

Allied World Assurance Co Holdings, AG

Form 10-Q

November 09, 2011

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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: September 30, 2011

OR

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

For the transition period from _____ to

Commission file number: 001-32938

ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG

(Exact Name of Registrant as Specified in Its Charter)

Switzerland

*(State or Other Jurisdiction of
Incorporation or Organization)*

98-0681223

*(I.R.S. Employer
Identification No.)*

**Lindenstrasse 8, 6340 Baar
Zug, Switzerland**

(Address of Principal Executive Offices and Zip Code)

41-41-768-1080

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting
company

(Do not check if a 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

As of November 1, 2011, 38,156,652 common shares were outstanding.

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements.

ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

as of September 30, 2011 and December 31, 2010

(Expressed in thousands of United States dollars, except share and per share amounts)

	As of September 30, 2011	As of December 31, 2010
ASSETS:		
Fixed maturity investments available for sale, at fair value (amortized cost: 2011: \$264,050; 2010: \$828,544)	\$ 284,966	\$ 891,849
Fixed maturity investments trading, at fair value	6,279,615	5,769,097
Equity securities trading, at fair value	424,104	174,976
Other invested assets trading, at fair value	552,074	347,632
Total investments	7,540,759	7,183,554
Cash and cash equivalents	869,320	756,995
Restricted cash	33,253	96,373
Insurance balances receivable	607,270	529,927
Prepaid reinsurance	218,514	187,287
Reinsurance recoverable	1,009,643	927,588
Accrued investment income	39,743	40,520
Net deferred acquisition costs	115,070	96,803
Goodwill	268,376	268,376
Intangible assets	54,576	56,876
Balances receivable on sale of investments	349,327	188,408
Net deferred tax assets	26,872	19,740
Other assets	50,424	75,184
Total assets	\$ 11,183,147	\$ 10,427,631
LIABILITIES:		
Reserve for losses and loss expenses	\$ 5,245,553	\$ 4,879,188
Unearned premiums	1,158,842	962,203
Reinsurance balances payable	95,463	99,732
Balances due on purchases of investments	754,451	506,978
Senior notes	797,885	797,700
Dividends payable	14,305	
Accounts payable and accrued liabilities	113,574	106,010
Total liabilities	\$ 8,180,073	\$ 7,351,811
SHAREHOLDERS EQUITY:		
Common shares: 2011: par value CHF 14.38 per share and 2010: par value CHF 15.00 per share (2011: 40,003,642; 2010: 40,003,642 shares issued and	571,455	600,055

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2011: 38,145,557; 2010: 38,089,226 shares outstanding)

Additional paid-in capital	73,797	170,239
Treasury shares, at cost (2011: 1,858,085; 2010: 1,914,416)	(112,624)	(112,811)
Retained earnings	2,452,650	2,361,202
Accumulated other comprehensive income: net unrealized gains on investments, net of tax	17,796	57,135
Total shareholders' equity	3,003,074	3,075,820
Total liabilities and shareholders' equity	\$ 11,183,147	\$ 10,427,631

See accompanying notes to the consolidated financial statements.

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ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE (LOSS) INCOME

for the three and nine months ended September 30, 2011 and 2010
(Expressed in thousands of United States dollars, except share and per share amounts)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2011	2010	2011	2010
REVENUES:				
Gross premiums written	\$ 442,698	\$ 378,445	\$ 1,522,984	\$ 1,376,455
Premiums ceded	(92,438)	(76,276)	(296,050)	(271,199)
Net premiums written	350,260	302,169	1,226,934	1,105,256
Change in unearned premiums	21,080	37,327	(165,411)	(88,512)
Net premiums earned	371,340	339,496	1,061,523	1,016,744
Net investment income	47,883	59,479	150,459	193,975
Net realized investment (losses) gains	(130,809)	116,930	(21,555)	289,350
Net impairment charges recognized in earnings:				
Total other-than-temporary impairment charges				(168)
Portion of loss recognized in other comprehensive income, before taxes				
Net impairment charges recognized in earnings				(168)
Other income	35,000		35,000	913
	323,414	515,905	1,225,427	1,500,814
EXPENSES:				
Net losses and loss expenses	205,546	126,988	745,811	547,864
Acquisition costs	39,680	41,919	120,733	120,641
General and administrative expenses	66,007	69,871	201,164	201,423
Amortization and impairment of intangible assets	767	892	2,300	2,675
Interest expense	13,748	9,533	41,235	28,592
Foreign exchange loss (gain)	2,966	(1,387)	3,708	248
	328,714	247,816	1,114,951	901,443
(Loss) Income before income taxes	(5,300)	268,089	110,476	599,371
Income tax expense	5,672	13,569	19,028	27,152
NET (LOSS) INCOME	(10,972)	254,520	91,448	572,219

Other comprehensive (loss) income:

Unrealized gains on investments arising during the period net of applicable deferred income tax expense for the three months ended September 30, 2011: \$5,476; 2010: \$2,449 and nine months ended September 30, 2011: \$3,051; 2010: \$3,138	20	47,954	5,656	149,276
Reclassification adjustment for net realized investment gains included in net (loss) income, net of applicable income tax	(5,319)	(32,550)	(44,995)	(145,476)
Other comprehensive (loss) income	(5,299)	15,404	(39,339)	3,800
COMPREHENSIVE (LOSS) INCOME	\$ (16,271)	\$ 269,924	\$ 52,109	\$ 576,019
PER SHARE DATA				
Basic (loss) earnings per share	\$ (0.29)	\$ 5.59	\$ 2.40	\$ 11.78
Diluted (loss) earnings per share	\$ (0.29)	\$ 5.21	\$ 2.30	\$ 11.03
Weighted average common shares outstanding	38,110,368	45,544,060	38,078,116	48,580,541
Weighted average common shares and common share equivalents outstanding	38,110,368	48,839,991	39,759,780	51,887,390
Dividends paid per share	\$ 0.375	\$ 0.20	\$ 0.375	\$ 0.60

See accompanying notes to the consolidated financial statements.

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ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

for the nine months ended September 30, 2011 and 2010

(Expressed in thousands of United States dollars)

	Share Capital	Additional Paid-in Capital	Treasury Shares	Accumulated Other Comprehensive Income	Retained Earnings	Total
December 31, 2010	\$ 600,055	\$ 170,239	\$ (112,811)	\$ 57,135	\$ 2,361,202	\$ 3,075,820
Net income					91,448	91,448
Dividends par value reduction	(28,600)					(28,600)
Other comprehensive loss				(39,339)		(39,339)
Stock compensation		(42,822)	60,187			17,365
Share repurchases			(60,000)			(60,000)
Repurchase of founder warrants		(53,620)				(53,620)
September 30, 2011	\$ 571,455	\$ 73,797	\$ (112,624)	\$ 17,796	\$ 2,452,650	\$ 3,003,074
December 31, 2009	\$ 1,492	\$ 1,359,934	\$	\$ 149,849	\$ 1,702,020	\$ 3,213,295
Cumulative effect adjustment upon adoption of ASU 2010-11, net of deferred taxes				(41,889)	41,889	
Net income					572,219	572,219
Dividends					(28,774)	(28,774)
Other comprehensive income				3,800		3,800
Stock compensation	32	28,570				28,602
Share repurchase			(415,009)			(415,009)
Repurchase of founder warrants		(32,819)				(32,819)
September 30, 2010	\$ 1,524	\$ 1,355,685	\$ (415,009)	\$ 111,760	\$ 2,287,354	\$ 3,341,314

See accompanying notes to the consolidated financial statements.

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ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

for the nine months ended September 30, 2011 and 2010

(Expressed in thousands of United States dollars)

	Nine Months Ended	
	September 30,	
	2011	2010
CASH FLOWS PROVIDED BY OPERATING ACTIVITIES:		
Net income	\$ 91,448	\$ 572,219
Adjustments to reconcile net income to cash provided by operating activities:		
Net realized gains on sales of investments	(78,001)	(145,700)
Mark to market adjustments	61,912	(143,650)
Net impairment charges recognized in earnings		168
Stock compensation expense	16,917	25,177
Insurance balances receivable	(77,343)	(71,266)
Prepaid reinsurance	(31,227)	(682)
Reinsurance recoverable	(82,055)	(19,965)
Accrued investment income	777	9,760
Net deferred acquisition costs	(18,267)	(14,479)
Net deferred tax assets	(4,081)	15,401
Other assets	24,650	10,797
Reserve for losses and loss expenses	366,365	128,053
Unearned premiums	196,639	89,195
Reinsurance balances payable	(4,269)	(5,690)
Accounts payable and accrued liabilities	7,564	(27,837)
Other items, net	20,476	(2,310)
Net cash provided by operating activities	491,505	419,191
CASH FLOWS (USED IN) PROVIDED BY INVESTING ACTIVITIES:		
Purchases of fixed maturity investments available for sale	(727)	(138,918)
Purchases of fixed maturity investments trading	(5,209,039)	(8,739,173)
Purchases of equity securities	(346,210)	(122,929)
Purchases of other invested assets	(265,720)	(138,249)
Sales of fixed maturity investments available for sale	627,392	2,057,431
Sales of fixed maturity investments trading	4,772,552	7,583,380
Sales of equity securities	69,028	5,721
Sales of other invested assets	40,129	2,858
Purchases of fixed assets	(7,792)	(7,809)
Change in restricted cash	63,120	(282,595)
Net cash (used in) provided by investing activities	(257,267)	219,717
CASH FLOWS USED IN FINANCING ACTIVITIES:		
Dividends paid		(28,774)
Dividends paid par value reduction	(14,295)	
Proceeds from the exercise of stock options	5,317	7,053
Share repurchases	(60,000)	(415,009)

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Repurchase of founder warrants	(53,620)	(32,819)
Net cash used in financing activities	(122,598)	(469,549)
Effect of exchange rate changes on foreign currency cash	685	(261)
NET INCREASE IN CASH AND CASH EQUIVALENTS	112,325	169,098
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	756,995	292,188
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 869,320	\$ 461,286
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	\$ 6,294	\$ 12,820
Cash paid for interest expense	45,750	37,500

See accompanying notes to the consolidated financial statements.

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ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States dollars, except share, per share, percentage and ratio information)

1. GENERAL

Allied World Assurance Company Holdings, AG, a Swiss holding company (Allied World Switzerland), through its wholly-owned subsidiaries (collectively, the Company), provides property and casualty insurance and reinsurance on a worldwide basis through operations in Bermuda, the United States, Europe, Hong Kong and Singapore.

2. BASIS OF PREPARATION AND CONSOLIDATION

These unaudited condensed consolidated financial statements include the accounts of the Company and have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and with Article 10 of Regulation S-X as promulgated by the U.S. Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, these unaudited condensed consolidated financial statements reflect all adjustments that are normal and recurring in nature and necessary for a fair presentation of financial position and results of operations as of the end of and for the periods presented. The results of operations for any interim period are not necessarily indicative of the results for a full year.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The significant estimates reflected in the Company s financial statements include, but are not limited to:

The premium estimates for certain reinsurance agreements,

Recoverability of deferred acquisition costs,

The reserve for outstanding losses and loss expenses,

Valuation of ceded reinsurance recoverables,

Determination of impairment of goodwill and other intangible assets,

Valuation of financial instruments, and

Determination of other-than-temporary impairment of available for sale investments.

Inter-company accounts and transactions have been eliminated on consolidation and all entities meeting consolidation requirements have been included in the consolidation.

These unaudited condensed consolidated financial statements, including these notes, should be read in conjunction with the Company s audited consolidated financial statements, and related notes thereto, included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

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ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States dollars, except share, per share, percentage and ratio information)

3. NEW ACCOUNTING PRONOUNCEMENTS

In July 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2010-20, Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses (ASU 2010-20). ASU 2010-20 enhances disclosures about credit quality of financing receivables and the allowance of credit losses by requiring additional information regarding the Company's credit risk exposures and evaluating the adequacy of its allowance for credit losses. The balance sheet related disclosures for ASU 2010-20 were effective for the year ended December 31, 2010 and the income statement related disclosures were effective for the quarter ended March 31, 2011. Refer to Note 15 for the Company's related disclosures.

In October 2010, the FASB issued ASU 2010-26, Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts (ASU 2010-26). ASU 2010-26 clarifies what costs associated with acquiring or renewing insurance contracts can be deferred and amortized over the coverage period. Under the revised guidance of ASU 2010-26, incremental direct costs that result directly from and are essential to the insurance contract and would not have been incurred had the insurance contract not been written are costs that may be capitalized, including costs relating to activities specifically performed by the Company such as underwriting, policy issuance and processing. ASU 2010-26 will be effective January 1, 2012 and early adoption is permitted. The Company has not elected early adoption and is currently evaluating the provisions of ASU 2010-26 and its potential impact on future financial statements.

In January 2011, the FASB issued ASU 2011-01, Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20 . In April 2011, the FASB issued ASU 2011-02 A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring (ASU 2011-02). ASU 2011-02 provides further guidance on what constitutes a troubled debt restructuring. The guidance is effective for interim and annual periods beginning on or after June 15, 2011 and applies retrospectively to restructurings within the fiscal year of adoption. Refer to Note 15 for the Company's related disclosures.

In May 2011, the FASB issued ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (ASU 2011-04). ASU 2011-04 provides a consistent meaning for the term fair value between the FASB and International Accounting Standards Board and establishes common requirements for measuring and disclosing information related thereto. ASU 2011-04 is effective on a prospective basis for interim and annual periods beginning on or after December 15, 2011 and early adoption is prohibited. The Company is currently assessing the provisions of ASU 2011-04 and its potential impact on future financial statements.

In June 2011, the FASB issued ASU 2011-05, Presentation of Comprehensive Income (ASU 2011-05). ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity, requires consecutive presentation of the statement of net income and other comprehensive income and requires the presentation of reclassification adjustments on the face of the financial statements from other comprehensive income to net income. ASU 2011-05 is effective on a retrospective basis for interim and annual periods beginning on or after December 15, 2011 and will not have an impact on the presentation of future financial statements.

In September 2011, the FASB issued ASU 2011-08, Testing Goodwill for Impairment (ASU 2011-08). ASU 2011-08 simplifies how goodwill is tested for impairment by permitting entities 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. The qualitative assessment will determine if an entity needs to proceed with the two-step goodwill impairment test. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011 and early adoption is permitted. The Company has not elected early adoption and is currently evaluating the provisions of ASU 2011-08 and its potential impact on future financial statements.

4. INVESTMENTS

a) Available for Sale Securities

The amortized cost, gross unrealized gains, gross unrealized losses and fair value of the Company's available for sale investments by category are as follows:

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ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of United States dollars, except share, per share, percentage and ratio information)

	Amortized	Gross Unrealized	Gross Unrealized	Fair Value
	Cost	Gains	Losses	
September 30, 2011				
U.S. Government and Government agencies	\$ 32,971	\$ 2,327	\$	\$ 35,298
States, municipalities and political subdivisions	29,099	4,008		33,107
Corporate debt:				
Financial institutions	38,368	1,501	(302)	39,567
Industrials	87,661	6,250		93,911
Utilities	75,951	7,132		83,083
Total fixed maturity investments, available for sale	\$ 264,050	\$ 21,218	\$ (302)	\$ 284,966
December 31, 2010				
U.S. Government and Government agencies	\$ 85,030	\$ 6,923	\$	\$ 91,953
Non-U.S. Government and Government agencies	138,386	9,539	(2,541)	145,384
States, municipalities and political subdivisions	107,289	10,901	(13)	118,177
Corporate debt:				
Financial institutions	66,660	6,776	(38)	73,398
Industrials	310,664	20,548	(2)	331,210
Utilities	120,515	11,212		131,727
Total fixed maturity investments, available for sale	\$ 828,544	\$ 65,899	\$ (2,594)	\$ 891,849

b) Trading Securities

Securities accounted for at fair value with changes in fair value recognized in the unaudited condensed consolidated statements of operations and comprehensive (loss) income (consolidated income statements) by category are as follows: