PROASSURANCE CORP
Form 10-Q
May 07, 2015
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)
ý Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2015 or
¨ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from to
Commission file number 0-16533
ProAssurance Corporation
(Exact Name of Registrant as Specified in Its Charter)

Delaware	63-1261433
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)
100 Brookwood Place, Birmingham, AL	35209
(Address of Principal Executive Offices)	(Zip Code)
(205) 877-4400	
(Registrant's Telephone Number, Including Area Code)	(Former Name, Former Address, and Former Fiscal Year, if Changed Since Last Report)

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 ý 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 ý 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	ý	Accelerated filer	¨
Non-accelerated filer	¨ (Do not check if a 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 ý
As of April 30, 2015, there were 55,014,196 shares of the registrant's common stock outstanding.

Forward-Looking Statements

Any statements in this Form 10-Q that are not historical facts are specifically identified as forward-looking statements. These statements are based upon our estimates and anticipation of future events and are subject to certain risks and uncertainties that could cause actual results to vary materially from the expected results described in the forward-looking statements. Forward-looking statements are identified by words such as, but not limited to, "anticipate," "believe," "estimate," "expect," "hope," "hopeful," "intend," "likely," "may," "optimistic," "possible," "potential," "preliminary," "project," "should," "will" and other analogous expressions. There are numerous factors that could cause our actual results to differ materially from those in the forward-looking statements. Thus, sentences and phrases that we use to convey our view of future events and trends are expressly designated as forward-looking statements as are sections of this Form 10-Q that are identified as giving our outlook on future business.

Forward-looking statements relating to our business include among other things: statements concerning future liquidity and capital requirements, investment valuation and performance, return on equity, financial ratios, net income, premiums, losses and loss reserve, premium rates and retention of current business, competition and market conditions, the expansion of product lines, the development or acquisition of business in new geographical areas, the availability of acceptable reinsurance, actions by regulators and rating agencies, court actions, legislative actions, payment or performance of obligations under indebtedness, payment of dividends, and other matters.

These forward-looking statements are subject to significant risks, assumptions and uncertainties, including, among other things, the following factors that could affect the actual outcome of future events:

- changes in general economic conditions, including the impact of inflation or deflation and unemployment;
- our ability to maintain our dividend payments;
- regulatory, legislative and judicial actions or decisions that could affect our business plans or operations;
- the enactment or repeal of tort reforms;
- formation or dissolution of state-sponsored insurance entities providing coverages now offered by ProAssurance which could remove or add sizable numbers of insureds from or to the private insurance market;
- changes in the interest rate environment;
- changes in U.S. laws or government regulations regarding financial markets or market activity that may affect the U.S. economy and our business;
- changes in the ability of the U.S. government to meet its obligations that may affect the U.S. economy and our business;
- performance of financial markets affecting the fair value of our investments or making it difficult to determine the value of our investments;
- changes in requirements or accounting policies and practices that may be adopted by our regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission (SEC), the Public Company Accounting Oversight Board (PCAOB), or the New York Stock Exchange (NYSE) and that may affect our business;
- changes in laws or government regulations affecting the financial services industry, the property and casualty insurance industry or particular insurance lines underwritten by our subsidiaries;
- the effect on our insureds, particularly the insurance needs of our insureds, and our loss costs, of changes in the healthcare delivery system, including changes attributable to the Patient Protection and Affordable Care Act (the Affordable Care Act);
- consolidation of our insureds into or under larger entities which may be insured by competitors, may not have a risk profile that meets our underwriting criteria or which may not use external providers for insuring or otherwise managing substantial portions of their liability risk;
- uncertainties inherent in the estimate of our loss and loss adjustment expense reserve and reinsurance recoverable;
- changes in the availability, cost, quality, or collectability of insurance/reinsurance;
- the results of litigation, including pre- or post-trial motions, trials and/or appeals we undertake;
- effects on our claims costs from mass tort litigation that are different from that anticipated by us;

allegations of bad faith which may arise from our handling of any particular claim, including failure to settle;
loss or consolidation of independent agents, agencies, brokers, or brokerage firms;
changes in our organization, compensation and benefit plans;
changes in the business or competitive environment may limit the effectiveness of our business strategy and impact our revenues;

Table of Contents

- our ability to retain and recruit senior management;
- the availability, integrity and security of our technology infrastructure or that of our third party providers of technology infrastructure, including any susceptibility to cyber-attacks which might result in a loss of information or operating capability;
- the impact of a catastrophic event, as it relates to both our operations and our insured risks;
- the impact of acts of terrorism and acts of war;
- the effects of terrorism related insurance legislation and laws;
- assessments from guaranty funds;
- our ability to achieve continued growth through expansion into new markets or through acquisitions or business combinations;
- changes to the ratings assigned by rating agencies to our insurance subsidiaries, individually or as a group;
- provisions in our charter documents, Delaware law and state insurance laws may impede attempts to replace or remove management or may impede a takeover;
- state insurance restrictions may prohibit assets held by our insurance subsidiaries, including cash and investment securities, from being used for general corporate purposes;
- taxing authorities can take exception to our tax positions and cause us to incur significant amounts of legal and accounting costs and, if our defense is not successful, additional tax costs, including interest and penalties; and
- expected benefits from completed and proposed acquisitions may not be achieved or may be delayed longer than expected due to business disruption; loss of customers, employees and key agents; increased operating costs or inability to achieve cost savings; and assumption of greater than expected liabilities, among other reasons.

Additional risks that could arise from our membership in the Lloyd's of London market (Lloyd's) and our participation in Lloyd's Syndicate 1729 (Syndicate 1729) include, but are not limited to, the following:

- members of Lloyd's are subject to levies by the Council of Lloyd's based on a percentage of the member's underwriting capacity, currently a maximum of 3%, but can be increased by Lloyd's;
- Syndicate operating results can be affected by decisions made by the Council of Lloyd's over which the management of Syndicate 1729 has little ability to control, such as a decision to not approve the business plan of the Syndicate, or a decision to increase the capital required to continue operations, and by our obligation to pay levies to Lloyd's;
- Lloyd's insurance and reinsurance relationships and distribution channels could be disrupted or Lloyd's trading licenses could be revoked making it more difficult for Syndicate 1729 to distribute and market its products; and
- rating agencies could downgrade their ratings of Lloyd's as a whole.

Our results may differ materially from those we expect and discuss in any forward-looking statements. The principal risk factors that may cause these differences are described in "Item 1A, Risk Factors" in our Form 10-K and other documents we file with the SEC, such as our current reports on Form 8-K, and our regular reports on Form 10-Q. We caution readers not to place undue reliance on any such forward-looking statements, which are based upon conditions existing only as of the date made, and advise readers that these factors could affect our financial performance and could cause actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements. Except as required by law or regulations, we do not undertake and specifically decline any obligation to publicly release the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

TABLE OF CONTENTS

Table of Contents

ProAssurance Corporation and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)
(In thousands, except share data)

	March 31, 2015	December 31, 2014
Assets		
Investments		
Fixed maturities, available for sale, at fair value; amortized cost, $2,942,635 and $3,055,477, respectively	$3,045,497	$3,145,027
Equity securities, trading, at fair value; cost, $300,863 and $283,107, respectively	332,649	314,482
Short-term investments	114,761	131,259
Business owned life insurance	56,837	56,381
Investment in unconsolidated subsidiaries	289,378	276,501
Other investments, $31,664 and $28,958 at fair value, respectively, otherwise at cost or amortized cost	92,487	86,057
Total Investments	3,931,609	4,009,707
Cash and cash equivalents	203,576	197,040
Premiums receivable	209,272	202,528
Receivable from reinsurers on paid losses and loss adjustment expenses	13,366	6,494
Receivable from reinsurers on unpaid losses and loss adjustment expenses	238,604	237,966
Prepaid reinsurance premiums	34,958	32,115
Deferred policy acquisition costs	40,954	38,790
Real estate, net	39,670	39,799
Intangible assets	98,666	100,733
Goodwill	210,725	210,725
Other assets	92,680	93,263
Total Assets	$5,114,080	$5,169,160
Liabilities and Shareholders’ Equity		
Liabilities		
Policy liabilities and accruals		
Reserve for losses and loss adjustment expenses	$2,044,230	$2,058,266
Unearned premiums	373,451	345,828
Reinsurance premiums payable	26,458	17,451
Total Policy Liabilities	2,444,139	2,421,545
Deferred tax liability	30,392	18,818
Other liabilities	160,905	320,853
Long-term debt	350,000	250,000
Total Liabilities	2,985,436	3,011,216
Shareholders’ Equity		
Common shares, par value $0.01 per share, 100,000,000 shares authorized, 62,474,956 and 62,297,214 shares issued, respectively	625	623
Additional paid-in capital	359,135	359,577
Accumulated other comprehensive income (loss), net of deferred tax expense (benefit) of $35,473 and $31,342, respectively	65,877	58,204
Retained earnings	2,012,328	1,991,704
Treasury shares, at cost, 7,022,298 shares and 5,763,388 shares, respectively	(309,321)	(252,164)
Total Shareholders’ Equity	2,128,644	2,157,944
Total Liabilities and Shareholders’ Equity	$5,114,080	$5,169,160

See accompanying notes.

5

Table of Contents

ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Changes in Capital (Unaudited)
(In thousands)

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock	Total
Balance at December 31, 2014	$623	$359,577	$ 58,204	$1,991,704	$(252,164)	$2,157,944
Common shares reacquired	—	—	—	—	(57,157)	(57,157)
Common shares issued for compensation and effect of shares reissued to stock purchase plan	—	1,270	—	—	—	1,270
Share-based compensation	—	2,703	—	—	—	2,703
Net effect of restricted and performance shares issued and stock options exercised	2	(4,415)	—	—	—	(4,413)
Dividends to shareholders	—	—	—	(17,190)	—	(17,190)
Other comprehensive income (loss)	—	—	7,673	—	—	7,673
Net income	—	—	—	37,814	—	37,814
Balance at March 31, 2015	$625	$359,135	$ 65,877	$2,012,328	$(309,321)	$2,128,644

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock	Total
Balance at December 31, 2013	$621	$349,894	$ 59,661	$2,015,603	$(31,365)	$2,394,414
Common shares reacquired	—	—	—	—	(83,658)	(83,658)
Common shares issued for compensation and effect of shares reissued to stock purchase plan	—	1,416	—	—	—	1,416
Share-based compensation	—	3,240	—	—	—	3,240
Net effect of restricted and performance shares issued and stock options exercised	2	(3,002)	—	—	—	(3,000)
Dividends to shareholders	—	—	—	(17,906)	—	(17,906)
Other comprehensive income (loss)	—	—	10,745	—	—	10,745
Net income	—	—	—	46,731	—	46,731
Balance at March 31, 2014	$623	$351,548	$ 70,406	$2,044,428	$(115,023)	$2,351,982

See accompanying notes.

Table of Contents

ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Income and Comprehensive Income (Unaudited)
(In thousands, except per share data)

	Three Months Ended March 31	
	2015	2014
Revenues		
Net premiums earned	$171,899	$171,730
Net investment income	27,304	29,732
Equity in earnings (loss) of unconsolidated subsidiaries	1,622	1,751
Net realized investment gains (losses):		
Other-than-temporary impairment (OTTI) losses	(3,271)	(50)
Portion of OTTI losses recognized in (reclassified from) other comprehensive income before taxes	1,441	—
Net impairment losses recognized in earnings	(1,830)	(50)
Other net realized investment gains (losses)	6,669	2,794
Total net realized investment gains (losses)	4,839	2,744
Other income	2,169	2,094
Total revenues	207,833	208,051
Expenses		
Losses and loss adjustment expenses	118,169	96,052
Reinsurance recoveries	(13,029)	(6,544)
Net losses and loss adjustment expenses	105,140	89,508
Underwriting, policy acquisition and operating expenses	51,356	52,515
Segregated portfolio cells dividend expense	2,184	1,049
Interest expense	3,631	3,570
Total expenses	162,311	146,642
Income before income taxes	45,522	61,409
Provision for income taxes		
Current expense (benefit)	352	7,905
Deferred expense (benefit)	7,356	6,773
Total income tax expense (benefit)	7,708	14,678
Net income	37,814	46,731
Other comprehensive income (loss), after tax, net of reclassification adjustments	7,673	10,745
Comprehensive income	$45,487	$57,476
Earnings per share:		
Basic	$0.67	$0.76
Diluted	$0.67	$0.76
Weighted average number of common shares outstanding:		
Basic	56,592	61,251
Diluted	56,813	61,497
Cash dividends declared per common share	$0.31	$0.30

See accompanying notes.

Table of Contents

ProAssurance Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)
(In thousands)

	Three Months Ended March 31	
	2015	2014
Operating Activities		
Net income	$37,814	$46,731
Adjustments to reconcile income to net cash provided by operating activities:		
Depreciation and amortization, net of accretion	12,086	11,587
Net realized investment gains	(4,839)	(2,744)
Share-based compensation	2,703	3,240
Deferred income taxes	7,356	6,773
Policy acquisition costs, net amortization (net deferral)	(2,164)	(2,370)
Other	(4,856)	2,057
Other changes in assets and liabilities, excluding effect of business combinations:		
Premiums receivable	(6,744)	(16,698)
Reinsurance related assets and liabilities	(1,346)	(12,609)
Other assets	(3,919)	(1,803)
Reserve for losses and loss adjustment expenses	(14,036)	(20,230)
Unearned premiums	27,623	30,439
Other liabilities	(12,835)	(13,938)
Net cash provided (used) by operating activities	$36,843	$30,435
Investing Activities		
Purchases of:		
Fixed maturities, available for sale	$(215,122)	$(130,311)
Equity securities, trading	(97,626)	(20,976)
Other investments	(9,288)	(5,246)
Funding of tax credit limited partnerships	(590)	(1,811)
Investment in unconsolidated subsidiaries	(15,416)	(8,995)
Proceeds from sales or maturities of:		
Fixed maturities, available for sale	323,386	110,647
Equity securities, trading	82,984	62,786
Other investments	3,052	397
Distributions from unconsolidated subsidiaries	4,159	—
Net sales or maturities (purchases) of short-term investments	16,479	110,843
Cash received in acquisitions	—	35,013
Unsettled security transactions, net change	9,246	4,024
(Increase) decrease in restricted cash	—	78,000
Other	(2,857)	4,968
Net cash provided (used) by investing activities	$98,407	$239,339

Continued on following page.

Table of Contents

	Three Months Ended March 31	
	2015	2014
Financing Activities		
Borrowing under revolving credit agreement	$100,000	$—
Repurchase of common stock	(57,157)	(78,976)
Dividends to shareholders	(167,211)	(18,358)
Other	(4,346)	(5,580)
Net cash provided (used) by financing activities	(128,714)	(102,914)
Increase (decrease) in cash and cash equivalents	6,536	166,860
Cash and cash equivalents at beginning of period	197,040	129,383
Cash and cash equivalents at end of period	$203,576	$296,243
Significant non-cash transactions		
Deposit transferred as consideration for acquisition	$—	$205,244
Dividends declared and not yet paid	$17,190	$17,906

See accompanying notes.

1. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of ProAssurance Corporation and its consolidated subsidiaries (ProAssurance, PRA or the Company). The financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation, consisting of normal recurring adjustments, have been included. ProAssurance’s results for the three-month period ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015. The accompanying Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes contained in ProAssurance’s December 31, 2014 report on Form 10-K. In connection with its preparation of the Condensed Consolidated Financial Statements, ProAssurance evaluated events that occurred subsequent to March 31, 2015 for recognition or disclosure in its financial statements and notes to financial statements.

ProAssurance operates in four reportable segments as follows: Specialty Property and Casualty (Specialty P&C), Workers' Compensation, Lloyd's Syndicate, and Corporate. For more information on the nature of products and services provided and for financial information by segment, refer to Note 12 of the Notes to Condensed Consolidated Financial Statements.

Other Liabilities

Other liabilities consisted of the following:

(In millions)	March 31, 2015	December 31, 2014
Segregated portfolio cell dividends payable	$18.0	$15.8
Unpaid dividends	17.2	167.7
All other	125.7	137.4
Total other liabilities	$160.9	$320.9

Segregated portfolio cells (SPCs) are segregated pools of assets and liabilities that provide an insurance facility for a defined set of risks, with the net operating results of the SPC due to the preferred shareholders of that cell. ProAssurance uses SPCs to offer risk-sharing insurance solutions to certain customer groups, and typically owns some portion of each cell. SPC dividends payable represents the cumulative undistributed earnings of SPCs that are contractually payable to external preferred shareholders of the cells.

Unpaid dividends represents common stock dividends declared by ProAssurance's Board of Directors that have not yet been paid. Unpaid dividends were higher at December 31, 2014 due to a special dividend declared in late 2014 that was paid in January 2015.

Accounting Changes Adopted

Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity

Effective for fiscal years beginning after December 15, 2014, the FASB issued guidance which changes the requirements for reporting discontinued operations. Under the new guidance, reporting entities are required to report disposals of business components only if the disposal represents a strategic shift in the entity’s operations that will have a major effect on the entity’s operations and financial results. The new guidance expands disclosure requirements for reported discontinued operations and requires disclosure of pre-tax profit or loss attributable to significant disposals that are not reported as discontinued operations. ProAssurance adopted the guidance as of January 1, 2015. Adoption of the guidance had no effect on ProAssurance’s results of operations or financial position.

Accounting Changes Not Yet Adopted

Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period

Effective for fiscal years beginning after December 15, 2015, the FASB issued guidance for share-based payments in which the terms of the award provide that a performance target can be achieved after completion of the requisite service period. The new guidance provides that compensation cost for such awards should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. ProAssurance plans to adopt the guidance beginning January 1, 2016. Adoption of the guidance is expected to have no effect on ProAssurance’s results of operations or financial position as ProAssurance has no awards with performance targets extending beyond the requisite service period.

Revenue from Contracts with Customers

Effective for fiscal years beginning after December 15, 2016, the FASB issued guidance related to revenue from contracts with customers. The core principle of the new guidance is that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ProAssurance plans to adopt the guidance beginning January 1, 2017. As the majority of ProAssurance's revenues come from insurance contracts which fall under the scope of other FASB standards, adoption of the guidance is expected to have no material effect on ProAssurance’s results of operations or financial position.

Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern

Effective for fiscal years ending after December 15, 2016 and interim periods beginning after December 15, 2016, the FASB issued guidance that establishes principles and definitions related to management's evaluation of whether there is substantial doubt about the organization's ability to continue as a going concern. For each interim and annual reporting period, the new guidance requires management to evaluate the organization's ability to meet its obligations as they are due within one year of the date the financial statements are issued and requires disclosure when there is substantial doubt regarding the organization's ability to continue as a going concern. ProAssurance plans to adopt the guidance on its effective date. Adoption is expected to have no effect on ProAssurance’s results of operations or financial position.

Simplifying the Presentation of Debt Issuance Costs

Effective for fiscal years beginning after December 15, 2015, the FASB issued guidance related to the presentation of debt issuance costs. The new guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ProAssurance plans to adopt the guidance beginning January 1, 2016. Adoption of the guidance is not expected to have a material effect on ProAssurance’s results of operations or financial position.

Amendments to the Consolidation Analysis

Effective for fiscal years beginning after December 15, 2015, the FASB issued additional guidance regarding the consolidation of legal entities such as limited partnerships, limited liability corporations, and securitization structures (collateralized debt obligations, collateralized loan obligations, and mortgage-backed security transactions). The new standard modifies the evaluation of whether or not entities are variable interest entities (VIEs) and the consolidation analysis of entities involved with VIEs, particularly those having fee arrangements and related party relationships. ProAssurance is in the process of evaluating the effect, if any, of the new guidance on its results of operations and financial position and plans to adopt the guidance beginning January 1, 2016. The effect is not expected to be material.

Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement

Effective for fiscal years beginning after December 15, 2015, the FASB issued additional guidance regarding accounting for cloud computing arrangements. Under the new guidance, customers participating in cloud computing arrangements that include a software license should account for the software license element of the arrangement consistent with the acquisition of other software licenses. Customers should account for cloud computing arrangements that do not include a software license as a service contract, following existing guidance for service contracts. ProAssurance is in the process of evaluating the effect that the use of the new method would have on its results of operations and financial position and plans to adopt the guidance beginning January 1, 2016. The effect is not expected to be material.

2. Fair Value Measurement

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A three level hierarchy has been established for valuing assets and liabilities based on how transparent (observable) the inputs are that are used to determine fair value, with the inputs considered most observable categorized as Level 1 and those that are the least observable categorized as Level 3. Hierarchy levels are defined as follows:

Level 1:	quoted (unadjusted) market prices in active markets for identical assets and liabilities. For ProAssurance, Level 1 inputs are generally quotes for debt or equity securities actively traded in exchange or over-the-counter markets.
Level 2:	market data obtained from sources independent of the reporting entity (observable inputs). For ProAssurance, Level 2 inputs generally include quoted prices in markets that are not active, quoted prices for similar assets or liabilities, and results from pricing models that use observable inputs such as interest rates and yield curves that are generally available at commonly quoted intervals.
Level 3:	the reporting entity's own assumptions about market participant assumptions based on the best information available in the circumstances (non-observable inputs). For ProAssurance, Level 3 inputs are used in situations where little or no Level 1 or 2 inputs are available or are inappropriate given the particular circumstances. Level 3 inputs include results from pricing models for which some or all of the inputs are not observable, discounted cash flow methodologies, single non-binding broker quotes and adjustments to externally quoted prices that are based on management judgment or estimation.

Fair values of assets measured at fair value on a recurring basis as of March 31, 2015 and December 31, 2014 are shown in the following tables. The tables also indicate the fair value hierarchy of the valuation techniques utilized to determine those fair values. For some assets, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. When this is the case, the asset is categorized based on the level of the most significant input to the fair value measurement. Assessments of the significance of a particular input to the fair value measurement require judgment and consideration of factors specific to the assets being valued.

Table of Contents
ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

	March 31, 2015			
	Fair Value Measurements Using			Total
(In thousands)	Level 1	Level 2	Level 3	Fair Value
Assets:				
Fixed maturities, available for sale				
U.S. Treasury obligations	$—	$89,389	$—	$89,389
U.S. Government-sponsored enterprise obligations	—	37,558	—	37,558
State and municipal bonds	—	1,020,129	5,025	1,025,154
Corporate debt, multiple observable inputs	—	1,433,002	—	1,433,002
Corporate debt, limited observable inputs:				
Other corporate debt, NRSRO ratings available	—	—	9,293	9,293
Other corporate debt, NRSRO ratings not available	—	—	684	684
Residential mortgage-backed securities	—	281,122	—	281,122
Agency commercial mortgage-backed securities	—	13,898	—	13,898
Other commercial mortgage-backed securities	—	44,826	—	44,826
Other asset-backed securities	—	105,783	4,788	110,571
Equity securities				
Financial	81,753	—	—	81,753
Utilities/Energy	31,690	—	—	31,690
Consumer oriented	66,053	—	—	66,053
Industrial	60,755	—	—	60,755
Bond funds	69,945	—	—	69,945
All other	22,453	—	—	22,453
Short-term investments	114,761	—	—	114,761
Financial instruments carried at fair value, classified as a part of:				
Investment in unconsolidated subsidiaries	—	—	145,888	145,888
Other investments	6,245	25,419	—	31,664
Total assets	$453,655	$3,051,126	$165,678	$3,670,459

	December 31, 2014			
	Fair Value Measurements Using			Total
(In thousands)	Level 1	Level 2	Level 3	Fair Value
Assets:				
Fixed maturities, available for sale				
U.S. Treasury obligations	$—	$166,512	$—	$166,512
U.S. Government-sponsored enterprise obligations	—	39,563	—	39,563
State and municipal bonds	—	1,057,590	5,025	1,062,615
Corporate debt, multiple observable inputs	—	1,404,020	—	1,404,020
Corporate debt, limited observable inputs:				
Other corporate debt, NRSRO ratings available	—	—	10,474	10,474
Other corporate debt, NRSRO ratings not available	—	—	2,607	2,607
Residential mortgage-backed securities	—	276,056	—	276,056
Agency commercial mortgage-backed securities	—	15,493	—	15,493
Other commercial mortgage-backed securities	—	51,063	—	51,063
Other asset-backed securities	—	111,855	4,769	116,624
Equity securities				
Financial	79,341	—	—	79,341
Utilities/Energy	25,629	—	—	25,629
Consumer oriented	65,670	—	—	65,670
Industrial	55,460	—	—	55,460
Bond funds	55,196	—	—	55,196
All other	33,186	—	—	33,186
Short-term investments	131,199	60	—	131,259
Financial instruments carried at fair value, classified as a part of:				
Investment in unconsolidated subsidiaries	—	—	133,250	133,250
Other investments	6,050	22,908	—	28,958
Total assets	$451,731	$3,145,120	$156,125	$3,752,976

The fair values for securities included in the Level 2 category, with the few exceptions described below, were developed by one of several third party, nationally recognized pricing services, including services that price only certain types of securities. Each service uses complex methodologies to determine values for securities and subject the values they develop to quality control reviews. Management selected a primary source for each type of security in the portfolio, and reviewed the values provided for reasonableness by comparing data to alternate pricing services and to available market and trade data. Values that appeared inconsistent were further reviewed for appropriateness. If a value did not appear reasonable, the valuation was discussed with the service that provided the value and would have been adjusted, if necessary. No such adjustments were necessary in 2015 or 2014.

Level 2 Valuations

Below is a summary description of the valuation methodologies primarily used by the pricing services for securities in the Level 2 category, by security type:

U.S. Treasury obligations were valued based on quoted prices for identical assets, or, in markets that are not active, quotes for similar assets, taking into consideration adjustments for variations in contractual cash flows and yields to maturity.

U.S. Government-sponsored enterprise obligations were valued using pricing models that consider current and historical market data, normal trading conventions, credit ratings, and the particular structure and characteristics of the security being valued, such as yield to maturity, redemption options, and contractual cash flows. Adjustments to model inputs or model results were included in the valuation process when necessary to reflect recent regulatory, government or corporate actions or significant economic, industry or geographic events affecting the security's fair value.

State and municipal bonds were valued using a series of matrices that considered credit ratings, the structure of the security, the sector in which the security falls, yields, and contractual cash flows. Valuations were further adjusted, when necessary, to reflect the expected effect on fair value of recent significant economic or geographic events or ratings changes.

Corporate debt with multiple observable inputs consisted primarily of corporate bonds, but also included a small number of bank loans. The methodology used to value Level 2 corporate bonds was the same as the methodology previously described for U.S. Government-sponsored enterprise obligations. Bank loans were valued based on an average of broker quotes for the loans in question, if available. If quotes are not available, the loans are valued based on quoted prices for comparable loans or, if the loan is newly issued, by comparison to similar seasoned issues. Broker quotes are compared to actual trade prices on a regular basis to permit assessment of the reliability of the quotes; unreliable quotes are not considered in quoted averages.

Residential and commercial mortgage backed securities. Agency pass-through securities were valued using a pricing matrix which considers the issuer type, coupon rate and longest cash flows outstanding. The matrix used was based on the most recently available market information. Agency and non-agency collateralized mortgage obligations were both valued using models that consider the structure of the security, current and historical information regarding prepayment speeds, ratings and ratings updates, and current and historical interest rate and interest rate spread data.

Other asset-backed securities were valued using models that consider the structure of the security, monthly payment information, current and historical information regarding prepayment speeds, ratings and ratings updates, and current and historical interest rate and interest rate spread data. Spreads and prepayment speeds considered collateral type.

Short-term investments are securities maturing within one year, carried at cost which approximated the fair value of the security due to the short term to maturity.

Other investments consisted of convertible bonds valued using a pricing model that incorporated selected dealer quotes as well as current market data regarding equity prices and risk free rates. If dealer quotes were unavailable for the security being valued, quotes for securities with similar terms and credit status were used in the pricing model. Dealer quotes selected for use were those considered most accurate based on parameters such as underwriter status and historical reliability.

Level 3 Valuations

Below is a summary description of the valuation processes and methodologies used as well as quantitative information regarding securities in the Level 3 category.

Level 3 Valuation Processes

- Level 3 securities are priced by the Chief Investment Officer.
- Level 3 valuations are computed quarterly. Prices are evaluated quarterly against prior period prices and the expected change in price.
- Exclusive of Investments in unconsolidated subsidiaries, which are valued at net asset value (NAV), the securities noted in the disclosure are primarily NRSRO rated debt instruments for which comparable market inputs are commonly available for evaluating the securities in question. Valuation of these debt instruments is not overly sensitive to changes in the unobservable inputs used.

Level 3 Valuation Methodologies

State and municipal bonds consisted of auction rate municipal bonds valued internally using either published quotes for similar securities or values produced by discounted cash flow models using yields currently available on fixed rate securities with a similar term and collateral, adjusted to consider the effect of a floating rate and a premium for illiquidity. At March 31, 2015, 100% of the securities were rated; the average rating was A-.

Corporate debt with limited observable inputs consisted of corporate bonds valued using dealer quotes for similar securities or discounted cash flow models using yields currently available for similar securities. Similar securities are defined as securities of comparable credit quality that have like terms and payment features. Assessments of credit quality were based on NRSRO ratings, if available, or were subjectively determined by management if not available. At March 31, 2015, the average rating of rated securities was BBB+.

Other asset-backed securities consisted of securitizations of receivables valued using dealer quotes for similar securities or discounted cash flow models using yields currently available for similar securities.

Investment in unconsolidated subsidiaries consisted of limited partnership (LP) and limited liability company (LLC) interests valued using the NAV provided by the LP/LLC, which approximated the fair value of the interest. Such interests include the following:

	Unfunded Commitments	Fair Value	
(In thousands)	March 31, 2015	March 31, 2015	December 31, 2014
Investments in LPs/LLCs:			
Private debt funds (1)	$24,285	$40,325	$37,296
Long equity fund (2)	None	6,949	6,747
Long/short equity funds (3)	None	25,262	25,301
Non-public equity funds (4)	$59,893	61,060	51,811
Multi-strategy fund of funds (5)	None	8,402	8,271
Structured credit fund (6)	None	3,890	3,824
		$145,888	$133,250

(1) Comprised of interests in two unrelated LP funds that are structured to provide interest distributions primarily through diversified portfolios of private debt instruments. One LP allows redemption by special consent; the other does not permit redemption. Income and capital are to be periodically distributed at the discretion of the LPs over an anticipated time frame that spans from 3 to 8 years.

(2) The fund is an LP that holds long equities of public international companies. Redemptions are allowed at the end of any calendar month with a prior notice requirement of 15 days and are paid within 10 days of the end of the calendar month of the redemption request.

(3) Comprised of interests in multiple unrelated LP funds. The funds hold primarily long and short North American equities, and target absolute returns using strategies designed to take advantage of event-driven market opportunities. The funds generally permit quarterly or semi-annual capital redemptions subject to notice requirements of 30 to 90 days. For some funds, redemptions above specified thresholds (lowest threshold is 90%) may be only partially payable until after a fund audit is completed and are then payable within 30 days.

(4) Comprised of interests in three unrelated LP funds, each structured to provide capital appreciation through diversified investments in private equity, which can include investments in buyout, venture capital, mezzanine debt, distressed debt and other private equity-oriented LPs. One LP allows redemption by special consent; the others do not permit redemption. Income and capital are to be periodically distributed at the discretion of the LP over time frames that are anticipated to span of up to 9 years.

(5) This fund is an LLC structured to build and manage low volatility, multi-manager portfolios that have little or no correlation to the broader fixed income and equity security markets. Redemptions are not permitted but the LLC Board is permitted discretion to periodically extend offers to repurchase units of the LLC.

(6) This fund is an LP seeking to obtain superior risk-adjusted absolute returns by acquiring and actively managing a diversified portfolio of debt securities, including bonds, loans and other asset-backed instruments. Redemptions are allowed at any quarter-end with a prior notice requirement of 90 days.

ProAssurance may not sell, transfer or assign its interest in any of the above LPs/LLCs without special consent from the LPs/LLCs.

Table of Contents

ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

Quantitative Information Regarding Level 3 Valuations
Quantitative Information about Level 3 Fair Value Measurements

(In millions)	Fair Value at March 31, 2015	Fair Value at December 31, 2014	Valuation Technique	Unobservable Input	Range (Weighted Average)
Assets:					
State and municipal bonds	$5.0	$5.0	Market Comparable Securities	Comparability Adjustment	0% - 10% (5%)
			Discounted Cash Flows	Comparability Adjustment	0% - 10% (5%)
Corporate debt with limited observable inputs	$10.0	$13.1	Market Comparable Securities	Comparability Adjustment	0% - 5% (2.5%)
			Discounted Cash Flows	Comparability Adjustment	0% - 5% (2.5%)
Other asset-backed securities	$4.8	$4.8	Market Comparable Securities	Comparability Adjustment	0% - 5% (2.5%)
			Discounted Cash Flows	Comparability Adjustment	0% - 5% (2.5%)

The significant unobservable inputs used in the fair value measurement of the above listed securities were the valuations of comparable securities with similar issuers, credit quality and maturity. Changes in the availability of comparable securities could result in changes in the fair value measurements.

Fair Value Measurements - Level 3 Assets

The following tables (the Level 3 Tables) present summary information regarding changes in the fair value of assets measured at fair value using Level 3 inputs.

(In thousands)	March 31, 2015 Level 3 Fair Value Measurements – Assets U.S. Government-sponsored Enterprise Obligations	State and Municipal Bonds	Corporate Debt	Asset-backed Securities	Investment in Unconsolidated Subsidiaries	Total
Balance December 31, 2014	$—	$5,025	$13,081	$4,769	$ 133,250	$156,125
Total gains (losses) realized and unrealized:						
Included in earnings, as a part of:						
Net investment income	—	—	17	—	—	17
Equity in earnings of unconsolidated subsidiaries	—	—	—	—	3,501	3,501
Net realized investment gains (losses)	—	—	2	—	—	2
Included in other comprehensive income	—	—	(283)	19	—	(264)
Purchases	—	—	1,516	—	13,570	15,086
Sales	—	—	(301)	—	(4,433)	(4,734)

Transfers in	—	—	—	—	—	—
Transfers out	—	—	(4,055)	—	—	(4,055)
Balance March 31, 2015	$—	$5,025	$9,977	$4,788	$ 145,888	$165,678
Change in unrealized gains (losses) included in earnings for the above period for Level 3 assets held at period-end	$—	$—	$—	$—	$ 3,501	$3,501

Table of Contents
ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

(In thousands)	March 31, 2014 Level 3 Fair Value Measurements – Assets U.S. Government-sponsored Enterprise Obligations	State and Municipal Bonds	Corporate Debt	Asset-backed Securities	Investment in Unconsolidated Subsidiaries	Total
Balance December 31, 2013	$—	$7,338	$14,176	$6,814	$ 72,062	$100,390
Total gains (losses) realized and unrealized:						
Included in earnings, as a part of:						
Net investment income	—	(2)	16	—	—	14
Equity in earnings of unconsolidated subsidiaries	—	—	—	—	2,865	2,865
Net realized investment gains (losses)	—	(95)	3	—	—	(92)
Included in other comprehensive income	(1)	68	669	44	—	780
Purchases	1,000	1,861	—	2,165	18,436	23,462
Sales	—	(257)	(458)	—	(1,456)	(2,171)
Transfers in	—	570	—	305	—	875
Transfers out	—	(1,993)	(2,025)	(2,102)	—	(6,120)
Balance March 31, 2014	$999	$7,490	$12,381	$7,226	$ 91,907	$120,003
Change in unrealized gains (losses) included in earnings for the above period for Level 3 assets held at period-end	$—	$—	$—	$—	$ 2,865	$2,865

Transfers
There were no transfers between the Level 1 and Level 2 categories during the three months ended March 31, 2015 or 2014.
Transfers shown in the preceding Level 3 Tables were as of the end of the period and were to or from Level 2, unless otherwise noted.
All transfers during the three months ended March 31, 2015 and March 31, 2014 related to securities held for which the level of market activity for identical or nearly identical securities varies from period to period. The securities were valued using multiple observable inputs when those inputs were available; otherwise the securities were valued using limited observable inputs.

Financial Instruments - Methodologies Other Than Fair Value

The following table provides the estimated fair value of our financial instruments that, in accordance with GAAP for the type of investment, are measured using a methodology other than fair value. All fair values provided fall within the Level 3 fair value category.

	March 31, 2015		December 31, 2014	
(In thousands)	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
Business Owned Life Insurance (BOLI)	$56,837	$56,837	$56,381	$56,381
Other investments	$60,823	$58,855	$57,099	$57,994
Other assets	$24,017	$23,989	$22,440	$22,399
Financial liabilities:				
Senior notes due 2023	$250,000	$277,100	$250,000	$276,503
Revolving credit agreement	$100,000	$100,000	$—	$—
Other liabilities	$15,117	$15,111	$14,656	$14,645

The fair value of the BOLI was equal to the cash surrender value associated with the policies on the valuation date.

Other investments listed in the table above include interests in certain investment fund LPs/LLCs accounted for using the cost method, investments in Federal Home Loan Bank (FHLB) common stock carried at cost, and an annuity investment carried at amortized cost. The estimated fair value of the LP/LLC interests was based on the NAVs provided by the LP/LLC managers. The estimated fair value of the FHLB common stock was based on the amount ProAssurance would receive if its membership were canceled, as the membership cannot be sold. The fair value of the annuity represents the present value of the expected future cash flows discounted using a rate available in active markets for similarly structured instruments.

Other assets and Other liabilities primarily consisted of related investment assets and liabilities associated with funded deferred compensation agreements. Fair values of the funded deferred compensation assets and liabilities were based on the NAVs of the underlying securities. Other assets also included a secured note receivable and an unsecured receivable under a revolving credit agreement. Fair value of these receivables was based on the present value of expected cash flows from the receivables, discounted at market rates on the valuation date for receivables with similar credit standings and similar payment structures. Other liabilities also included certain contractual liabilities related to prior business combinations. The fair values of the business combination liabilities were based on the present value of the expected future cash outflows, discounted at ProAssurance’s assumed incremental borrowing rate on the valuation date for unsecured liabilities with similar repayment structures.

The fair value of the long-term debt was estimated based on the present value of expected future cash outflows, discounted at rates available on the valuation date for similar debt issued by entities with a similar credit standing to ProAssurance.

3. Investments

Available-for-sale securities at March 31, 2015 and December 31, 2014 included the following:

	March 31, 2015			
(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities				
U.S. Treasury obligations	$86,729	$2,732	$72	$89,389
U.S. Government-sponsored enterprise obligations	35,972	1,616	30	37,558
State and municipal bonds	978,713	46,830	389	1,025,154
Corporate debt	1,402,723	52,957	12,701	1,442,979
Residential mortgage-backed securities	270,934	10,403	215	281,122
Agency commercial mortgage-backed securities	13,635	285	22	13,898
Other commercial mortgage-backed securities	43,852	1,005	31	44,826
Other asset-backed securities	110,077	545	51	110,571
	$2,942,635	$116,373	$13,511	$3,045,497

	December 31, 2014			
(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities				
U.S. Treasury obligations	$163,714	$3,785	$987	$166,512
U.S. Government-sponsored enterprise obligations	38,022	1,641	100	39,563
State and municipal bonds	1,015,555	47,395	335	1,062,615
Corporate debt	1,389,970	44,234	17,103	1,417,101
Residential mortgage-backed securities	266,306	10,198	448	276,056
Agency commercial mortgage-backed securities	15,344	208	59	15,493
Other commercial mortgage-backed securities	50,025	1,137	99	51,063
Other asset-backed securities	116,541	288	205	116,624
	$3,055,477	$108,886	$19,336	$3,145,027

Table of Contents
ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

The recorded cost basis and estimated fair value of available-for-sale fixed maturities at March 31, 2015, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(In thousands)	Amortized Cost	Due in one year or less	Due after one year through five years	Due after five years through ten years	Due after ten years	Total Fair Value
Fixed maturities, available for sale						
U.S. Treasury obligations	$86,729	$5,317	$69,599	$11,131	$3,342	$89,389
U.S. Government-sponsored enterprise obligations	35,972	2,807	25,696	8,710	345	37,558
State and municipal bonds	978,713	53,150	361,772	443,677	166,555	1,025,154
Corporate debt	1,402,723	106,913	733,014	573,797	29,255	1,442,979
Residential mortgage-backed securities	270,934	—	—	—	—	281,122
Agency commercial mortgage-backed securities	13,635	—	—	—	—	13,898
Other commercial mortgage-backed securities	43,852	—	—	—	—	44,826
Other asset-backed securities	110,077	—	—	—	—	110,571
	$2,942,635					$3,045,497

Excluding obligations of the U.S. Government or U.S. Government-sponsored enterprises, no investment in any entity or its affiliates exceeded 10% of Shareholders' equity at March 31, 2015.

Cash and securities with a carrying value of $50.0 million at March 31, 2015 were on deposit with various state insurance departments to meet regulatory requirements. ProAssurance also held securities with a carrying value of $127.5 million at March 31, 2015 that are pledged as collateral security for advances under the Revolving Credit Agreement (see Note 8 of the Notes to Condensed Consolidated Financial Statements).

As a member of Lloyd's and a capital provider to Syndicate 1729, ProAssurance is required to maintain capital at Lloyd's, referred to as Funds at Lloyd's (FAL). ProAssurance investments at March 31, 2015 included fixed maturities with a fair value of $84.7 million and short term investments with a fair value of approximately $1.0 million on deposit with Lloyd's in order to satisfy these FAL requirements.

BOLI

ProAssurance holds BOLI policies that are carried at the current cash surrender value of the policies (original cost $33 million). All insured individuals were management employees at the time the policies were acquired. The primary purpose of the program is to offset future employee benefit expenses through earnings on the cash value of the policies. ProAssurance is the owner and principal beneficiary of these policies.

Other Investments

Other investments at March 31, 2015 and December 31, 2014 were comprised as follows:

(In thousands)	March 31, 2015	December 31, 2014
Investments in LPs/LLCs, at cost	$57,218	$53,258
Convertible securities, at fair value	31,664	28,958
Other, principally FHLB capital stock, at cost	3,605	3,841
	$92,487	$86,057

Investments in convertible securities are carried at fair value as permitted by the accounting guidance for hybrid financial instruments, with changes in fair value recognized in income as a component of Net realized investment

gains or losses during the period of change. Interest on convertible securities is recorded on an accrual basis based on contractual interest rates and is included in Net investment income.
FHLB capital stock is not marketable, but may be liquidated by terminating membership in the FHLB. The liquidation process can take up to five years.

Table of Contents
ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

Unconsolidated Subsidiaries
ProAssurance holds investments in unconsolidated subsidiaries, accounted for under the equity method. The investments include the following:

(In thousands)	March 31, 2015 Unfunded Commitments*	Percentage Ownership		Carrying Value March 31, 2015	December 31, 2014
Investment in LPs/LLCs:					
Qualified affordable housing tax credit partnerships	$14,947	See below		$130,622	$133,143
Other tax credit partnerships	$17,881	See below		2,119	—
Private debt funds	$24,285	<	20%	40,325	37,296
Long equity fund	None	<	20%	6,949	6,747
Long/short equity funds	None	<	25%	25,262	25,301
Non-public equity funds	$73,419	<	20%	67,646	58,128
Multi-strategy fund of funds	None	<	20%	8,402	8,271
Structured credit fund	None	<	20%	3,890	3,824
Real estate fund	$6,526	<	20%	4,163	3,791
				$289,378	$276,501

* Unfunded commitments are included in the carrying value of tax credit partnerships only.

Qualified affordable housing tax credit partnership interests held by ProAssurance generate investment returns by providing tax benefits to fund investors in the form of tax credits and project operating losses. ProAssurance's ownership percentage relative to two of the tax credit partnership interests is almost 100%; these interests had a carrying value of $56.9 million at March 31, 2015. ProAssurance's ownership percentage relative to the remaining tax credit partnership interests is less than 20%; these interests had a carrying value of $73.7 million at March 31, 2015. ProAssurance does not have the ability to exert control over the partnerships; all are accounted for using the equity method.

Other tax credit partnerships are comprised entirely of historic tax credits. The historic tax credits generate investment returns by providing tax benefits to fund investors in the form of tax credits, project operating losses as well as returns of cash from operations. ProAssurance's ownership percentage relative to the tax credit partnership is almost 100%. ProAssurance does not have the ability to exert control over the partnership; the interests are accounted for using the equity method.

The Private debt funds are structured to provide interest distributions primarily through a diversified portfolio of private debt investments.

The Long equity fund targets long-term total returns through holdings in public international companies.

The Long/Short equity funds target absolute returns using strategies designed to take advantage of event-driven market opportunities.

The Non-public equity funds hold diversified private equities and are structured to provide capital appreciation.

The Multi-strategy fund of funds holds portfolios having little or no correlation to the broader fixed income and equity security markets.

The Structured credit fund seeks to obtain superior risk-adjusted absolute returns by acquiring and actively managing a diversified portfolio of debt securities.

The Real estate fund invests in multi-tenant industrial real estate with the objective of achieving superior absolute returns in all market cycles.

Table of Contents
ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

Investments Held in a Loss Position
The following tables provide summarized information with respect to investments held in an unrealized loss position at March 31, 2015 and December 31, 2014, including the length of time the investment had been held in a continuous unrealized loss position.

	March 31, 2015					
	Total		Less than 12 months		12 months or longer	
(In thousands)	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Fixed maturities, available for sale						
U.S. Treasury obligations	$16,584	$72	$10,446	$26	$6,138	$46
U.S. Government-sponsored enterprise obligations	5,210	30	5,210	30	—	—
State and municipal bonds	41,323	389	34,413	214	6,910	175
Corporate debt	251,302	12,701	198,137	9,631	53,165	3,070
Residential mortgage-backed securities	41,413	215	31,352	121	10,061	94
Agency commercial mortgage-backed securities	428	22	—	—	428	22
Other commercial mortgage-backed securities	8,260	31	4,225	11	4,035	20
Other asset-backed securities	32,062	51	31,157	51	905	—
	$396,582	$13,511	$314,940	$10,084	$81,642	$3,427
Other investments						
Investments in LPs/LLCs carried at cost	$31,660	$3,208	$31,660	$3,208	$—	$—

	December 31, 2014					
	Total		Less than 12 months		12 months or longer	
(In thousands)	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Fixed maturities, available for sale						
U.S. Treasury obligations	$61,209	$987	$46,869	$617	$14,340	$370
U.S. Government-sponsored enterprise obligations	6,268	100	2,775	44	3,493	56
State and municipal bonds	39,831	335	18,910	84	20,921	251
Corporate debt	423,107	17,103	326,804	13,236	96,303	3,867
Residential mortgage-backed securities	45,006	448	14,406	31	30,600	417
Agency commercial mortgage-backed securities	4,783	59	70	—	4,713	59
Other commercial mortgage-backed securities	13,860	99	7,005	28	6,855	71
Other asset-backed securities	62,577	205	59,176	109	3,401	96
	$656,641	$19,336	$476,015	$14,149	$180,626	$5,187
Other investments						
Investments in LPs/LLCs carried at cost	$23,683	$3,948	$22,265	$3,711	$1,418	$237

As of March 31, 2015, excluding U.S. government backed securities, there were 364 debt securities (13.0% of all available-for-sale fixed maturity securities held) in an unrealized loss position representing 301 issuers. The greatest and second greatest unrealized loss position among those securities were approximately $1.1 million and $0.9 million, respectively. The securities were evaluated for impairment as of March 31, 2015.

As of December 31, 2014, excluding U.S. government backed securities, there were 588 debt securities (20.5% of all available-for-sale fixed maturity securities held) in an unrealized loss position representing 434 issuers. Both the greatest and second greatest unrealized loss position among those securities approximated $1.7 million. The securities were evaluated for impairment as of December 31, 2014.

Each quarter, ProAssurance performs a detailed analysis for the purpose of assessing whether any of the securities it holds in an unrealized loss position have suffered an other-than-temporary impairment in value. A detailed discussion of the factors considered in the assessment is included in Note 1 of the Notes to Consolidated Financial Statements included in ProAssurance's December 31, 2014 Form 10-K.

Fixed maturity securities held in an unrealized loss position at March 31, 2015, excluding asset-backed securities, have paid all scheduled contractual payments and are expected to continue doing so. Expected future cash flows of asset-backed securities held in an unrealized loss position were estimated as part of the March 31, 2015 impairment evaluation using the most recently available six-month historical performance data for the collateral (loans) underlying the security or, if historical data was not available, sector based assumptions, and equaled or exceeded the current amortized cost basis of the security.

Net Investment Income

Net investment income by investment category was as follows:

	Three Months Ended March 31	
(In thousands)	2015	2014
Fixed maturities	$24,959	$28,041
Equities	3,013	2,267
Short-term and Other investments	504	1,412
Business owned life insurance	456	446
Investment fees and expenses	(1,628)	(2,434)
Net investment income	$27,304	$29,732

Equity in Earnings (Loss) from Unconsolidated Subsidiaries

Equity in earnings (loss) from unconsolidated subsidiaries included losses due to amortization resulting from the allocable portion of the projected operating losses of qualified affordable housing project tax credits investments of $2.5 million and $1.7 million for the three-month periods ended March 31, 2015, and 2014, respectively.

Net Realized Investment Gains (Losses)

Realized investment gains and losses are recognized on the specific identification basis. The following table provides detailed information regarding net realized investment gains (losses):

	Three Months Ended March 31	
(In thousands)	2015	2014
Total other-than-temporary impairment losses:		
State and municipal bonds	$—	$(50)
Corporate debt	(3,271)	—
Portion recognized in (reclassified from) Other Comprehensive Income:		
Corporate debt	1,441	—
Net impairments recognized in earnings	$(1,830)	$(50)
Gross realized gains, available-for-sale securities	4,013	805
Gross realized (losses), available-for-sale securities	(1,255)	(54)
Net realized gains (losses), trading securities	2,667	13,783
Net realized gains (losses), Other investments	116	198
Change in unrealized holding gains (losses), trading securities	858	(12,946)
Change in unrealized holding gains (losses), convertible securities, carried at fair value	270	1,008
Net realized investment gains (losses)	$4,839	$2,744

During the first quarter of 2015, ProAssurance recognized credit-related impairments of $1.8 million related to its investments in high-yield securities from three issuers in the energy industry. ProAssurance also recognized non-credit impairments of $1.4 million related to these securities as the fair value of the securities was less than the future cash flows expected to be received from the securities.

The following table presents a roll forward of cumulative credit losses recorded in earnings related to impaired debt securities for which a portion of the other-than-temporary impairment was recorded in Other comprehensive income.

	Three Months Ended March 31	
(In thousands)	2015	2014
Balance beginning of period	$232	$83
Additional credit losses recognized during the period, related to securities for which:		
No OTTI has been previously recognized	1,830	—
Balance March 31	$2,062	$83

Other information regarding sales and purchases of available-for-sale securities is as follows:

	Three Months Ended March 31	
(In millions)	2015	2014
Proceeds from sales (exclusive of maturities and paydowns)	$205.9	$16.8
Purchases	$215.1	$130.3

4. Income Taxes
ProAssurance estimates its annual effective tax rate at the end of each quarterly reporting period and uses this estimated rate to record the provision for income taxes in the interim financial statements. The provision for income taxes is different from that which would be obtained by applying the statutory Federal income tax rate to income before taxes primarily because a portion of ProAssurance’s investment income is tax-exempt and because ProAssurance utilizes tax credit benefits transferred from tax credit partnership investments.
ProAssurance had receivables for federal income taxes of $1.2 million at March 31, 2015 and $1.1 million at December 31, 2014, both carried as a part of Other Assets. The liability for unrecognized tax benefits was $0.6 million at both March 31, 2015 and December 31, 2014.
5. Deferred Policy Acquisition Costs
Policy acquisition costs that are primarily and directly related to the successful production of new and renewal insurance contracts, most significantly agent commissions, premium taxes, and underwriting salaries and benefits, are capitalized as policy acquisition costs and amortized to expense, net of ceding commissions earned, as the related premium revenues are earned.
Amortization of deferred policy acquisition costs was $19.0 million and $19.8 million for the three months ended March 31, 2015 and 2014, respectively.
6. Reserve for Losses and Loss Adjustment Expenses
The reserve for losses is established based on estimates of individual claims and actuarially determined estimates of future losses based on ProAssurance’s past loss experience, available industry data and projections as to future claims frequency, severity, inflationary trends and settlement patterns. Estimating the reserve, particularly the reserve appropriate for liability exposures, is a complex process. Claims may be resolved over an extended period of time, often five years or more, and may be subject to litigation. Estimating losses requires ProAssurance to make and revise judgments and assessments regarding multiple uncertainties over an extended period of time. As a result, the reserve estimate may vary significantly from the eventual outcome. The assumptions used in establishing ProAssurance’s reserve are regularly reviewed and updated by management as new data becomes available. Changes to estimates of previously established reserves are included in earnings in the period in which the estimate is changed.
During the three months ended March 31, 2015, ProAssurance recognized favorable net loss development of $33.5 million, related to prior accident years. The favorable net loss development primarily reflected reductions in the Company's estimates of claims severity related to the 2008 through 2012 accident years.
For the three months ended March 31, 2014, ProAssurance recognized favorable net loss development of $48.1 million which primarily reflected reductions in estimated claims severity related to the 2007 through 2011 accident years.
7. Commitments and Contingencies
ProAssurance is involved in various legal actions related to insurance policies and claims handling including, but not limited to, claims asserted by policyholders. These types of legal actions arise in the Company's ordinary course of business and, in accordance with GAAP for insurance entities, are considered as a part of the Company's loss reserving process, which is described in detail under the heading "Losses and Loss Adjustment Expenses" in the Accounting Policies section in Note 1 of the Notes to Consolidated Financial Statements in ProAssurance's 2014 Form 10-K.
ProAssurance has funding commitments primarily related to non-public investment entities totaling approximately $152.8 million, expected to be paid as follows: $76.9 million in 2015, $74.4 million in 2016 and 2017 combined, $0.7 million in 2018 and 2019 combined, and $0.8 million thereafter. Of these funding commitments, $14.9 million are related to qualified affordable housing project tax credit investments and are expected to be paid as follows: $13.5 million in 2015, $0.5 million in 2016 and 2017 combined, $0.3 million in 2018 and 2019 combined and $0.6 million thereafter.

As a member of Lloyd's and a capital provider to Syndicate 1729, ProAssurance is required to provide capital, referred to as FAL. At March 31, 2015, ProAssurance was satisfying the FAL requirement with investment securities on deposit with Lloyd's with a carrying value of $85.7 million (see Note 3).

ProAssurance has issued an unconditional revolving credit agreement (the "Syndicate Credit Agreement") of up to £10 million to the Premium Trust Fund of Syndicate 1729 for the purpose of providing working capital. Advances under the Syndicate Credit Agreement bear interest at 8.5% annually, and are repayable upon demand after December 31, 2016. As of

March 31, 2015, the unused commitment under the Syndicate Credit Agreement approximated £2.0 million ($3.0 million as of March 31, 2015).

8. Long-term Debt

ProAssurance’s outstanding long-term debt consisted of the following:

(In thousands)	March 31, 2015	December 31, 2014
Senior notes due 2023, unsecured, interest at 5.3% annually	$250,000	$250,000
Revolving credit agreement, outstanding borrowings not permitted to exceed $200 million aggregately, expires in 2016. The interest rate on a borrowing is set at the time the borrowing is initiated or renewed. The outstanding borrowing at March 31, 2015 was fully secured, see Note 3, and carried at an interest rate of 0.75%. The current borrowing can be repaid or renewed in July 2015. If renewed, the interest rate will reset.	100,000	—
	$350,000	$250,000

Covenant Compliance

There are no financial covenants associated with the Senior Notes due 2023.

The revolving credit agreement (the Revolving Credit Agreement) contains customary representations, covenants and events constituting default, and remedies for default. The Revolving Credit Agreement also defines financial covenants regarding permitted leverage ratios and minimum net worth. ProAssurance is currently in compliance with all covenants of the Agreement.

Additional Information

For additional information regarding ProAssurance's long-term debt, see Note 10 of the Notes to Consolidated Financial Statements included in ProAssurance's December 31, 2014 Form 10-K.

9. Shareholders' Equity
At March 31, 2015 and December 31, 2014, ProAssurance had 100 million shares of authorized common stock and 50 million shares of authorized preferred stock. The Board has the authority to determine provisions for the issuance of preferred shares, including the number of shares to be issued, the designations, powers, preferences and rights, and the qualifications, limitations or restrictions of such shares. To date, the Board has not approved the issuance of preferred stock.
ProAssurance declared cash dividends of $0.31 per share during the first quarter of 2015, totaling $17.2 million. ProAssurance declared cash dividends of $0.30 per share during the first quarter of 2014, totaling $17.9 million.
At March 31, 2015, Board authorizations for the repurchase of common shares or the retirement of outstanding debt of $124.4 million remained available for use. ProAssurance repurchased approximately 1.3 million and 1.8 million shares at a total cost of $57.2 million and $83.7 million, during the three-month period ended March 31, 2015 and 2014, respectively.
Share-based compensation expense was $2.7 million for the three months ended March 31, 2015 and $3.2 million for the three months ended March 31, 2014. Related tax benefits were $0.9 million for the three months ended March 31, 2015, and$1.1 million for the three months ended March 31, 2014.
ProAssurance awarded approximately 92,000 restricted share units and 106,500 base performance share units to employees in February 2015. The fair value of each unit awarded was estimated at $46.30, equal to the market value of a ProAssurance common share on the date of grant. All awards are charged to expense as an increase to equity over the service period (generally the vesting period) associated with the award. Restricted share units and performance share units vest in their entirety at the end of a three-year period following the grant date based on a continuous service requirement and, for performance share units, achievement of a performance objective. Partial vesting is permitted for retirees. A ProAssurance common share is issued for each unit once vesting requirements are met, except that units sufficient to satisfy required tax withholdings are paid in cash. The number of common shares issued for performance share units varies from 75% to 125% of base awards depending upon the degree to which stated performance objectives are achieved. ProAssurance issued approximately 28,000 and 116,000 common shares to employees in February 2015 related to restricted share units and performance share units, respectively, granted in 2012. Performance share units, for the 2012 award, were issued at levels ranging from 104% to 125%.
ProAssurance issued approximately 28,000 common shares to employees in February 2015 as bonus compensation, as approved by the Compensation Committee of the Board. The shares issued were valued at fair value (the market price of a ProAssurance common share on the date of award).
Other Comprehensive Income (Loss) (OCI) and Accumulated Other Comprehensive Income (Loss) (AOCI)
For the three months ended March 31, 2015 and March 31, 2014, OCI was primarily comprised of unrealized gains and losses, including non-credit impairment losses, arising during the period related to available-for-sale securities, less reclassification adjustments as shown in the table that follows, net of tax. In 2015, OCI also included losses related to unrecognized changes in defined benefit plan liabilities of $1.0 million, net of tax from the reestimation of two defined benefit plans assumed in the Eastern acquisition. Both plans are frozen as to the earning of additional benefits, but the unrecognized plan benefit liability is reestimated annually.
At March 31, 2015 and December 31, 2014, AOCI was primarily comprised of unrealized gains and losses from available-for-sale securities, including non-credit impairments recognized in OCI of $1.5 million and $0.5 million, respectively, net of tax. At March 31, 2015 AOCI also included losses of $1.0 million related to unrecognized changes in defined benefit plan liabilities, net of tax. All tax effects were computed using a 35% rate. OCI and AOCI also included immaterial amounts of foreign currency translation adjustments.

Table of Contents
ProAssurance Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
March 31, 2015

Amounts reclassified from accumulated other comprehensive income to net income and the amounts of deferred tax expense (benefit) included in OCI were as follows:

	Three Months Ended March 31	
(In thousands)	2015	2014
Reclassifications from accumulated other comprehensive income to net income, available-for-sale securities:		
Realized investment gains (losses)	$916	$701
Tax effect (at 35%)	(321)	(245)
Net reclassification adjustments	$595	$456
Deferred tax expense (benefit) included in OCI	$4,131	$5,703

10. Variable Interest Entities

ProAssurance holds passive interests in a number of entities that are considered to be VIEs under GAAP guidance. ProAssurance's VIE interests principally consist of interests in LPs/LLCs formed for the purpose of achieving diversified equity and debt returns. ProAssurance's VIE interests carried as a part of Other investments totaled $37.2 million at March 31, 2015 and $33.3 million at December 31, 2014. ProAssurance's VIE interests carried as a part of Investment in unconsolidated subsidiaries totaled $73.8 million at March 31, 2015 and $65.0 million at December 31, 2014.

ProAssurance has not consolidated these VIEs because it has either very limited or no power to control the activities that most significantly affect the economic performance of these entities and is not the primary beneficiary of any of the entities. ProAssurance’s involvement with each entity is limited to its direct ownership interest in the entity. ProAssurance has no arrangements with any of the entities to provide other financial support to or on behalf of the entity. At March 31, 2015, ProAssurance’s maximum loss exposure relative to these investments was limited to the carrying value of ProAssurance’s investment in the VIE.

11. Earnings Per Share

Diluted weighted average shares is calculated as basic weighted average shares plus the effect, calculated using the treasury stock method, of assuming that dilutive stock options have been exercised and that performance, restricted and purchase share units have vested. All outstanding stock options, performance, restricted and purchase share units had a dilutive effect for the three months ended March 31, 2015 and 2014.

12. Segment Information
ProAssurance operates in four segments that are organized around the nature of the products and services provided: Specialty P&C, Workers' Compensation, Lloyd's Syndicate, and Corporate. A description of each segment follows.
Specialty P&C is primarily focused on professional liability insurance and medical technology and life sciences products liability insurance. The professional liability business primarily offers professional liability insurance to healthcare providers and institutions and to attorneys and their firms. The medical technology and life sciences business offers products liability insurance for medical technology and life sciences companies that manufacture or distribute products. The Specialty P&C segment cedes certain premium to the Lloyd's Syndicate segment under an agreement with Syndicate 1729. As discussed below, Syndicate 1729 operating results are reported on a quarter delay. The ceded premium associated with the Syndicate 1729 reinsurance agreement has been reported within the Specialty P&C segment on a similar delay, as this results in the ceded premium being reported in the same period in which the Lloyd's Syndicate segment reports the corresponding assumed premium.
Workers' Compensation provides workers' compensation products primarily to employers with 1,000 or fewer employees. The segment also offers alternative market solutions whereby policies written are 100% ceded either to a captive insurer unaffiliated with ProAssurance or to SPCs operated by a wholly owned subsidiary of ProAssurance. The SPCs are fully or partially owned by the employer (or employer group, association or affiliate) insured by the policies ceded. Financial results (underwriting profit or loss, plus investment income) of the SPCs accrue to the owners of that cell.
Lloyd's Syndicate includes operating results from ProAssurance's 58% participation in Lloyd's of London Syndicate 1729. Syndicate 1729 underwrites risks over a wide range of property and casualty insurance and reinsurance lines in both the U.S and international markets. The results of this segment are reported on a quarter delay, except that investment results associated with the FAL investments and certain U.S. paid administrative expenses, primarily start-up costs, are reported concurrently as that information is available on an earlier time frame.
Corporate includes ProAssurance's U.S. investment operations, interest expense and U.S. income taxes, all of which are managed at the corporate level, non-premium revenues generated outside of our insurance entities, and corporate expenses.
The accounting policies of the segments are the same as those described in Note 1 of the Notes to Consolidated Financial Statements in ProAssurance’s December 31, 2014 report on Form 10-K and Note 1 of the Notes to Condensed Consolidated Financial Statements. ProAssurance evaluates performance of its Specialty P&C and Workers' Compensation segments based on before tax underwriting profit or loss, and excludes investment performance. Performance of the Lloyd's Syndicate segment is evaluated based on underwriting profit or loss, plus investment results of investment assets solely allocated to Syndicate 1729 operations, net of United Kingdom income tax expense. Performance of the Corporate segment is evaluated based on the contribution made to consolidated after tax results. ProAssurance accounts for inter-segment sales and transfers as if the sales or transfers were to third parties at current market prices. Assets are not allocated to segments because investments and assets are not managed at the segment level.

Financial data by segment for the three months ended March 31, 2015 and 2014 were as follows:

	Three Months Ended March 31, 2015					
(In thousands)	Specialty P&C	Workers' Compensation	Lloyd's Syndicate	Corporate	Inter-segment Eliminations	Consolidated
Net premiums earned	$114,864	$ 51,277	$5,758	$—	$ —	$ 171,899
Net investment income	—	—	204	27,100	—	27,304
Equity in earnings (loss) of unconsolidated subsidiaries	—	—	—	1,622	—	1,622
Net realized gains (losses)	—	—	11	4,828	—	4,839
Other income	1,496	137	490	157	(111)	2,169
Net losses and loss adjustment expenses	(69,030)	(32,102)	(4,008)	—	—	(105,140)
Underwriting, policy acquisition and operating expenses*	(27,159)	(15,358)	(3,580)	(5,370)	111	(51,356)
Segregated portfolio cells dividend expense	—	(2,184)	—	—	—	(2,184)
Interest expense	—	—	—	(3,631)	—	(3,631)
Income tax benefit (expense)	—	—	—	(7,708)	—	(7,708)
Segment operating results	$20,171	$ 1,770	$(1,125)	$16,998	$ —	$ 37,814
Significant non-cash items						
Depreciation and amortization	$2,163	$ 1,440	$130	$8,352	$ —	$ 12,085

	Three Months Ended March 31, 2014					
(In thousands)	Specialty P&C	Workers' Compensation	Lloyd's Syndicate	Corporate	Inter-segment Eliminations	Consolidated
Net premiums earned	$126,236	$ 45,494	$—	$—	$ —	$ 171,730
Net investment income	—	—	15	29,717	—	29,732
Equity in earnings (loss) of unconsolidated subsidiaries	—	—	—	1,751	—	1,751
Net realized gains (losses)	—	—	—	2,744	—	2,744
Other income	1,563	140	—	509	(118)	2,094
Net losses and loss adjustment expenses	(60,960)	(28,548)	—	—	—	(89,508)
Underwriting, policy acquisition and operating expenses*	(33,720)	(15,589)	(875)	(2,449)	118	(52,515)
Segregated portfolio cells dividend expense	—	(1,049)	—	—	—	(1,049)
Interest expense	—	—	—	(3,570)	—	(3,570)
Income tax benefit (expense)	—	—	—	(14,678)	—	(14,678)
Segment operating results	$33,119	$ 448	$(860)	$14,024	$ —	$ 46,731
Significant non-cash items						
Depreciation and amortization	$2,076	$ 1,482	$—	$8,029	$ —	$ 11,587

* Beginning with the first quarter of 2015, the operating subsidiaries within the Specialty P&C and Workers' Compensation segments were charged a management fee by the Corporate segment for various management services provided to the subsidiary. Under the new arrangement, the expenses associated with such services are reported as expenses of the Corporate segment, and the management fees charged are reported as an offset to Corporate operating

expenses. Prior to 2015, a substantial portion of expenses associated with corporate services were directly allocated to the insurance subsidiaries included in the Specialty P&C segment.

The following table provides detailed information regarding ProAssurance's gross premiums earned by product as well as a reconciliation to net premiums earned. All gross premiums earned are from external customers except as noted. ProAssurance's insured risks are primarily within the United States.

	Three Months Ended March 31	
(In thousands)	2015	2014
Specialty P&C Segment		
Gross premiums earned:		
Healthcare professional liability	$115,831	$120,850
Legal professional liability	7,200	6,987
Medical technology and life sciences products liability	8,972	8,758
Other	382	590
Ceded premiums earned*	(17,521)	(10,949)
Segment net premiums earned	114,864	126,236
Workers' Compensation Segment		
Gross premiums earned:		
Traditional business	42,003	37,453
Alternative market business	15,730	12,682
Ceded premiums earned	(6,456)	(4,641)
Segment net premiums earned	51,277	45,494
Lloyd's Syndicate Segment		
Gross premiums earned:		
Property and casualty*	6,537	—
Ceded premiums earned	(779)	—
Segment net premiums earned	5,758	—
Consolidated net premiums earned	$171,899	$171,730

* Includes premium ceded from the Specialty P&C Segment to the Lloyd's Syndicate Segment of $3.4 million for the three months ended March 31, 2015. There was no inter-segment reinsurance reported for the first quarter of 2014 as the reinsurance agreement was not in effect until January 1, 2014 and the cession is reported on a one quarter delay.

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion should be read in conjunction with the Condensed Consolidated Financial Statements and Notes to those statements which accompany this report. A glossary of insurance terms and phrases is available on the investor section of our website. Throughout the discussion, references to "ProAssurance," "PRA," "Company," "we," "us" and "our" refer to ProAssurance Corporation and its consolidated subsidiaries. The discussion contains certain forward-looking information that involves risks and uncertainties. As discussed under the heading "Forward-Looking Statements," our actual financial condition and operating results could differ significantly from these forward-looking statements.

ProAssurance Overview

We report our results in four distinct segments that are organized around the nature of the products and services provided: Specialty Property & Casualty (Specialty P&C), Workers' Compensation, Lloyd's Syndicate, and Corporate. Our Specialty P&C segment includes our professional liability business and our medical technology and life sciences products (medical technology liability) business. Our Workers' Compensation segment includes workers' compensation insurance for employers, groups and associations. Our Lloyd's Syndicate segment includes operating results from our 58% participation in Lloyd's of London Syndicate 1729 (Syndicate 1729). Syndicate 1729 underwrites risks over a wide range of property and casualty insurance and reinsurance lines in both the U.S. and international markets. Our Corporate segment includes our U.S. investment operations which are managed at the corporate level, non-premium revenues generated outside of our insurance entities, corporate expenses, interest and U.S. income taxes. Additional information regarding our segments is included in Note 12 of the Notes to Condensed Consolidated Financial Statements and in Part I of our 2014 Form 10-K.

Critical Accounting Estimates

Our Condensed Consolidated Financial Statements are prepared in conformity with U.S. generally accepted accounting principles (GAAP). Preparation of these financial statements requires us to make estimates and assumptions that affect the amounts we report on those statements. We evaluate these estimates and assumptions on an ongoing basis based on current and historical developments, market conditions, industry trends and other information that we believe to be reasonable under the circumstances. There can be no assurance that actual results will conform to our estimates and assumptions; reported results of operations may be materially affected by changes in these estimates and assumptions.

Management considers the following accounting estimates to be critical because they involve significant judgment by management and the effect of those judgments could result in a material effect on our financial statements.

Reserve for Losses and Loss Adjustment Expenses

The largest component of our liabilities is our reserve for losses and loss adjustment expenses ("reserve for losses" or "reserve"), and the largest component of expense for our operations is incurred losses and loss adjustment expenses (also referred to as “losses and loss adjustment expenses,” “incurred losses,” “losses incurred,” and “losses”). Incurred losses reported in any period reflect our estimate of losses incurred related to the premiums earned in that period as well as any changes to our previous estimate of the reserve required for prior periods.

As of March 31, 2015 our reserve is almost entirely comprised of long-tail exposures. The estimation of long-tailed losses is inherently difficult and is subject to significant judgment on the part of management. Due to the nature of our claims, our loss costs, even for claims with similar characteristics, can vary significantly depending upon many factors, including but not limited to the specific characteristics of the claim and the manner in which the claim is resolved. Long-tailed insurance is characterized by the extended period of time typically required to assess the viability of a claim, potential damages, if any, and to then reach a resolution of the claim. The claims resolution process may extend to more than five years. The combination of continually changing conditions and the extended time required for claim resolution results in a loss cost estimation process that requires actuarial skill and the application of significant judgment, and such estimates require periodic modification.

Our reserve is established by management after taking into consideration a variety of factors including premium rates, claims frequency, historical paid and incurred loss development trends, the expected effect of inflation, general economic trends, the legal and political environment, and the conclusions reached by our internal and consulting actuaries. We update and review the data underlying the estimation of our reserve for losses each reporting period and make adjustments to loss estimation assumptions that we believe best reflect emerging data. Both our internal and consulting actuaries perform an in-depth review of our reserve for losses on at least a semi-annual basis using the loss and exposure data of our insurance subsidiaries. In periods in which business combinations occur, we must also establish a reserve for the loss exposure assumed.

Table of Contents

Our reserving process can be broadly grouped into two areas: the establishment of the reserve for the current accident year (the initial reserve) and the re-estimation of the reserve for prior accident years (development of prior accident years).

Current Accident Year - Initial Reserve

Considerable judgment is required in establishing our initial reserve for any current accident year period, as there is limited data available upon which to base our case reserves. Our process for setting an initial reserve considers the unique characteristics of each product, but in general we rely heavily on the loss assumptions that were used to price business, as our pricing reflects our analysis of loss costs that we expect to incur relative to the insurance product being priced.

Specialty P&C Segment. Professional and medical technology liability loss costs are impacted by many factors, including but not limited to, the nature of the claim, including whether or not the claim is an individual or a mass tort claim, the personal situation of the claimant or the claimant's family, the outcome of jury trials, the legislative and judicial climate where any potential litigation may occur, general economic conditions and, for claims involving bodily injury, the trend of healthcare costs. Within our Specialty P&C segment, for our healthcare professional liability (HCPL) business (81% of our consolidated gross reserve for losses and loss adjustment expenses as of December 31, 2014), we set an initial reserve using the average loss ratio used in our pricing, plus an additional provision in consideration of the historical loss volatility we and others in the industry have experienced. For our HCPL business our target loss ratio during recent accident years has approximated 75% and the provision for loss volatility has ranged from 8 to 10 percentage points, producing an overall average initial loss ratio for our HCPL business of approximately 85%. We believe use of a provision for volatility considers inherent risks associated with our rate development process and the historic volatility of professional liability losses (the industry has experienced accident year loss ratios as high as 163% and as low as 53% over the past 30 years) and produces a reasonable best estimate of the reserve required to cover actual ultimate unpaid losses. A similar practice is followed for our legal professional liability business (5% of our consolidated gross reserve for losses and loss adjustment expenses as of December 31, 2014).

The risks insured in our medical technology liability business (6% of our consolidated gross reserve for losses and loss adjustment expenses as of December 31, 2014) are more varied, and policies are individually priced based on the risk characteristics of the policy. Therefore, for this business we establish an initial reserve using our most recently developed actuarial estimates of losses expected to be incurred based on factors which include: results from prior analysis of similar business, industry indications, observed trends and judgment. The medical technology liability line of business exhibits similar volatility to HCPL, and the actuarial pricing estimate includes a provision for this volatility.

Workers' Compensation Segment. Many factors affect the ultimate losses incurred for our workers' compensation coverages (8% of our consolidated gross reserve for losses and loss adjustment expenses as of December 31, 2014), including, but not limited to, the type and severity of the injury, the age and occupation of the injured worker, the estimated length of disability, medical treatment and related costs, and the jurisdiction of the injury occurrence. We use various actuarial methodologies in developing our workers’ compensation reserve combined with a review of the exposure base generally based upon payroll. For the current accident year, given the lack of seasoned information, the different actuarial methodologies produce results with significant variability; therefore, more emphasis is placed on supplementing the actuarial methodologies used with trends in exposure base, medical expense inflation, general inflation, severity, and claim counts, among other things, to select an expected loss ratio.

Development of Prior Accident Years

We re-evaluate the reserve for prior accident years each period based on our most recently available claims data and currently available industry trend information. Changes to previously established reserve estimates are recognized in the current period if management’s best estimate of ultimate losses differs from the estimate previously established. While management considers a variety of variables in determining its best estimate, in general, as claims age, our methodologies give more weight to actual loss costs which, for the majority of our reserves, continue to indicate that ultimate loss costs will be lower than our previous estimates. The discussion in our Critical Accounting Estimates section in Item 7 of our 2014 Form 10-K includes additional information regarding the methodologies used to evaluate our reserve.

Any change in our estimate of net ultimate losses for prior years is reflected in net income in the period in which such changes are made. Over the past several years such changes have reduced our estimate of net ultimate losses, resulting in a reduction of reported losses for the period and a corresponding increase in pre-tax income.

We recognized net favorable reserve development of $33.5 million during the three months ended March 31, 2015, of which $31.8 million related to our Specialty P&C segment and $1.7 million related to our Workers' Compensation segment. The development recognized within the Specialty P&C segment was primarily attributable to the favorable resolution of HCPL claims during the period and an evaluation of established case reserves and paid claims data that indicated that the actual severity trend associated with the remaining HCPL claims continues to be less than we had previously estimated. Development recognized within our Workers' Compensation segment includes amortization of the purchase accounting fair value adjustment

Table of Contents

of $0.4 million for the three months ended March 31, 2015; the remaining development of $1.3 million for the three-month period, was attributable to our segregated portfolio cells (SPCs) which are evaluated at the cell level. Because a relatively small number of claims are open per cell, the closing of claims can affect the actuarial projections for the remaining open claims in the cell to an extent that indicates development should be recognized for the cell.
Due to the size of our consolidated reserve for losses and the large number of claims outstanding at any point in time, even a small percentage adjustment to our total reserve estimate could have a material effect on our results of operations for the period in which the adjustment is made.

Use of Judgment

Even though the actuarial process is highly technical, it is also highly judgmental, both as to the selection of the data used in the various actuarial methodologies (e.g., initial expected loss ratios and loss development factors) and in the interpretation of the output of the various methods used. Each actuarial method generally returns a different value and for the more recent accident years the variations among the various methodologies can be significant. For each partition of our reserves, the results of the various methods, along with the supplementary statistical data regarding such factors as closed with and without indemnity ratios, claim severity trends, the expected duration of such trends, changes in the legal and legislative environment and the current economic environment, are used to develop a point estimate based upon management's judgment and past experience. The process of selecting the point estimate is based upon the judgment of management taking into consideration the actuarial methods and other environmental factors discussed previously. The series of selected point estimates is then combined to produce an overall point estimate for ultimate losses.

Given the potential for unanticipated volatility for long-tailed lines of business, we are cautious in giving full credibility to emerging trends that, when more fully mature, may lead to the recognition of either favorable or adverse development of our losses. There may be trends, both positive and negative, reflected in the numerical data both within our own information and in the broader marketplace that mitigate or reverse as time progresses and additional data becomes available. This is particularly true for our HCPL business which has historically exhibited significant volatility as previously discussed.

HCPL. Over the past several years the most influential factor affecting the analysis of our HCPL reserves and the related development recognized has been the change, or lack thereof, in the severity of claims. The severity trend is an explicit component of our pricing models, whereas in our reserving process the severity trend's impact is implicit. Our estimate of this trend and our expectations about changes in this trend impact a variety of factors, from the selection of expected loss ratios to the ultimate point estimates established by management.

Because of the implicit and wide-ranging nature of severity trend assumptions on the loss reserving process it is not practical to specifically isolate the impact of changing severity trends. However, because severity is an explicit component of our HCPL pricing process we can better isolate the impact that changing severity can have on our loss costs and loss ratios as regards our pricing models for this business component. Our current HCPL pricing models assume a severity trend of 2% to 3% in most states and products. If the severity trend were to be higher by 1 percentage point, the impact would be an increase in our expected loss ratio for this business of 3.2 percentage points, based on current claim disposition patterns. An increase in the severity trend of 3 percentage points would result in a 10.1 percentage point increase in our expected loss ratio. Due to the long tailed nature of our claims and the previously discussed historical volatility of loss costs, selection of a severity trend assumption is a subjective process that is inherently likely to prove inaccurate over time. Given the long-tail and volatility, we are generally cautious in making changes to the severity assumptions within our pricing models. Also of note is that all open claims and accident years are generally impacted by a change in the severity trend, which compounds the effect of such a change.
For the 2004 to 2009 accident years, both our internal and consulting actuaries observed an unprecedented reduction in the frequency of HCPL claims (or number of claims per exposure unit) that cannot be attributed to any single factor. We believe that much of the reduction in claim frequency is the result of a decline in the filing of non-meritorious lawsuits that have historically been dismissed or otherwise resulted in no payment of indemnity on behalf of our insureds. With fewer non-meritorious claims being filed we expect that the claims that are filed have the potential for greater average losses, or greater severity. As a result, we cannot be certain as to the impact this decline will ultimately have on the average cost of claims, and this has complicated the selection of an appropriate severity

trend for our pricing model for these lines. It has also made it more challenging to factor severity into the various actuarial methodologies we use to evaluate our reserve. Based on the weighted average of payments, typically 85% of our HCPL claims are resolved after eight years for a given accident year. Due to this long tail, we continue to be uncertain of the full impact of the observed decline in frequency and whether the expected increase in severity will materialize.

Although we remain uncertain regarding the ultimate severity trend to project into the future due to the long-tailed nature of our business, we have given consideration to observed loss costs in setting our rates. For our HCPL business this practice has resulted in rate reductions in recent years. For example, on average, excluding our podiatry business acquired in 2009, we have gradually reduced the premium rates we charge on our standard physician renewal business (our largest HCPL line) by

Table of Contents

approximately 18% from the beginning of 2006 to March 31, 2015. Loss ratios for the current accident years have thus remained fairly constant because expected loss reductions have been reflected in our rates.

Workers' Compensation. Severity has not historically been an influential factor affecting our workers' compensation analysis of reserves, as claims are typically resolved more quickly than the industry norm. As previously mentioned, the determination and calculation of loss development factors requires considerable judgment. In particular the selection of tail factors requires considerable judgment as they are determined in the absence of direct loss development history and thus require reliance upon industry data which may not be representative of the Company’s data and experience.

Investment Valuations

We record the majority of our investments at fair value as shown in the table below. At March 31, 2015 the distribution of our investments based on GAAP fair value hierarchies (levels) was as follows:

	Distribution by GAAP Fair Value Hierarchy			March 31, 2015
	Level 1	Level 2	Level 3	Total Investments
Investments recorded at:				
Fair value	12%	78%	3%	93%
Other valuations				7%
Total Investments				100%

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. All of our fixed maturity and equity security investments are carried at fair value. Our short-term securities are carried at amortized cost, which approximates fair value.

Because of the number of securities we own and the complexity and cost of developing accurate fair values, we utilize multiple independent pricing services to assist us in establishing the fair value of individual securities. The pricing services provide fair values based on exchange traded prices, if available. If an exchange traded price is not available, the pricing services, if possible, provide a fair value that is based on multiple broker/dealer quotes or that has been developed using pricing models. Pricing models vary by asset class and utilize currently available market data for securities comparable to ours to estimate a fair value for our security. The pricing services scrutinize market data for consistency with other relevant market information before including the data in the pricing models. The pricing services disclose the types of pricing models used and the inputs used for each asset class. Determining fair values using these pricing models requires the use of judgment to identify appropriate comparable securities and to choose a valuation methodology that is appropriate for the asset class and available data.

The pricing services provide a single value per instrument quoted. We review the values provided for reasonableness each quarter by comparing market yields generated by the supplied value versus market yields observed in the market place. We also compare yields indicated by the provided values to appropriate benchmark yields and review for values that are unchanged or that reflect an unanticipated variation as compared to prior period values. In addition, we compare provided information for consistency with our other pricing services, known market data and information from our own trades, considering both values and valuation trends. We also review weekly trades versus the prices supplied by the services. If a supplied value appears unreasonable, we discuss the valuation in question with the pricing service and make adjustments if deemed necessary. To date, our review has not resulted in any changes to the values supplied by the pricing services.

The pricing services do not provide a fair value unless an exchange traded price or multiple observable inputs are available. As a result, the pricing services may provide a fair value for a security in some periods but not others, depending upon the level of recent market activity for the security or comparable securities.

Level 1 Investments

Fair values for our equity securities, a portion of our convertible securities and our short-term securities are determined using exchange traded prices. There is little judgment involved when fair value is determined using an exchange traded price. In accordance with GAAP, for disclosure purposes we classify securities valued using an exchange traded price as Level 1 securities.

Table of Contents

Level 2 Investments

Most fixed income securities do not trade daily, and thus exchange traded prices are generally not available for these securities. However, market information (often referred to as observable inputs or market data, including but not limited to, last reported trade, non-binding broker quotes, bids, benchmark yield curves, issuer spreads, two sided markets, benchmark securities, offers and recent data regarding assumed prepayment speeds, cash flow and loan performance data) is available for most of our fixed income securities. We determine fair value for a large portion of our fixed income securities using available market information. In accordance with GAAP, for disclosure purposes we classify securities valued based on multiple market observable inputs as Level 2 securities.

Level 3 Investments

When a pricing service does not provide a value for one of our fixed maturity securities, management estimates fair value using either a single non-binding broker quote or pricing models that utilize market based assumptions which have limited observable inputs. The process involves significant judgment in selecting the appropriate data and modeling techniques to use in the valuation process. For disclosure purposes we classify fixed maturity securities valued using limited observable inputs as Level 3 securities.

We also classify as Level 3 our investment interests that are carried at equity, valued using a fund-provided net asset value (NAV) for our interest, which approximates fair value. All investments valued in this manner are LP or LLC interests that hold debt and equity securities. At March 31, 2015 interests valued using a fund-provided NAV totaled $145.9 million, or 4% of total investments, and were classified as part of our Investment in Unconsolidated Subsidiaries.

Investments - Other Valuation Methodologies

Certain of our investments, in accordance with GAAP for the type of investment, are measured using methodologies other than fair value. At March 31, 2015 these investments represented approximately 7% of total investments and are detailed in the following table. Additional information about these investments is provided in Notes 2 and 3 of the Notes to Condensed Consolidated Financial Statements.

(In millions)	Carrying Value	GAAP Measurement Method
Other investments:		
Investments in LPs	$57.2	Cost
Other, principally Federal Home Loan Bank capital stock	3.6	Cost
Total other investments	60.8	
Investment in unconsolidated subsidiaries:		
Investments in tax credit partnerships	132.7	Equity
Equity method LPs/LLCs	10.7	Equity
Total investment in unconsolidated subsidiaries	143.4	
Business owned life insurance	56.8	Cash surrender value
Total investments - Other valuation methodologies	$261.0	

Investment Impairments

We evaluate our investments on at least a quarterly basis for declines in fair value that represent other than temporary impairment (OTTI). We consider an impairment to be an OTTI if we intend to sell the security or if we believe we will be required to sell the security before we fully recover the amortized cost basis of the security. Otherwise, we consider various factors in our evaluation, as discussed below.

For debt securities, we consider whether we expect to fully recover the amortized cost basis of the security, based upon consideration of some or all of the following:

- third party research and credit rating reports;
- the current credit standing of the issuer, including credit rating downgrades;
- the extent to which the decline in fair value is attributable to credit risk specifically associated with the security or its issuer;

Table of Contents

- our internal assessments and those of our external portfolio managers regarding specific circumstances surrounding a security, which can cause us to believe the security is more or less likely to recover its value than other securities with a similar structure;
- for asset-backed securities, the origination date of the underlying loans, the remaining average life, the probability that credit performance of the underlying loans will deteriorate in the future, and our assessment of the quality of the collateral underlying the loan;
- failure of the issuer of the security to make scheduled interest or principal payments;
- any changes to the rating of the security by a rating agency; and
- recoveries or additional declines in fair value subsequent to the balance sheet date.

In assessing whether we expect to recover the cost basis of debt securities, particularly asset-backed securities, we must make a number of assumptions regarding the cash flows that we expect to receive from the security in future periods. These judgments are subjective in nature and may subsequently be proved to be inaccurate.

We evaluate our cost method interests in LPs/LLCs for OTTI by considering whether there has been a decline in fair value below the recorded value, which involves assumptions and estimates. We receive a report from each of the LPs/LLCs at least quarterly which provides us a NAV for our interest. The NAV is based on the fair values of securities held by the LP/LLC as determined by the LP/LLC manager. We consider the most recent NAV provided, the performance of the LP/LLC relative to the market, the stated objectives of the LP/LLC, the cash flows expected from the LP/LLC and audited financial statements of the entity, if available, in considering whether an OTTI exists.

Our investments in tax credit partnerships are evaluated for OTTI by considering both qualitative and quantitative factors which include: whether cash flows, primarily tax benefits, currently expected from the investment equal or exceed the carrying value of the investment, whether currently expected cash flows are less than those expected at the time the investment was acquired, and our ability and intent to hold the investment until the recovery of its carrying value.

We also evaluate our holdings of Federal Home Loan Bank (FHLB) securities for impairment. We consider the current capital status of the FHLB, whether the FHLB is in compliance with regulatory minimum capital requirements, and the FHLB’s most recently reported operating results.

Deferred Policy Acquisition Costs

Policy acquisition costs (primarily commissions, premium taxes and underwriting salaries) which are directly related to the successful acquisition of new and renewal premiums are capitalized as deferred policy acquisition costs and charged to expense, net of ceding commissions earned, as the related premium revenue is recognized. We evaluate the recoverability of our deferred policy acquisition costs each reporting period, and any amounts estimated to be unrecoverable are charged to expense in the current period. As of March 31, 2015 we have not determined that any amounts are unrecoverable.

Deferred Taxes

Deferred federal income taxes arise from the recognition of temporary differences between the bases of assets and liabilities determined for financial reporting purposes and the bases determined for income tax purposes. Our temporary differences principally relate to our loss reserve, unearned premiums, compensation recognition, deferred policy acquisition costs, unrealized investment gains (losses), intangibles, and basis differences on investment assets. Deferred tax assets and liabilities are measured using the enacted tax rates expected to be in effect when such benefits are realized. We review our deferred tax assets quarterly for impairment. If we determine that it is more likely than not that some or all of a deferred tax asset will not be realized, a valuation allowance is recorded to reduce the carrying value of the asset. In assessing the need for a valuation allowance, management is required to make certain judgments and assumptions about our future operations based on historical experience and information as of the measurement period regarding reversal of existing temporary differences, carryback capacity, future taxable income (including its capital and operating characteristics) and tax planning strategies. We did not have any significant valuation allowances as of March 31, 2015.

Unrecognized Tax Benefits

We evaluate tax positions taken on tax returns and recognize positions in our financial statements when it is more likely than not that we will sustain the position upon resolution with a taxing authority. If recognized, the benefit is measured as the largest amount of benefit that has a greater than fifty percent probability of being realized. We review uncertain tax positions each period, considering changes in facts and circumstances, such as changes in tax law, interactions with taxing authorities and developments in case law, and make adjustments as we consider necessary. Adjustments to our unrecognized tax benefits may affect our income tax expense, and settlement of uncertain tax positions may require the use of cash.

Table of Contents

Goodwill

Management evaluates the carrying value of goodwill at the segment (or reporting unit) level annually as of October 1st. If, at any time during the year, events occur or circumstances change that would more likely than not reduce the fair value below the carrying value, we also evaluate goodwill at that time.

The goodwill impairment assessment requires evaluating qualitative factors or performing a quantitative assessment to determine if a reporting unit's carrying value is likely to exceed its fair value. For our reporting units, we elected 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 of October 1, 2014, through our qualitative evaluation of goodwill, we concluded that the fair value of our reporting units exceeded the carrying value and deemed it unnecessary to perform further testing.

Additional information regarding our goodwill evaluation at the segment level is included in Note 1 of the Notes to Consolidated Financial Statements included in ProAssurance's December 31, 2014 Form 10-K. Note 12 of the Notes to Condensed Consolidated Financial Statements provides additional information regarding our segments.

Intangibles

Intangible assets with definite lives are amortized over the estimated useful life of the asset. Amortizable intangible assets primarily consist of agency and policyholder relationships, renewal rights and trade names. Intangible assets with an indefinite life, primarily state licenses, are not amortized. Intangible assets are evaluated for impairment on an annual basis. Additional information regarding intangible assets is included in Note 1 of the Notes to Consolidated Financial Statements included in ProAssurance's December 31, 2014 Form 10-K.

Audit Premium

Workers' compensation premiums are determined based upon the payroll of the insured, the applicable premium rates and an experience based modification factor, where applicable. An audit of the policyholders' records is conducted after policy expiration to make a final determination of applicable premiums. Audit premium due from or due to a policyholder as a result of an audit is reflected in net premiums earned when billed. We track, by policy, the amount of additional premium billed in final audit invoices as a percentage of payroll exposure and use this information to estimate the probable additional amount of earned, but unbilled (EBUB), premium as of the balance sheet date. We include changes to the EBUB premium estimate in net premiums earned in the period recognized.

Accounting Changes

We are not aware of any accounting changes not yet adopted as of March 31, 2015 that would have a material effect on our results of operations or financial position. Note 1 of the Notes to Condensed Consolidated Financial Statements provides additional detail regarding accounting changes.

Table of Contents

Liquidity and Capital Resources and Financial Condition

Overview

ProAssurance Corporation is a holding company and is a legal entity separate and distinct from its subsidiaries. The holding company has no substantial external revenues other than its investment revenues, thus dividends from its operating subsidiaries represent a significant source of funds for its obligations, including debt service and shareholder dividends. At March 31, 2015, we held cash and liquid investments of approximately $136.7 million outside our insurance subsidiaries that were available for use without regulatory approval. Our holding company also has an additional $100 million available under a revolving credit agreement, as discussed in this section under the heading "Debt."

During April 2015, our insurance subsidiaries declared dividends of $124.0 million, including an approved extraordinary dividend of $112.2 million, to be paid in May 2015. Our domestic insurance subsidiaries, in aggregate, are permitted to pay additional dividends of approximately $155.7 million over the remainder of 2015 without the prior approval of state insurance regulators. The payment of any dividend requires prior notice to the insurance regulator in the state of domicile, and the regulator may prevent the dividend if, in its judgment, payment of the dividend would have an adverse effect on the surplus of the insurance subsidiary.

Operating Activities and Related Cash Flows

The principal components of our operating cash flows are the excess of premiums collected and net investment income over losses paid and operating costs, including income taxes. Timing delays exist between the collection of premiums and the payment of losses associated with the premiums. Premiums are generally collected within the twelve-month period after the policy is written, while our claim payments are generally paid over a more extended period of time. Likewise, timing delays exist between the payment of claims and the collection of any associated reinsurance recoveries.

Operating cash flows for the three months ended March 31, 2015 and 2014 compare as follows:

	Operating Cash Flow	
	Three Months Ended March 31	
(In millions)	2015	2014
Cash provided by operating activities	$37	$30

Reconciliation of Operating Cash Flows	2015 vs 2014	2014 vs 2013
Cash provided by operating activities, prior year	$30	$(13)
Increase (decrease) in operating cash flows attributable to:		
Premium receipts	7	(9)
Payments to reinsurers	1	(3)
Losses paid, net of reinsurance recoveries	(11)	(5)
Cash received from investments	(4)	4
Net payments to Syndicate reported on a delay		