

INFINITY PROPERTY & CASUALTY CORP
Form 10-Q
August 07, 2006
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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, 2006

OR

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly 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, Birmingham, Alabama 35243

03-0483872
(I.R.S. Employer

Identification No.)

(Address of principal executive offices and zip code)

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(205) 870-4000

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large Accelerated Filer Accelerated filer Non-accelerated filer

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 August 1, 2006, there were 20,271,573 shares of the Registrant's Common Stock outstanding.

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Exhibit 31.2 -	Certification of the Chief Financial Officer Pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002
Exhibit 32 -	Certification of the Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Table of Contents**INFINITY PROPERTY AND CASUALTY CORPORATION 10-Q****PART I****FINANCIAL INFORMATION****ITEM 1****Financial Statements****INFINITY 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		
	2006	2005	% Change	2006	2005	% Change
Revenues:						
Earned premiums	\$ 235,863	\$ 248,028	(4.9)%	\$ 469,895	\$ 478,769	(1.9)%
Net investment income	17,670	16,124	9.6%	34,551	32,734	5.6%
Realized gains (losses) on investments	(61)	8,431	(100.7)%	14	20,511	(99.9)%
Other income	567	952	(40.4)%	1,295	2,160	(40.0)%
Total revenues	254,039	273,535	(7.1)%	505,755	534,174	(5.3)%
Costs and Expenses:						
Losses and loss adjustment expenses	159,327	172,832	(7.8)%	308,193	339,776	(9.3)%
Commissions and other underwriting expenses	59,291	57,546	3.0%	113,014	109,703	3.0%
Interest expense	2,766	2,765	0.0%	5,531	5,530	0.0%
Corporate general and administrative expenses	1,857	1,566	18.6%	3,778	3,242	16.5%
Other expenses	1,148	3,157	(63.6)%	1,883	3,651	(48.4)%
Total costs and expenses	224,389	237,866	(5.7)%	432,399	461,902	(6.4)%
Earnings before income taxes	29,650	35,669	(16.9)%	73,356	72,272	1.5%
Provision for income taxes	9,669	11,979	(19.3)%	24,309	24,600	(1.2)%
Net Earnings	\$ 19,981	\$ 23,690	(15.7)%	\$ 49,047	\$ 47,672	2.9%
Earnings per Common Share:						
Basic	\$ 0.97	\$ 1.15	(15.7)%	\$ 2.38	\$ 2.31	3.0%
Diluted	0.96	1.13	(15.0)%	2.35	2.28	3.1%
Average number of Common Shares:						
Basic	20,582	20,646	(0.3)%	20,628	20,627	0.0%
Diluted	20,797	20,882	(0.4)%	20,863	20,880	(0.1)%
Cash dividends per Common Share	\$ 0.075	\$ 0.06	25.0%	\$ 0.15	\$ 0.12	25.0%

See Notes to Consolidated Financial Statements

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	June 30, 2006 (unaudited)	December 31, 2005
Assets		
Investments		
Fixed maturities - at fair value (amortized cost - \$1,304,378 and \$1,327,980)	\$ 1,272,439	\$ 1,323,045
Equity securities - at fair value (amortized cost - \$66,047 and \$60,380)	65,619	59,706
Total investments	1,338,058	1,382,751
Cash and cash equivalents	68,311	64,934
Accrued investment income	16,259	16,779
Agents' balances and premiums receivable, net of allowances for doubtful accounts of \$11,920 and \$11,859	310,020	289,917
Prepaid reinsurance premiums	7,552	9,008
Recoverables from reinsurers	19,362	19,364
Deferred policy acquisition costs	73,436	70,380
Current and deferred income taxes	41,890	29,519
Prepaid expenses, deferred charges and other assets	16,358	13,801
Goodwill	75,275	75,275
Total assets	\$ 1,966,521	\$ 1,971,728
Liabilities and Shareholders' Equity		
Liabilities:		
Unpaid losses and loss adjustment expenses	\$ 592,129	\$ 625,492
Unearned premiums	417,880	402,198
Payable to reinsurers	61	3,319
Long term debt (fair value - \$186,547 and \$195,341)	199,397	199,366
Commissions payable	29,011	28,345
Accounts payable, accrued expenses and other liabilities	84,889	86,414
Total liabilities	1,323,367	1,345,134
Shareholders' Equity:		
Common stock, no par value -50,000,000 shares authorized -20,815,752 and 20,727,939 shares issued	20,823	20,728
Additional paid-in capital	334,771	331,511
Retained earnings	325,124	279,171
Unearned compensation (restricted stock)		(30)
Net unrealized loss	(21,043)	(3,648)
Treasury stock, at cost (404,951 and 34,014 shares)	(16,521)	(1,138)

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Total shareholders' equity	643,154	626,594
Total liabilities and shareholders' equity	\$ 1,966,521	\$ 1,971,728

See Notes to Consolidated Financial Statements

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	Common Stock	Additional Paid-in Capital	Retained Earnings	Unearned Compensation (Restricted Stock)	Unrealized Gain (Loss)	Treasury Stock	Total
Balance at December 31, 2004	\$ 20,671	\$ 329,994	\$ 166,710	\$ (314)	\$ 30,360	\$	\$ 547,421
Net earnings	\$	\$	\$ 47,672	\$	\$	\$	\$ 47,672
Change in unrealized gain (loss)					(17,014)		(17,014)
Comprehensive income							\$ 30,658
Dividends paid to common shareholders			(2,482)				(2,482)
Employee stock purchases	5	137					142
Exercise of stock options including tax benefit	22	337					359
Stock granted to directors	4	121					125
Acquisition of treasury stock						(138)	(138)
Amortization of unearned compensation including tax benefit		254		165			419
Balance at June 30, 2005	\$ 20,702	\$ 330,843	\$ 211,900	\$ (149)	\$ 13,346	\$ (138)	\$ 576,504
Net earnings	\$	\$	\$ 58,636	\$	\$	\$	\$ 58,636
Change in unrealized gain (loss)					(16,994)		(16,994)
Comprehensive income							\$ 41,642
Dividends paid to common shareholders			(2,483)				(2,483)
Employee stock purchases	5	131					136
Exercise of stock options including tax benefit	21	396					417
Stock granted to directors							
Acquisition of treasury stock						(1,000)	(1,000)
Amortization of unearned compensation including tax benefit		141		119			260
Correction of an immaterial error related to prior periods			11,118				11,118
Balance at December 31, 2005	\$ 20,728	\$ 331,511	\$ 279,171	\$ (30)	\$ (3,648)	\$ (1,138)	\$ 626,594
Net earnings	\$	\$	\$ 49,047	\$	\$	\$	\$ 49,047
Change in unrealized gain (loss)					(17,395)		(17,395)
Comprehensive income							\$ 31,652
Dividends paid to common shareholders			(3,094)				(3,094)
Employee stock purchases	4	119					123
Exercise of stock options, including tax benefit and compensation expense	88	2,661					2,749

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Stock granted to directors	3	122						125
Acquisition of treasury stock						(15,384)		(15,384)
Amortization of unearned compensation including tax benefit		358			30			388
Balance at June 30, 2006		\$ 20,823	\$ 334,771	\$ 325,124	\$	\$ (21,043)	\$ (16,521)	\$ 643,154

See Notes to Consolidated Financial Statements

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	For the Three Months Ended	
	June 30,	
	2006	2005
Operating Activities:		
Net earnings	\$ 19,981	\$ 23,690
Adjustments:		
Depreciation and amortization	1,098	3,297
Realized (gains) losses on investing activities	61	(8,431)
Share-based compensation expense	252	
Decrease (increase) in accrued investment income	(1,195)	399
Decrease (increase) in agents balances & premiums receivable	4,315	(5,026)
Decrease (increase) in reinsurance receivables	(17)	6,677
Decrease (increase) in deferred policy acquisition costs	2,628	(1,431)
Decrease (increase) in other assets	(9,640)	2,701
Increase (decrease) in insurance claims and reserves	(18,760)	(5,264)
Increase (decrease) in payable to reinsurers	(653)	380
Increase (decrease) in other liabilities	3,756	(1,903)
Other, net	124	83
Net cash provided by operating activities	1,950	15,172
Investing Activities:		
Purchases of and additional investments in:		
Fixed maturities	(51,884)	(84,605)
Equity Securities	(10,679)	(19,192)
Property and equipment	(1,421)	(2,091)
Maturities and redemptions of fixed maturity investments	22,448	34,564
Sales:		
Fixed maturities	36,856	185,161
Equity securities	3,709	2,309
Property and equipment		270
Net cash (used in) provided by investing activities	(971)	116,416
Financing Activities:		
Proceeds from stock option exercise and employee stock purchase plan	989	166
Acquisition of treasury stock	(11,588)	(5)
Dividends paid to shareholders	(1,542)	(1,241)
Net cash used in financing activities	(12,141)	(1,080)
Net (decrease) increase in cash and cash equivalents	(11,162)	130,508
Cash and cash equivalents at beginning of period	79,473	96,761

Cash and cash equivalents at end of period	\$ 68,311	\$ 227,269
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See Notes to Consolidated Financial Statements

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	For the Six Months Ended June 30,	
	2006	2005
Operating Activities:		
Net earnings	\$ 49,047	\$ 47,672
Adjustments:		
Depreciation and amortization	3,188	7,396
Realized (gains) losses on investing activities	(14)	(20,511)
Share-based compensation expense	503	
Decrease (increase) in accrued investment income	520	1,576
Decrease (increase) in agents balances & premiums receivable	(20,103)	(41,959)
Decrease (increase) in reinsurance receivables	1,458	5,533
Decrease (increase) in deferred policy acquisition costs	(3,056)	(10,729)
Decrease (increase) in other assets	(5,146)	10,054
Increase (decrease) in insurance claims and reserves	(17,681)	21,121
Increase (decrease) in payable to reinsurers	(3,258)	301
Increase (decrease) in other liabilities	549	2,329
Other, net	480	81
Net cash provided by operating activities	6,487	22,864
Investing Activities:		
Purchases of and additional investments in:		
Fixed maturities	(98,648)	(246,400)
Equity Securities	(18,696)	(27,933)
Property and equipment	(1,831)	(3,435)
Maturities and redemptions of fixed maturity investments	60,165	60,669
Sales:		
Fixed maturities	58,028	300,907
Equity securities	13,978	10,363
Property and equipment		301
Net cash provided by investing activities	12,996	94,472
Financing Activities:		
Proceeds from stock option exercise and employee stock purchase plan	2,372	501
Acquisition of treasury stock	(15,384)	(138)
Dividends paid to shareholders	(3,094)	(2,482)
Net cash used in financing activities	(16,106)	(2,119)
Net increase in cash and cash equivalents	3,377	115,217
Cash and cash equivalents at beginning of period	64,934	112,052

Cash and cash equivalents at end of period	\$ 68,311	\$ 227,269
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See Notes to Consolidated Financial Statements

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INFINITY PROPERTY AND CASUALTY CORPORATION 10-Q

Notes to Consolidated Financial Statements

Note 1 Reporting and Accounting Policies

The accompanying Consolidated Financial Statements are unaudited and should be read in conjunction with Infinity Property and Casualty Corporation's (Infinity or the Company) Annual Report on Form 10-K for the year ended December 31, 2005. This Quarterly Report on Form 10-Q, including the Notes to the Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations, focuses on Infinity's financial performance since the beginning of the year.

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

Certain accounts and balances within these financial statements are based upon management's estimates and assumptions. The amount of reserves for claims not yet paid, for example, is an item that can only be recorded by estimation. Unrealized capital gains and losses on investments are subject to market fluctuations, and managerial judgment is required 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 effects on Infinity's results of operations could be material. The results of operations for the periods presented may not be indicative of the Company's results for the entire year.

Reclassifications

In addition, certain reclassification adjustments have been made to historical results to achieve consistency in presentation.

Effective January 1, 2006, as discussed in the Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's Annual Report on Form 10-K, Infinity began including in the GAAP combined ratio corporate litigation expense on losses (except for class action lawsuits) and bad debt charge-offs on agents' balances and premiums receivable. The reclassification of corporate litigation expense on losses for the three-month and six-month periods ending June 30, 2005 was \$1.6 million and \$7.3 million, respectively, which is reflected in the Consolidated Statements of Earnings as a decrease in other expenses and an increase in losses and loss adjustment expenses (LAE), and \$6.6 million and \$14.2 million, respectively, reflected in the Consolidated Statements of Cash Flows for the corresponding periods ended June 30, 2005 between change in insurance claims and reserves and change in other liabilities. The reclassification also included other immaterial amounts reflected in the Consolidated Balance Sheets and Statements of Cash Flows for the same periods. The reclassification of bad debt charge-offs on agents' balances and premiums receivable for the three-month and six-month periods ending June 30, 2005 was \$5.6 million and \$8.6 million, respectively, which is reflected in the Consolidated Statements of Earnings as a decrease in other expenses and an increase in commissions and other underwriting expenses. Neither reclassification impacted the current period or any previously presented period net earnings, shareholders equity or net cash provided by operating activities.

New Accounting Standards

Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of Statement of Financial Accounting Standard No. 109 (SFAS 109), was issued by the FASB in June 2006 effective for fiscal years beginning after December 15, 2006. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS 109. SFAS 109 does not prescribe a recognition threshold or measurement attribute for the financial statement recognition and measurement of a tax position taken in a tax return. Additionally, FIN 48 provides guidance on measurement, derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. We will adopt the provisions of FIN 48 effective January 1, 2007. We have not yet determined the impact of the adoption of FIN 48 on our financial position or results of operation.

Note 2 Share-Based Compensation

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS 123(R)). SFAS 123(R) requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors including employee stock options and employee stock purchases related to the Employee Stock Purchase Plan (ESPP) based on estimated fair values. SFAS 123(R) supersedes the Company's previous accounting under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25), for periods beginning in fiscal 2006. In accordance with the modified prospective

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transition method as set forth in SFAS 123(R), the Company's Consolidated Financial Statements for prior periods have not been restated to reflect, and do not include, the impact of compensation expense for all share-based payment awards. As previously allowed under APB 25, no share-based compensation expense related to employee stock options and employee stock purchases was recognized during the six months of 2005.

As permitted by SFAS 123(R), the Company used the Black-Scholes model to estimate the value of employee stock options on the date of grant, though no options have been granted since the Company adopted SFAS 123(R). Prior to the adoption of SFAS 123(R), the value of each employee stock option was estimated on the date of grant using the Black-Scholes model for the purpose of the pro-forma financial information in accordance with SFAS 123. The determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the expected stock price volatility over the term of the awards and projected employee stock option exercise behavior.

Restricted Stock Plans

Infinity's Restricted Stock Plan was established in 2002. There were 500,000 shares of Infinity common stock reserved for issuance under the Restricted Stock Plan, of which 134,375 shares have been issued as of June 30, 2006. The fair value of shares issued under Infinity's Restricted Stock Plan is recorded as unearned compensation and expensed over the vesting periods of the awards. In February 2006, 44,792 shares of restricted stock vested under Infinity's Restricted Stock Plan. Consequently, as of June 30, 2006 the Company had no unvested restricted stock outstanding and therefore no related unearned compensation.

In May 2005, Infinity's shareholders approved the Non-Employee Directors' Stock Ownership Plan (Directors Plan). There were 200,000 shares of Infinity common stock reserved for issuance under the Directors Plan, of which 6,895 shares have been issued as of June 30, 2006. The purpose of the Directors Plan is to include Infinity common stock as part of the compensation provided to its non-employee directors. Under the terms of the Directors Plan, shares are granted on or about June 1 of each year and are restricted from sale or transfer by any recipient for six months from the date of grant. On June 1, 2006, a total of 2,990 shares of Infinity common stock, valued pursuant to the plan at \$125,000, were issued to Infinity's non-employee directors.

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Infinity established the Employee Stock Purchase Plan in 2004. Under this plan, all eligible full-time employees may purchase shares of Infinity common stock at a 15% discount to the current market price. Employees may allocate up to 25% of their base salary with a maximum annual participation amount of \$25,000. The source of shares issued to participants is treasury shares and/or authorized but previously unissued shares. The maximum number of shares which may be issued under the ESPP may not exceed 1,000,000, of which 15,606 have been issued as of June 30, 2006. Infinity's ESPP is qualified under Section 423 of the Internal Revenue Code of 1986, as amended. The 15% discount approximated \$10,000 and \$22,000 for the three-month and six-month periods ended June 30, 2006, respectively, and was recognized as compensation expense in the Consolidated Statements of Earnings in each period. Participants' shares are issued and outstanding for earnings per share calculations.

Stock Option Plan

Infinity's Stock Option Plan was established in 2002 with 2,000,000 shares of Infinity common stock reserved for issuance under the Stock Option Plan. Through June 30, 2006, net of forfeitures, 615,280 options have been issued. The plan allows forfeited options to be reissued. Options, which have a 10-year contractual life, generally become exercisable at the rate of 20% per year commencing one year after grant.

The following chart describes activity for Infinity's Stock Option Plan for the six month period ending June 30, 2006:

Options Outstanding	Number of Options	Weighted Average Exercise Price
As of January 1, 2006	555,584	\$ 22.31
Granted		
Exercised (a)	(81,268)	17.95
Forfeited		
As of June 30, 2006	474,316	\$ 23.06

(a) Cash received from the exercise of options for the six-month period ended June 30, 2006 was \$1,459 (in thousands).

The following chart describes by exercise price Infinity's stock options outstanding and exercisable as of June 30, 2006 (dollars in thousands):

Exercise Price	Options Outstanding		Options Exercisable		Remaining Contractual Life (in years)
	Number of Options	Intrinsic Value (a)	Options Exercisable	Intrinsic Value (a)	
\$ 16.00	281,316	\$ 7,033	129,644	\$ 3,241	6.6
25.56	5,000	77	5,000	77	7.2
33.58	185,500	1,376	74,800	555	7.6
31.94	2,500	23	2,500	23	8.0
	474,316	\$ 8,509	211,944	\$ 3,896	

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- (a) Intrinsic value (in thousands) represents the total pre-tax intrinsic value, based on the Company's closing stock price of \$41.00 on June 30, 2006, which would have been received by the option holders had all option holders exercised and sold their options as of that date.

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The following table illustrates the assumptions used to obtain, for the current period, the share-based compensation expense, and for the prior year, the pro-forma share-based compensation expense.

Assumptions:	As of June 30,	
	2006	2005
Options issued less all forfeitures	615,280	615,280
Add: Vested forfeitures	2,900	2,900
Options issued less non-vested forfeitures	618,180	618,180
Weighted average fair value per option granted (a)	\$ 8.56	\$ 8.56
Weighted average per option issued less non-vested forfeitures:		
Dividend yield	1.1%	1.1%
Expected volatility	33.0%	33.0%
Risk-free interest rate	4.1%	4.1%
Expected option life	7.5 years	7.5 years

(a) No options were granted during 2005 or during the six-month period ending June 30, 2006.

The following table shows the effects on net earnings and earnings per share had the fair value method been applied to all outstanding awards in each of the years 2006 and 2005 (in thousands).

	Three months ended		Six months ended	
	June 30,		June 30,	
	2006	2005	2006	2005
Net earnings, as reported	\$ 19,981	\$ 23,690	\$ 49,047	\$ 47,672
Share-based compensation expense included in reported net earnings (a)	252		503	
Other	88			
Compensation expense included in net earnings, net of tax effects	340		503	
Total share-based compensation expense under fair value method for all awards (b)	(252)	(241)	(503)	(485)
Other	(88)	(85)		
Compensation expense, net of tax effects	(340)	(326)	(503)	(485)
Net earnings, including the effects of share-based compensation expense (c)	\$ 19,981	\$ 23,364	\$ 49,047	\$ 47,187
Basic earnings per share				
As reported (a)	\$ 0.97	\$ 1.15	\$ 2.38	\$ 2.31
Pro-forma (c)	N/A	1.13	N/A	2.29
Diluted earnings per share				
As reported (a)	\$ 0.96	\$ 1.13	2.35	\$ 2.28
Pro-forma (c)	N/A	1.12	N/A	2.26

(a) Net earnings and earnings per share prior to fiscal year 2006 did not include share-based compensation expense for employee stock options and employee stock purchases under SFAS 123 because the Company did not at the time adopt the recognition provisions of SFAS 123.

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- (b) Share-based compensation expense prior to fiscal year 2006 is calculated based on pro-forma application of SFAS 123.
- (c) Net earnings and net earnings per share prior to fiscal year 2006 represent pro-forma information based on the application of SFAS 123.

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The following table provides the computations of Infinity's basic and diluted earnings per common share (in thousands, except per share figures):

	For the three months ended June 30,		For the six months ended June 30,	
	2006	2005	2006	2005
Net earnings for basic and diluted earnings per share	\$ 19,981	\$ 23,690	\$ 49,047	\$ 47,672
Average basic shares outstanding	20,582	20,646	20,628	20,627
Basic earnings per share (a)	\$ 0.97	\$ 1.15	\$ 2.38	\$ 2.31
Average basic shares outstanding	20,582	20,646	20,628	20,627
Restricted stock not yet vested		45	12	57
Dilutive effect of assumed option exercises	215	191	223	196
Average diluted shares outstanding	20,797	20,882	20,863	20,880
Diluted earnings per share	\$ 0.96	\$ 1.13	\$ 2.35	\$ 2.28

(a) The prior-year basic and diluted earnings per share exclude the effects of share-based compensation expense as calculated in accordance with SFAS 123 on a pro-forma basis. See Note 2 for additional information.

Note 4 Long-Term Debt

In February 2004, Infinity issued \$200 million principal of senior notes due February 2014 (the Senior Notes). The Senior Notes accrue interest at an effective yield of 5.55% and bear a coupon of 5.5%, payable semiannually. At the time the Senior Notes were issued, Infinity capitalized \$2.1 million of debt issuance costs, which are being amortized over the term of the Senior Notes. The June 30, 2006 fair value for the Senior Notes of \$186.5 million was calculated using a 150 basis point spread to the ten-year U.S. Treasury Note of 5.14%, which was obtained from Bloomberg, a national broker quotation network.

In August 2005, Infinity entered into an agreement for a \$50 million three-year revolving credit facility that includes requirements to meet certain financial and other covenants. Infinity is currently in compliance with all covenants under the agreement. Under this agreement, there were no borrowings outstanding at June 30, 2006.

Note 5 Investments

Summarized information for Infinity's investment portfolio follows (in thousands):

	Amortized Cost	Fair Value	June 30, 2006	Gross Unrealized	
			% of Total Fair Value	Gain	Loss
Fixed maturities	\$ 1,304,378	\$ 1,272,439	95%	\$ 4,884	\$ (36,823)
Equity securities	66,047	65,619	5%	3,891	(4,319)
Total	\$ 1,370,425	\$ 1,338,058	100%	\$ 8,775	\$ (41,142)

	Amortized Cost	Fair Value	December 31, 2005 % of Total Fair Value	Gross Unrealized Gain	Gross Unrealized Loss
Fixed maturities	\$ 1,327,980	\$ 1,323,045	96%	\$ 11,589	\$ (16,524)
Equity securities	60,380	59,706	4%	1,870	(2,544)
Total	\$ 1,388,360	\$ 1,382,751	100%	\$ 13,459	\$ (19,068)

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	June 30, 2006	December 31, 2005
Number of positions held with unrealized:		
Gains	116	220
Losses	379	306
Number of positions held that individually exceed unrealized:		
Gains of \$500,000		1
Losses of \$500,000	7	
Percentage of positions held with unrealized:		
Gains that were investment grade	76%	82%
Losses that were investment grade	93%	94%

The following table sets forth the amount of unrealized loss by age and severity at June 30, 2006 (in thousands):

Age of unrealized loss:	Fair Value of Securities with Unrealized Losses	Total Gross Unrealized Losses	Greater than		
			Less than 5%*	5% to 10%*	10%*
Less than or equal to:					
Three months	\$ 106,182	\$ (2,428)	\$ (941)	\$ (1,487)	\$
Six months	167,414	(3,827)	(3,542)	(285)	
Nine months	102,846	(5,606)	(1,518)	(4,088)	
Twelve months	419,399	(17,064)	(10,768)	(6,296)	
Greater than twelve months	296,264	(12,217)	(9,009)	(3,208)	
Total	\$ 1,092,105	\$ (41,142)	\$ (25,778)	\$ (15,364)	\$

* As compared to amortized cost.

The change in unrealized gains (losses) on marketable securities included the following (in thousands):

	Fixed Maturities	Pre-tax Equity Securities	Tax Effects	Net
Six months ended June 30, 2006				
Unrealized holding gains (losses) on securities arising during the period	\$ (27,940)	\$ 1,195	\$ 9,359	\$ (17,386)
Realized (gains) losses included in net income	936	(950)	5	(9)
Change in unrealized gains (losses) on marketable securities, net	\$ (27,004)	\$ 245	\$ 9,364	\$ (17,395)
Six months ended June 30, 2005				
Unrealized holding gains (losses) on securities arising during the period	\$ (6,720)	\$ 1,071	\$ 1,967	\$ (3,682)
Realized (gains) losses included in net income	(16,806)	(3,705)	7,179	(13,332)
Change in unrealized gains (losses) on marketable securities, net	\$ (23,526)	\$ (2,634)	\$ 9,146	\$ (17,014)

Table of Contents**INFINITY PROPERTY AND CASUALTY CORPORATION 10-Q****Notes to Consolidated Financial Statements****Note 6 Effective Tax Rate**

As shown below, income tax expense for the three-month and six-month periods ended June 30, 2006 was \$9.7 million and \$24.3 million, respectively, compared to \$12.0 million and \$24.6 million for the same periods of 2005. The following table reconciles Infinity's statutory federal income tax rate to its effective tax rate (in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2006	2005	2006	2005
Earnings before income taxes	\$ 29,650	\$ 35,669	\$ 73,356	\$ 72,272
Incomes taxes at statutory rates	10,378	12,484	25,675	25,295
Effect of:				
Dividends received deduction	(66)	(75)	(146)	(124)
Tax-exempt interest	(505)	(518)	(1,012)	(1,009)
Adjustment to valuation allowance	(355)		(427)	
Other	217	88	219	438
Provision for income taxes as show on the Consolidated Statements of Earnings	\$ 9,669	\$ 11,979	\$ 24,309	\$ 24,600