was stressed by using projected property performance and projected capitalization rates. Term risk is triggered if projected debt service coverage rate falls below 1x. Balloon risk is triggered if a property s projected performance does not satisfy new, tighter mortgage standards.

Corporate bonds and loans - As of September 30, 2013, gross unrealized losses related to corporate bonds and loans were $0.675 million. Of this amount, $0.060 million have been in an unrealized loss position for twelve months or greater. The Company s investment manager s analysis for this sector includes maintaining detailed financial models that include a projection of each issuer s future financial performance, including prospective debt servicing capabilities, capital structure composition, and the value of the collateral. The analysis incorporates the macroeconomic environment, industry conditions in which the issuer operates, issuer s current competitive position, vulnerability to changes in the competitive environment, regulatory environment, issuer liquidity, issuer commitment to bondholders, issuer creditworthiness, and asset protection. Part of the process also includes running downside scenarios to evaluate the expected likelihood of default as well as potential losses in the event of default.

Common stocks As of September 30, 2013, gross unrealized losses related to common stock were $0.534 million. Of this amount, $0.203 million have been in an unrealized loss position for twelve months or greater. To determine if an other than temporary impairment of an equity security has occurred, the Company considers, among other things, the severity and duration of the decline in fair value of the equity security. The Company also examines other factors to determine if the equity security could recover its value in a reasonable period of time.

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The Company recorded the following other than temporary impairments (OTTI) on its investment portfolio for the quarters and nine months ended September 30, 2013 and 2012:

(Dollars in thousands)	**Quarters Ended September 30, 2013**	**2012**	**Nine Months Ended September 30, 2013**	**2012**
Fixed maturities:				
OTTI losses, gross	$ (160)	$ (14)	$ (271)	$ (1,073)
Portion of loss recognized in other comprehensive income (pre-tax)				541
Net impairment losses on fixed maturities recognized in earnings	(160)	(14)	(271)	(532)
Equity securities	(17)	(175)	(959)	(2,735)
Total	$ (177)	$ (189)	$ (1,230)	$ (3,267)

The following table is an analysis of the credit losses recognized in earnings on debt securities held by the Company for the quarters and nine months ended September 30, 2013 and 2012 for which a portion of the OTTI loss was recognized in other comprehensive income.

(Dollars in thousands)	**Quarters Ended September 30, 2013**	**2012**	**Nine Months Ended September 30, 2013**	**2012**
Balance at beginning of period	$ 86	$ 86	$ 86	$ 86
Additions where no OTTI was previously recorded				55
Additions where an OTTI was previously recorded				
Reductions for securities for which the company intends to sell or more likely than not will be required to sell before recovery				
Reductions reflecting increases in expected cash flows to be collected				
Reductions for securities sold during the period	(32)		(32)	(55)
Balance at end of period	$ 54	$ 86	$ 54	$ 86

Accumulated Other Comprehensive Income, Net of Tax

Accumulated other comprehensive income as of September 30, 2013 and December 31, 2012 was as follows:

(Dollars in thousands)	**September 30, 2013**	**December 31, 2012**
Net unrealized gains (losses) from:		
Fixed maturities	$ 21,273	$ 42,228
Common stock	58,290	29,896
Other	(65)	83
Deferred taxes	(25,042)	(18,857)
Accumulated other comprehensive income, net of tax	$ 54,456	$ 53,350

The changes in accumulated other comprehensive income, net of tax, by component for the nine months ended September 30, 2013 was as follows:

Nine Months Ended September 30, 2013 (Dollars in thousands)	Unrealized Gains and Losses on Available for Sale Securities, Net of Tax	Foreign Currency Items, Net of Tax	Accumulated Other Comprehensive Income, Net of Tax
Beginning balance	$ 53,435	$ (85)	$ 53,350
Other comprehensive income (loss) before reclassification	7,774	(12)	7,762
Amounts reclassified from accumulated other comprehensive income (loss)	(6,844)	188	(6,656)
Other comprehensive income (loss)	930	176	1,106
Ending balance	$ 54,365	$ 91	$ 54,456

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The reclassifications out of accumulated other comprehensive income for the quarter and nine months ended September 30, 2013 were as follows:

(Dollars in thousands)		Amount Reclassified from Accumulated Other Comprehensive Income	
Details about Accumulated Other Comprehensive Income Components	**Affected Line Item in the Statement Where Net Income is Presented**	**Quarter Ended September 30, 2013**	**Nine Months Ended September 30, 2013**
Unrealized gains and losses on available for sale securities	Other net realized investment gains	$ (1,818)	$ (11,724)
	Other than temporary impairment losses on investments	177	1,230
	Total before tax	(1,641)	(10,494)
	Income tax (expense) benefit	637	3,650
	Net of tax	$ (1,004)	$ (6,844)
Foreign Currency Items	Other net realized investment gains		290
	Income tax (expense) benefit		(102)
	Net of tax	$	$ 188
Total reclassifications	Net of tax	$ (1,004)	$ (6,656)

Net Realized Investment Gains

The components of net realized investment gains for the quarters and nine months ended September 30, 2013 and 2012 were as follows:

	Quarters Ended September 30,	Nine Months Ended September 30,

(Dollars in thousands)	2013	2012	2013	2012
Fixed maturities:				
Gross realized gains	$ 105	$ 827	$ 779	$ 3,523
Gross realized losses	(195)	(31)	(591)	(1,573)
Net realized gains (losses)	(90)	796	188	1,950
Common stock:				
Gross realized gains	2,383	3,333	12,396	8,724
Gross realized losses	(652)	(918)	(2,380)	(3,761)
Net realized gains	1,731	2,415	10,016	4,963
Total net realized investment gains	$ 1,641	$ 3,211	$ 10,204	$ 6,913

The proceeds from sales of available-for-sale securities resulting in net realized investment gains for the nine months ended September 30, 2013 and 2012 were as follows:

	Nine Months Ended September 30,	
(Dollars in thousands)	2013	2012
Fixed maturities	$ 240,658	$ 380,713
Equity securities	55,174	40,299
Other invested assets		1,114

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Net Investment Income

The sources of net investment income for the quarters and nine months ended September 30, 2013 and 2012 were as follows:

(Dollars in thousands)	Quarters Ended September 30, 2013	Quarters Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Fixed maturities	$ 8,319	$ 10,320	$ 27,185	$ 32,146
Equity securities	1,184	1,174	4,136	3,885
Cash and cash equivalents	15	13	96	99
Other invested assets		4,330	141	4,486
Total investment income	9,518	15,837	31,558	40,616
Investment expense	(1,032)	(1,060)	(3,273)	(3,351)
Net investment income	$ 8,486	$ 14,777	$ 28,285	$ 37,265

The Company s total investment return on a pre-tax basis for the quarters and nine months ended September 30, 2013 and 2012 were as follows:

(Dollars in thousands)	Quarters Ended September 30, 2013	Quarters Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Net investment income	$ 8,486	$ 14,777	$ 28,285	$ 37,265
Net realized investment gains	1,641	3,211	10,204	6,913
Net unrealized investment gains	10,471	11,388	7,291	23,222
Net investment return	12,112	14,599	17,495	30,135
Total investment return	$ 20,598	$ 29,376	$ 45,780	$ 67,400
Total investment return % **(1)**	1.3%	1.9%	3.0%	4.2%

Average investment portfolio **(2)**	$ 1,535,589	$ 1,556,450	$ 1,537,693	$ 1,599,472

(1) Not annualized.
(2) Average of total cash and invested assets, net of receivable/payable for securities purchased and sold, as of the beginning and ending of the period.

Insurance Enhanced Municipal Bonds

As of September 30, 2013, the Company held insurance enhanced municipal bonds of approximately $32.5 million, which represented approximately 2.1% of the Company s total cash and invested assets, net of payable/receivable for securities purchased and sold. These securities had an average rating of AA-. Approximately $3.0 million of these bonds are pre-refunded with U.S. treasury securities, of which $1.4 million are backed by financial guarantors, meaning that funds have been set aside in escrow to satisfy the future interest and principal obligations of the bond. Of the remaining $29.5 million of insurance enhanced municipal bonds, $15.1 million would have carried a lower credit rating had they not been insured. The following table provides a breakdown of the ratings for these municipal bonds with and without insurance.

(Dollars in thousands) Rating	Ratings with Insurance	Ratings without Insurance
AAA	$ 8,840	$
AA		8,840
A	6,250	6,250
Total	$ 15,090	$ 15,090

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A summary of the Company s insurance enhanced municipal bonds that are backed by financial guarantors, including the pre-refunded bonds that are escrowed in U.S. government obligations, as of September 30, 2013, is as follows:

(Dollars in thousands) Financial Guarantor	Total	Pre-refunded Securities	Government Guaranteed Securities	Exposure Net of Pre-refunded & Government Guaranteed Securities
Ambac Financial Group	$ 2,315	$ 1,256	$	$ 1,059
Assured Guaranty Corporation	11,176			11,176
Municipal Bond Insurance Association	7,123			7,123
Gov t National Housing Association	1,404	137	1,267	
Permanent School Fund Guaranty	8,840		8,840	
Total backed by financial guarantors	30,858	1,393	10,107	19,358
Other credit enhanced municipal bonds	1,630	1,630		
Total	$ 32,488	$ 3,023	$ 10,107	$ 19,358

In addition to the $32.5 million of insurance enhanced municipal bonds, the Company also held insurance enhanced asset-backed and credit securities with a market value of approximately $18.4 million, which represented approximately 1.2% of the Company s total invested assets net of receivable/payable for securities purchased and sold. The financial guarantors of the Company s $18.4 million of insurance enhanced asset-backed and credit securities include Municipal Bond Insurance Association ($4.4 million), Ambac ($1.6 million), Assured Guaranty Corporation ($7.2 million), and Other ($5.2 million).

The Company had no direct investments in the entities that have provided financial guarantees or other credit support to any security held by the Company at September 30, 2013.

Bonds Held on Deposit

Certain cash balances, cash equivalents, equity securities and bonds available for sale were deposited with various governmental authorities in accordance with statutory requirements, were held as collateral pursuant to borrowing arrangements, or were held in trust pursuant to intercompany reinsurance agreements. The fair values were as follows as of September 30, 2013 and December 31, 2012:

(Dollars in thousands)	Estimated Fair Value September 30, 2013	December 31, 2012
On deposit with governmental authorities	$ 41,825	$ 42,492
Intercompany trusts held for the benefit of U.S. policyholders	572,644	553,893
Held in trust pursuant to third party requirements	115,492	132,684
Held in trust pursuant to U.S. regulatory requirements for the benefit of U.S. policyholders	6,355	6,368
Securities held as collateral for borrowing arrangements	77,441(a)	
Total	$ 813,757	$ 735,437

(a) Amount required to collateralize margin borrowing facility.

5. Fair Value Measurements

The accounting standards related to fair value measurements define fair value, establish a framework for measuring fair value, outline a fair value hierarchy based on inputs used to measure fair value, and enhance disclosure requirements for fair value measurements. These standards do not change existing guidance as to whether or not an instrument is carried at fair value. The Company has determined that its fair value measurements are in accordance with the requirements of these accounting standards.

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The Company s invested assets are carried at their fair value and are categorized based upon a fair value hierarchy:

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets that the Company has the ability to access at the measurement date.

Level 2 inputs utilize other than quoted prices included in Level 1 that are observable for similar assets, either directly or indirectly.

Level 3 inputs are unobservable for the asset, and include situations where there is little, if any, market activity for the asset.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company 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 asset.

Both observable and unobservable inputs may be used to determine the fair value of positions that the Company has classified within the Level 3 category. As a result, the unrealized gains and losses for invested assets within the Level 3 category presented in the tables below may include changes in fair value that are attributed to both observable (e.g., changes in market interest rates) and unobservable (e.g., changes in unobservable long-dated volatilities) inputs.

The following table presents information about the Company s invested assets measured at fair value on a recurring basis as of September 30, 2013 and December 31, 2012, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value.

As of September 30, 2013	**Fair Value Measurements**			
(Dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Fixed maturities:				
U.S. treasury and agency obligations	$ 81,810	$ 10,935	$	$ 92,745
Obligations of states and political subdivisions		190,026		190,026
Mortgage-backed securities		245,540		245,540
Commercial mortgage-backed securities		53,164		53,164
Asset-backed securities		134,108		134,108

Corporate bonds and loans		423,841		423,841
Foreign corporate bonds		56,851		56,851
Total fixed maturities	81,810	1,114,465		1,196,275
Common stock	233,415			233,415
Other invested assets			3,269	3,269
Total invested assets	$ 315,225	$ 1,114,465	$ 3,269	$ 1,432,959

As of December 31, 2012	**Fair Value Measurements**			
(Dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Fixed maturities:				
U.S. treasury and agency obligations	$ 89,981	$ 18,763	$	$ 108,744
Obligations of states and political subdivisions		201,077		201,077
Mortgage-backed securities		255,942		255,942
Commercial mortgage-backed securities		8,117		8,117
Asset-backed securities		113,351		113,351
Corporate bonds and loans		486,171		486,171
Foreign corporate bonds		55,920		55,920
Total fixed maturities	89,981	1,139,341		1,229,322
Common stock	197,075			197,075
Other invested assets			3,132	3,132
Total invested assets	$ 287,056	$ 1,139,341	$ 3,132	$ 1,429,529

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The securities classified as Level 1 in the above table consist of U.S. Treasuries and equity securities actively traded on an exchange.

The securities classified as Level 2 in the above table consist primarily of fixed maturity securities. Based on the typical trading volumes and the lack of quoted market prices for fixed maturities, security prices are derived through recent reported trades for identical or similar securities making adjustments through the reporting date based upon available market observable information. If there are no recent reported trades, matrix or model processes are used to develop a security price where future cash flow expectations are developed based upon collateral performance and discounted at an estimated market rate. Included in the pricing of asset-backed securities, collateralized mortgage obligations, and mortgage-backed securities are estimates of the rate of future prepayments of principal over the remaining life of the securities. Such estimates are derived based on the characteristics of the underlying structure and prepayment speeds previously experienced at the interest rate levels projected for the underlying collateral. For corporate loans, price quotes from multiple dealers along with recent reported trades for identical or similar securities are used to develop prices.

There were no transfers between Level 1 and Level 2 during the quarters and nine months ended September 30, 2013 or 2012.

The following table presents changes in Level 3 investments measured at fair value on a recurring basis for the quarters and nine months ended September 30, 2013 and 2012:

	Other Invested Assets			
(Dollars in thousands)	**Quarters Ended September 30,**		**Nine Months Ended September 30,**	
	2013	**2012**	**2013**	**2012**
Beginning balance	$ 3,226	$ 8,590	$ 3,132	$ 6,617
Total gains (losses) (realized / unrealized):				
Included in accumulated other comprehensive income (loss)	37	(4,546)	121	(2,579)
Purchases	6	7	16	13
Sales		(1,114)		(1,114)
Ending balance	$ 3,269	$ 2,937	$ 3,269	$ 2,937
Losses included in earnings of the period attributable to the change in unrealized losses related to assets still held at the end of the period	$	$	$	$

The investments classified as Level 3 in the above table relate to investments in limited partnerships that have invested primarily in publicly traded companies. However, not all of the partnerships investments are publicly traded, nor does the Company have access to daily valuations, therefore the estimated fair values of these limited partnerships are measured utilizing net asset value as a practical expedient for the limited partnerships. Material assumptions and factors utilized in pricing these investments include future cash flows, constant default rates, recovery rates, and any market clearing activity that may have occurred since the previous pricing period.

Fair Value of Alternative Investments

Included in Other invested assets in the fair value hierarchy at September 30, 2013 are limited liability partnerships measured at fair value. The following table provides the fair value and future funding commitments related to these investments at September 30, 2013.

(Dollars in thousands)	**Fair Value**	**Future Funding Commitments**
Equity Fund, LP **(1)**	$ 3,269	$ 2,490
Real Estate Fund, LP **(2)**		
Total	$ 3,269	$ 2,490

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(1) This limited partnership invests in companies from various business sectors whereby the partnership has acquired control of the operating business as a lead or organizing investor. The Company does not have the contractual option to redeem its limited partnership interest but receives distributions based on the liquidation of the underlying assets. The Company does not have the ability to sell or transfer its limited partnership interest without consent from the general partner.

(2) This limited partnership invests in real estate assets through a combination of direct or indirect investments in partnerships, limited liability companies, mortgage loans, and lines of credit. The Company does not have the contractual option to redeem its limited partnership interest but receives distributions based on the liquidation of the underlying assets. The Company does not have the ability to sell or transfer its limited partnership interest without consent from the general partner. The Company continues to hold an investment in this limited partnership and has written the fair value down to zero.

Pricing

The Company s pricing vendors provide prices for all investment categories except for investments in limited partnerships. One vendor provides prices for equity securities and all fixed maturity categories except for corporate loans. A second vendor provides prices for the corporate loan securities.

The following is a description of the valuation methodologies used by the Company s pricing vendors for investment securities carried at fair value:

Equity prices are received from all primary and secondary exchanges.

Corporate and agency bonds are evaluated by utilizing a multi-dimensional relational model. For bonds with early redemption options, an option adjusted spread model is utilized. Both asset classes use standard inputs and incorporate security set up, defined sector breakdown, benchmark yields, apply base spreads, yield to maturity, and adjust for corporate actions.

A volatility-driven multi-dimensional spread table or an option-adjusted spread model and prepayment model is used for agency commercial mortgage obligations (CMO). For non-agency CMOs, a prepayment/spread/yield/price adjustment model is utilized. CMOs are categorized with mortgage-backed securities in the tables listed above. For ABSs, a multi-dimensional, collateral specific spread / prepayment speed tables is utilized. For both asset classes, evaluations utilize standard inputs plus new issue data, monthly payment information, and collateral performance. The evaluated pricing models incorporate security set-up, prepayment speeds, cash flows, and treasury swap curves and spread adjustments.

For municipals, a multi-dimensional relational model is used to evaluate securities within this asset class. The evaluated pricing models for this asset class incorporate security set-up, benchmark yields, apply base spreads, yield to worst or market convention, ratings updates, prepayment schedules and adjustments for material events notices.

U.S. treasuries are evaluated by obtaining feeds from a number of live data sources including active market makers and inter-dealer brokers.

For MBSs, a matrix model correlation to TBA (a forward MBS trade) or benchmarking is utilized to value a security.

Corporate loans are priced using averages of bids and offers obtained from the broker/dealer community involved in trading such loans.

The Company performs certain procedures to validate whether the pricing information received from the pricing vendors is reasonable, to ensure that the fair value determination is consistent with accounting guidance, and to ensure that its assets are properly classified in the fair value hierarchy. The Company s procedures include, but are not limited to:

Reviewing periodic reports provided by the Investment Manager that provides information regarding rating changes and securities placed on watch. This procedure allows the Company to understand why a particular security s market value may have changed.

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Understanding and periodically evaluating the various pricing methods and procedures used by the Company s pricing vendors to ensure that investments are properly classified within the fair value hierarchy.

On a quarterly basis, the Company corroborates investment security prices received from its pricing vendors by obtaining pricing from a second pricing vendor for a sample of securities.

During the quarter and nine months ended September 30, 2013, the Company has not adjusted quotes or prices obtained from the pricing vendors.

The reported value of financial instruments not carried at fair value, principally cash and cash equivalents, margin borrowing facility, and notes payable, approximate fair value.

6. Income Taxes

The statutory income tax rates of the countries where the Company does business are 35.0% in the United States, 0.0% in Bermuda, 0.0% in the Cayman Islands, 0.0% in Gibraltar, 28.8% in the Duchy of Luxembourg, and 25.0% on non-trading income, 30.0% on capital gains and 12.5% on trading income in the Republic of Ireland. The statutory income tax rate of each country is applied against the expected annual taxable income of the Company in each country to estimate the annual income tax expense. Total estimated annual income tax expense is divided by total estimated annual pre-tax income to determine the expected annual income tax rate used to compute the income tax provision. On an interim basis, the expected annual income tax rate is applied against interim pre-tax income, excluding net realized gains and losses and discrete items such as limited partnership distributions and make whole provisions (see Note 8), and then that amount is added to income taxes on net realized gains and losses, discrete items and limited partnership distributions. The Company s income before income taxes from its non-U.S. subsidiaries and U.S. subsidiaries, including the results of the quota share and stop-loss agreements between Wind River Reinsurance and the Insurance Operations, for the quarters and nine months ended September 30, 2013 and 2012 were as follows:

Quarter Ended September 30, 2013:

(Dollars in thousands)	Non-U.S. Subsidiaries	U.S. Subsidiaries	Eliminations	Total
Revenues:				
Gross premiums written	$ 37,676	$ 59,746	$ (28,637)	$ 68,785
Net premiums written	$ 37,673	$ 26,357	$	$ 64,030

Net premiums earned	$ 40,282	$ 24,187	$	$ 64,469
Net investment income	8,443	4,983	(4,940)	8,486
Net realized investment gains (losses)	(180)	1,821		1,641
Other income	21	162		183
Total revenues	48,566	31,153	(4,940)	74,779
Losses and Expenses:				
Net losses and loss adjustment expenses	18,300	17,183		35,483
Acquisition costs and other underwriting expenses	17,009	11,019		28,028
Corporate and other operating expenses	663	1,964		2,627
Interest expense	292	8,233	(4,940)	3,585
Income (loss) before income taxes	$ 12,302	$ (7,246)	$	$ 5,056

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GLOBAL INDEMNITY PLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - *(Continued)*

(Unaudited)

Quarter Ended September 30, 2012:

(Dollars in thousands)	Non-U.S. Subsidiaries	U.S. Subsidiaries	Eliminations	Total
Revenues:				
Gross premiums written	$ 29,595	$ 51,205	$ (23,851)	$ 56,949
Net premiums written	$ 29,595	$ 21,860	$	$ 51,455
Net premiums earned	$ 34,198	$ 21,131	$	$ 55,329
Net investment income	13,687	5,726	(4,636)	14,777
Net realized investment gains	584	2,627		3,211
Other income (loss)	(21)	122		101
Total revenues	48,448	29,606	(4,636)	73,418
Losses and Expenses:				
Net losses and loss adjustment expenses				