SCPIE HOLDINGS INC
Form 10-Q
August 12, 2004

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT

PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTER ENDED JUNE 30, 2004

Commission File No. 1-12449

SCPIE HOLDINGS INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**95-4557980**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1888 Century Park East, Los Angeles, California 90067

www.scpie.com

(Address of principal executive offices and internet site)

(310) 551-5900

(Registrant s telephone number, including area code)

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

Yes x No ¨

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

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

Class	Outstanding at August 6, 2004
Preferred stock, par value $l.00 per share	No shares outstanding
Common stock, par value $0.0001 per share	9,910,576 shares

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SCPIE HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(DOLLARS IN THOUSANDS, EXCEPT SHARE DATA)

	JUNE 30, 2004	DECEMBER 31, 2003
	(unaudited)	
ASSETS		
Securities available-for-sale:		
Fixed maturity investments, at fair value (amortized cost 2004 - $496,131; 2003 - $550,794)	$ 487,248	$ 554,141
Equity investments, at fair value (cost 2004 - $12,380; 2003 - $15,766)	16,385	20,543
Total securities available-for-sale	503,633	574,684
Mortgages	10,400	10,400
Cash and cash equivalents	74,756	62,095
Total investments and cash and cash equivalents	588,789	647,179
Accrued investment income	6,534	7,526
Premiums receivable	145,557	120,112
Reinsurance recoverable	181,177	151,829
Deferred policy acquisition costs	10,949	9,416
Deferred federal income taxes	48,407	43,725
Property and equipment, net	3,351	3,816
Other assets	6,907	7,647
Total assets	$ 991,671	$ 991,250
LIABILITIES		
Reserves:		
Losses and loss adjustment expenses	$ 625,186	$ 643,046
Unearned premiums	75,282	50,707
Total reserves	700,468	693,753
Amounts held for reinsurance	79,822	67,223
Other liabilities	17,323	26,086
Total liabilities	797,613	787,062
Commitments and contingencies		
STOCKHOLDERS EQUITY		
Preferred stock par value $1.00, 5,000,000 shares authorized, no shares issued or outstanding		

Common stock, par value $.0001, 30,000,000 shares authorized, 12,792,091 shares issued, 2004 9,410,576 shares outstanding 2003 9,371,933 shares outstanding	1	1
Additional paid-in capital	36,750	37,281
Retained earnings	262,574	264,063
Treasury stock, at cost 2004 2,881,515 shares and 2003 2,920,158 shares	(97,234)	(98,006)
Subscription notes receivable	(3,494)	(3,312)
Accumulated other comprehensive income (loss)	(4,539)	4,161
Total stockholders equity	194,058	204,188
Total liabilities and stockholders equity	$ 991,671	$ 991,250

See accompanying notes to Consolidated Financial Statements.

SCPIE HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)

(UNAUDITED)

	SIX MONTHS ENDED JUNE 30,		THREE MONTHS ENDED JUNE 30,	
	2004	**2003**	**2004**	**2003**
Revenues:				
Net premiums earned	$ 67,641	$ 94,000	$ 31,228	$ 39,744
Net investment income	10,550	10,920	5,118	5,330
Realized investment gains (loss)	1,715	3,927	(631)	837
Other revenue	365	2,020	85	1,514
Total revenues	80,271	110,867	35,800	47,425
Expenses:				
Losses and loss adjustment expenses	65,769	82,875	32,828	34,324
Underwriting and other operating expenses	16,806	29,278	6,576	11,844
Total expenses	82,575	112,153	39,404	46,168
Income (loss) before federal income taxes	(2,304)	(1,286)	(3,604)	1,257
Federal income tax expense (benefit)	(815)	(676)	(1,288)	645
Net income (loss)	$ (1,489)	$ (610)	$ (2,316)	$ 612
Basic earnings (loss) per share	$ (0.16)	$ (0.07)	$ (0.25)	$ 0.07
Diluted earnings (loss) per share	$ (0.16)	$ (0.07)	$ (0.25)	$ 0.07
Cash dividend declared and paid per share of common stock	$	$ 0.20	$	$ 0.10

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

(DOLLARS IN THOUSANDS)

(UNAUDITED)

COMMON STOCK	ADDITIONAL PAID-IN	RETAINED EARNINGS	TREASURY STOCK	STOCK SUBSCRIPTON	ACCUMULATED OTHER COMPREHENSIVE	TOTAL STOCKHOLDERS

		CAPITAL			NOTES RECEIVABLE	INCOME (LOSS)	EQUITY
BALANCE AT JANUARY 1, 2004	$ 1	$ 37,281	$ 264,063	$ (98,006)	$ (3,312)	$ 4,161	$ 204,188
Net loss			(1,489)				(1,489)
Unrealized losses on securities, net of reclassification adjustments of $493 for gains included in net appreciation, net of applicable income taxes of $4,647						(8,625)	(8,625)
Change in minimum pension liability, net of applicable income taxes of ($105)						(195)	(195)
Unrealized foreign currency gain						120	120
Comprehensive income							(10,189)
Treasury stock reissued		(531)		772	(192)		49
Stock subscription notes repaid					10		10
BALANCE AT JUNE 30, 2004	$ 1	$ 36,750	$ 262,574	$ (97,234)	$ (3,494)	$ (4,539)	$ 194,058

See accompanying notes to Consolidated Financial Statements.

SCPIE HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(DOLLARS IN THOUSANDS)

(UNAUDITED)

	SIX MONTHS ENDED JUNE 30,	
	2004	**2003**
OPERATING ACTIVITIES		
Net loss	$ (1,489)	$ (610)
Adjustments to reconcile net loss to net cash used in operating activities:		
Provisions for amortization and depreciation	3,788	2,474
Provision for deferred federal income taxes	(815)	(676)
Realized investment gains	(1,715)	(4,302)
Changes in operating assets and liabilities:		
Deferred acquisition costs	(1,533)	(4,028)
Accrued investment income	992	637
Unearned premiums	24,575	11,413
Loss and loss adjustment expense reserves	(17,860)	(14,376)
Reinsurance recoverable	(29,348)	12,171
Amounts held for reinsurance	12,599	(8,037)
Other liabilities	(8,763)	(8,702)
Premium receivable	(25,445)	(23,876)
Other assets	1,275	(63)
Net cash used in operating activities	(43,739)	(37,975)
INVESTING ACTIVITIES		
Purchases fixed maturities	(171,844)	(273,923)
Sales fixed maturities	217,225	256,025
Maturities fixed maturities	7,391	1,600
Short-term purchases and sales - net	(195)	
Sales equities	3,764	3,926
Net cash provided by (used in) investing activities	56,341	(12,372)
FINANCING ACTIVITIES		
Reissue of treasury shares	241	247
Repayment of stock subscription	(182)	279
Cash dividends		(1,967)
Net cash provided by (used) in financing activities	59	(1,441)
Increase (decrease) in cash and cash equivalents	12,661	(51,788)
Cash and cash equivalents at beginning of period	62,095	115,787
Cash and cash equivalents at end of period	$ 74,756	$ 63,999

See accompanying notes to Consolidated Financial Statements.

SCPIE HOLDINGS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

JUNE 30, 2004

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts and operations, after intercompany eliminations, of SCPIE Holdings Inc. (SCPIE Holdings) and its direct and indirect wholly-owned subsidiaries, principally SCPIE Indemnity Company (SCPIE Indemnity), American Healthcare Indemnity Company (AHI), American Healthcare Specialty Insurance Company (AHSIC), SCPIE Underwriting Limited (SUL) and SCPIE Management Company (SMC), collectively, the Company.

These financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and with instructions to Form 10-Q and Article 7 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six-month period ended June 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. For further information, refer to the consolidated financial statements and notes thereto included in the SCPIE Holdings Annual Report on Form 10-K for the year ended December 31, 2003.

Certain 2003 amounts have been reclassified to conform to the 2004 presentation.

2. EARNINGS (LOSS) PER SHARE

The following table sets forth the computation of basic and diluted earnings (loss) per share:

	SIX MONTHS ENDED JUNE 30,		**THREE MONTHS ENDED JUNE 30,**	
	2004	**2003**	**2004**	**2003**
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
Numerator				

Net income (loss)	$ (1,489)	$ (610)	$ (2,316)	$ 612
Numerator for:				
Basic earnings (loss) per share of common stock	(1,489)	(610)	(2,316)	612
Diluted earnings (loss) per share of common stock	(1,489)	(610)	(2,316)	612
Denominator				
Denominator for basic earnings (loss) per share of common stock weighted-average shares outstanding	9,395	9,345	9,411	9,345
Effect of dilutive securities:				
Stock options				70
Denominator for diluted earnings (loss) per share of common stock adjusted weighted-average shares outstanding	9,395	9,345	9,411	9,415
Basic earnings (loss) per share of common stock	$ (0.16)	$ (0.07)	$ (0.25)	$ 0.07
Diluted earnings (loss) per share of common stock	$ (0.16)	$ (0.07)	$ (0.25)	$ 0.07

3. INVESTMENTS

The Company s investments in available-for-sale securities at June 30, 2004 are summarized as follows:

	COST OR AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
	(IN THOUSANDS)			
Fixed-maturity securities:				
Bonds:				
U.S. government and agencies	$ 143,780	$ 827	$ 2,032	$ 142,575
Mortgage-backed and asset-backed	98,466	192	1,774	96,884
Corporate	253,885	768	6,864	247,789
Total fixed-maturity securities	496,131	1,787	10,670	487,248
Common stocks	12,380	4,005		16,385
Total	$ 508,511	$ 5,792	$ 10,670	$ 503,633

The following table illustrates the gross unrealized losses included in the Company s investment portfolio and the fair value of those securities, aggregated by investment category. The table also illustrates the length of time that they have been in a continuous unrealized loss position as of June 30, 2004.

	LESS THAN 12 MONTHS		12 MONTHS OR MORE		TOTAL	
	GROSS UNREALIZED LOSSES	FAIR VALUE	GROSS UNREALIZED LOSSES	FAIR VALUE	GROSS UNREALIZED LOSSES	FAIR VALUE
	(IN THOUSANDS)					
Fixed-maturity securities:						
Bonds:						
U.S. government and agencies	$ 1,849	$ 93,309	$ 183	$ 6,485	$ 2,032	$ 99,794
Mortgage-backed and asset-backed	1,390	68,996	384	12,821	1,774	81,817
Corporate	4,530	145,167	2,334	46,843	6,864	192,010
Total fixed-maturity securities	7,769	307,472	2,901	66,149	10,670	373,621
Total common stock		16,385				16,385
Total	$ 7,769	$ 323,857	$ 2,901	$ 66,149	$ 10,670	$ 390,006

The unrealized losses are represented by a large number of individual securities with unrealized losses of less than 20% of each security s amortized cost.

The Company has the ability and intent to hold securities with unrealized losses until they recover their value. In the future, information may come to light or circumstances may change that would cause the Company to write-down or sell these securities and incur a realized loss.

4. FEDERAL INCOME TAXES

A reconciliation of income tax benefit in the accompanying statements of income are summarized as follows:

	SIX MONTHS ENDED JUNE 30,	
	2004	**2003**
	(IN THOUSANDS)	
Federal income tax benefit at 35%	$ (806)	$ (450)
Decrease in taxes resulting from non-taxable items	(9)	(226)
Total	$ (815)	$ (676)

5. COMPREHENSIVE INCOME (LOSS)

The following table reconciles net income (loss) and comprehensive income (loss) for the periods presented:

	SIX MONTHS ENDED JUNE 30,		THREE MONTHS ENDED JUNE 30,	
	2004	2003	2004	2003
	(IN THOUSANDS)			
Net income (loss)	$ (1,489)	$ (610)	$ (2,316)	$ 612
Other comprehensive income (loss) before tax:				
Unrealized gains (losses) on securities	(13,272)	9,820	(20,090)	9,002
Unrealized foreign currency gains	120	220	47	220
Change in minimum pension liability	(300)	(300)	(150)	(150)
Other comprehensive income (loss) before tax	(14,941)	9,130	(22,509)	9,684
Income tax expense (benefit) related to securities	(4,647)	2,777	(7,032)	2,491
Income tax benefit related to pension liability	(105)	(105)	(53)	(52)
Comprehensive income (loss)	$ (10,189)	$ 6,458	$ (15,424)	$ 7,245

6. BUSINESS SEGMENTS

The Company classifies its business into two segments: Direct Healthcare Liability Insurance and Assumed Reinsurance. Segments are designated based on the types of products provided and based on the risks associated with the products. Direct healthcare liability insurance represents professional liability insurance for physicians, oral and maxillofacial surgeons and dentists, healthcare facilities and other healthcare providers. Assumed reinsurance represents the book of assumed worldwide reinsurance of professional, commercial and personal liability coverages, commercial and residential property risks and accident and health, workers compensation and marine coverages. Other includes items not directly related to the operating segments such as net investment income, realized investment gains and losses, and other revenue. In December 2002, the Company entered into a 100% quota share reinsurance agreement with Rosemont Reinsurance Ltd. (Rosemont Re) (formerly known as GoshawK Re), a subsidiary of GoshawK Insurance Holdings plc, a publicly held London-based insurer and reinsurer, that divested substantially all of the Company s ongoing assumed reinsurance operations. The Company had one ongoing assumed reinsurance treaty for the 2003 underwriting year.

The following tables present information about reportable segment income (loss) and segment assets as of and for the periods indicated (dollars in thousands):

SIX MONTHS ENDED JUNE 30, 2004	DIRECT HEALTHCARE LIABILITY INSURANCE	ASSUMED REINSURANCE	OTHER	TOTAL

Premiums written	$ 95,493	$ (3,278)		$ 92,215
Premiums earned	$ 61,934	$ 5,707		$ 67,641
Net investment income			$ 10,550	10,550
Realized investment gains			1,715	1,715
Other revenue			365	365
Total revenues	61,934	5,707	12,630	80,271
Losses and loss adjustment expenses	55,833	9,936		65,769
Other operating expenses	12,671	4,135		16,806
Total expenses	68,504	14,071		82,575
Segment income (loss) before income taxes	$ (6,570)	$ (8,364)	$ 12,630	$ (2,304)
Segment assets	$ 62,852	$ 274,831	$ 653,988	$ 991,671

SIX MONTHS ENDED JUNE 30, 2003	DIRECT HEALTHCARE LIABILITY INSURANCE	ASSUMED REINSURANCE	OTHER	TOTAL
Premiums written	$ 97,667	$ 8,572		$ 106,239
Premiums earned	$ 67,310	$ 26,690		$ 94,000
Net investment income			$ 10,920	10,920
Realized investment gains			3,927	3,927
Other revenue			2,020	2,020
Total revenues	67,310	26,690	16,867	110,867
Losses and loss adjustment expenses	64,863	18,012		82,875
Other operating expenses	13,153	16,125		29,278
Total expenses	78,016	34,137		112,153
Segment income (loss) before income taxes	$ (10,706)	$ (7,447)	$ 16,867	$ (1,286)
Segment assets	$ 62,895	$ 230,620	$ 755,566	$ 1,049,081

THREE MONTHS ENDED JUNE 30, 2004	DIRECT HEALTHCARE LIABILITY INSURANCE	ASSUMED REINSURANCE	OTHER	TOTAL
Premiums written	$ 2,753	$ 7		$ 2,760
Premiums earned	$ 29,986	$ 1,242		$ 31,228
Net investment income			$ 5,118	5,118
Realized investment loss			(631)	(631)
Other revenue			85	85
Total revenues	29,986	1,242	4,572	35,800
Losses and loss adjustment expenses	25,224	7,604		32,828
Other operating expenses	6,272	304		6,576
Total expenses	31,496	7,908		39,404
Segment income (loss) before income taxes	$ (1,510)	$ (6,666)	$ 4,572	$ (3,604)
Segment assets	$ 62,852	$ 274,831	$ 653,988	$ 991,671

THREE MONTHS ENDED JUNE 30, 2003	DIRECT HEALTHCARE LIABILITY INSURANCE	ASSUMED REINSURANCE	OTHER	TOTAL
Premiums written	$ 2,239	$ 10,096		$ 12,335
Premiums earned	$ 31,660	$ 8,084		$ 39,744
Net investment income			$ 5,330	5,330
Realized investment gains			837	837
Other revenue			1,514	1,514
Total revenues	31,660	8,084	7,681	47,425
Losses and loss adjustment expenses	27,302	7,022		34,324
Other operating expenses	5,430	6,414		11,844
Total expenses	32,732	13,436		46,168
Segment income (loss) before income taxes	$ (1,072)	$ (5,352)	$ 7,681	$ 1,257
Segment assets	$ 62,895	$ 230,620	$ 755,566	$ 1,049,081

Premiums written represents the premiums charged on policies issued during a fiscal period. Premiums earned represents the portion of premiums written that is recognized as income in the financial statements for the periods presented and earned on a pro-rata basis over the term of the policies.

7. COMMITMENTS AND CONTINGENCIES

The Company is named as defendant in various legal actions primarily arising from claims made under insurance policies and contracts. These actions are considered by the Company in estimating the loss and loss adjustment expense reserves. The Company s management believes that the resolution of these actions will not have a material adverse effect on the Company s financial position or results of operations.

Highlands Insurance Group

Between January 1, 2000, and April 30, 2001, the Company issued endorsements to certain policyholders of the insurance company subsidiaries of Highlands Insurance Group, Inc. (HIG). Under these endorsements, the Company agreed to assume the policy obligations of the HIG insurance company subsidiaries, if the subsidiaries became unable to pay their obligations by reason of having been declared insolvent by a court of competent jurisdiction. The coverages included property, workers compensation, commercial automobile, general liability and umbrella. The gross premiums written by the HIG subsidiaries were approximately $88.0 million for the subject policies. In February 2002, the Texas Department of Insurance placed the principal HIG insurance company subsidiaries under its supervision while HIG voluntarily liquidated their claim liabilities.

During 2002 and 2003, all of the HIG insurance company subsidiaries (with the exception of a California subsidiary) were merged into a single Texas domiciled subsidiary, Highlands Insurance Company (Highlands). Highlands has advised the Company that at June 30, 2004, the HIG insurance company subsidiaries had paid losses and LAE under the subject policies of $65.0 million and had established case loss reserves of $11.5 million, net of reinsurance. Based on a limited review of the exposures remaining, the Company estimates that incurred but not reported losses range from $6 million to $7 million for a total loss and loss expense reserve of $17.5 million to $18.5 million. This estimate is not based on a full reserve analysis of the exposures. To the extent Highlands is declared insolvent at some future date by a court of competent jurisdiction and is unable to pay losses under the subject policies, the Company would be responsible to pay the amount of the losses incurred and unpaid at such date and would be subrogated to the rights of the policyholders as creditors of Highlands. The Company may also be entitled to indemnification of a portion of this loss from certain of Highlands reinsurers.

On November 6, 2003, the State of Texas obtained an order in the Texas District Court appointing the Texas Insurance Commissioner as the permanent Receiver of Highlands and placing the Receiver in possession of all assets of Highlands. The order expressly provided that it did not constitute a finding of Highlands insolvency nor an authorization to liquidate Highlands. On December 1, 2003, however, the State of Texas filed an application to liquidate Highlands, to forestall certain actions taken by the plaintiff in a California litigation to perfect a $57.4 million judgment lien on certain assets of Highlands. The California plaintiff and the Receiver reached a complete settlement of the California litigation, which was approved by the Texas court on July 28, 2004. In connection with the settlement, the Receiver agreed to postpone any liquidation hearing to no earlier than 120 days after the court approval. If an order of liquidation is ultimately entered and becomes final, the Company would likely be required to assume Highlands then remaining obligations under the subject policies.

The California domiciled HIG subsidiary has been the subject of regulatory liquidation. On August 1, 2003, the Superior Court of the County of Orange, California, upon an application filed by the California Insurance Commissioner, declared the California domiciled HIG insurance company subsidiary insolvent and appointed the Insurance Commissioner liquidator of the subsidiary. That HIG subsidiary had established case loss reserves under the subject policies of $450,000 at June 30, 2003.

Letters of Credit

The Company has a letter of credit facility in the amount of $50 million with Barclays Bank PLC. Letters of credit issued under the facility fulfill the collateral requirements of Lloyd s and guarantee loss reserves under certain other reinsurance contracts. As of June 30, 2004, letter of credit issuance under the facility was approximately $49.4 million. Securities of $54.4 million are pledged as collateral under the facility.

California Franchise Tax Board

In the third quarter of 2002, the Company received a notice of assessment from the California Franchise Tax Board (FTB) for the 1997 to 2000 tax years in the total amount of $15.4 million, not including the federal tax benefits from the payment of such assessment or interest that might be included on amounts, if any, ultimately paid to the FTB. The assessment is the result of a memorandum issued by the FTB in April 2002. The memorandum, which is based partly on the California Court of Appeals Decision in *Ceridian v. Franchise Tax Board*, challenges the exclusion from California income tax of dividends received by holding companies from their insurance company subsidiaries during the tax years ended on or after December 1, 1997. The Company has protested these assessments and while the Company intends to vigorously protest the current and any future assessments, there can be no assurance as to the ultimate outcome of these protests.

8. STOCK-BASED COMPENSATION

The following table illustrates the effect on net income (loss) and earnings per share if the Company applied the fair value recognition provision as defined in Financial Accounting Standards Board Statement (FASB) No. 123, *Accounting of Stock-Based Compensation*:

	SIX MONTHS ENDED JUNE 30,		THREE MONTHS ENDED JUNE 30,	
	2004	2003	2004	2003
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
Net income (loss) as reported	$ (1,489)	$ (610)	$ (2,316)	$ 612

Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards net of related tax effects	(340)	(697)	(198)	(460)
Pro forma net income (loss)	$ (1,829)	$ (1,307)	$ (2,514)	$ 152
Earnings (loss) per share:				
Basic as reported	$ (0.16)	$ (0.07)	$ (0.25)	$ 0.07
Basic pro forma	$ (0.20)	$ (0.14)	$ (0.27)	$ 0.02
Diluted as reported	$ (0.16)	$ (0.07)	$ (0.25)	$ 0.07
Diluted pro forma	$ (0.20)	$ (0.14)	$ (0.27)	$ 0.02

For pro forma disclosure purposes, the fair value of stock options was estimated at each date of grant using a Black-Scholes option pricing model using the following assumptions: Risk-free interest rates ranging from 3.625% to 4.25%; dividend yields ranging from 0.66% to 1.14%; volatility factors of the expected market price of the Company s common stock of .5205 and a weighted average expected life of the options ranging from three to ten years.

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

Overview

SCPIE Holdings is a holding company owning subsidiaries engaged in providing insurance and reinsurance products. The Company is primarily a provider of medical malpractice insurance and related liability insurance products to physicians, healthcare facilities and others engaged in the healthcare industry in California and Delaware. Previously, the Company had also been actively engaged in the medical malpractice insurance business and related products in other states and the assumed reinsurance business. During 2002 and 2003, the Company largely completed its withdrawal from the assumed reinsurance market and medical malpractice insurance outside of California and Delaware.

The Company s insurance business is organized into two reportable business segments: direct healthcare liability insurance and assumed reinsurance operations. Primarily due to significant losses on medical malpractice insurance outside of the state of California and assumed reinsurance business losses arising out of the September 11, 2001, World Trade Center terrorist attack, the Company incurred significant losses in the three fiscal years 2001, 2002 and 2003. The resulting reductions in surplus and corresponding decrease in capital adequacy ratios under both the A.M. Best and National Association of Insurance Commissioners (NAIC) capital adequacy models has required the Company to take actions to improve its long-term capital adequacy position. The primary actions taken by the Company have been to effect an orderly withdrawal from healthcare liability insurance markets outside of California and Delaware and from the assumed reinsurance market in its entirety. At December 31, 2003, the Company had only 379 healthcare liability insurance policies remaining in force in these other markets, all of which expired during the first quarter of 2004. In December 2002, the Company entered into a 100% quota share reinsurance agreement to retrocede to another insurer the majority of reinsurance business written in 2002 and 2001. During 2003, the Company participated in only one ongoing reinsurance syndicate. The Company continues to run-off claims in its non-core businesses.

Critical Accounting Policies

The Company s discussion and analysis of its financial condition and results of operations are based upon the Company s consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). Preparation of financial statements in accordance with GAAP requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and the related notes. Management believes that the following critical accounting policies, among others, affect the more significant judgments and estimates used in the preparation of the consolidated financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Premium Revenue Recognition

Direct healthcare liability insurance premiums written are primarily earned on a daily pro rata basis over the terms of the policies. Accordingly, unearned premiums represent the portion of premiums written which is applicable to the unexpired portion of the policies in force. Reinsurance premiums assumed are estimated based on information provided by ceding companies. The information used in establishing these estimates is reviewed and subsequent adjustments are recorded in the period in which they are determined. These premiums are earned over the terms of the

related reinsurance contracts.

Loss and Loss Adjustment Expense Reserves

Unpaid losses and loss adjustment expenses are comprised of case reserves for known claims, incurred but not reported reserves for unknown claims and any potential development for known claims, and reserves for the cost of administration and settlement of both known and unknown claims. Such liabilities are established based on known facts and interpretation of circumstances, including the Company s experience with similar cases and historical trends involving claim payment patterns, loss payments and pending levels of unpaid claims, as well as court decisions and economic conditions. The effects of inflation are considered in the reserving process. Establishing appropriate reserves is an inherently uncertain process; the ultimate liability may be in excess of or less than the amount provided. Any increase in the amount of reserves, including reserves for insured events of prior years, could have an adverse effect on the Company s results for the period in which the adjustments are made. The Company utilizes both its internal actuarial staff and independent consulting actuaries in establishing its reserves. The Company does not discount its loss and loss adjustment expense reserves.

The Company had a growing volume of assumed reinsurance between 1999 and 2002. Assumed reinsurance is a line of business with inherent volatility. Ultimate loss experience for the assumed reinsurance operation is based primarily on reports received by the Company from the underlying ceding insurers. Many losses take several years to be reported through the system. The Company relies heavily on the ceding entity s, especially Lloyd s syndicates, estimates of ultimate incurred losses. Ceding entities, representing over 65% of the reinsurance assumed business for the 1999 to 2003 underwriting years (based on gross written premiums), submit reports to the Company containing ultimate incurred loss estimates reviewed by independent or internal actuaries of the ceding entities. These reported ultimate incurred losses are the primary basis for the Company s reserving estimates. In other cases, the Company relies on its own internal estimates determined primarily by experience to date, individual knowledge of the specific reinsurance contract, industry experience and other actuarial techniques to determine reserve requirements.

Because the reserve establishment process is by definition an estimate, actual results will vary from amounts established in earlier periods. The Company recognizes such differences in the periods they are determined. Since reserves accumulate on the balance sheet over several years until all claims are settled, a determination of inadequacy or redundancy could easily have a significant impact on earnings and therefore stockholders equity. The Company has established net reserves, after considering both prospective and retrospective reinsurance, of $449.8 million. The net reserves attributable to the operating segments of the Company are as follows:

Summary of Net Loss and LAE Reserves

by Segment
SIX MONTHS ENDED JUNE 30, 2004

Direct Healthcare Liability Insurance:	
Core	$ 248.6
Non-Core	120.5
Assumed Reinsurance Segment	80.7
Total	$ 449.8

A 1% difference in the ultimate value of reserves, net of reinsurance recoverable, would decrease or increase future pretax earnings by $4.5 million.

Deferred Policy Acquisition Costs

Deferred policy acquisition costs include commissions, premium taxes and other variable costs incurred in connection with writing business. Deferred policy acquisition costs are reviewed to determine if they are recoverable from future income, including investment income. If such costs are estimated to be unrecoverable, they are expensed. Recoverability is analyzed based on the Company s assumptions related to the underlying policies written, including the lives of the underlying policies, future investment income, and level of expenses necessary to maintain the policies over their entire lives. Deferred policy acquisition costs are amortized over the period in which the related premiums are earned.

Investments

The Company considers its fixed maturity and equity securities as available-for-sale securities. Available-for-sale securities are sold in response to a number of issues, including the Company s liquidity needs, the Company s statutory surplus requirements and tax management strategies, among others. During the fourth quarters of 2002 and 2003, the Company sold significant amounts of its available-for-sale securities to increase surplus for statutory accounting purposes. In late 2001 and 2002, the Company began to shift the character of its investment income to fully taxable as part of the Company s tax strategy. Available-for-sale securities are recorded at fair value. The related unrealized gains and losses, net of income tax effects, are excluded from net income and reported as a component of stockholders equity.

The Company evaluates the securities in its available-for-sale investment portfolio on at least a quarterly basis for declines in market value below cost for the purpose of determining whether these declines represent other than temporary declines. Some of the factors the Company considers in the evaluation of its investments are:

- the extent to which the market value of the security is less than its cost basis;
- the length of time for which the market value of the security has been less than its cost basis;
- the financial condition and near-term prospects of the security s issuer, taking into consideration the economic prospects of the issuers industry and geographical region, to the extent that information is publicly available; and
- the Company s ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value.

A decline in the fair value of an available-for-sale security below cost that is judged to be other than temporary is realized as a loss in the current period and reduces the cost basis of the security.

Income taxes

At June 30, 2004, the Company had $48.4 million of net deferred income tax assets. Net deferred income tax assets consist of the net temporary differences created as a result of amounts deductible or revenue recognized in periods different for tax return purposes than for accounting purposes. These deferred income tax assets include an asset of $18.8 million for a net operating loss carryforward that will expire in 2021. A net operating loss carryforward is a tax loss that may be carried forward into future years. It reduces taxable income in future years and the tax liability that would otherwise be incurred.

The Company believes it is more likely than not that the deferred income tax assets will be realized through its future earnings. As a result, the Company has not recorded a valuation allowance. The Company has been historically profitable except during the last three years because of losses primarily related to the non-core healthcare liability and assumed reinsurance operations. Since those operations are now in run-off, the Company believes it should return to a position of taxable income, thus enabling it to utilize the net operation loss carryforward.

The Company s estimate of future taxable income uses the same assumptions and projections as in its internal financial projections. These projections are subject to uncertainties primarily related to future underwriting results. If the Company s results are not as profitable as expected, the Company may be required in future periods to record a valuation allowance for all or a portion of the deferred income tax assets. Any valuation allowance would reduce the Company s earnings.

Forward Looking Statements

Certain statements in this report on Form 10-Q that are not historical in fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors based on the Company s estimates and expectations concerning future events that may cause the actual results of the Company to be materially different from historical results or from any results expressed or implied by such forward-looking statements. Actuarial estimates of losses and loss expenses (LAE), expectations concerning the Company s ability to retain current insureds at profitable levels, successful withdrawal from the assumed reinsurance business, obtaining necessary rate change regulatory approvals, expansion of liability insurance business in its principal market and improved performance are dependent upon a variety of factors, including future economic, competitive and market conditions, frequency and severity of catastrophic events, future legislative and regulatory actions, uncertainties and potential delays in obtaining premium rate approvals, the level of ratings from recognized rating services, the inherent uncertainty of loss and loss expense estimates in both the core and discontinued non-core businesses (including a contingent liability related to Highlands Insurance Company), and the cyclical nature of the property and casualty industry, all of which are difficult or impossible to predict accurately and many of which are beyond the control of the Company. The Company is also subject to certain structural risks as an insurance holding company, including statutory restrictions on dividends and other intercompany transactions. In light of the significant uncertainties inherent in the forward-looking information herein, the inclusion of such information should not be regarded as a representation by the Company or any other person that the Company s objectives or plans will be realized. These risks and uncertainties, as well as the Company s critical accounting policies, are discussed in more detail under Business Risk Factors, Management s Discussion and Analysis Overview, and Management s Discussion and Analysis Critical Accounting Policies in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2003.

Information Regarding Non-GAAP Measures

The Company has presented information in this report with respect to premiums written, an operating measure which in management s opinion provides investors useful industry specific information to evaluate and perform meaningful comparisons of the Company s performance. Premiums written is a non-GAAP financial measure which represents the premiums charged on policies issued during a fiscal period less any reinsurance. Premiums written is a statutory measure of production levels. Premiums earned, a comparable GAAP measure, represents the

portion of premiums written that is recognized as income in the financial statements for the periods presented and earned on a pro-rata basis over the term of the policies.

RESULTS OF OPERATIONS

SIX MONTHS ENDED JUNE 30, 2004 COMPARED TO SIX MONTHS ENDED JUNE 30, 2003

Direct Healthcare Liability Insurance Segment

The Company underwrites professional and related liability policy coverages for physicians (including oral and maxillofacial surgeons), physician medical groups and clinics, hospitals, dentists, managed care organizations and other providers in the healthcare industry. As a result of the Company s withdrawal from certain segments of the healthcare industry, the premiums earned are allocated between core and non-core premium. Core premium represents California and Delaware business excluding dentist and hospital business. Non-core business represents business related to physician and dental programs formerly conducted for the Company primarily in states outside California and Delaware by a national independent insurance agency, other state non-standard physician programs and hospital programs including those in California.

The following table summarizes by core and non-core businesses the underwriting results of the direct healthcare liability insurance segment for the periods indicated (dollars in thousands):

Direct Healthcare Liability Insurance Segment

Underwriting Results

	CORE	NON-CORE*	TOTAL*
SIX MONTHS ENDED JUNE 30, 2004			
Premiums written	$ 96,189	$ (696)	$ 95,493
Premiums earned	$ 62,542	$ (608)	$ 61,934
Losses and LAE incurred	52,063	3,770	55,833
Underwriting expenses	12,571	100	12,671
Underwriting loss	$ (2,092)	$ (4,478)	$ (6,570)
Loss ratio	83.2%		
Expense ratio	20.1%		
Combined ratio	103.3%		
SIX MONTHS ENDED JUNE 30, 2003			
Premiums written	$ 92,580	$ 5,087	$ 97,667
Premiums earned	$ 58,283	$ 9,027	$ 67,310
Losses and LAE incurred	54,250	10,613	64,863
Underwriting expenses	10,100	3,053	13,153

Underwriting loss	$ (6,067)	$ (4,639)	$ (10,706)
Loss ratio	93.1%		
Expense ratio	17.3%		
Combined ratio	110.4%		

* The ratios for the segment total and non-core business are not meaningful due to the run-off status of non-core business.

Core Business

Premiums written were $96.2 million and premiums earned were $62.5 million in the six months ended June 30, 2004; compared to $92.6 million and $58.3 million in the six months ended June 30, 2003. Premiums written and earned increased primarily due to a 9.9% rate increase effective October 1, 2003. This increase was partially offset by a decline in policies in-force.

The loss ratio (losses and LAE expenses related to premiums earned) for the six months ended June 30, 2004 was 83.2% compared to 93.7% in the second quarter 2003. The decrease in the loss ratio is due primarily to the full effect on earned premiums of the 9.9% rate increase effective October 1, 2003, as well as lower estimates of loss trends for 2004.

The underwriting expense ratio for the six months ended June 30, (expenses related to premiums earned) increased to 20.1% in the first six months of 2004 from 17.3% in the first six months ended of 2003. The change is primarily attributable to a decline in premium in the non-core business. As a result of that decline, most underwriting expenses are attributable to the core business.

Non-Core Business

Premiums written decreased in the six months ended June 30, 2004, to $(0.7) from $5.1 million for the same period in 2003. This resulted from a significant decline in the number of policies in-force in the non-core business from 1,155 at June 30, 2003 to zero at June 30, 2004. After March 6, 2003, no new or renewal business was written in the non-core programs, as the Company exited these markets. Premium earned in the non-core direct healthcare liability insurance business decreased as the written premium declined.

The underwriting loss incurred in the six months ended June 30, 2004, is primarily due to adverse litigation decisions on a few cases and multiple losses related to one insured dentist. These losses are all from prior years activity and are considered unusual circumstances not anticipated by the normal actuarial process. In addition, the Company had reinsurance reinstatement premiums which are accounted for as negative premiums.

Assumed Reinsurance Segment

Assumed reinsurance represents the book of assumed worldwide reinsurance of professional, commercial and personal liability coverages, commercial and residential property risks and accident and health, workers compensation and marine coverages.

The following table summarizes the underwriting results of the assumed reinsurance segment for the periods indicated (dollars in thousands):

	Assumed Reinsurance Segment Underwriting Results	
FOR THE SIX MONTHS ENDED JUNE 30,	**2004**	**2003**
Premiums written	$ (3,278)	$ 8,572
Premiums earned	$ 5,707	$ 26,690
Underwriting expenses		
Losses	9,936	18,012
Underwriting and other operating expenses	4,135	16,125
Underwriting loss	$ (8,364)	$ (7,447)

The earned premium in 2004 is a result of one ongoing assumed reinsurance program for the 2003 underwriting year.

The underwriting loss incurred in the six months ended June 30, 2004, primarily results from upward development of losses on the Company s participation in two of the three Lloyd s of London syndicates that the Company is a participant and capital provider for the 2001 underwriting year which were only partially ceded under the Rosemont Re reinsurance treaty.

The Rosemont Re reinsurance treaty entered into in December 2002 effectively cedes all of the unearned premium and future reported premium after June 30, 2002, for the assumed reinsurance business written for underwriting years 2001 and 2002 by the Company. This treaty relieves the Company of significant underwriting risk and written premium leverage in 2002 and 2003 and significantly improves the Company s risk-based capital adequacy ratios under both the A.M. Best and NAIC models. The treaty has no limitations on loss recoveries and includes a profit-sharing provision should the combined ratios calculated on the base premium ceded be below 100%. The treaty requires Rosemont Re to reimburse the Company for its acquisition and administrative expenses. In addition, the Company is required to pay Rosemont Re additional premium in excess of the base premium ceded of 14.3%. The additional premium paid to Rosemont Re was $(0.7) million and $3.8 million for the six month periods ending June 30, 2004 and 2003, respectively.

The Rosemont Re reinsurance treaty has both prospective and retroactive elements as defined in FASB No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*. As such, any gains under the contract will be deferred and amortized to income based upon the expected recovery. No gains are anticipated currently. Losses related to future earned premium ceded, as well as development on losses related to existing earned premium ceded after June 30, 2002, will ultimately determine whether a gain will be recorded under the contract. The retroactive accounting treatment required under FASB 113 requires that a charge to income be recorded to the extent premiums ceded under the contract are in excess of the estimated losses and expenses ceded under the contract.

Other Operations

Net investment income decreased to $10.6 million for the six months ended June 30, 2004, a decrease of 3.4% from $10.9 million for the six months ended June 30, 2003. The reduction in investment income is a result of a reduction in invested assets partially offset by a slight increase in the average rate of return. The decline in invested assets was as a result of the claim payments related to the run-off of the non-core healthcare liability and assumed reinsurance businesses. The average rate of return on invested assets was 3.8% and 3.6% for the six months ended June 30, 2004, and June 30, 2003, respectively.

THREE MONTHS ENDED JUNE 30, 2004 COMPARED TO THREE MONTHS ENDED JUNE 30, 2003

Direct Healthcare Liability Insurance Segment

The following table summarizes by core and non-core businesses the underwriting results of the direct healthcare liability insurance segment for the periods indicated (dollars in thousands):

Direct Healthcare Liability Insurance Segment

Underwriting Results

	CORE	NON-CORE*	TOTAL*
THREE MONTHS ENDED JUNE 30, 2004			
Premiums written	$ 3,707	$ (954)	$ 2,753
Premiums earned	$ 30,946	$ (960)	$ 29,986

Losses and LAE incurred	24,685	539	25,224
Underwriting expenses	6,284	(12)	6,272
Underwriting loss	$ (23)	$ (1,487)	$ (1,510)
Loss ratio	79.8%		
Expense ratio	20.3%		
Combined ratio	100.1%		
THREE MONTHS ENDED JUNE 30, 2003			
Premiums written	$ 2,318	$ (79)	$ 2,239
Premiums earned	$ 28,736	$ 2,924	$ 31,660
Losses and LAE incurred	26,555	747	27,302
Underwriting expenses	5,104	326	5,430
Underwriting (loss) gain	$ (2,923)	$ 1,851	$ (1,072)
Loss ratio	92.4%		
Expense ratio	17.8%		
Combined ratio	110.2%		

* The ratios for the segment total and non-core business are not meaningful due to the run-off status of non-core business.

Core Business

Premiums written were $3.7 million and premiums earned were $30.9 million in the three months ended June 30, 2004, compared to $2.3 million and $28.7 million in the three months ended June 30, 2003. Premiums written and earned increased primarily due to a 9.9% rate increase effective October 1, 2003. This increase was partially offset by a slight decline in policies in-force.

The loss ratio (losses and LAE expenses related to premiums earned) for the second quarter 2004 was 79.8% compared to 92.4% in the second quarter 2003. The decrease in the loss ratio is due primarily to the full effect on earned premiums of the 9.9% rate increase effective October 1, 2003, as well as lower estimates in loss trends in 2004.

The underwriting expense ratio (expenses related to premiums earned) increased to 20.3% in the second quarter 2004 from 17.8% in the second quarter 2003. The change is primarily attributable to a decline in premium in the non-core business. As a result of that decline, most underwriting expenses are attributable to the core business.

Non-Core Business

After March 6, 2003, no new or renewal business was written in the non-core programs as the Company exited these markets. Premium earned in the non-core direct healthcare liability insurance business decreased as the written premium declined.

The underwriting loss incurred in the three months ended June 30, 2004 is primarily due to reinstatement reinsurance premiums on older policy years. The reinstatement premiums are reported as negative premium.

Assumed Reinsurance Segment

The following table summarizes the underwriting results of the assumed reinsurance segment for the periods indicated (dollars in thousands):

	Assumed Reinsurance Segment Underwriting Results	
FOR THE THREE MONTHS ENDED JUNE 30,	**2004**	**2003**
Premiums written	$ 7	$ 10,096
Premiums earned	$ 1,242	$ 8,084
Underwriting expenses		
Losses	7,604	7,022
Underwriting and other operating expenses	304	6,414

Underwriting loss	$ (6,666)	$ (5,352)

The earned premium in 2004 is a result of one ongoing assumed reinsurance program for the 2003 underwriting year.

The underwriting loss increased in the three months ended June 30, 2004, primarily due to significant upward development upon closing of the 2001 underwriting year for two of the three Lloyd s of London syndicates that the Company is a participant and capital provider. The Rosemont Re reinsurance treaty only partially offset the losses reported.

The Rosemont Re reinsurance treaty entered into in December 2002 effectively cedes all of the unearned premium and future reported premium after June 30, 2002, for the assumed reinsurance business written for underwriting years 2001 and 2002 by the Company. This treaty relieves the Company of significant underwriting risk and written premium leverage in 2002 and 2003 and significantly improves the Company s risk-based capital adequacy ratios under both the A.M. Best and NAIC models. The treaty has no limitations on loss recoveries and includes a profit-sharing provision should the combined ratios calculated on the base premium ceded be below 100%. The treaty requires Rosemont Re to reimburse the Company for its acquisition and administrative expenses. In addition, the Company is required to pay Rosemont Re additional premium in excess of the base premium ceded of 14.3%. The additional premium paid to Rosemont Re was $(0.7) million and $3.8 million for the six month periods ending June 30, 2004 and 2003, respectively.

The Rosemont Re reinsurance treaty has both prospective and retroactive elements as defined in FASB No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*. As such, any gains under the contract will be deferred and amortized to income based upon the expected recovery. No gains are anticipated currently. Losses related to future earned premium ceded, as well as development on losses related to existing earned premium ceded after June 30, 2002, will ultimately determine whether a gain will be recorded under the contract. The retroactive accounting treatment required under FASB 113 requires that a charge to income be recorded to the extent premiums ceded under the contract are in excess of the estimated losses and expenses ceded under the contract.

Other Operations

Net investment income decreased to $5.1 million for the three months ended June 30, 2004, a decrease of 4.0% from $5.3 million for the three months ended June 30, 2003. The reduction in investment income is a result of a reduction in invested assets offset by a slight increase in the average rate of return. The decline in invested assets was as a result of the claim payments related to the run-off of the non-core healthcare liability and assumed reinsurance businesses. The average rate of return on invested assets was 3.7% and 3.1% for the three months ended June 30, 2004 and 2003, respectively.

LIQUIDITY AND CAPITAL RESOURCES

The primary sources of the Company s liquidity are insurance premiums, net investment income, recoveries from reinsurers and proceeds from the maturity or sale of invested assets. Funds are used to pay losses, LAE, operating expenses, reinsurance premiums and taxes.

Because of uncertainty related to the timing of the payment of claims, cash from operations for a property and casualty insurance company can vary substantially from period to period. During the first six months of 2004, the Company had negative cash flow from operations of $43.7 million compared to a negative cash flow of $38.0 million in 2003. The negative cash flow in 2004 is primarily related to claims payments associated with the non-core physician and assumed reinsurance programs, which are now in run-off. The Company maintains a portion of its investment portfolio in high-quality short-term securities and cash to meet short-term operating liquidity requirements, including the payment of losses and LAE. Cash and cash equivalents investments totaled $74.8 million or 12.7% of invested assets, at June 30, 2004. The Company believes that all of its short-term and fixed-maturity securities are readily marketable.

The Company invests its cash flow from operations principally in taxable fixed maturity securities. The Company s current policy is to limit its investment in unaffiliated equity securities and mortgage loans to no more than 8% of the total market value of its investments. The market value of the Company s portfolio of unaffiliated equity securities was $16.4 million at June 30, 2004. The Company plans to continue its emphasis on fixed maturity securities investments for the indefinite future.

The Company leases approximately 95,000 square feet of office space for its headquarters. The lease is for a term of 10 years ending in 2009, and the Company has two options to renew the lease for a period of five years each.

SCPIE Holdings is an insurance holding company whose assets primarily consist of all of the capital stock of its insurance company subsidiaries. Its principal sources of funds are dividends from its subsidiaries and proceeds from the issuance of debt and equity securities. The insurance company subsidiaries are restricted by state regulation in the amount of dividends they can pay in relation to earnings or surplus, without the consent of the applicable state regulatory authority, principally the California Department of Insurance. SCPIE Holdings principal insurance company subsidiary, SCPIE Indemnity, may pay dividends to SCPIE Holdings in any 12-month period, without regulatory approval, to the extent such dividends do not exceed the greater of (i) 10% of its statutory surplus at the end of the preceding year or (ii) its statutory net income for the preceding year. Applicable regulations further require that an insurer s statutory surplus following a dividend or other distribution be reasonable in relation to its outstanding liabilities and adequate to meet its financial needs, and permit the payment of dividends only out of statutory earned (unassigned) surplus unless the payment out of other funds receives regulatory approval. The amount of dividends that SCPIE Indemnity is able to pay to SCPIE Holdings during 2004 without prior regulatory approval is approximately $14.0 million. As of June 30, 2004, no dividends had been paid to SCPIE Holdings.

Common stock dividends paid to stockholders were $0.10 per share in the second quarter 2003. These dividends were funded through dividends from the Company s insurance subsidiaries received in prior years. In March 2004, the Board of Directors suspended the Company s quarterly dividends. The payment and amount of cash dividends will depend upon, among other factors, the Company s operating results, overall financial condition, capital requirements and general business conditions. As of June 30, 2004, SCPIE Holdings held cash and short-term securities of $8.2 million. Based on historical trends, market conditions and its business plans, the Company believes that its sources of funds (including dividends from the insurance company subsidiaries) will be sufficient to meet the liquidity needs of SCPIE Holdings over the next 18 months.

The Company s capital adequacy position has been weakened by the continuing losses in the non-core business. On November 14, 2003, A.M. Best, after a review of the third quarter 2003 results, reduced the rating of the Insurance Subsidiaries to B (Fair), with a negative outlook. A.M. Best assigns this rating to companies that have, in its opinion, a fair ability to meet their current obligations to policyholders, but are financially vulnerable to adverse changes in underwriting and economic conditions. The NAIC has developed a methodology for measuring the adequacy of an insurer s surplus which includes a risk-based capital (RBC) formula designed to measure state statutory capital and surplus needs. The RBC rules provide for different levels of regulatory attention based on four thresholds determined under the formula. At December 31, 2003, the RBC level of each insurance company subsidiary exceeded the threshold requiring the least regulatory attention. At December 31, 2003, SCPIE Indemnity exceeded this threshold by $47.6 million.

The Company believes that it has the ability to fund its continuing operations from its premiums written and investment income. The Company plans to continue its focus on the efficient operation of its core business, while at the same time continuing to adjudicate and settle claims incurred in its discontinued non-core business. As the Company continues to run-off the non-core loss and LAE reserves, its capital adequacy position should improve. The Company believes it has, at best, only limited opportunities to raise capital, if that becomes necessary.

EFFECT OF INFLATION

The primary effect of inflation on the Company is considered in pricing and estimating reserves for unpaid losses and LAE for claims in which there is a long period between reporting and settlement, such as medical malpractice claims. The actual effect of inflation on the Company s results cannot be accurately known until claims are ultimately settled. Based on actual results to date, the Company believes that loss and LAE reserve levels and the Company s rate making process adequately incorporate the effects of inflation.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is subject to various market risk exposures, including interest rate risk and equity price risk.

The Company invests its assets primarily in fixed-maturity securities, which at June 30, 2004 comprised 82.7% of total investments at market value. Corporate bonds represent 42.1% and U.S. government bonds represent 24.2% of the fixed-maturity investments, with the remainder consisting of mortgage-backed and asset-backed securities. Equity securities, consisting primarily of common stocks, account for 2.8% of total investments at market value. Mortgage loans represent 1.6% of the investment portfolio. The remainder of the investment portfolio consists of cash and highly liquid short-term investments, which are primarily overnight bank repurchase agreements and short-term money market funds.

The value of the fixed-maturity portfolio is subject to interest rate risk. As market interest rates decrease, the value of the portfolio increases with the opposite holding true in rising interest rate environments. A common measure of the interest sensitivity of fixed-maturity assets is modified duration, a calculation that takes maturity, coupon rate, yield and call terms to calculate an average age of the expected cash flows. The longer the duration, the more sensitive the asset is to market interest rate fluctuations.

The value of the common stock equity investments is dependent upon general conditions in the securities markets and the business and financial performance of the individual companies in the portfolio. Values are typically based on future economic prospects as perceived by investors in the equity markets.

At June 30, 2004, the carrying value of the investment portfolio included $4.9 million in net unrealized losses. At December 31, 2003, the investment portfolio included $8.1 million in net unrealized gains.

ITEM 4. DISCLOSURE CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in its reports under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (SEC), and that such information is accumulated and communicated to the Company s management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by Securities and Exchange Commission Rule 13a-15(b), the Company carried out an evaluation, under the supervision and with the participation of its management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company s disclosure controls and procedures as of the end of the quarter covered by this report. Based on the foregoing, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures were effective at the reasonable assurance level.

There have been no significant changes in the Company s internal controls over financial reporting during the Company s most recent fiscal quarter that may have materially affected, or are reasonably likely to materially affect the Company s internal controls over financial reporting.

PART II OTHER INFORMATION

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

At the Annual Meeting of Stockholders held on May 20, 2004, the following individuals were reelected to the Board of Directors for a term ending in 2007; Mitchell S. Karlan, MD, 5,459,422 votes for, 1,171,689 withheld authority; Jack E. McCleary, MD, 5,536,596 votes for, 1,094,515 withheld authority; Wendell L. Moseley, MD, 5,464,293 votes for, 1,166,818 withheld authority; Donald P. Newell 5,553,447 votes for, 1,077,664 withheld authority. The other directors, whose terms of office continued after the meeting were Willis T. King, Jr., Louis H. Masotti, PhD, Charles B. McElwee, MD, Harriet M. Opfell, MD, William A. Renert, MD, Henry L. Stoutz, MD, Reinhold A. Ullrich, MD, Ronald H. Wender, MD and Donald J. Zuk.

In addition, the SCPIE Holdings Inc. Senior Executive Incentive Bonus Plan was approved with 4,904,542 votes for, 1,489,487 votes against, 237,082 abstentions. There were no broker non-votes.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following exhibits are included herewith.

NUMBER	**DOCUMENT**
31.1	Certifications of Registrant s Chief Executive Officer and Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 and Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certifications of Registrant s Chief Executive Officer and Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002. These certifications are being furnished solely to accompany this Quarterly Report on Form 10-Q and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and are not to be incorporated by reference into any filing of the Company.

(b) None.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SCPIE HOLDINGS INC.

Date: August 12, 2004 By: /s/ DONALD J. ZUK

		Donald J. Zuk President and Chief Executive Officer
Date: August 12, 2004	By:	/s/ ROBERT B. TSCHUDY
		Robert B. Tschudy Senior Vice President and Chief Financial Officer