EVEREST REINSURANCE HOLDINGS INC
Form 10-Q
November 14, 2012

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

QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED: September 30, 2012	Commission file number: 1-14527

EVEREST REINSURANCE HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	22-3263609 (I.R.S. Employer Identification No.)

477 Martinsville Road
Post Office Box 830
Liberty Corner, New Jersey 07938-0830
(908) 604-3000

(Address, including zip code, and telephone number, including area code,
of registrant's principal executive office)

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 during the preceding 12 months (or for such shorter period that the 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 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 X (Do not check if smaller reporting company)	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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Number of Shares Outstanding At November 1, 2012
Common Shares, $0.01 par value	1,000

The Registrant meets the conditions set forth in General Instruction H (1)(a) and (b) of Form 10-Q and is therefore filing this form with the reduced disclosure format permitted by General Instruction H of Form 10-Q.

EVEREST REINSURANCE HOLDINGS, INC.

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Part I

ITEM 1. FINANCIAL STATEMENTS

EVEREST REINSURANCE HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except par value per share)	September 30, 2012 (unaudited)	December 31, 2011
ASSETS:		
Fixed maturities - available for sale, at market value	$ 5,326,118	$ 5,107,028
(amortized cost: 2012, $5,060,968; 2011, $4,880,654)		
Fixed maturities - available for sale, at fair value	52,217	113,606
Equity securities - available for sale, at market value (cost: 2012, $15; 2011, $15)	13	10
Equity securities - available for sale, at fair value	1,247,445	1,207,053
Short-term investments	640,698	423,663
Other invested assets (cost: 2012, $420,510; 2011, $379,342)	420,510	379,342
Other invested assets, at fair value	1,039,648	817,352
Cash	309,059	348,267
Total investments and cash	9,035,708	8,396,321
Accrued investment income	56,639	55,849
Premiums receivable	990,571	856,375
Reinsurance receivables - unaffiliated	633,893	570,128
Reinsurance receivables - affiliated	2,851,472	2,901,174
Funds held by reinsureds	153,312	176,156
Deferred acquisition costs	90,088	166,806
Prepaid reinsurance premiums	597,498	625,391
Deferred tax asset	208,090	366,490
Income taxes recoverable	16,153	39,014
Other assets	235,593	195,476
TOTAL ASSETS	$ 14,869,017	$ 14,349,180
LIABILITIES:		
Reserve for losses and loss adjustment expenses	$ 7,954,633	$ 8,290,619
Unearned premium reserve	1,143,252	1,239,705
Funds held under reinsurance treaties	84,798	123,479
Losses in the course of payment	93,575	11,002
Commission reserves	32,979	40,353
Other net payable to reinsurers	894,866	629,871
5.4% Senior notes due 10/15/2014	249,894	249,858
6.6% Long term notes due 5/1/2067	238,356	238,354
Junior subordinated debt securities payable	329,897	329,897
Accrued interest on debt and borrowings	12,092	4,781
Unsettled securities payable	74,097	8,793
Other liabilities	276,651	241,075
Total liabilities	11,385,090	11,407,787

Commitments and Contingencies (Note 6)				
STOCKHOLDER'S EQUITY:				
Common stock, par value: $0.01; 3,000 shares authorized;				
1,000 shares issued and outstanding (2012 and 2011)		-		-
Additional paid-in capital		338,478		333,416
Accumulated other comprehensive income (loss), net of deferred income tax expense				
(benefit) of $116,254 at 2012 and $94,118 at 2011		215,900		174,790
Retained earnings		2,929,549		2,433,187
Total stockholder's equity		3,483,927		2,941,393
TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY	$	14,869,017	$	14,349,180

The accompanying notes are an integral part of the consolidated financial statements.

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EVEREST REINSURANCE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME (LOSS)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2012	2011	2012	2011
	(unaudited)		(unaudited)	
REVENUES:				
Premiums earned	$ 427,112	$ 442,862	$ 1,299,293	$ 1,354,305
Net investment income	76,342	78,325	231,790	249,916
Net realized capital gains (losses):				
Other-than-temporary impairments on fixed maturity securities	(486)	(911)	(6,627)	(14,522)
Other-than-temporary impairments on fixed maturity securities transferred to other comprehensive income (loss)	-	-	-	-
Other net realized capital gains (losses)	96,429	(178,125)	361,300	(192,222)
Total net realized capital gains (losses)	95,943	(179,036)	354,673	(206,744)
Other income (expense)	425	(8,865)	19,599	(20,401)
Total revenues	599,822	333,286	1,905,355	1,377,076
CLAIMS AND EXPENSES:				
Incurred losses and loss adjustment expenses	242,877	322,099	786,851	1,187,936
Commission, brokerage, taxes and fees	70,464	70,842	251,320	239,659
Other underwriting expenses	45,938	42,708	126,551	120,148
Corporate expenses	2,019	1,143	5,317	3,498
Interest, fee and bond issue cost amortization expense	12,682	12,706	38,061	38,083
Total claims and expenses	373,980	449,498	1,208,100	1,589,324
INCOME (LOSS) BEFORE TAXES	225,842	(116,212)	697,255	(212,248)
Income tax expense (benefit)	69,857	(116,473)	200,893	(123,783)
NET INCOME (LOSS)	$ 155,985	$ 261	$ 496,362	$ (88,465)
Other comprehensive income (loss), net of tax :				
Unrealized appreciation (depreciation) ("URA(D)") on securities arising during the period	18,036	8,842	23,511	12,640
Less: reclassification adjustment for realized losses (gains) included in net income (loss)	261	(1,049)	1,696	19,661
Total URA(D) on securities arising during the period	18,297	7,793	25,207	32,301
Foreign currency translation adjustments	15,301	(4,558)	12,737	4,695
Pension adjustments	1,199	746	3,166	2,238
Total other comprehensive income (loss), net of tax	34,797	3,981	41,110	39,234
COMPREHENSIVE INCOME (LOSS)	$ 190,782	$ 4,242	$ 537,472	$ (49,231)

The accompanying notes are an integral part of the consolidated financial statements.

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EVEREST REINSURANCE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF
CHANGES IN STOCKHOLDER'S EQUITY

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands, except share amounts)	2012	2011	2012	2011
	(unaudited)		(unaudited)	
COMMON STOCK (shares outstanding):				
Balance, beginning of period	1,000	1,000	1,000	1,000
Balance, end of period	1,000	1,000	1,000	1,000
ADDITIONAL PAID-IN CAPITAL:				
Balance, beginning of period	$ 336,813	$ 330,990	$ 333,416	$ 327,767
Share-based compensation plans	1,665	1,657	5,062	4,880
Balance, end of period	338,478	332,647	338,478	332,647
ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS), NET OF DEFERRED INCOME TAXES:				
Balance, beginning of period	181,103	199,219	174,790	163,966
Net increase (decrease) during the period	34,797	3,981	41,110	39,234
Balance, end of period	215,900	203,200	215,900	203,200
RETAINED EARNINGS:				
Balance, beginning of period	2,773,564	2,547,282	2,433,187	2,636,008
Net income (loss)	155,985	261	496,362	(88,465)
Balance, end of period	2,929,549	2,547,543	2,929,549	2,547,543
TOTAL STOCKHOLDER'S EQUITY, END OF PERIOD	$ 3,483,927	$ 3,083,390	$ 3,483,927	$ 3,083,390

The accompanying notes are an integral part of the consolidated financial statements.

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EVEREST REINSURANCE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
	(unaudited)		(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net income (loss)	$ 155,985	$ 261	$ 496,362	$ (88,465)
Adjustments to reconcile net income to net cash provided by operating activities:				
Decrease (increase) in premiums receivable	(233,296)	(21,017)	(129,749)	(149,561)
Decrease (increase) in funds held by reinsureds, net	2,646	(94,290)	(14,878)	(102,102)
Decrease (increase) in reinsurance receivables	(39,772)	112,376	(9,281)	(243,523)
Decrease (increase) in current income taxes	18,495	16,559	23,123	15,515
Decrease (increase) in deferred tax asset	22,640	(137,225)	136,264	(122,876)
Decrease (increase) in prepaid reinsurance premiums	(66,455)	(33,514)	28,866	28,649
Increase (decrease) in reserve for losses and loss adjustment expenses	(109,811)	(96,587)	(406,946)	489,779
Increase (decrease) in unearned premiums	98,935	29,928	(102,067)	(73,434)
Increase (decrease) in other net payable to reinsurers	220,948	66,568	263,498	155,372
Change in equity adjustments in limited partnerships	(8,800)	(12,190)	(28,850)	(44,544)
Change in other assets and liabilities, net	59,520	28,444	158,864	44,148
Non-cash compensation expense	1,737	1,584	4,981	4,638
Amortization of bond premium (accrual of bond discount)	3,330	(17)	12,939	6,897
Amortization of underwriting discount on senior notes	13	12	38	36
Net realized capital (gains) losses	(95,943)	179,036	(354,673)	206,744
Net cash provided by (used in) operating activities	30,172	39,928	78,491	127,273
CASH FLOWS FROM INVESTING ACTIVITIES:				
Proceeds from fixed maturities matured/called - available for sale, at market value	273,497	262,235	648,218	525,768
Proceeds from fixed maturities matured/called - available for sale, at fair value	1,300	-	1,300	12,775
Proceeds from fixed maturities sold - available for sale, at market value	114,610	255,913	290,911	1,042,803
Proceeds from fixed maturities sold - available for sale, at fair value	11,783	12,512	72,926	62,632
	-	-	-	27,096

Proceeds from equity securities sold - available for sale, at market value				
Proceeds from equity securities sold - available for sale, at fair value	85,277	61,080	377,157	150,776
Distributions from other invested assets	16,130	13,487	31,513	103,262
Cost of fixed maturities acquired - available for sale, at market value	(404,009)	(285,414)	(1,066,080)	(995,210)
Cost of fixed maturities acquired - available for sale, at fair value	(1,658)	(9,801)	(7,164)	(25,025)
Cost of equity securities acquired - available for sale, at market value	-	-	-	(27,059)
Cost of equity securities acquired - available for sale, at fair value	(107,330)	(340,493)	(288,218)	(679,764)
Cost of other invested assets acquired	(20,065)	(2,393)	(43,831)	(47,471)
Cost of other invested assets acquired, at fair value	-	-	-	(37,611)
Cost of businesses acquired	-	-	-	(63,100)
Net change in short-term investments	(58,681)	29,080	(216,270)	(18,105)
Net change in unsettled securities transactions	33,600	(14,007)	38,712	30,834
Net cash provided by (used in) investing activities	(55,546)	(17,801)	(160,826)	62,601
CASH FLOWS FROM FINANCING ACTIVITIES:				
Tax benefit from share-based compensation	(72)	73	81	242
Revolving credit borrowings	-	(40,000)	-	(50,000)
Net cash provided by (used in) financing activities	(72)	(39,927)	81	(49,758)
EFFECT OF EXCHANGE RATE CHANGES ON CASH	28,772	(5,553)	43,046	6,804
Net increase (decrease) in cash	3,326	(23,353)	(39,208)	146,920
Cash, beginning of period	305,733	288,365	348,267	118,092
Cash, end of period	$ 309,059	$ 265,012	$ 309,059	$ 265,012
SUPPLEMENTAL CASH FLOW INFORMATION:				
Income taxes paid (recovered)	$ 27,119	$ 4,149	$ 36,498	$ (16,616)
Interest paid	5,202	5,228	30,244	30,269
Non-cash transaction:				
Net assets acquired and liabilities assumed from business acquisitions	-	-	-	19,130

The accompanying notes are an integral part of the consolidated financial statements.

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NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

For the Three and Nine Months Ended September 30, 2012 and 2011

1. GENERAL

As used in this document, "Holdings" means Everest Reinsurance Holdings, Inc., a Delaware company and direct subsidiary of Everest Underwriting Group (Ireland) Limited ("Holdings Ireland"); "Group" means Everest Re Group, Ltd. (Holdings Ireland's parent); "Bermuda Re" means Everest Reinsurance (Bermuda), Ltd., a subsidiary of Group; "Everest Re" means Everest Reinsurance Company and its subsidiaries, a subsidiary of Holdings (unless the context otherwise requires); and the "Company" means Holdings and its subsidiaries.

2. BASIS OF PRESENTATION

The unaudited consolidated financial statements of the Company for the three and nine months ended September 30, 2012 and 2011 include all adjustments, consisting of normal recurring accruals, which, in the opinion of management, are necessary for a fair statement of the results on an interim basis. Certain financial information, which is normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"), has been omitted since it is not required for interim reporting purposes. The December 31, 2011 consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. The results for the three and nine months ended September 30, 2012 and 2011 are not necessarily indicative of the results for a full year. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the years ended December 31, 2011, 2010 and 2009 included in the Company's most recent Form 10-K filing.

All intercompany accounts and transactions have been eliminated.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Application of Recently Issued Accounting Standard Changes

Intangibles-Goodwill or Other. In September 2011, the Financial Accounting Standards Board ("FASB") amended the authoritative guidance for disclosures on Goodwill Impairment. The amendment allows an entity first to assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis in determining whether it is necessary to perform the two-step goodwill impairment test. This guidance is effective for periods beginning after December 15, 2011. The Company implemented this guidance as of January 1, 2012.

Presentation of Comprehensive Income. In June 2011, FASB issued amendments to existing guidance to provide two alternatives for the presentation of comprehensive income. Components of net income and comprehensive income can either be presented within a single, continuous financial statement or be presented in two separate but consecutive financial statements. The Company has chosen to present the components of net income and comprehensive income in a single, continuous financial statement. The guidance is effective for reporting periods beginning after December 15, 2011. The Company implemented this guidance as of January 1, 2012.

Common Fair Value Measurement. In May 2011, FASB issued amendments to existing guidance to achieve common fair value measurement and disclosure requirements between GAAP and International Financial Reporting Standards.

The amendments change wording used to describe many GAAP fair value measurement requirements and disclosures. FASB does not intend for the amendments to cause a change in application of fair value accounting guidance. The guidance is effective for reporting periods beginning after December 15, 2011. The Company implemented this guidance prospectively as of January 1, 2012.

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Treatment of Insurance Contract Acquisition Costs. In October 2010, the FASB issued authoritative guidance for the accounting for costs associated with acquiring or renewing insurance contracts. The guidance identifies the incremental direct costs of contract acquisition and costs directly related to acquisition activities that should be capitalized. This guidance is effective for reporting periods beginning after December 15, 2011. The Company implemented this guidance as of January 1, 2012 and determined that $7,215 thousand of previously deferrable acquisition costs will be expensed during 2012 and the first quarter of 2013, including $1,356 thousand and $4,727 thousand of previously deferrable acquisition costs expensed in the three and nine months ended September 30, 2012, respectively. If the guidance had been applicable for the prior periods, the Company would have expensed $2,789 thousand and $6,160 thousand of deferrable acquisition costs during the three and nine months ended September 30, 2011, respectively.

Improving Disclosures About Fair Value Measurements. In January 2010, the FASB amended the authoritative guidance for disclosures on fair value measurements. Effective for interim and annual reporting periods beginning after December 15, 2009, the guidance requires a new separate disclosure for: significant transfers in and out of Level 1 and 2 and the reasons for the transfers; and provided clarification on existing disclosures to include: fair value measurement disclosures by class of assets and liabilities and disclosure on valuation techniques and inputs used to measure fair value that fall in either Level 2 or Level 3. The Company implemented this guidance effective January 1, 2010. Effective for interim and annual reporting periods beginning after December 15, 2010, the guidance requires another new separate disclosure in regards to Level 3 fair value measurements in that, the period activity will present separately information about purchases, sales, issuances and settlements. Comparative disclosures shall be required only for periods ending after initial adoption. The Company implemented this guidance beginning with the third quarter of 2010.

3. INVESTMENTS

The amortized cost, market value and gross unrealized appreciation and depreciation of available for sale, fixed maturity and equity security investments, carried at market value, are as follows for the periods indicated:

	At September 30, 2012			
(Dollars in thousands)	Amortized Cost	Unrealized Appreciation	Unrealized Depreciation	Market Value
Fixed maturity securities				
U.S. Treasury securities and obligations of U.S. government agencies and corporations	$77,754	$ 1,658	$ (817)	$78,595
Obligations of U.S. states and political subdivisions	1,275,967	90,415	(53)	1,366,329
Corporate securities	1,342,335	65,091	(6,198)	1,401,228
Asset-backed securities	48,695	2,228	-	50,923
Mortgage-backed securities				
Commercial	45,345	8,066	(404)	53,007
Agency residential	559,808	15,901	(541)	575,168
Non-agency residential	2,148	357	(25)	2,480
Foreign government securities	759,964	56,900	(4,176)	812,688
Foreign corporate securities	948,952	46,681	(9,933)	985,700
Total fixed maturity securities	$5,060,968	$ 287,297	$ (22,147)	$5,326,118
Equity securities	$15	$ -	$ (2)	$13

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(Dollars in thousands)	At December 31, 2011 Amortized Cost	Unrealized Appreciation	Unrealized Depreciation	Market Value
Fixed maturity securities				
U.S. Treasury securities and obligations of				
U.S. government agencies and corporations	$77,351	$ 2,475	$ (287)	$79,539
Obligations of U.S. states and political subdivisions	1,558,615	102,815	(525)	1,660,905
Corporate securities	1,200,941	45,070	(17,776)	1,228,235
Asset-backed securities	44,351	758	(6)	45,103
Mortgage-backed securities				
Commercial	41,953	7,187	(1,266)	47,874
Agency residential	528,946	16,209	(1,762)	543,393
Non-agency residential	24,139	470	(320)	24,289
Foreign government securities	733,814	57,437	(2,602)	788,649
Foreign corporate securities	670,544	29,421	(10,924)	689,041
Total fixed maturity securities	$4,880,654	$ 261,842	$ (35,468)	$5,107,028
Equity securities	$15	$ -	$ (5)	$10

The $812,688 thousand of foreign government securities at September 30, 2012 included $89,412 thousand of European sovereign securities. Approximately 48.6%, 15.1%, 11.8%, 7.3% and 5.4% of European Sovereign Securities represented securities held in the governments of France, the United Kingdom, Sweden, the Netherlands and Austria, respectively. No other countries represented more than 5% of the European sovereign securities. The Company held no sovereign securities of Portugal, Italy, Ireland, Greece or Spain at September 30, 2012.

In accordance with FASB guidance, the Company reclassified the non-credit portion of other-than-temporary impairments from retained earnings into accumulated other comprehensive income (loss), on April 1, 2009. The table below presents the pre-tax cumulative unrealized appreciation (depreciation) on those corporate securities, for the periods indicated:

(Dollars in thousands)	At September 30, 2012	At December 31, 2011
Pre-tax cumulative unrealized appreciation (depreciation)	$ 490	$ 635

The amortized cost and market value of fixed maturity securities are shown in the following table by contractual maturity. Mortgage-backed securities are generally more likely to be prepaid than other fixed maturity securities. As the stated maturity of such securities may not be indicative of actual maturities, the totals for mortgage-backed and asset-backed securities are shown separately.

(Dollars in thousands)	At September 30, 2012 Amortized Cost	Market Value	At December 31, 2011 Amortized Cost	Market Value
Fixed maturity securities – available for sale				
Due in one year or less	$351,241	$349,065	$224,406	$223,507
Due after one year through five years	2,272,775	2,360,911	2,055,299	2,129,437
Due after five years through ten years	977,030	1,040,976	955,253	1,009,893
Due after ten years	803,926	893,588	1,006,307	1,083,532
Asset-backed securities	48,695	50,923	44,351	45,103
Mortgage-backed securities				

Commercial	45,345	53,007	41,953	47,874
Agency residential	559,808	575,168	528,946	543,393
Non-agency residential	2,148	2,480	24,139	24,289
Total fixed maturity securities	$5,060,968	$5,326,118	$4,880,654	$5,107,028

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The changes in net unrealized appreciation (depreciation) for the Company's investments are derived from the following sources for the periods as indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2012	2011	2012	2011
Increase (decrease) during the period between the market value and cost of investments carried at market value, and deferred taxes thereon:				
Fixed maturity securities	$ 28,226	$ 11,911	$ 38,923	$ 51,341
Fixed maturity securities, other-than-temporary impairment	(77)	(137)	(146)	(132)
Equity securities	-	(1)	3	(1)
Other invested assets	-	215	-	(1,515)
Change in unrealized appreciation (depreciation), pre-tax	28,149	11,988	38,780	49,693
Deferred tax benefit (expense)	(9,879)	(4,243)	(13,624)	(17,438)
Deferred tax benefit (expense), other-than-temporary impairment	27	48	51	46
Change in unrealized appreciation (depreciation), net of deferred taxes, included in stockholder's equity	$ 18,297	$ 7,793	$ 25,207	$ 32,301

The Company frequently reviews all of its fixed maturity, available for sale securities for declines in market value and focuses its attention on securities whose fair value has fallen below 80% of their amortized cost at the time of review. The Company then assesses whether the decline in value is temporary or other-than-temporary. In making its assessment, the Company evaluates the current market and interest rate environment as well as specific issuer information. Generally, a change in a security's value caused by a change in the market, interest rate or foreign exchange environment does not constitute an other-than-temporary impairment, but rather a temporary decline in market value. Temporary declines in market value are recorded as unrealized losses in accumulated other comprehensive income (loss). If the Company determines that the decline is other-than-temporary and the Company does not have the intent to sell the security; and it is more likely than not that the Company will not have to sell the security before recovery of its cost basis, the carrying value of the investment is written down to fair value. The fair value adjustment that is credit or foreign exchange related is recorded in net realized capital gains (losses) in the Company's consolidated statements of operations and comprehensive income (loss). The fair value adjustment that is non-credit related is recorded as a component of other comprehensive income (loss), net of tax, and is included in accumulated other comprehensive income (loss) in the Company's consolidated balance sheets. The Company's assessments are based on the issuers current and expected future financial position, timeliness with respect to interest and/or principal payments, speed of repayments and any applicable credit enhancements or breakeven constant default rates on mortgage-backed and asset-backed securities, as well as relevant information provided by rating agencies, investment advisors and analysts.

Retrospective adjustments are employed to recalculate the values of asset-backed securities. All of the Company's asset-backed and mortgage-backed securities have a pass-through structure. Each acquisition lot is reviewed to recalculate the effective yield. The recalculated effective yield is used to derive a book value as if the new yield were applied at the time of acquisition. Outstanding principal factors from the time of acquisition to the adjustment date are used to calculate the prepayment history for all applicable securities. Conditional prepayment rates, computed with life to date factor histories and weighted average maturities, are used in the calculation of projected prepayments for pass-through security types.

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The tables below display the aggregate market value and gross unrealized depreciation of fixed maturity and equity securities, by security type and contractual maturity, in each case subdivided according to length of time that individual securities had been in a continuous unrealized loss position for the periods indicated:

	Duration of Unrealized Loss at September 30, 2012 By Security Type					
	Less than 12 months		Greater than 12 months		Total	
(Dollars in thousands)	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation
Fixed maturity securities - available for sale						
U.S. Treasury securities and obligations of						
U.S. government agencies and corporations	$ -	$ -	$ 11,543	$ (817)	$ 11,543	$ (817)
Obligations of U.S. states and political subdivisions	-	-	5,779	(53)	5,779	(53)
Corporate securities	56,805	(411)	108,100	(5,787)	164,905	(6,198)
Asset-backed securities	-	-	-	-	-	-
Mortgage-backed securities						
Commercial	-	-	10,332	(404)	10,332	(404)
Agency residential	74,338	(354)	12,983	(187)	87,321	(541)
Non-agency residential	-	-	496	(25)	496	(25)
Foreign government securities	37,667	(592)	38,281	(3,584)	75,948	(4,176)
Foreign corporate securities	66,424	(1,290)	80,924	(8,643)	147,348	(9,933)
Total fixed maturity securities	$ 235,234	$ (2,647)	$ 268,438	$ (19,500)	$ 503,672	$ (22,147)
Equity securities	-	-	13	(2)	13	(2)
Total	$ 235,234	$ (2,647)	$ 268,451	$ (19,502)	$ 503,685	$ (22,149)

	Duration of Unrealized Loss at September 30, 2012 By Maturity					
	Less than 12 months		Greater than 12 months		Total	
(Dollars in thousands)	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation
Fixed maturity securities						
Due in one year or less	$ 12,962	$ (287)	$ 35,341	$ (5,663)	$ 48,303	$ (5,950)
Due in one year through five years	116,020	(1,805)	149,214	(11,175)	265,234	(12,980)
Due in five years through ten years	29,938	(175)	45,936	(1,587)	75,874	(1,762)
Due after ten years	1,976	(26)	14,136	(459)	16,112	(485)

Asset-backed securities	-	-	-	-	-	-
Mortgage-backed securities	74,338	(354)	23,811	(616)	98,149	(970)
Total fixed maturity securities	$ 235,234	$ (2,647)	$ 268,438	$ (19,500)	$ 503,672	$ (22,147)

The aggregate market value and gross unrealized losses related to investments in an unrealized loss position at September 30, 2012 were $503,685 thousand and $22,149 thousand, respectively. There were no unrealized losses on a single issuer that exceeded 0.03% of the market value of the fixed maturity securities at September 30, 2012. In addition, as indicated on the above table, there was no significant concentration of unrealized losses in any one market sector. The $2,647 thousand of unrealized losses related to fixed maturity securities that have been in an unrealized loss position for less than one year were comprised of domestic and foreign corporate securities, foreign government securities as well as agency residential mortgage-backed securities. Of these unrealized losses, $2,039 thousand were related to securities that were rated investment grade by at least one nationally recognized statistical rating organization. The $19,500 thousand of unrealized losses related to fixed maturity securities in an unrealized loss position for more than one year related primarily to domestic and foreign corporate securities and foreign government securities. Of these unrealized losses, $17,181 thousand were related to securities that were rated investment grade by at least one nationally recognized statistical rating organization. The non-investment grade securities with unrealized losses were mainly comprised of corporate securities, with the majority representing a large number of short duration, floating interest rate bank loan securities. The gross unrealized depreciation for mortgage-backed securities included $25 thousand related to sub-prime and alt-A loans. In all instances, there were no projected cash flow shortfalls to recover the full book value of the investments and the related interest obligations. The mortgage-backed securities still have excess credit coverage and are current on interest and principal payments.

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The Company, given the size of its investment portfolio and capital position, does not have the intent to sell these securities; and it is more likely than not that the Company will not have to sell the security before recovery of its cost basis. In addition, all securities currently in an unrealized loss position are current with respect to principal and interest payments.

The tables below display the aggregate market value and gross unrealized depreciation of fixed maturity and equity securities, by security type and contractual maturity, in each case subdivided according to length of time that individual securities had been in a continuous unrealized loss position for the periods indicated:

	Duration of Unrealized Loss at December 31, 2011 By Security Type					
	Less than 12 months		Greater than 12 months		Total	
(Dollars in thousands)	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation
Fixed maturity securities - available for sale						
U.S. Treasury securities and obligations of U.S. government agencies and corporations	$ -	$ -	$ 3,452	$ (287)	$ 3,452	$ (287)
Obligations of U.S. states and political subdivisions	-	-	7,518	(525)	7,518	(525)
Corporate securities	342,959	(8,449)	75,998	(9,327)	418,957	(17,776)
Asset-backed securities	819	(6)	-	-	819	(6)
Mortgage-backed securities						
Commercial	9,292	(1,266)	-	-	9,292	(1,266)
Agency residential	151,951	(1,695)	7,199	(67)	159,150	(1,762)
Non-agency residential	41	-	20,693	(320)	20,734	(320)
Foreign government securities	12,777	(269)	40,743	(2,333)	53,520	(2,602)
Foreign corporate securities	77,458	(2,025)	94,182	(8,899)	171,640	(10,924)
Total fixed maturity securities	$ 595,297	$ (13,710)	$ 249,785	$ (21,758)	$ 845,082	$ (35,468)
Equity securities	-	-	10	(5)	10	(5)
Total	$ 595,297	$ (13,710)	$ 249,795	$ (21,763)	$ 845,092	$ (35,473)

	Duration of Unrealized Loss at December 31, 2011 By Maturity					
	Less than 12 months		Greater than 12 months		Total	
(Dollars in thousands)	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation	Market Value	Gross Unrealized Depreciation
Fixed maturity securities						
Due in one year or less	$ 9,583	$ (59)	$ 26,204	$ (4,486)	$ 35,787	$ (4,545)
	213,809	(4,754)	137,972	(9,576)	351,781	(14,330)

Due in one year through five years						
Due in five years through ten years	186,061	(5,484)	37,964	(2,391)	224,025	(7,875)
Due after ten years	23,741	(446)	19,753	(4,918)	43,494	(5,364)
Asset-backed securities	819	(6)	-	-	819	(6)
Mortgage-backed securities	161,284	(2,961)	27,892	(387)	189,176	(3,348)
Total fixed maturity securities	$ 595,297	$ (13,710)	$ 249,785	$ (21,758)	$ 845,082	$ (35,468)

The aggregate market value and gross unrealized losses related to investments in an unrealized loss position at December 31, 2011 were $845,092 thousand and $35,473 thousand, respectively. There were no unrealized losses on a single issuer that exceeded 0.09% of the market value of the fixed maturity securities at December 31, 2011. In addition, as indicated on the above table, there was no significant concentration of unrealized losses in any one market sector. The $13,710 thousand of unrealized losses related to fixed maturity securities that have been in an unrealized loss position for less than one year were generally comprised of domestic and foreign corporate securities as well as commercial and agency residential mortgage-backed securities. Of these unrealized losses, $5,635 thousand were related to securities that were rated investment grade by at least one nationally recognized statistical rating organization. The $21,758 thousand of unrealized losses related to fixed maturity securities in an unrealized loss position for more than one year related primarily to domestic and foreign corporate and foreign government securities. Of these unrealized losses, $15,880 thousand were related to securities that were rated investment grade by at least one nationally recognized statistical rating organization. The non-investment grade securities with unrealized losses were mainly comprised of corporate securities, with the

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majority representing a large number of short duration, floating interest rate bank loan securities. The gross unrealized depreciation for mortgage-backed securities included $56 thousand related to sub-prime and alt-A loans. In all instances, there were no projected cash flow shortfalls to recover the full book value of the investments and the related interest obligations. The mortgage-backed securities still have excess credit coverage and are current on interest and principal payments.

Other invested assets, at fair value, is comprised of common shares of the Company's ultimate parent, Group. At September 30, 2012, the Company held 9,719,971 shares of Group representing 15.8% of the total outstanding shares.

The components of net investment income are presented in the table below for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2012	2011	2012	2011
Fixed maturity securities	$ 55,495	$ 58,248	$ 164,248	$ 178,006
Equity securities	8,849	8,726	29,281	20,366
Short-term investments and cash	330	296	758	890
Other invested assets				
Limited partnerships	9,096	12,399	29,940	44,753
Dividends from Parent's shares	4,666	4,665	13,997	13,979
Other	1,427	(1,520)	2,453	3,203
Total gross investment income	79,863	82,814	240,677	261,197
Interest debited (credited) and other investment expense	(3,521)	(4,489)	(8,887)	(11,281)
Total net investment income	$ 76,342	$ 78,325	$ 231,790	$ 249,916

The Company records results from limited partnership investments on the equity method of accounting with changes in value reported through net investment income. Due to the timing of receiving financial information from these partnerships, the results are generally reported on a one month or quarter lag. If the Company determines there has been a significant decline in value of a limited partnership during this lag period, a loss will be recorded in the period in which the Company identifies the decline.

The Company had contractual commitments to invest up to an additional $71,741 thousand in limited partnerships at September 30, 2012. These commitments will be funded when called in accordance with the partnership agreements, which have investment periods that expire, unless extended, through 2016.

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The components of net realized capital gains (losses) are presented in the table below for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2012	2011	2012	2011
Fixed maturity securities, market value:				
Other-than-temporary impairments	$ (486)	$ (911)	$ (6,627)	$ (14,522)
Gains (losses) from sales	85	2,699	4,018	(15,589)
Fixed maturity securities, fair value:				
Gains (losses) from sales	512	(16)	5,539	(966)
Gains (losses) from fair value adjustments	298	(5,014)	1,623	(8,537)
Equity securities, market value:				
Gains (losses) from sales	-	-	-	37
Equity securities, fair value:				
Gains (losses) from sales	3,154	637	23,101	2,303
Gains (losses) from fair value adjustments	58,667	(153,395)	104,739	(115,288)
Other invested assets, fair value:				
Gains (losses) from fair value adjustments	33,729	(23,036)	222,296	(54,181)
Short-term investment gains (losses)	(16)	-	(16)	(1)
Total net realized capital gains (losses)	$ 95,943	$ (179,036)	$ 354,673	$ (206,744)

The Company recorded as net realized capital gains (losses) in the consolidated statements of operations and comprehensive income (loss) both fair value re-measurements and write-downs in the value of securities deemed to be impaired on an other-than-temporary basis as displayed in the table above. The Company had no other-than-temporary impaired securities where the impairment had both a credit and non-credit component.

The proceeds and split between gross gains and losses, from sales of fixed maturity and equity securities, are presented in the table below for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2012	2011	2012	2011
Proceeds from sales of fixed maturity securities	$ 126,393	$ 268,425	$ 363,837	$ 1,105,435
Gross gains from sales	2,704	11,572	15,371	29,154
Gross losses from sales	(2,107)	(8,889)	(5,814)	(45,709)
Proceeds from sales of equity secuities	$ 85,277	$ 61,080	$ 377,157	$ 177,872
Gross gains from sales	5,204	6,022	33,005	9,124
Gross losses from sales	(2,050)	(5,385)	(9,904)	(6,784)

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4. FAIR VALUE

The Company's fixed maturity and equity securities are primarily managed by third party investment asset managers. The investment asset managers obtain prices from nationally recognized pricing services. These services seek to utilize market data and observations in their evaluation process. They use pricing applications that vary by asset class and incorporate available market information and when fixed maturity securities do not trade on a daily basis the services will apply available information through processes such as benchmark curves, benchmarking of like securities, sector groupings and matrix pricing. In addition, they use model processes, such as the Option Adjusted Spread model to develop prepayment and interest rate scenarios for securities that have prepayment features.

In limited instances where prices are not provided by pricing services or in rare instances when a manager may not agree with the pricing service, price quotes on a non-binding basis are obtained from investment brokers. The investment asset managers do not make any changes to prices received from either the pricing services or the investment brokers. In addition, the investment asset managers have procedures in place to review the reasonableness of the prices from the service providers and may request verification of the prices. In addition, the Company continually performs analytical reviews of price changes and tests the prices on a random basis to an independent pricing source. No material variances were noted during these price validation procedures. In limited situations, where financial markets are inactive or illiquid, the Company may use its own assumptions about future cash flows and risk-adjusted discount rates to determine fair value. The Company made no such adjustments at September 30, 2012 and December 31, 2011.

The Company internally manages a small public equity portfolio which had a fair value at September 30, 2012 of $52,009 thousand and all prices were obtained from publically published sources.

Equity securities in U.S. denominated currency are categorized as Level 1, Quoted Prices in Active Markets for Identical Assets, since the securities are actively traded on an exchange and prices are based on quoted prices from the exchange. Equity securities traded on foreign exchanges are categorized as Level 2 due to potential foreign exchange adjustments to fair or market value.

Fixed maturity securities are generally categorized as Level 2, Significant Other Observable Inputs, since a particular security may not have traded but the pricing services are able to use valuation models with observable market inputs such as interest rate yield curves and prices for similar fixed maturity securities in terms of issuer, maturity and seniority. Valuations that are derived from techniques in which one or more of the significant inputs are unobservable (including assumptions about risk) are categorized as Level 3, Significant Unobservable Inputs. These securities include broker priced securities.

As of September 30, 2012 and December 31, 2011, all Level 3 fixed maturity securities, were priced using single non-binding broker quotes since prices for these securities were not provided by normal pricing service companies. The single broker quotes are provided by market makers or broker-dealers who are recognized as market participants in the markets in which they are providing the quotes. The prices received from brokers are reviewed for reasonableness by our asset managers and management.

Other invested assets, at fair value, are categorized as Level 1, Quoted Prices in Active Markets for Identical Assets, since the securities are shares of the Company's parent, which are actively traded on an exchange and the price is based on a quoted price.

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The following table presents the fair value measurement levels for all assets, which the Company has recorded at fair value (fair and market value) as of the period indicated:

(Dollars in thousands)	September 30, 2012	Fair Value Measurement Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Fixed maturities, market value				
U.S. Treasury securities and obligations of				
U.S. government agencies and corporations	$ 78,595	$ -	$ 78,595	$ -
Obligations of U.S. States and political subdivisions	1,366,329	-	1,366,329	-
Corporate securities	1,401,228	-	1,401,228	-
Asset-backed securities	50,923	-	43,331	7,592
Mortgage-backed securities				
Commercial	53,007	-	53,007	-
Agency residential	575,168	-	575,168	-
Non-agency residential	2,480	-	2,475	5
Foreign government securities	812,688	-	812,688	-
Foreign corporate securities	985,700	-	980,754	4,946
Total fixed maturities, market value	5,326,118	-	5,313,575	12,543
Fixed maturities, fair value	52,217	-	52,217	-
Equity securities, market value	13	13	-	-
Equity securities, fair value	1,247,445	1,113,526	133,919	-
Other invested assets, fair value	1,039,648	1,039,648	-	-

There were no transfers between Level 1 and Level 2 for the three and nine months ended September 30, 2012.

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The following table presents the fair value measurement levels for all assets, which the Company has recorded at fair value (fair and market value) as of the period indicated:

		Fair Value Measurement Using:		
(Dollars in thousands)	December 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Fixed maturities, market value				
U.S. Treasury securities and obligations of				
U.S. government agencies and corporations	$ 79,539	$ -	$ 79,539	$ -
Obligations of U.S. States and political subdivisions	1,660,905	-	1,660,905	-
Corporate securities	1,228,235	-	1,228,235	-
Asset-backed securities	45,103	-	29,057	16,046
Mortgage-backed securities				
Commercial	47,874	-	47,874	-
Agency residential	543,393	-	543,393	-
Non-agency residential	24,289	-	24,282	7
Foreign government securities	788,649	-	788,649	-
Foreign corporate securities	689,041	-	686,505	2,536
Total fixed maturities, market value	5,107,028	-	5,088,439	18,589
Fixed maturities, fair value	113,606	-	113,606	-
Equity securities, market value	10	10	-	-
Equity securities, fair value	1,207,053	1,090,959	116,094	-
Other invested assets, fair value	817,352	817,352	-	-

The following tables present the activity under Level 3, fair value measurements using significant unobservable inputs by asset type, for the periods indicated:

	Three Months Ended September 30, 2012				Nine Months Ended September 30, 2012			
(Dollars in thousands)	Asset-backed Securities	Foreign Corporate	Non-agency RMBS	Total	Asset-backed Securities	Foreign Corporate	Non-agency RMBS	Total
Beginning balance	$ 8,996	$ 7,383	$ 5	$ 16,384	$ 16,046	$ 2,536	$ 7	$ 18,589
Total gains or (losses) (realized/unrealized)								
Included in earnings (or changes in net assets)	56	(14)	1	43	111	(33)	3	81
Included in other comprehensive income (loss)	390	275	-	665	728	387	(2)	1,113
Purchases, issuances and settlements	(61)	(576)	(1)	(638)	4,407	6,640	(3)	11,044
	(1,789)	(2,122)	-	(3,911)	(13,700)	(4,584)	-	(18,284)

Transfers in and/or (out) of Level 3								
Ending balance	$ 7,592	$ 4,946	$ 5	$ 12,543	$ 7,592	$ 4,946	$ 5	$ 12,543
The amount of total gains or losses for the period included in earnings (or changes in net assets) attributable to the change in unrealized gains or losses relating to assets still held at the reporting date	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
(Some amounts may not reconcile due to rounding.)								

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	Three Months Ended September 30, 2011				Nine Months Ended September 30, 2011			
(Dollars in thousands)	Asset-backed Securities	Foreign Corporate	Non-agency RMBS	Total	Asset-backed Securities	Foreign Corporate	Non-agency RMBS	Total
Beginning balance	$ 2,466	$ -	$ 381	$ 2,847	$ 961	$ 3,635	$ 458	$ 5,054
Total gains or (losses) (realized/unrealized)								