

INFINITY PROPERTY & CASUALTY CORP
Form 10-K
February 28, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2007

OR

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

For the transition period from _____ to _____

Commission file number 0-50167

INFINITY PROPERTY AND CASUALTY CORPORATION

(Exact name of registrant as specified in its charter)

OHIO
*(State of other jurisdiction of
incorporation or organization)*

03-0483872
*(I.R.S. Employer
Identification No.)*

3700 COLONNADE PARKWAY

BIRMINGHAM, ALABAMA
(Address of principal executive offices)

(205) 870-4000
(Registrant's telephone number, including area code)

35243
(Zip Code)

Securities registered pursuant to Section 12(b) of the Act:
Common Stock, no par value

Name of each exchange on which registered:
NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act: None

(Title of class)

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange from their obligations under those Sections.

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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

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

As of June 29, 2007, the aggregate market value of the voting Common Stock held by non-affiliates of the registrant was \$978,050,335 based on the last sale price of Common Stock on that date as reported by The NASDAQ Global Select Market.

As of February 15, 2008, there were 16,200,996 shares of the registrant's Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's proxy statement for the annual meeting of shareholders to be held on May 20, 2008, are incorporated by reference in Part III hereof.

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains certain statements that may be deemed to be forward-looking statements that anticipate results based on our estimates, assumptions and plans that are subject to uncertainty. These statements are made subject to the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995. All statements in this report not dealing with historical results or current facts are forward-looking and are based on estimates, assumptions, and projections. Statements which include the words believes, seeks, expects, may, should, intends, likely, targets, plans, anticipates, estimates or the negative version of those words and similar statements of a future or forward-looking nature identify forward-looking statements. Examples of such forward-looking statements include statements relating to expectations concerning market conditions, premiums, growth, earnings, investment performance, expected losses, rate changes and loss experience.

Actual results could differ materially from those expected by Infinity depending on: changes in economic conditions and financial markets (including interest rates), the adequacy or accuracy of Infinity's pricing methodologies, actions of competitors, the approval of requested form and rate changes, judicial and regulatory developments affecting the automobile insurance industry, the outcome of pending or new litigation against Infinity, weather conditions (including the severity and frequency of storms, hurricanes, snowfalls, hail and winter conditions), changes in driving patterns and loss trends. Infinity undertakes no obligation to publicly update or revise any of the forward-looking statements. For a more detailed discussion of some of the foregoing risks and uncertainties which could cause actual results to differ from those contained in the forward-looking statements, see Risk Factors contained in Item 1A.

PART I

ITEM 1

Business

Introduction

Infinity Property and Casualty Corporation (Infinity or the Company) is a holding company that, through subsidiaries, provides personal automobile insurance with a concentration on nonstandard auto insurance. Infinity is headquartered in Birmingham, Alabama. The Company employed approximately 2,100 persons at December 31, 2007.

Infinity files its Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and other reports as required with the United States Securities and Exchange Commission (SEC). Any of these documents may be read and copied at the SEC's Public Reference Room at 100 F Street NE, Washington, D.C. 20549. Information regarding the operation of the SEC Public Reference Room may be obtained by calling 1-800-SEC-0330. Infinity's filed documents may also be accessed via the SEC Internet site at: <http://www.sec.gov>. All of Infinity's SEC filings, news releases and other information may also be accessed free of charge on Infinity's Internet site at: <http://www.ipacc.com>. Information on Infinity's website is not part of this Form 10-K.

Please see Note 1 to the Consolidated Financial Statements for additional information regarding the history and organization of Infinity. References to Infinity, unless the context requires otherwise, include the combined operations of its subsidiaries (collectively the NSA Group) and the in-force personal insurance business assumed through a reinsurance contract (the Assumed Agency Business) from American Financial Group Inc.'s (AFG), formerly Infinity's parent company, principal property and casualty subsidiary, Great American Insurance Company (GAI). Unless indicated otherwise, the financial information herein is presented on a GAAP basis.

The Personal Automobile Market

Personal auto insurance is the largest line of property and casualty insurance, accounting for approximately 36% of the estimated \$451 billion of annual industry premiums. Personal auto insurance is comprised of preferred, standard and nonstandard risks. Nonstandard auto insurance is intended for drivers who, due to factors such as their driving record, age or vehicle type, represent a higher than normal risk. As a result, customers who purchase nonstandard auto insurance generally pay higher premiums for similar coverage than the drivers qualifying for standard or preferred policies. While there is no established industry-recognized distinction between nonstandard risks and all other personal auto risks, Infinity believes that nonstandard auto risks generally constitute between 15% and 20% of the personal automobile insurance market, with this range fluctuating according to competitive conditions in the market. Independent agents sell approximately one-third of all personal automobile insurance. The remainder is sold by captive agents or directly by insurance companies to their customers. Infinity believes that, relative to the

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standard and preferred auto insurance market, a disproportionately larger portion of nonstandard auto insurance is sold through independent agents.

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The personal auto insurance industry is cyclical, characterized by periods of price competition and excess capacity, followed by periods of high premium rates and shortages of underwriting capacity. In the late 1990s, many automobile insurers attempted to capture more business by reducing rates. Infinity believes that these industry-wide rate reductions, combined with increased severity and frequency trends during the years 1998 through 2000, contributed to the deterioration of industry loss ratios in that period. Infinity reacted by increasing personal auto rates by 15% in 2001 and 12% in 2002. During the same period, most of the industry, including some of the largest companies, raised rates and tightened underwriting standards in order to address poor results, and other insurance companies withdrew from the market because of their inability to compete successfully, impaired capital positions, or because of a decrease in the availability of reinsurance. However, beginning in the second half of 2003, competitors who remained in the marketplace began to compete more aggressively for independent agents' business by offering increased sales and commission incentives. This competition for the independent agents' business through enhanced incentives has continued for the last several years, including 2007. Infinity also noted that during 2005 and 2006 some competitors were reducing their overall rates with larger rate reductions in certain segments of the business. The personal automobile component of the Consumer Price Index (CPI) reflects this trend as it indicates personal automobile insurance rates have increased just 0.8% and 1.0% during 2006 and 2005, respectively, after increasing 3.4% and 4.5% during 2004 and 2003, respectively. During 2007, Infinity observed competitors continuing to reduce rates in certain segments of the business, but also observed, in the latter part of the year, a few competitors in certain states increasing rates and tightening underwriting standards. Industry rates in 2007, as measured by the CPI, increased 0.5%. Infinity's average rate increases on its personal auto business were 3.5%, 0.8%, 2.2% and 2.7% for 2007, 2006, 2005 and 2004, respectively.

The personal auto insurance industry is highly competitive and, except for regulatory considerations, there are relatively few barriers to entry. Infinity generally competes with other insurers on the basis of price, coverages offered, claims handling, customer service, agent commission, geographic coverage and financial strength ratings. Infinity competes with both large national writers and smaller regional companies. In 2006, the five largest automobile insurance companies accounted for approximately 49% of the industry's net written premiums and the largest ten accounted for approximately 65% (2007 industry data not available). Approximately 352 insurance groups compete in the personal auto insurance industry, according to A.M. Best. Some of these groups specialize in nonstandard auto insurance, while others insure a broad spectrum of personal auto insurance risks.

Operations

Infinity is organized into two regions, East and West. Each region has its own product management and business development staff. The regions are also supported by the following centralized departments: marketing, claims, customer service, accounting, treasury, human resources and information technology resources. Monthly executive team meetings, which include the Chief Executive Officer, the Chief Financial Officer, the Chief Legal Officer, the Chief Human Resources Officer, the Chief Information Technology Officer, the Chief Actuary, the Chief Claims Officer and the two regional presidents, allow for sharing of information among regions and for setting policies and making key strategic decisions.

Infinity estimates that approximately 98% of its personal auto business is nonstandard auto insurance. Based on data published by A.M. Best, Infinity believes that it is the third largest provider of nonstandard auto coverage through independent agents in the United States. Infinity also writes standard and preferred personal auto insurance, monoline commercial auto insurance and classic collector automobile insurance.

Summarized historical financial data for Infinity is presented below (in thousands):

	Twelve months ended December 31,		
	2007	2006	2005
Gross written premium	\$ 1,019,119	\$ 992,409	\$ 1,002,813
Net written premium	1,014,262	982,190	979,635
Net earnings	71,944	87,282	106,308
	as of December 31,		
	2007	2006	

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Total assets	\$ 1,916,610	\$ 2,014,354
Total liabilities	1,315,386	1,349,753
Total shareholders equity	601,224	664,601

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Infinity has a history of favorable underwriting results. The following table compares Infinity's statutory combined ratio in past years with those of the private passenger auto industry. The statutory combined ratio is the sum of the loss ratio (the ratio of losses and loss adjustment expenses (LAE) to net earned premiums) and the expense ratio (when calculated on a statutory accounting basis, the ratio of underwriting expenses to net written premiums). When the combined ratio is under 100%, underwriting results are generally considered profitable; when the ratio is over 100%, underwriting results are generally considered unprofitable. Infinity has consistently performed better than the industry as shown below:

	2007	2006	2005	2004	2003	2003-2007	1998-2007
Infinity	91.8%	88.7%	90.0%	90.3%	94.9%	90.8%	96.3%
Industry (a)	97.5%	95.5%	95.1%	94.3%	98.4%	96.1%	100.2%
Percentage points better than industry	5.7%	6.8%	5.1%	4.0%	3.5%	5.3%	3.9%

- (a) Private passenger auto industry combined ratios were obtained from A.M. Best. The industry combined ratio for 2007 is an estimate based on data obtained from A.M. Best.

Products

Personal Automobile is Infinity's primary insurance product. It provides coverage to individuals for liability to others for bodily injury and property damage and for physical damage to an insured's own vehicle from collision and various other perils. In addition, many states require policies to provide for first party personal injury protection, frequently referred to as no-fault coverage. Infinity offers three primary products to individual drivers: the Low-Cost product, which offers the most restricted coverage, the Value-Added product, which offers broader coverage and higher limits, and the Premier product, which offers the broadest coverage and is designed for standard and preferred risk drivers. For the year ended December 31, 2007, Infinity's mix of personal automobile written premium was 14% Low-Cost, 84% Value-Added and 2% Premier.

Commercial Vehicle provides coverage to businesses for liability to others for bodily injury and property damage and for physical damage to vehicles from collision and various other perils. Infinity offers monoline commercial automobile insurance to businesses with fleets of 12 or fewer vehicles. Businesses that are involved in what Infinity considers to be hazardous operations or interstate commerce are generally avoided.

Classic Collector provides protection for classic collectible automobiles. Infinity's Classic Collector program provides coverage to individuals with classic or antique automobiles for liability to others for bodily injury and property damage and for physical damage to an insured's own vehicle from collision and various other perils.

Infinity's three product groups contributed the following percentages of total gross written premiums:

	Twelve months ended December 31,		
	2007	2006	2005
Personal Automobile	94%	93%	90%
Commercial Vehicle	4%	4%	4%
Classic Collector	2%	2%	2%
Other Lines	0%	1%	4%
Total	100%	100%	100%

Distribution and Marketing

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Infinity distributes its products primarily through a network of over 13,000 independent agencies (with approximately 17,000 locations). Independent agencies were responsible for approximately 95% of Infinity's gross written premiums for the twelve-month period ended December 31, 2007. In 2007, three independent agencies each accounted for between 2% and 3% of Infinity's gross written premiums, and five other agencies each accounted for between 1% and 2% of the Company's gross written premiums. Infinity pays each agent a commission, based on contractual rates multiplied by the premiums the agent generates. On a limited basis, Infinity also offers contingent commission arrangements, typically in the form of higher commission rates, to agencies in order to spur premium growth in profitable areas. In 2007, contingent commission arrangements represented approximately 1% of total agency compensation.

Infinity also fosters agent relationships by providing them with access to Infinity's Internet web-based software applications along with programs and services designed to strengthen and expand their marketing, sales and service capabilities. Infinity's

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Internet-based software applications provide many of its agents with real-time underwriting, claims and policy information. Infinity believes the array of services that it offers to its agents adds significant value to the agents' businesses. For example, Providing Agents Service and Support Program is Infinity's incentive-based program through which agents receive assistance in critical areas such as training, advertising and promotion. In 2007, Infinity spent \$9.6 million on co-op advertising and promotions.

Strategic partnerships are another mode of distribution for Infinity. These are relationships with non-affiliated property and casualty insurers that have their own captive agency forces. These companies usually provide standard and preferred auto coverage through one of their own companies while utilizing Infinity's companies for their nonstandard risks. Infinity believes these relationships are mutually beneficial because its partners gain access to Infinity's nonstandard auto expertise, and Infinity gains access to a new distribution channel. This channel represented approximately 5% of gross written premiums in 2007.

Infinity also has two pilot programs for alternative methods of distribution. In November 2006, Infinity launched a pilot program based on considerable market research that suggested a need in urban Hispanic communities for a one-stop financial service center. This led to the establishment of an Infinity Plus retail store in Los Angeles. Through conveniently located and readily accessible Infinity Plus stores, consumers can purchase automobile insurance from Infinity, as well as, other insurance products, such as life insurance, offered by partner insurance companies. In addition, services such as check cashing, wire transfers and travel services are also available. Infinity currently has 5 company-owned Infinity Plus locations: one in suburban Los Angeles, one in Phoenix, and three in Chicago. Infinity also extends opportunities to select agents to offer Infinity Plus services and products in agent-owned stores. In 2007, Infinity launched a direct-to-consumer pilot program in Arizona through which consumers can quote and purchase automobile insurance over the Internet. Although 2007 gross written premiums from these two pilot programs represented less than 1% of total gross written premiums, the company views each of these initiatives as strategically important measures to ensure that Infinity is best positioned and prepared to meet the evolving needs and preferences of its targeted consumers. Infinity will continue to monitor the progress of these pilot programs to determine if they will be expanded beyond the test markets.

Infinity is licensed to write insurance in all 50 states and the District of Columbia, but is committed to growth in targeted urban areas (Urban Zones) identified within selected focus states that management believes offer the greatest opportunity for premium growth and profitability.

Infinity classifies the states in which it operates into three categories:

Focus States Infinity has identified current and future Urban Zones in these states which include: Arizona, California, Colorado, Connecticut, Florida, Georgia, Illinois, Missouri, Nevada, Pennsylvania, Tennessee and Texas.

Maintenance States Infinity is maintaining its writings in these states which include: Alabama, Indiana, Mississippi, Ohio, South Carolina and Virginia. These states contain no Urban Zones, but Infinity believes each Maintenance State offers the Company an opportunity for underwriting profit.

Other States Includes all remaining states.

Infinity further classifies the Focus States into two categories:

Urban Zones include the following urban areas:

Arizona Phoenix

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California Los Angeles, Sacramento, San Diego, San Francisco and San Joaquin Valley

Connecticut Hartford

Florida Jacksonville, Miami, Orlando and Tampa

Georgia Atlanta

Missouri Saint Louis

Pennsylvania Philadelphia

Tennessee Nashville

Texas Dallas, El Paso, Fort Worth, Houston and San Antonio

Non-Urban Zones include all remaining areas in the Focus States outside of a designated Urban Zone.

Infinity continually evaluates its market opportunities, thus the Focus States, Urban Zones or Maintenance States may change over time as new market opportunities arise, as the allocation of resources changes, or as regulatory environments change.

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Total gross written premiums among the three state categories are as follows:

	Twelve months ended December, 31		
	2007	2006	2005
Personal Auto Insurance			
Focus States:			
California			
Urban Zones	51%	48%	45%
Non-Urban Zones	2%	2%	2%
Florida			
Urban Zones	7%	7%	7%
Non-Urban Zones	6%	8%	8%
Georgia			
Urban Zones	3%	3%	2%
Non-Urban Zones	3%	4%	4%
Texas			
Urban Zones	4%	3%	2%
Non-Urban Zones	*	*	*
Pennsylvania			
Urban Zones	3%	3%	3%
Non-Urban Zones	2%	2%	2%
Arizona			
Urban Zones	3%	3%	2%
Non-Urban Zones	*	*	*
Connecticut			
Urban Zones	2%	2%	1%
Non-Urban Zones	*	*	*
Nevada			
Urban Zones			
Non-Urban Zones	2%	*	
Missouri			
Urban Zones	*	*	*
Non-Urban Zones	*	*	*
Tennessee			
Urban Zones	*	*	*
Non-Urban Zones	*	*	*
Colorado			
Urban Zones			
Non-Urban Zones	*	*	*
Illinois			
Urban Zones			
Non-Urban Zones	*		*
Total Focus States	90%	87%	82%
Maintenance States	3%	5%	5%
Other States	1%	1%	3%
Subtotal	94%	93%	90%
Commercial Vehicle	4%	4%	4%

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Classic Collector	2%	2%	2%
Other	0%	1%	4%
 Total All States and All Lines	 100%	 100%	 100%
Total \$ (in thousands) - All States and All Lines	1,019,011	986,741	988,670

- (1) 2007, 2006 and 2005 exclude \$0.1 million, \$5.0 million and \$9.8 million, respectively, of premiums written on behalf of other companies. 2006 and 2005 also exclude \$0.7 million and \$4.3 million, respectively, of unearned premium transfers.
- (2) * denotes less than one percent

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Infinity's distribution and marketing efforts are implemented with a focus on maintaining a low-cost structure. Controlling expenses allows Infinity to price competitively and achieve better underwriting returns. Over the five years ended 2006, years for which industry data are available from A.M. Best, Infinity's statutory ratio of underwriting expenses to premiums written has averaged 22.2%, which is 3.7 points better than the independent agency segment of the private passenger automobile industry average of 25.9% for the same period.

Claims Handling

Infinity strives for accuracy, consistency and fairness in its claim resolutions. Infinity's claims organization employs approximately 1,000 people and has 31 field locations. Infinity provides a 24-hour, seven days per week toll-free service for its customers to report claims. Infinity predominantly uses its own local adjusters and appraisers, who typically respond to claims within 24 hours of a report. In 2005, Infinity began operating claims service centers, which allow a customer to conveni