

INFINITY PROPERTY & CASUALTY CORP

Form 10-Q

August 08, 2013

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 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 _____

Commission File No. 0-50167

INFINITY PROPERTY AND CASUALTY CORPORATION

(Exact name of registrant as specified in its charter)

Incorporated under

the Laws of Ohio

(State or other jurisdiction of

incorporation or organization)

3700 Colonnade Parkway, Suite 600, Birmingham, Alabama 35243

(Address of principal executive offices and zip code)

(205) 870-4000

(Registrant's telephone number, including area code)

Not Applicable

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

03-0483872

(I.R.S. Employer

Identification No.)

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 and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 No

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

As of July 31, 2013 there were 11,496,098 shares of the registrant's common stock outstanding.

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PART I
FINANCIAL INFORMATIONITEM 1
Financial StatementsINFINITY PROPERTY AND CASUALTY CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS(in thousands, except per share data)
(unaudited)

	Three months ended June 30,			Six months ended June 30,				
	2013	2012	% Change	2013	2012	% Change		
Revenues:								
Earned premium	\$331,215	\$294,118	12.6	%	\$649,804	\$571,266	13.7	%
Net investment income	8,622	9,600	(10.2)	)%	16,960	19,346	(12.3))%
Net realized gains on investments ¹	794	2,166	(63.4)	)%	4,617	2,405	92.0	%
Other income	73	98	(25.3)	)%	125	367	(66.0))%
Total revenues	340,704	305,983	11.3	%	671,506	593,385	13.2	%
Costs and Expenses:								
Losses and loss adjustment expenses	257,079	230,907	11.3	%	507,449	445,685	13.9	%
Commissions and other underwriting expenses	66,986	60,863	10.1	%	129,359	123,003	5.2	%
Interest expense	3,460	2,703	28.0	%	6,998	5,405	29.5	%
Corporate general and administrative expenses	2,335	2,084	12.0	%	4,072	4,100	(0.7))%
Other expenses	717	103	596.4	%	1,394	347	302.1	%
Total costs and expenses	330,575	296,660	11.4	%	649,272	578,540	12.2	%
Earnings before income taxes	10,129	9,323	8.6	%	22,234	14,845	49.8	%
Provision for income taxes	2,721	2,369	14.9	%	6,164	3,597	71.3	%
Net Earnings	\$7,408	\$6,954	6.5	%	\$16,070	\$11,248	42.9	%
Net Earnings per Common Share:								
Basic	\$0.65	\$0.59	10.2	%	\$1.40	\$0.96	45.8	%
Diluted	0.64	0.58	10.3	%	1.37	0.94	45.7	%
Average Number of Common Shares:								
Basic	11,448	11,709	(2.2)	)%	11,485	11,719	(2.0))%
Diluted	11,643	11,937	(2.5)	)%	11,698	11,993	(2.5))%
Cash Dividends per Common Share	\$0.300	\$0.225	33.3	%	\$0.600	\$0.450	33.3	%
¹ Net realized gains before impairment losses								
Total other-than-temporary impairment (OTTI) losses	\$1,093	\$2,584	(57.7)	)%	\$4,988	\$3,470	43.8	%
Non-credit portion in other comprehensive income	(486)	(418)	16.3	%	(558)	(1,034)	(46.1))%
OTTI losses reclassified from other comprehensive income	187	0	NM		187	1	NM	
Net impairment losses recognized in earnings	0	0	0.0	%	0	(32)	(100.0))%
Total net realized gains on investments	(299)	(418)	(28.4)	)%	(371)	(1,065)	(65.2))%
	\$794	\$2,166	(63.4)	)%	\$4,617	\$2,405	92.0	%

NM = Not Meaningful

See Condensed Notes to Consolidated Financial Statements.

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

INFINITY PROPERTY AND CASUALTY CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(unaudited)

	Three months ended		Six months ended June 30,	
	June 30, 2013	2012	2013	2012
Net earnings	\$7,408	\$6,954	\$16,070	\$11,248
Other comprehensive income (loss) before tax:				
Net change in postretirement benefit liability	50	(6	) 100	(11
Unrealized gains (losses) on investments:				
Unrealized holding gains (losses) arising during the period	(29,998	) 3,455	(27,310	) 10,118
Less: Reclassification adjustments for gains included in net income	(794	) (2,166	) (4,617	) (2,405
Unrealized gains (losses) on investments, net	(30,792	) 1,289	(31,928	) 7,713
Other comprehensive income (loss), before tax	(30,742	) 1,283	(31,828	) 7,702
Income tax benefit (expense) related to components of other comprehensive income	10,760	(449	) 11,140	(2,696
Other comprehensive income (loss), net of tax	(19,982	) 834	(20,688	) 5,006
Comprehensive income (loss)	\$(12,575) \$7,788	\$(4,618) \$16,254

See Condensed Notes to Consolidated Financial Statements.

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

INFINITY PROPERTY AND CASUALTY CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(in thousands, except share amounts in line descriptions)

	June 30, 2013 (unaudited)	December 31, 2012
Assets		
Investments:		
Fixed maturities – at fair value (amortized cost \$1,313,845 and \$1,278,051)	\$1,323,336	\$1,321,828
Equity securities – at fair value (cost \$64,604 and \$69,992)	70,077	73,106
Short-term investments - at fair value (amortized cost \$3,617 and \$0)	3,616	0
Total investments	\$1,397,029	\$1,394,934
Cash and cash equivalents	115,861	165,182
Accrued investment income	12,784	11,926
Agents' balances and premium receivable, net of allowances for doubtful accounts of \$15,499 and \$16,124	456,447	427,156
Property and equipment, net of accumulated depreciation of \$49,131 and \$45,339	44,479	39,301
Prepaid reinsurance premium	3,548	2,637
Recoverables from reinsurers (includes \$786 and \$750 on paid losses and LAE)	14,606	14,428
Deferred policy acquisition costs	92,268	88,251
Current and deferred income taxes	30,931	25,798
Receivable for securities sold	5,399	48,467
Other assets	11,800	10,236
Goodwill	75,275	75,275
Total assets	\$2,260,428	\$2,303,593
Liabilities and Shareholders' Equity		
Liabilities:		
Unpaid losses and loss adjustment expenses	\$612,004	\$572,894
Unearned premium	581,795	538,142
Payable to reinsurers	0	137
Long-term debt (fair value \$272,767 and \$288,879)	275,000	275,000
Commissions payable	30,813	18,073
Payable for securities purchased	24,344	132,440
Other liabilities	97,802	110,665
Total liabilities	\$1,621,759	\$1,647,351
Commitments and contingencies (See Note 9)		
Shareholders' equity:		
Common stock, no par value (50,000,000 shares authorized; 21,538,888 and 21,493,354 shares issued)	\$21,589	\$21,529
Additional paid-in capital	364,599	361,845
Retained earnings	675,341	666,199
Accumulated other comprehensive income, net of tax	9,163	29,851
Treasury stock, at cost (10,043,372 and 9,888,680 shares)	(432,022)	(423,181)
Total shareholders' equity	\$638,669	\$656,242
Total liabilities and shareholders' equity	\$2,260,428	\$2,303,593

See Condensed Notes to Consolidated Financial Statements.

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

INFINITY PROPERTY AND CASUALTY CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(in thousands)

(unaudited)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net of Tax	Treasury Stock	Total
Balance at December 31, 2011	\$21,358	\$355,911	\$652,423	\$35,319	\$(403,221)	\$661,789
Net earnings	—	—	11,248	—	—	11,248
Net change in postretirement benefit liability	—	—	—	(7)	—	(7)
Change in unrealized gain on investments	—	—	—	4,180	—	4,180
Change in non-credit component of impairment losses on fixed maturities	—	—	—	833	—	833
Comprehensive income	—	—	—	—	—	\$16,254
Dividends paid to common shareholders	—	—	(5,300)	—	—	(5,300)
Shares issued and share-based compensation expense, including tax benefit	68	2,911	—	—	—	2,978
Acquisition of treasury stock	—	—	—	—	(8,562)	(8,562)
Balance at June 30, 2012	\$21,425	\$358,821	\$658,371	\$40,325	\$(411,783)	\$667,160
Net earnings	\$—	\$—	\$13,072	\$—	\$—	\$13,072
Net change in postretirement benefit liability	—	—	—	(959)	—	(959)
Change in unrealized gain on investments	—	—	—	(10,047)	—	(10,047)
Change in non-credit component of impairment losses on fixed maturities	—	—	—	531	—	531
Comprehensive income	—	—	—	—	—	\$2,597
Dividends paid to common shareholders	—	—	(5,244)	—	—	(5,244)
Shares issued and share-based compensation expense, including tax benefit	104	3,023	—	—	—	3,127
Acquisition of treasury stock	—	—	—	—	(11,398)	(11,398)
Balance at December 31, 2012	\$21,529	\$361,845	\$666,199	\$29,851	\$(423,181)	\$656,242
Net earnings	\$—	\$—	\$16,070	\$—	\$—	\$16,070
Net change in postretirement benefit liability	—	—	—	65	—	65
Change in unrealized gain on investments	—	—	—	(20,945)	—	(20,945)
Change in non-credit component of impairment losses on fixed maturities	—	—	—	192	—	192
Comprehensive loss	—	—	—	—	—	\$(4,618)
Dividends paid to common shareholders	—	—	(6,928)	—	—	(6,928)
Shares issued and share-based compensation expense, including tax benefit	60	2,754	—	—	—	2,814

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Acquisition of treasury stock	—	—	—	—	(8,841)	(8,841)
Balance at June 30, 2013	\$21,589	\$364,599	\$675,341	\$9,163	\$(432,022)	\$638,669

See Condensed Notes to Consolidated Financial Statements.

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

INFINITY PROPERTY AND CASUALTY CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Three months ended June 30,	
	2013	2012
Operating Activities:		
Net earnings	\$7,408	\$6,954
Adjustments:		
Depreciation	2,031	2,159
Amortization	5,091	2,353
Net realized gains on investments	(794)	(2,166)
Gain on disposal of property and equipment	(1)	(10)
Share-based compensation expense	1,446	968
Activity related to rabbi trust	(12)	(16)
Decrease (increase) in accrued investment income	(958)	505
Decrease (increase) in agents' balances and premium receivable	9,676	8,159
Decrease (increase) in reinsurance receivables	240	1,104
Decrease (increase) in deferred policy acquisition costs	3,824	1,076
Decrease (increase) in other assets	2,681	(4,086)
Increase (decrease) in unpaid losses and loss adjustment expenses	15,203	16,942
Increase (decrease) in unearned premium	(10,861)	(5,502)
Increase (decrease) increase in payable to reinsurers	0	(185)
Increase (decrease) in other liabilities	2,913	5,948
Net cash provided by operating activities	37,889	34,201
Investing Activities:		
Purchases of fixed maturities	(183,985)	(131,418)
Purchases of equity securities	(1,100)	0
Purchases of short-term investments	(3,616)	0
Purchases of property and equipment	(7,463)	(6,943)
Maturities and redemptions of fixed maturities	57,128	34,786
Proceeds from sale of fixed maturities	88,206	86,724
Proceeds from sale of equity securities	3,726	0
Net cash used in investing activities	(47,105)	(16,852)
Financing Activities:		
Proceeds from stock options exercised and employee stock purchases, including tax benefit	201	350
Principal payments under capital lease obligation	(145)	0
Acquisition of treasury stock	(5,167)	(7,037)
Dividends paid to shareholders	(3,453)	(2,644)
Net cash used in financing activities	(8,564)	(9,330)
Net (decrease) increase in cash and cash equivalents	(17,781)	8,020
Cash and cash equivalents at beginning of period	133,641	61,295
Cash and cash equivalents at end of period	\$115,861	\$69,314

See Condensed Notes to Consolidated Financial Statements.

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

INFINITY PROPERTY AND CASUALTY CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Six months ended June 30,	
	2013	2012
Operating Activities:		
Net earnings	\$ 16,070	\$ 11,248
Adjustments:		
Depreciation	4,053	4,086
Amortization	9,714	4,556
Net realized gains on investments	(4,617)	(2,405)
Loss on disposal of property and equipment	0	15
Share-based compensation expense	2,087	2,146
Activity related to rabbi trust	25	35
Decrease (increase) in accrued investment income	(858)	(102)
Decrease (increase) in agents' balances and premium receivable	(29,291)	(44,463)
Decrease (increase) in reinsurance receivables	(1,088)	(37)
Decrease (increase) in deferred policy acquisition costs	(4,017)	(9,959)
Decrease (increase) in other assets	4,478	(5,319)
Increase (decrease) in unpaid losses and loss adjustment expenses	39,110	35,469
Increase (decrease) in unearned premium	43,653	61,575
Increase (decrease) increase in payable to reinsurers	(137)	(45)
Increase (decrease) in other liabilities	205	(997)
Net cash provided by operating activities	79,386	55,803
Investing Activities:		
Purchases of fixed maturities	(490,415)	(255,436)
Purchases of equity securities	(1,100)	0
Purchases of short-term investments	(3,616)	0
Purchases of property and equipment	(9,231)	(7,585)
Maturities and redemptions of fixed maturities	103,282	81,993
Proceeds from sale of fixed maturities	280,935	123,542
Proceeds from sale of equity securities	7,244	0
Net cash used in investing activities	(112,901)	(57,487)
Financing Activities:		
Proceeds from stock options exercised and employee stock purchases, including tax benefit	728	833
Principal payments under capital lease obligation	(449)	0
Acquisition of treasury stock	(9,157)	(8,303)
Dividends paid to shareholders	(6,928)	(5,300)
Net cash used in financing activities	(15,806)	(12,770)
Net decrease in cash and cash equivalents	(49,321)	(14,453)
Cash and cash equivalents at beginning of period	165,182	83,767
Cash and cash equivalents at end of period	\$ 115,861	\$ 69,314

See Condensed Notes to Consolidated Financial Statements.

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2013

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| 3. <u>Fair Value</u> | 8. <u>Insurance Reserves</u> |
| 4. <u>Investments</u> | 9. <u>Commitments and Contingencies</u> |
| 5. <u>Long-Term Debt</u> | 10. <u>Accumulated Other Comprehensive Income</u> |

Note 1 Reporting and Accounting Policies

Nature of Operations

We are a holding company that, through subsidiaries, provides personal automobile insurance with a concentration on nonstandard auto insurance. Although licensed to write insurance in all 50 states and the District of Columbia, we focus on select states that we believe offer the greatest opportunity for premium growth and profitability.

Basis of Consolidation and Reporting

The accompanying consolidated financial statements are unaudited and should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2012. This Quarterly Report on Form 10-Q, including the Condensed Notes to Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations, focuses on our financial performance since the beginning of the year.

These financial statements reflect certain adjustments necessary for a fair presentation of our results of operations and financial position. Such adjustments consist of normal, recurring accruals recorded to match expenses with their related revenue streams and the elimination of all significant inter-company transactions and balances.

We have evaluated events that occurred after June 30, 2013 for recognition or disclosure in our financial statements and the notes to the financial statements.

Schedules may not foot due to rounding.

Estimates

We based certain accounts and balances within these financial statements upon our estimates and assumptions. The amount of reserves for claims not yet paid, for example, is an item that we can only record by estimation. Unrealized capital gains and losses on investments are subject to market fluctuations, and we use judgment in the determination of whether unrealized losses on certain securities are temporary or other-than-temporary. Should actual results differ significantly from these estimates, the effect on our results of operations could be material. The results of operations for the periods presented may not be indicative of our results for the entire year.

Recently Adopted Accounting Standards

Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income

In February 2013, the FASB issued guidance requiring expanded disclosures about amounts reclassified out of accumulated other comprehensive income (AOCI). Entities are required to present reclassifications by component when reporting changes in AOCI balances. The guidance requires the presentation of significant amounts reclassified out of AOCI by income statement line item. We adopted the new guidance as of March 31, 2013. The new guidance affects disclosures only and therefore had no impact on our results of operations or financial position.

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Condensed Notes to Consolidated Financial Statements

Note 2 Computation of Net Earnings per Share

The following table illustrates our computations of basic and diluted net earnings per common share (in thousands, except per share figures):

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Net earnings	\$7,408	\$6,954	\$16,070	\$11,248
Average basic shares outstanding	11,448	11,709	11,485	11,719
Basic net earnings per share	\$0.65	\$0.59	\$1.40	\$0.96
Average basic shares outstanding	11,448	11,709	11,485	11,719
Restricted stock not yet vested	47	23	45	22
Dilutive effect of assumed option exercises	31	99	34	105
Dilutive effect of Performance Share Plan	117	106	135	148
Average diluted shares outstanding	11,643	11,937	11,698	11,993
Diluted net earnings per share	\$0.64	\$0.58	\$1.37	\$0.94

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

Condensed Notes to Consolidated Financial Statements

Note 3 Fair Value

Fair values of instruments are based on:

- (i) quoted prices in active markets for identical assets (Level 1),
quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in
- (ii) markets that are not active and model-derived valuations in which all significant inputs are observable in active markets (Level 2) or
- (iii) valuations derived from valuation techniques in which one or more significant inputs are unobservable in the marketplace (Level 3).

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Condensed Notes to Consolidated Financial Statements

The following tables present, for each of the fair value hierarchy levels, our assets and liabilities for which we report fair value on a recurring basis (in thousands):

June 30, 2013	Fair Value			Total	
	Level 1	Level 2	Level 3		
Cash and cash equivalents	\$115,861	\$0	\$0	\$115,861	
Fixed maturity securities:					
U.S. government	75,897	227	3,124	79,248	
Government-sponsored entities	0	13,613	0	13,613	
State and municipal	0	458,522	0	458,522	
Mortgage-backed securities:					
Residential	0	284,338	0	284,338	
Commercial	0	38,828	0	38,828	
Total mortgage-backed securities	\$0	\$323,166	\$0	\$323,166	
Collateralized mortgage obligations	0	11,647	0	11,647	
Asset-backed securities	0	63,833	0	63,833	
Corporates	0	365,254	8,055	373,308	
Total fixed maturities	\$75,897	\$1,236,260	\$11,179	\$1,323,336	
Equity securities	70,077	0	0	70,077	
Short-term investments	\$3,616	\$0	\$0	\$3,616	
Total cash and investments	\$265,451	\$1,236,260	\$11,179	\$1,512,890	
Percentage of total cash and investments	17.5	% 81.7	% 0.7	% 100.0	%

December 31, 2012	Fair Value			Total	
	Level 1	Level 2	Level 3		
Cash and cash equivalents	\$165,182	\$0	\$0	\$165,182	
Fixed maturity securities:					
U.S. government	81,529	296	3,712	85,537	
Government-sponsored entities	0	22,140	0	22,140	
State and municipal	0	457,113	0	457,113	
Mortgage-backed securities:					
Residential	0	281,907	0	281,907	
Commercial	0	13,768	0	13,768	
Total mortgage-backed securities	\$0	\$295,675	\$0	\$295,675	
Collateralized mortgage obligations	0	19,307	0	19,307	
Asset-backed securities	0	79,257	0	79,257	
Corporates	0	353,697	9,101	362,797	
Total fixed maturities	\$81,529	\$1,227,486	\$12,813	\$1,321,828	
Equity securities	73,106	0	0	73,106	
Total cash and investments	\$319,817	\$1,227,486	\$12,813	\$1,560,116	
Percentage of total cash and investments	20.5	% 78.7	% 0.8	% 100.0	%

We do not report our long-term debt at fair value in the Consolidated Balance Sheets. The \$272.8 million and \$288.9 million fair value of our long-term debt at June 30, 2013 and December 31, 2012, respectively, would be included in Level 2 of the fair value hierarchy if it were reported at fair value.

Level 1 includes cash and cash equivalents, U.S. Treasury securities, an exchange-traded fund and equities invested in a rabbi trust. Level 2 includes securities whose fair value was determined using observable market inputs. Level 3 securities are

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INFINITY PROPERTY AND CASUALTY CORPORATION FORM 10-Q

Condensed Notes to Consolidated Financial Statements

comprised of (i) securities for which there is no active or inactive market for similar instruments, (ii) securities whose fair value is determined based on unobservable inputs and (iii) securities, other than those backed by the U.S. Government, that are not rated by a nationally recognized statistical rating organization ("NRSRO"). We recognize transfers between levels at the beginning of the reporting period.

A third party nationally recognized pricing service provides the fair value of securities in Level 2. We review the third party pricing methodologies quarterly and test for significant differences between the market price used to value the security and recent sales activity.

The following tables present the changes in the Level 3 fair value category (in thousands):

	Three months ended June 30, 2013						
	U.S. Government	State and Municipal	Mortgage-Backed Securities	Collateralized Mortgage Obligations	Corporates	ABS	Total
Balance at beginning of period	\$3,115	\$0	\$0	\$0	\$8,899	\$0	\$12,014
Total gains or (losses), unrealized or realized							
Included in net earnings	(9	) 0	0	0	350	0	341
Included in other comprehensive income	18	0	0	0	(216	) 0	(198
Settlements	0	0	0	0	(979	) 0	(979
Balance at end of period	\$3,124	\$0	\$0	\$0	\$8,055	\$0	\$11,179

	Three months ended June 30, 2012						
	U.S. Government	State and Municipal	Mortgage-Backed Securities	Collateralized Mortgage Obligations	Corporates	ABS	Total
Balance at beginning of period	\$3,897	\$0	\$0	\$499	\$9,644	\$0	\$14,040
Total gains or (losses), unrealized or realized							
Included in net earnings	(39	) (15	) 0	0	181	0	128
Included in other comprehensive income	41	(16	) 32	1	86	1	146
Purchases	0	0	7,156	0	0	1,360	8,516
Settlements	0	0	0	(14	) (915	) 0	(929
Transfers in	0	2,781	0	0	969	0	3,749
Balance at end of period	\$3,899	\$2,750	\$7,188	\$486	\$9,966	\$1,361	\$25,651

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	Six months ended June 30, 2013						Total
	U.S. Government	State and Municipal	Mortgage-Backed Securities	Collateralized Mortgage Obligations	Corporates	ABS	
Balance at beginning of period	\$3,712	\$0	\$0	\$0	\$9,101	\$0	\$12,813
Total gains or (losses), unrealized or realized							
Included in net earnings	(31	) 0	0	0	472	0	441
Included in other comprehensive income	(71	) 0	0	0	(321	) 0	(393)
Settlements	(485	) 0	0	0	(1,197	) 0	(1,682)
Balance at end of period	\$3,124	\$0	\$0	\$0	\$8,055	\$0	\$11,179
	Six months ended June 30, 2012						
	U.S. Government	State and Municipal	Mortgage-Backed Securities	Collateralized Mortgage Obligations	Corporates	ABS	Total
Balance at beginning of period	\$4,438	\$0	\$0	\$509	\$10,426	\$0	\$15,374
Total gains or (losses), unrealized or realized							
Included in net earnings	(70	) (15	) 0	0	62	0	(22)
Included in other comprehensive income	(13	) (16	) 32	4	233	1	241
Purchases	0	0	7,156	0	0	1,360	8,516
Sales	0	0	0	0	(253	) 0	(253)
Settlements	(456	) 0	0	(26	) (1,268	) 0	(1,751)
Transfers in	0	2,781	0	0	1,836	0	4,617
Transfers out	0	0	0	0	(1,070	) 0	(1,070)
Balance at end of period	\$3,899	\$2,750	\$7,188	\$486	\$9,966	\$1,361	\$25,651

Of the \$11.2 million fair value of securities in Level 3 at June 30, 2013, which consists of 12 securities, we priced five based on non-binding broker quotes, four prices were provided by our unaffiliated money managers and one security, which is included in Level 3 because it is not rated by a nationally recognized statistical rating organization, was priced by a nationally recognized pricing service. We manually calculated the remaining two securities, which have a combined fair value of \$0.7 million.

Quantitative information about the significant unobservable inputs used in the fair value measurement of these manually priced securities at June 30, 2013 is as follows (in millions):

	Fair Value	Valuation Technique	Unobservable Input	Value Used
Corporate bond	\$0.1	Recovery rate ¹	Probability of default	100%
Corporate bond	0.6	Discounted cash flow	Comparable credit rating ²	CCC
Total	\$0.7			

¹ Recovery rate for senior unsecured bonds as indicated in Moody's Investor's Service Annual Default Study: Corporate Default and Recovery Rates, 1920-2012.

² This bond is not rated, but is supported by JC Penney Corporation trust assets; therefore a JC Penney comparable bond rating is used.

The significant unobservable inputs used in the fair value measurement of our manually-priced corporate bonds are a probability of default assumption and an assigned credit rating. Significant changes in either of these inputs in isolation could result in a significant change in fair value measurement for these corporate bonds. Generally, a reduction in probability of

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default would increase security valuation. A change in the credit rating assumption would change the yield spread associated with that bond, and thus the yield used in discounting the cash flows to arrive at the security's valuation. There were no transfers between Levels 1, 2 or 3 during the six months ended June 30, 2013.

The gains or losses included in net earnings are included in the line item net realized gains on investments in the Consolidated Statements of Earnings. We recognize the net gains or losses included in other comprehensive income in the line item unrealized gains (losses) on investments, net in the Consolidated Statements of Comprehensive Income and the line item change in unrealized gain on investments or the line item change in non-credit component of impairment losses on fixed maturities in the Consolidated Statements of Changes in Shareholders' Equity.

The following table presents the carrying value and estimated fair value of our financial instruments (in thousands):

	June 30, 2013		December 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Cash and cash equivalents	\$ 115,861	\$ 115,861	\$ 165,182	\$ 165,182
Investments				
Fixed maturities	1,323,336	1,323,336	1,321,828	1,321,828
Equity securities	70,077	70,077	73,106	73,106
Short-term	\$3,616	\$3,616	\$0	\$0
Total cash and investments	\$1,512,890	\$1,512,890	\$1,560,116	\$1,560,116
Liabilities:				
Long-term debt	\$275,000	\$272,767	\$275,000	\$288,879

See Note 4 to the Consolidated Financial Statements for additional information on investments and Note 5 for additional information on long-term debt.

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Note 4 Investments

We consider all fixed maturity and equity securities to be available-for-sale and report them at fair value with the net unrealized gains or losses reported after-tax (net of any valuation allowance) as a component of other comprehensive income. The proceeds from sales of securities for the three and six months ended June 30, 2013 were \$91.9 million and \$288.2 million, respectively. The proceeds from sales of securities for the three and six months ended June 30, 2012 were \$86.7 million and \$123.5 million, respectively. The proceeds for the six months ended June 30, 2013 were net of \$5.4 million of receivable for securities sold during the second quarter of 2013 that had not settled at June 30, 2013.

Gains or losses on securities are determined on a specific identification basis.

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Summarized information for the major categories of our investment portfolio follows (in thousands):

June 30, 2013

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	OTTI Recognized in Accumulated OCI ⁽¹⁾
Fixe					