ALFA CORP Form 10-Q November 13, 2002 Table of Contents

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended September 30, 2002

Commission File Number 0-11773

ALFA CORPORATION

(Exact name of registrant as specified in its charter)

Delaware (State of Other Jurisdiction of Incorporation or Organization) 063-0838024 (IRS Employer Identification No.)

2108 East South Boulevard, Montgomery, Alabama 36116 (Mail: P. O Box 11000, Montgomery, Alabama 36191-0001) (Address and Zip Code of Principal Executive Offices)

Registrant s Telephone Number Including Area Code

(334) 288-3900

None

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 x No o

Indicate the number of shares outstanding of each of the issuer s classes of Common Stock, as of the close of the period covered by this report.

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Class
Common Stock, \$1.00 par value

Outstanding September 30, 2002 78,990,673 shares

ALFA CORPORATION

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ALFA CORPORATION CONSOLIDATED BALANCE SHEETS

		September 30, 2002 (Unaudited)		December 31, 2001
Assets				
Investments:				
Fixed Maturities Held for Investment, at amortized cost (fair value \$361,90	62			
n				
2002 and \$477,422 in 2001)	\$	331,694	\$	441,740
Fixed Maturities Available for Sale, at fair value (amortized cost \$1,005,480,096 in 2002 and \$932,488,619 in 2001)		1,080,954,960		960,415,249
Equity Securities, at fair value (cost \$54,400,227 in 2002 and \$46,889,245	in			
2001)		52,224,680		74,664,030
Mortgage Loans on Real Estate		47,337		109,556
Investment Real Estate (net of accumulated depreciation of \$1,554,023 in				
002 and \$1,444,946 in 2001)		2,636,134		2,712,165
Policy Loans		52,321,306		49,945,528
Collateral Loans		104,111,124		88,561,085
Other Long-term Investments		203,972,726		164,056,234
Short-term Investments		154,913,856		150,255,275
Short term investments		154,713,630		130,233,273
Total Investments		1,651,513,817		1,491,160,862
Cash		12,370,151		10,224,827
Accrued Investment Income		16,947,877		14,140,097
Accounts Receivable		19,232,106		19,843,577
Reinsurance Balances Receivable		2,206,508		3,166,591
Due from Affiliates		1,829,677		2,670,993
Deferred Policy Acquisition Costs		155,284,737		149,820,302
Other Assets		12,615,006		6,577,215
Office Assets		12,013,000		0,577,215
Total Assets	\$	1,871,999,879	\$	1,697,604,464
Liabilities	Φ.	150.052.25	.	110.1=1.15
Policy Liabilities and Accruals - Property and Casualty Insurance	\$	150,853,230	\$	140,174,162
Policy Liabilities and Accruals - Life Insurance		610,128,346		558,043,631
Unearned Premiums		157,073,229		138,384,495
Dividends to Policyholders		10,360,739		10,195,930
Premium Deposit and Retirement Deposit Funds		6,471,267		5,472,522
Deferred Income Taxes		43,260,317		41,312,681
Other Liabilities		74,129,124		76,295,259
Due to Affiliates		15,861,072		16,146,574
Commercial Paper		133,512,317		165,415,905
Notes Payable		70,000,000		

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Notes Payable to Affiliates	48,587,658	37,051,467
Total Liabilities	1,320,237,299	1,188,492,626
Commitments and Contingencies		
Stockholders Equity		
Preferred Stock, \$1 par value Shares authorized: 1,000,000 Issued: None		
Common Stock, \$1 par value Shares authorized: 110,000,000 Issued: 83,783,024 Outstanding: 2002 - 78,990,673; 2001 - 78,359,356	83,783,024	41,891,512
Capital in Excess of Par Value	2,780,791	26,436,168
Accumulated Other Comprehensive Income	35,812,443	33,996,936
Retained Earnings	470,263,022	446,032,558
Treasury Stock: at cost (2002 - 4,792,351 shares; 2001 - 5,423,668 shares)	(40,876,700)	(39,245,336)
Total Stockholders Equity	551,762,580	509,111,838
Total Liabilities and Stockholders Equity	\$ 1,871,999,879	\$ 1,697,604,464

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

ALFA CORPORATION CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

		ths Ended aber 30,	Three Montl	
	2002	2001	2002	2001
Revenues				
Premiums - Property and Casualty Insurance	\$ 317,859,583	\$ 295,360,960	\$ 108,447,938 \$	100,133,110
Premiums and Policy Charges - Life Insurance	46,868,792	42,658,144	15,205,966	14,005,207
Net Investment Income	65,951,535	62,212,315	21,955,649	22,635,959
Realized Investment Gains (Losses)	3,672,351	3,073,113	2,462,802	1,921,978
Other Income	2,056,014	2,080,488	920,621	632,348
Total Revenues	436,408,275	405,385,020	148,992,976	139,328,602
Benefits and Expenses				
Benefits & Settlement Expenses	260,922,196	235,367,411	90,721,888	80,523,430
Dividends to Policyholders	2,749,402	2,780,276	863,617	876,026
Amortization of Deferred Policy				
Acquisition Costs	59,042,848	55,459,983	20,469,422	18,746,640
Other Operating Expenses	42,966,476	41,466,549	13,008,872	13,705,379
Total Expenses	365,680,922	335,074,219	125,063,799	113,851,475
Income Before Provision for Income Taxes	70,727,353	70,310,801	23,929,177	25,477,127
Provision for Income Taxes	19,277,753	19,706,801	6,479,063	6,879,644
Net Income Before Cumulative Effect of Change in Accounting Principle, Net of Tax Benefit	51,449,600	50,604,000	17,450,114	18,597,483
Cumulative Effect of Change in Accounting Principle, Net of Income Tax Benefit of \$140,394 in 2001	0	(260,731)	0	(1,950)
Net Income	\$ 51,449,600	\$ 50,343,269	\$ 17,450,114 \$	18,595,533

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Operating Income	\$	49,062,573 \$	48,606,477	\$ 15,849,293	\$ 17,348,198
Earnings Per Share:					
_					
Operating Income	Ф	0.62 #	0.62	Φ 0.20	Φ 0.20
- Basic	\$	0.62 \$			
- Diluted	\$	0.62 \$	0.62	\$ 0.20	\$ 0.22
Net Income Before Cumulative Effect of Change in Accounting Principle, Net of Tax Benefit					
- Basic	\$	0.65 \$	0.64	\$ 0.22	\$ 0.24
- Diluted	\$	0.65 \$	0.64	\$ 0.22	\$ 0.24
Cumulative Effect of Change in Accounting Principle, Net of Tax Benefit					
- Basic	\$	0.00 \$	0.00	\$ 0.00	(\$0.00
- Diluted	\$	0.00 \$	0.00	\$ 0.00	(\$0.00
Net Income					
- Basic	\$	0.65 \$	0.64	\$ 0.22	\$ 0.24
- Diluted	\$	0.65 \$	0.64	\$ 0.22	\$ 0.24
Average Shares Outstanding					
- Basic		78,697,826	78,315,714	78,875,959	78,306,490
- Diluted		79,473,390	78,948,270	79,567,532	79,038,146

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

ALFA CORPORATION CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

Nine Months Ended September 30, Three Months Ended September 30,

	2002	 2001		2002	2001				
Net Income Other Comprehensive (Loss) Income, net of tax:	\$ 51,449,600	\$ 50,343,269	\$	17,450,114	\$	18,595,533			
Change in Fair Value of Securities Available for Sale Unrealized	9,374,843	531,877		11,277,281		2,086,810			
(Losses) on Interest Rate Swap Contracts	(5,172,308)			(4,154,278)					
Less: Reclassification Adjustment for Realized Investment									
Gains (Losses)	2,387,028	 1,997,523		1,600,821		1,249,285			
Total Other Comprehensive (Loss) Income	1,815,507	(1,465,646)		5,522,182		837,525			
	1,013,30/	(1,403,040)		3,322,102	_	631,323			
Total Comprehensive Income	\$ 53,265,107	\$ 48,877,623	\$	22,972,296	\$	19,433,058			

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

ALFA CORPORATION CONSOLIDATEDSTATEMENTS OF CASH FLOWS (Unaudited)

Nine Months Ended September 30,

		2002	2001		
Cash Flows From Operating Activities:					
Net Income	\$	51,449,600	\$	50,343,269	
Adjustments to Reconcile Net Income to Net Cash					
Provided by Operating Activities:					
Policy Acquisition Costs Deferred		(71,867,563)		(64,172,774	
Amortization of Deferred Policy Acquisition Costs		59,042,848		55,459,983	
Depreciation and Amortization		(743,904)		(207,654	
Provision for Deferred Taxes		1,891,818		1,920,753	
Interest Credited on Policyholders' Funds		19,047,168		16,986,343	
Net Realized Investment Gains		(3,672,351)		(3,073,113	
Other		(7,887,951)		103,245	
Changes in Operating Assets and Liabilities:					
Accrued Investment Income		(2,807,780)		(794,116	
Accounts Receivable		611,471		(5,032,673	
Reinsurance Balances Receivable		960,083		(847,954	
Due from Affiliates		555,814		1,188,510	
Other Assets		(6,037,791)		80,080	
Liability for Policy Reserves		22,955,993		2,303,000	
Liability for Unearned Premiums		18,688,734		17,622,635	
Amounts Held for Others		1,163,554		(2,584	
Other Liabilities		3,516,607		11,663,249	
Net Cash Provided by Operating Activities		86,866,350		83,540,205	
Cash Flows from Investing Activities:					
Maturities and Redemptions of Fixed Maturities Held for Investment		99,381		193,77:	
Maturities and Redemptions of Fixed Maturities Available for Sale		98,502,448		70,941,418	
Maturities and Redemptions of Other Investments		643,928		39,893,677	
Sales of Fixed Maturities Available for Sale		101,660,131		25,596,235	
Sales of Equity Securities		42,432,648		50,521,768	
Sales of Other Investments		3,837,673		830,490	
Purchases of Fixed Maturities Available for Sale		(271,968,471)		(131,609,922	
Purchases of Equity Securities		(45,628,091)		(51,822,985	
Purchases of Other Investments		(49,208,874)		(74,945,027	
Net Change in Collateral Loans		(15,550,039)		(10,160,971	
Net Change in Short-term Investments		(4,658,581)		(26,719,827	
Net Change in Receivable/Payable on Securities		(4,182,692)		, ,	

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Net Cash Used in Investing Activities		(144,020,539)		(117,424,019)
		_		_
Cash Flows From Financing Activities:				
(Decrease) Increase in Commercial Paper		(31,903,588)		24,792,378
Increase (Decrease) in Notes Payable		70,000,000		(103,806)
Increase in Notes Payable to Affiliates		11,536,191		7,634,223
Stockholder Dividends Paid		(17,408,810)		(16,487,023)
Purchases of Treasury Stock		(3,331,785)		(3,575,199)
Proceeds from Exercise of Stock Options		8,970,080		2,153,707
Deposits of Policyholders' Funds		57,144,223		54,579,566
Withdrawal of Policyholders' Funds		(35,706,798)		(35,197,508)
Net Cash Provided by Financing Activities		59,299,513		33,796,338
Net Change in Cash		2,145,324		(87,476)
Cash - Beginning of Period		10,224,827		4,475,672
Cash - End of Period	\$	12,370,151	\$	4,388,196
Supplemental Disclosures of Cash Flow Information:				
Cash Paid During the Period for:				
Interest	\$	3,754,984	\$	6,442,252
Income Taxes	\$	11,778,516	\$	10,681,000
INCOME TAXES	Ф	11,//6,310	Ф	10,081,000

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

ALFA CORPORATION NOTES TO CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS September 30, 2002

1. Significant Accounting Policies

In the opinion of the Company, the accompanying consolidated unaudited financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly its financial position, results of operations and cash flows. The accompanying financial statements have been prepared on the basis of accounting principles generally accepted in the United States of America. A summary of the more significant accounting policies related to the Company s business is set forth in the notes to its audited consolidated financial statements for the fiscal year ended December 31, 2001. The results of operations for the nine-month and three-month periods ended September 30, 2002 are not necessarily indicative of the results to be expected for the full year. For purposes of this report, the Company has defined operating income as income excluding net realized investment gains, net of related tax effects. Certain reclassifications have been made to conform previous classifications to September 30, 2002 classifications and descriptions.

2. Pooling Agreement

Effective August 1, 1987, the Company entered into a property and casualty insurance Pooling Agreement (the Pooling Agreement) with Alfa Mutual Insurance Company (Mutual), and other members of the Mutual Group (See Note 3). On January 1, 2001, Alfa Specialty Insurance Corporation (Specialty), a subsidiary of Mutual, also became a participant in the Pooling Agreement. The Mutual Group is a direct writer primarily of personal lines of property and casualty insurance in Alabama. The Company subsidiaries similarly are direct writers in Georgia and Mississippi. Both the Mutual Group and the Company write preferred risk automobile, homeowner, farmowner and mobile home insurance, fire and allied lines, standard risk automobile and homeowner insurance, and a limited amount of commercial insurance, including church and businessowner insurance. Specialty is a direct writer primarily of nonstandard risk automobile insurance. Under the terms of the Pooling Agreement, the Company cedes to Mutual all of its property and casualty business. Substantially all of the Mutual Group s direct property and casualty business (together with the property and casualty business ceded by the Company) is included in the pool. Mutual currently retrocedes 65% of the pool to the Company and retains 35% within the Mutual Group. Effective January 1, 2001, Specialty s property and casualty business likewise became included in the pool. On October 1, 1996, the Pooling Agreement was amended in conjunction with the restructuring of the Alfa Insurance Group s catastrophe protection program. Effective November 1, 1996, the allocation of catastrophe costs among the members of the pool was changed to better reflect the economics of catastrophe finance. The amendment limited Alfa Corporation s participation in any single catastrophic event or series of storms to its pool share (65%) of a lower catastrophe pool limit unless the loss exceeded an upper catastrophe pool limit. In cases where the upper catastrophe limit is exceeded on a

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(Note 2. Continued)

100% basis, the Company s share in the loss would be based upon its amount of surplus relative to other members of the group. Lower and upper catastrophe pool limits are adjusted periodically due to increases in insured property risks. The limits and participation levels since inception of the program are summarized below:

	Cata Pool	ower strophe Limit lions)	Cat Po	Upper astrophe ol Limit nillions)	Coinsurance Allocation of Catastrophes Exceeding Upper Catastrophe Pool Limit	
November 1, 1996	\$	10.0	5	249.0		13%
July 1, 1999		11.0		284.0		13%
January 1, 2001		11.4		284.0		14%
January 1, 2002		11.6		289.0		16%

The Company s participation in the Pooling Agreement may be changed or terminated without the consent or approval of the Company s shareholders. The Pooling Agreement may be terminated by any party thereto upon 90 days notice.

The following table sets forth the premiums and losses ceded to and assumed from the pool for the nine-month and three-month periods ended September 30, 2002 and 2001:

	Nine Mon Septem	ths Endo	ed	Three Months Ended September 30,				
	2002		2001		2002		2001	
			(in thou	ısands)				
Premiums ceded to pool	\$ 58,479	\$	54,545	\$	20,131	\$	19,932	
Premiums assumed from pool	\$ 319,226	\$	296,510	\$	108,959	\$	100,518	
Losses ceded to pool	\$ 43,926	\$	42,003	\$	15,539	\$	14,221	
Losses assumed from pool	\$ 203,417	\$	184,258	\$	71,784	\$	62,253	

The Company incurred \$1.8 million in storm losses in the third quarter of 2002 resulting in a reduction in the Company s net income of approximately \$0.01 per diluted share, after reinsurance and taxes. Through the first nine months of 2002, storm losses of \$7.0 million have been incurred, negatively impacting earnings by approximately \$0.06 per diluted share. The Company also incurred \$7.4 million in storm losses in the first quarter of 2001 which reduced the Company s net income by approximately \$0.06 per diluted share, after reinsurance and taxes. No catastrophe losses were incurred in the second or third quarters of 2001.

3. Contingent Liabilities

The property and casualty subsidiaries have entered into the reinsurance pooling agreement with Alfa Mutual Insurance Company and its affiliates as discussed in Note 2. Should any member of the affiliated group be unable to meet its obligation on a claim for a policy written by the Company s property and casualty subsidiaries, the obligation to pay the claim would remain with the Company s subsidiaries.

The liability for estimated unpaid property and casualty losses and loss adjustment expenses is based upon an evaluation of reported losses and on estimates of incurred but not reported losses. Adjustments to the liability based upon subsequent developments are included in current operations.

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(Note 3. Continued)

Certain legal proceedings are in process at September 30, 2002. Costs for these and similar legal proceedings, including accruals for outstanding cases, totaled \$3.4 million in the first nine months of 2002, \$930,000 in 2001, and \$3.0 million in 2000. These proceedings involve alleged breaches of contract, torts, including bad faith and fraud claims, and miscellaneous other causes of action. These lawsuits involve claims for mental anguish and punitive damages. Approximately 17 legal proceedings against Alfa Life Insurance Corporation (Life) were in process at September 30, 2002. Of the 17 proceedings, eight were filed in 2002, two were filed in 2001, one was filed in 2000, four were filed in 1999, one was filed in 1997, and one was filed in 1996. In a case tried in January 2001, in Barbour County, Alabama, the jury returned a verdict for the plaintiff against Life for \$500,000 in compensatory damages and \$5,000,000 in punitive damages. After Life filed post-trial motions, the trial court reduced the punitive damage award to \$1,500,000. Life has appealed the award to the Alabama Supreme Court. In a case tried in December 2001, in Bullock County, Alabama, the jury returned a verdict for the plaintiffs against Life for \$300,000 in compensatory damages and \$3,000,000 in punitive damages. After Life filed post-trial motions, the trial court reduced the punitive damage award to \$900,000. Life has appealed the award to the Alabama Supreme Court. Two of the 17 pending legal proceedings against Life have been certified as class actions by the trial court in each case. After the trial court certified the first class action against Life, Life appealed the class certification order to the Alabama Supreme Court. In November 2001, the Alabama Supreme Court reversed the trial court, decertified the class, and remanded the case to the trial court for further proceedings. The trial court has again certified the class and Life has appealed the certification to the Alabama Supreme Court. The trial court order certifying the second class action has also been appealed to the Alabama Supreme Court. In addition, one purported class action lawsuit is pending against both Alfa Builders, Inc. and Alfa Mutual Fire Insurance Company. Additionally, five purported class action lawsuits are pending against the property and casualty mutual companies involving a number of issues and allegations which could affect the Company because of a pooling agreement between the companies. No class has been certified in any of these six purported class action cases. In addition, Alfa Insurance Corporation and Alfa General Insurance Corporation have been served with a purported class action in the State of Georgia, alleging the two corporations improperly refused to evaluate and refused to pay diminution in value respecting automobile first-party physical damage claims. It should be noted that in Alabama, where the Company has substantial business, the likelihood of a judgment in any given suit, including a large mental anguish and/or punitive damage award by a jury, bearing little or no relation to actual damages, continues to exist, creating the potential for unpredictable material adverse financial results.

Based upon information presently available, contingent liabilities arising from any other threatened litigation are not presently considered by management to be material.

The Company periodically invests in partnerships that invest in affordable housing tax credits. At September 30, 2002, the Company had committed to fund a partnership of this type in the amount of approximately \$4.6 million.

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4. Segment Information

The following table sets forth the components of property and casualty insurance earned premiums, net underwriting income, GAAP basis loss, expense and combined ratios, underwriting margin, net investment income and operating income for the nine-month and three-month periods ended September 30, 2002 and 2001:

		Nine M	onths	Ended September 3	30,		Three Months Ended September 30,					
		2002		2001	% Change		2002		2001	% Change		
Earned					(in thous	sands	s)					
premiums												
Personal lines	\$	304,659	\$	282,805	8%	\$	103,963	\$	95,875	8%		
Commercial lines		11,131		10,466	6%		3,832		3,557	8%		
Pools, associations and fees		3,436		3,239	6%		1,164		1,086	7%		
Reinsurance ceded		(1,367)		(1,149)	(19%)		(511)		(385)	(33%)		
Total	\$	317,859	\$	295,361	8%	\$	108,448	\$	100,133	8%		
Net underwriting income	\$	21,614	\$	21,912	(1%)	¢	6,048	\$	7,092	(15%)		
meome	Ψ	21,014	Ψ	21,712	(170)	Ψ	0,040	Ψ	1,092	(1370)		
Loss ratio		64.1%		62.1%			66.2%		62.1%			
LAE ratio		4.2%		4.0%			3.7%		4.1%			
Expense ratio		24.9%		26.5%		_	24.5%		26.7%			
GAAP basis combined												
ratio		93.2%		92.6%			94.4%		92.9%			
Underwriting margin		6.8%		7.4%			5.6%		7.1%			
Net investment	¢	22.200	¢	22 474	(16)	¢	7 177	¢	0.216	(226)		
income	\$	23,299	\$	23,474	(1%)	\$	7,176	\$	9,216	(22%)		
	\$	44,986	\$	45,441	(1%)	\$	13,309	\$	16,226	(18%)		

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Pre-tax operating income						
Operating income, net of tax	\$ 34,248	\$ 33,445	2%	\$ 10,201	\$ 11,828	(14%)

(Note 4. Continued)

The following table sets forth life insurance premiums and policy charges, by type of policy, net investment income, benefits and expenses and life insurance operating income for the nine-month and three-month periods ended September 30, 2002 and 2001:

		Nine 1	Months 1	Ended Septembe	r 30,	Three Months Ended September 30,					
		2002		2001	% Change		2002		2001	% Change	
ъ.					(in thou	sands)					
Premiums and policy charges											
Universal life policy charges	\$	13,142	\$	12,059	9%	\$	4,458	\$	4,121	8%	
Universal life policy charges -	Ψ	13,112	Ψ	12,037	710	Ψ	1,150	Ψ	1,121	070	
COLI		2,578		2,210	17%		581		478	22%	
Interest sensitive life policy		- 0.44							0.500	200	
charges Traditional		7,944		7,591	5%		2,585		2,539	2%	
life insurance premiums		22,493		20,534	10%		7,582		6,802	11%	
Group life											
insurance premiums		712		264	170%		0		65	(100%)	
Total	\$	46,869	\$	42,658	10%	\$	15,206	\$	14,005	9%	
Net investment	Φ.	25.212	Φ.	24.450	200	Ф	12.050	ф	11.564	l er	
income	\$	35,213	\$	34,470	2%	\$	12,058	\$	11,564	4%	
Benefits and											
expenses	\$	56,208	\$	50,194	12%	\$	18,214	\$	17,274	5%	
Pre-tax operating income	\$	19,461	\$	20,913	(7%)	\$	6,929	\$	6,297	10%	
meome	Ψ	17,701	Ψ	20,913	(170)	Ψ	0,929	Ψ	0,291	10 //	
Operating											
income, net of tax	\$	13,730	\$	15,530	(12%)	\$	5,096	\$	5,099	0%	

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5. Acquisition of Commercial Lease Portfolio

During the first quarter of 2000, the Company signed a definitive agreement and completed the transaction to acquire the leasing portfolio and assets of OFC Capital (OFC), an Atlanta-based business unit of First Liberty Bank, that provides financing for commercial equipment leases. The transaction involved a cash purchase price of approximately \$23.1 million, which was primarily for the portfolio of leases. OFC operates as a business unit of Alfa Financial Corporation, a subsidiary of the Company. OFC s operations for the nine-month period ended September 30, 2002 resulted in income of approximately \$368,000 including earnings of approximately \$154,000 in the third quarter.

6. Note Payable and Interest Rate Swap Contract

The Company uses variable-rate debt to partially fund its consumer loan and commercial lease portfolios. In particular, it has issued variable-rate long-term debt and commercial paper. These debt obligations expose the Company to variability in interest payments due to changes in interest rates. If interest rates increase, interest expense increases. Conversely, if interest rates decrease, interest expense also decreases.

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(Note 6. Continued)

As part of its funding efforts, the Company issued a \$70 million long-term obligation with a life of fifteen years in the second quarter of 2002. Management believes it is prudent to limit the variability of a portion of its interest payments. It is the Company s objective to hedge 100 percent of its variable-rate long-term interest payments over the first five years of the life of the debt obligation.

To meet this objective, management entered into an interest rate swap to manage fluctuations in cash flows resulting from interest rate risk. The interest rate swap changes the variable-rate cash flow exposure of the variable-rate long term debt obligation to fixed-rate cash flows by entering into a receive-variable, pay-fixed interest rate swap. Under the interest rate swap, the Company receives variable interest payments and makes fixed interest rate payments, thereby creating fixed-rate long-term debt.

The Company does not enter into derivative instruments for any purpose other than cash flow hedging purposes. That is, the Company does not speculate using derivative instruments in the normal course of business.

The Company assesses interest rate cash flow risk by continually identifying and monitoring changes in interest rate exposures that may adversely impact expected future cash flows and by evaluating hedging opportunities.

The Company maintains risk management control systems to monitor interest rate cash flow risk attributable to both the Company s outstanding or forecasted debt obligations as well as the Company s offsetting hedge position. The risk management control systems involve the use of analytical techniques, including cash flow sensitivity analysis, to estimate the expected impact of changes in interest rates on the Company s future cash flows.

Interest expense for the nine months ended September 30, 2002 includes no gains or losses from the interest rate swap. Changes in fair value of the interest rate swap designated as a hedging instrument of the variability of cash flows associated with floating-rate, long-term debt obligation are reported in accumulated other comprehensive income. The interest rate swap involves a LIBOR for LIBOR exchange and meets the criteria for short-cut accounting. Therefore, the interest rate swap has no ineffectiveness, thereby eliminating the reclassification of this amount to interest expense in subsequent periods.

7. Financial Accounting Developments

The Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities in June 1998. This Statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in investment securities and other contracts, and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The accounting for changes in the fair value of a derivative are included in either earnings or other comprehensive income depending on the intended use of the derivative instrument. This standard, as amended by SFAS No. 137, became effective for the Company January 1, 2001. During, 2001, the Company recorded approximately \$229,000, net of tax, as the effect upon adoption of this standard.

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(Note 7. Continued)

The FASB also issued SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (a replacement of SFAS No. 125) in September 2000. This standard became effective April 1, 2001. At this time, the Company does not anticipate this standard having a significant impact on the Company s financial position or income.

The FASB issued SFAS No. 141, Business Combinations, and SFAS No. 142, Goodwill and Other Intangible Assets, in September 2001. These standards became effective July 1, 2001 and January 1, 2002, respectively. Based on current information available and the fact that the Company has not engaged in material transactions covered by these standards, the Company does not anticipate these standards having a significant impact on the Company s financial position or income.

In June 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. Subsequently, in August 2001, the FASB issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. These standards became effective for fiscal years beginning after June 15, 2002 and December 15, 2001, respectively. At this time, the Company does not anticipate either of these standards having a significant impact on the Company s financial position or income.

The FASB also issued SFAS No. 145, Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections, in April 2002. At this time, the Company does not anticipate this standard having a significant impact on the Company s financial position or income.

In August 2002, The FASB also issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities. The Company does not anticipate this standard having a significant impact on the Company s financial position or income.

In October 2002, the FASB issued SFAS No. 147, Acquisitions of Certain Financial Institutions. The Company does not anticipate this standard having a significant impact on the Company s financial position or income.

8. Stock Split

On April 25, 2002, the Company s Board of Directors approved a two-for-one stock split to be effected as a 100% stock dividend. The new shares were issued on June 17, 2002 to stockholders of record on June 3, 2002. Financial statements presented for 2002 within this filing reflect the impact of the stock split. Financial statements for prior periods reflect the impact of the stock split only in share and per share disclosures.

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INDEPENDENT AUDITORS REVIEW REPORT

To the Stockholders and Board of Directors Alfa Corporation:

We have reviewed the consolidated balance sheet of Alfa Corporation and subsidiaries as of September 30, 2002, and the related consolidated statements of income and comprehensive income for the three-month and nine-month periods ended September 30, 2002 and 2001, and the consolidated statements of cash flows for the nine-month periods ended September 30, 2002 and 2001. These consolidated financial statements are the responsibility of the Company s management.

We conducted our review in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with auditing standards generally accepted in the United States of America, the accompanying consolidated balance sheet of Alfa Corporation and subsidiaries as of December 31, 2001, and the related consolidated statements of income, stockholders—equity, cash flows and comprehensive income for the year then ended (not presented herein); and in our report dated February 8, 2002, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2001, is fairly stated in all material respects, in relation to the consolidated balance sheet from which it has been derived.

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KPMG LLP November 13, 2002 Birmingham, Alabama

MANAGEMENT S DISCUSSION AND ANALYSIS

RESULTS OF OPERATIONS

The following table sets forth consolidated summarized income statement information for the nine-month and three-month periods ended September 30, 2002 and 2001:

	Nine Mo	onths E	Ended September 30	,	Three Months Ended September 30,					
	2002		2001	% Change		2002		2001	% Change	
			(in tho	usands, except sha	re an	d per share data)				
Property and casualty insurance premiums Life insurance premiums and policy charges	\$ 317,859 46,869	\$	295,361 42,658	8%	\$	108,448	\$	100,133 14,005	8%	
Total premiums and										
policy charges	\$ 364,728	\$	338,019	8%	\$	123,654	\$	114,138	8%	
Net investment income	\$ 65,952	\$	62,212	6%	\$	21,956	\$	22,636	(3%)	
Total Revenues	\$ 436,408	\$	405,385	8%	\$	148,993	\$	139,329	7%	
Net income Property and casualty										
insurance Life insurance	\$ 34,277 13,730	\$	33,454 15,530	2% (12%)	\$	10,212 5,096	\$	11,844 5,099	(14%) 0%	
Total insurance						_				
operations Noninsurance operations	48,007 3,237		48,984 2,550	(2%)		15,308 1,265		16,943 1,203	(10%)	
Net realized investment gains	2,387		1,998	19%		1,600		1,249	28%	
Corporate expenses	(2,181)		(2,928) (261)	(26%) (100%)		(723) 0		(799) (2)	(10%) (100%)	

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Cumulative effect of change in accounting principle										
Net income	\$	51,450	\$	50,343	2%	\$	17,450	\$	18,596	(6%)
Net income per share	e									
Basic	\$	0.65	\$	0.64	2%	\$	0.22	\$	0.24	(7%)
			_			_		_		
Diluted	\$	0.65	\$	0.64	2%	\$	0.22	\$	0.24	(7%)
						_		_		
Weighted average shares outstanding		78,697,826		78,315,714			78,875,959		78,306,690	
Basic										
Diluted		79,473,390		78,948,270			79,567,532		79,038,146	
								_		

Total premiums and policy charges increased 8% in the first nine months of 2002 as a result of increased production in both property casualty and life business and continued good persistency. Net investment income

increased 6% in the first nine months of 2002 while invested assets have grown 9.8% in the nine months since December 31, 2001.

Operating income increased by 2% in the property casualty subsidiaries due primarily to a reduction in storm losses during the first nine months of 2002. The nonstorm loss ratio increased during the third quarter and combined with \$1.8 million in storm losses to produce a loss ratio of 66.2% The 12% decrease in operating income in the life subsidiary is largely due to increases made in legal reserves of \$2.2 million. Noninsurance operations were up 27% due to earnings growth from the finance and construction subsidiaries. An improved interest rate spread and gains on assets previously held under leases led to an increase in operating income of approximately \$445,000 in the finance subsidiary. Construction income increased \$186,000 due to higher levels of commercial construction activity.

The Company s net income was slightly impacted by an increase in realized investment gains. Corporate expenses decreased in the first nine months of 2002 due to significantly lower borrowing costs resulting from a decline in interest rates.

PROPERTY AND CASUALTY INSURANCE OPERATIONS

The following table sets forth the components of property and casualty insurance earned premiums, net underwriting income, GAAP basis loss, expense and combined ratios, underwriting margin, net investment income and operating income for the nine-month and three-month periods ended September 30, 2002 and 2001:

		Nine M	onths	Ended September 3	30,	Three Months Ended September 30,					
		2002		2001	% Change		2002		2001	% Change	
		_			(in thous	ands)		_		
Earned premiums											
Personal											
lines Commercia	\$ 1	304,659	\$	282,805	8%	\$	103,963	\$	95,875	8%	
lines	•	11,131		10,466	6%		3,832		3,557	8%	
Pools, associations											
and fees		3,436		3,239	6%		1,164		1,086	7%	
Reinsurance ceded	e 	(1,367)		(1,149)	(19%)		(511)		(385)	(33%)	
Total	\$	317,859	\$	295,361	8%	\$	108,448	\$	100,133	8%	
Net underwriting income	\$	21,614	\$	21,912	(1%)	\$	6,048	\$	7,092	(15%)	
meome	Ψ	21,011	Ψ	21,912	(170)	Ψ	0,010	Ψ	7,072	(1376)	
Loss ratio		64.1%		62.1%			66.2%		62.1%		
LAE ratio		4.2%		4.0%			3.7%		4.1%		
Expense ratio		24.9%		26.5%			24.5%		26.7%		
GAAP basis combined											
ratio		93.8%		92.6%			94.4%		92.9%		
		6.2%		7.4%			5.6%		7.1%		

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Underwriting margin										
Net investment	Φ.	22.200	Φ.	22.454	(161)	Φ.	5.15 <i>(</i>	•	0.016	(22.51)
income	\$	23,299	\$	23,474	(1%)	\$	7,176	\$	9,216	(22%)
Pre-tax										
operating income	\$	44,986	\$	45,441	(1%)	\$	13,309	\$	16,226	(18%)
Operating income, net										
of tax	\$	34,248	\$	33,445	2%	\$	10,201	\$	11,828	(14%)

Earned premiums increased 8% in both the third quarter and for the first nine months of 2002 due to greater automobile and homeowner production and the positive impact of homeowner rate increases which took effect in November 2001. Continued good persistency in the automobile and homeowner lines also contributed to premium increases.

The overall loss ratio increased to 64.1% for the first three quarters of 2002 as the ratio climbed to 66.2% for the third quarter following \$1.8 million in storm losses. Approximately \$7.4 million of storm losses were incurred in the first quarter of 2001. No storm losses were recorded in the second or third quarters of 2001. Loss adjustment expenses in the first nine months of 2002 were 4.2% of earned premiums compared to 4.0% in the same period of 2001 when a reduction in loss adjustment expense reserves was recorded following a review of reserve levels. The increase in business resulting from the mandatory insurance law becoming effective in Alabama in June 2000 has not resulted in the emergence of additional claims cost at the anticipated levels. Consequently, reserves were adjusted in the first quarter of 2001 to a more normal level. Another factor in the relatively stable underwriting margin was a decrease in the expense ratio from 2001 levels despite additional expenses related to the Company s implementation of new financial reporting systems.

Net investment income decreased 1% in the first nine months of 2002 in the property casualty subsidiaries due to declines in partnership income. Invested assets increased 10.1% since September 30, 2001.

LIFE INSURANCE OPERATIONS

The following table sets forth life insurance premiums and policy charges, by type of policy, net investment income, benefits and expenses and life insurance operating income for the nine-month and three-month periods ended September 30, 2002 and 2001:

			Months Ended otember 30,		Three Months Ended September 30,					
		2002	2001	% Change		2002		2001	% Change	
Premiums and policy charges				(in thousa	nds)					
Universal life policy charges	\$	13,142	\$ 12,059	9%	\$	4,458	\$	4,121	8%	
Universal life policy charges - COLI		2,578	2,210	17%		581		478	22%	
Interest sensitive life policy charges		7,944	7,591	5%		2,585		2,539	2%	
Traditiona life insurance premiums	1	22,493	20,534	10%		7,582		6,802	11%	
Group life insurance premiums		712	264	170%		0		65	(100%)	
Total	\$	46,869	\$ 42,658	10%	\$	15,206	\$	14,005	9%	

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Net investment income	\$ 35,213	\$ 34,470	2	2%	\$ 12,058	\$ 11,564	4%
Benefits and expenses	\$ 56,208	\$ 50,194	12	2%	\$ 18,214	\$ 17,274	5%
Pre-tax operating income	\$ 19,461	\$ 20,913	(°	7%)	\$ 6,929	\$ 6,297	10%
Operating income, net of tax	\$ 13,730	\$ 15,530	(12	2%)	\$ 5,096	\$ 5,099	0%

The Company s life insurance premiums and policy charges increased 10% in the first nine months of 2002 due to new business and good persistency. First year collected premiums increased over 12% in the first nine months of 2002 due to continued sales growth of term products introduced over the last two years. Total new annualized premium increased 6.2% in the first three quarters of 2002 and 8.7% in all of 2001.

Life insurance operating income decreased approximately 12% in the first nine months of 2002. This decrease was primarily the result of expenses related to increases in legal reserves of \$2.2 million. The mortality ratio of actual to expected death claims decreased to 89% in the first nine months of 2002 from 106% in the first three quarters of 2001. Despite the decline in earnings, positive cash flows resulted in a 7.5% increase in invested assets while investment income increased approximately 2%.

NONINSURANCE OPERATIONS

Noninsurance operations were up 27% due primarily to improved operating results in the finance and construction subsidiaries. More favorable interest rate spreads and gains on disposal of previously leased assets contributed to an increase in net income of approximately \$445,000 from the finance subsidiary. Operating income from the construction subsidiary increased by approximately \$186,000 in the first three quarters of 2002 due to higher levels of commercial construction activity. Income from the Company s subsidiary covering certain employee benefits increased by over \$52,000 to approximately \$611,000 while earnings from the real estate subsidiary increased slightly to \$13,000 in the first nine months of 2002 despite tighter profit margins.

CORPORATE

Corporate expenses decreased 26%, or approximately \$747,000, due primarily to lower interest expense related to the Company s commercial paper borrowing. Favorable trends in short-term interest rates allowed the Company s interest expense to decline significantly from levels experienced in the first nine months of 2001.

INVESTMENTS

The Company has historically produced positive cash flow from operations which has resulted in increasing amounts of funds available for investment and, consequently, higher investment income. Investment income is also affected by yield rates. Information about cash flows, invested assets and yield rates is presented below for the nine months ended September 30, 2002 and 2001:

	Nine Months September	
	2002	2001
Increase in invested assets since January 1, 2002 and 2001	9.8%	8.3%
Investment yield rate (annualized)	6.6%	7.0%
Increase in net investment income since September 30, 2001 and 2000	6.0%	14.8%

As a result of the overall positive cash flows from operations, invested assets grew 9.8% since January 1, 2002 and 12.6% since September 30, 2001 (based on amortized cost, which excludes the impact of SFAS 115), and net investment income increased 6.0%. The positive cash flow from operations is due primarily to the improved operating results in the Company's property and casualty subsidiaries, which had \$21.6 million in underwriting income in the first three quarters of 2002 which was somewhat offset by the decline in profitability of the

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Company s life subsidiary, which had \$13.7 million in operating income in the same period. The premium from the COLI plan in the life insurance subsidiary is collected in February and provided positive cash flow in the first quarter of both periods. Net increases in cash resulting from increased borrowings were primarily used to support growth in the loan and lease portfolios of the finance subsidiary. In addition to the increased investment income created by positive cash flow from operations, the Company also had improved investment income results from its finance subsidiary of approximately \$445,000 from its consumer loan and commercial lease portfolios. The overall yield rate, calculated using amortized cost, declined slightly to 6.6%. The Company had net realized investment gains of approximately \$3.7 million and \$3.1 million in the first nine months of 2002 and 2001, respectively. These net gains are primarily from sales of equity securities. Such realized gains are the result of market conditions and therefore can fluctuate from period to period.

The composition of the Company s investment portfolio is as follows at September 30, 2002 and December 31, 2001:

_	September 30, 2002	December 31, 2001
Fixed maturities		
Taxable		
Mortgage backed (CMO s)	24.2%	22.9%
Corporate bonds	25.1	27.6
Total taxable	49.3	50.5
Tax exempts	16.1	14.0
Total fixed maturities	65.4	64.5
-		
Equity securities	3.2	5.0
Real estate	0.2	0.2
Policy loans	3.2	3.3
Collateral loans	6.3	5.9
Other long term investments	12.3	11.0
Short term investments	9.4	10.1
	100.0%	100.0%

The majority of the Company s investment portfolio consists of fixed maturities which are diverse as to both industry and geographic concentration. Since year-end, the overall mix of investments has remained relatively stable with changes due to a shift from short term investments to fixed maturities and to market value fluctuations in fixed maturities.

The rating of the Company s portfolio of fixed maturities using the Standard & Poor s rating categories is as follows at September 30, 2002 and December 31, 2001:

	September 30, 2002	December 31, 2001
RATING		
AAA to A-	90.2%	88.8%
BBB+ to BBB-	9.5	10.8
BB+ and Below (Below		
investment grade)	0.3	0.4

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100.0%

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The fixed maturity portfolio was rated by an outside rating service. No securities were rated by Company management. The Company considers bonds with a quality rating of BB+ and below to be below investment grade or high yield bonds (also called junk bonds).

At September 30, 2002, approximately 37.0% of fixed maturities were mortgage-backed securities. Such securities are comprised of Collateralized Mortgage Obligations (CMO s) and pass through securities. Based on reviews of the Company s portfolio of mortgage-backed securities, the impact of prepayment risk on the Company s financial position is not believed to be significant. At September 30, 2002, the Company s total portfolio of fixed maturities had gross unrealized gains of \$77,487,471 and gross unrealized losses of \$1,982,339. Securities are priced by nationally recognized pricing services or by broker/dealer securities firms. No securities were priced by the Company.

During the first nine months of 2002, the Company sold approximately \$101.7 million in fixed maturities available for sale. These sales resulted in gross realized gains of \$4,864,343 and gross realized losses of \$6,402,985. During the same period in 2001, the Company sold approximately \$29.7 million in fixed maturities available for sale. These sales resulted in gross realized gains of \$115,559 and gross realized losses of \$1,635,745.

The Company monitors its level of investments in high yield fixed maturities and equity investments held in issuers of high yield debt securities. Management believes the level of such investments is not significant to the Company s financial condition. At September 30, 2002, the Company had unrealized gains of approximately \$764,000 in such investments. During the first nine months of 2002, the Company recognized a net loss of \$3,435,342 on disposals of high yield debt securities. At September 30, 2001, the Company had unrealized gains of approximately \$8.9 million in such investments.

In the first nine months of 2002, the Company wrote down eight equities totaling \$3,591,203, whose declines in value were deemed to be other than temporary and were recorded as a reduction in realized investment gains. In addition, the Company wrote down two bonds during the same period totaling \$948,209, whose declines in value were also deemed to be other than temporary and were recorded as a reduction in realized investment gains.

The Company s investment in other long term investments consists primarily of consumer loans and commercial leases originated by the finance subsidiary. These loans and leases are collateralized by automobiles, equipment and other property. At September 30, 2002, the delinquency ratio on the loan portfolio was 1.32%, down from 1.78% at December 31, 2001. The delinquency ratio on the lease portfolio at September 30, 2002 was 6.73%, up from 4.37% at December 31, 2001. Credit losses of approximately \$597,000 were incurred in the first nine months of 2002 including an increase of approximately \$135,000 in general reserves attributable to growth of the consumer loan portfolio. Leases charged off in the first three quarters of 2002 were approximately \$352,000. At September 30, 2002, the Company maintained an allowance for loan losses of \$1,050,267 or approximately 1.1% of the outstanding loan balance. In addition, at September 30, 2002, the Company maintained an allowance for lease losses of \$2,428,996 or approximately 2.3% of the outstanding lease balance. Other significant long term investments include assets leased under operating leases, partnership investments and certain other investments.

During the third quarter of 2002, the Company s finance subsidiary, Alfa Financial Corporation, invested \$13.5 million in MidCountry Financial, a financial services holding company with one wholly-owned subsidiary, Heights Finance Corp. Heights Finance Corp. was acquired by MidCountry Financial on August 30, 2002 and is a consumer finance company doing business in five Midwestern states. Alfa Financial s investment gave it a 44 percent ownership in the newly formed entity. As a result of this significant ownership percentage, Alfa Financial

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will account for earnings from MidCountry Financial using the equity method of accounting. Results from operations will be impacted beginning in the fourth quarter of 2002 since earnings will be incorporated into the Company on a one-month lag as allowed by accounting principles generally accepted in the United States of America.

INCOME TAXES

The effective tax rate in the first nine months of 2002 was 27.3% compared to 28.7% for the full year 2001 and 28.0% for the first nine months of 2001. The decrease in the effective tax rate in the first nine months of 2002 is due primarily to credits arising from an amended income tax return. The effective rate has also been impacted by increased tax preference credits on certain investments. Based on information available at September 30, 2002, the Company currently anticipates the effective tax rate for all of 2002 to be approximately 27.4%.

IMPACT OF INFLATION

Inflation increases consumers needs for both life and property and casualty insurance coverage. Inflation increases claims incurred by property and casualty insurers as property repairs, replacements and medical expenses increase. Such cost increases reduce profit margins to the extent that rate increases are not maintained on an adequate and timely basis. Since inflation has remained relatively low in recent years, financial results have not been significantly impacted by inflation.

LIQUIDITY AND CAPITAL RESOURCES

The Company receives funds from its subsidiaries consisting of dividends, payments for funding federal income taxes, and reimbursement of expenses incurred at the corporate level for the subsidiaries. These funds are used for paying dividends to stockholders, corporate interest and expenses, federal income taxes, and for funding additional investments in its subsidiaries—operations.

The Company s subsidiaries require cash in order to fund policy acquisition costs, claims, other policy benefits, interest expense, general operating expenses, and dividends to the Company. The major sources of the Company s liquidity are operations and cash provided by maturing or liquidated investments. A significant portion of the Company s investment portfolio consists of readily marketable securities which can be sold for cash. Based on a review of the Company s matching of asset and liability maturities and on the interest sensitivity of the majority of policies in force, management believes the ultimate exposure to loss from interest rate fluctuations is not significant.

Net cash provided by operating activities for the first nine months of 2002 and 2001 approximated \$86.9 million and \$83.5 million, respectively. Such net positive cash flows provide the foundation of the Company's assets/liability management program and are the primary drivers of the Company's liquidity. As previously discussed, the Company also maintains a diversified portfolio of fixed maturity and equity securities which provide a secondary source of liquidity should net cash flows from operating activities prove inadequate to fund current operating needs. Management believes that such an eventuality is unlikely given the Company's product mix (primarily short-duration personal lines property and casualty products), its ability to adjust premium rates (subject to regulatory oversight) to reflect emerging loss and expense trends and its catastrophe reinsurance program, amongst other factors.

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The Company has a limited number of contractual obligations in the form of operating leases and debt obligations. These leases have primarily been originated by its commercial leasing and real estate sales subsidiaries. Operating leases supporting the corporate headquarters are the responsibility of Alfa Mutual Insurance Company (Mutual), an affiliate. In turn, the Company reimburses Mutual monthly for a portion of these and other expenses based on a management and operating agreement. There are currently no plans to change the structure of this agreement. Included in the Company s contractual obligations is the repayment of a \$70 million debt obligation. This note, issued in the second quarter of 2002, is payable at the end of fifteen years. While the note carries a variable interest rate, the Company has entered into an interest rate swap contract to hedge interest rate variability and fix the interest rate for the first five years of the debt obligation at 4.945%.

The Company s contractual obligations at September 30, 2002 are summarized below:

		Pay	yments l	Due by Period		
	 Total	 Less than 1 year		1 - 3 years	4 - 5 years	 After 5 years
Operating Leases	\$ 70,177	\$ 31,825	\$	38,352	\$	\$
Capital Lease Obligation						
Unconditional Purchase Obligations						
Long-Term Obligations	70,000,000					70,000,000
Other Long-Term Obligations						
Total Contractual Obligations	\$ 70,070,177	\$ 31,825	\$	38,352	\$	\$ 70,000,000

The Company maintains a variety of funding agreements in the form of lines of credit with affiliated entities. The chart below depicts, at September 30, 2002, the cash outlay by the Company representing the potential full repayment of lines of credit it has outstanding with others. Also included with the amounts shown as lines of credit are the potential amounts the Company would have to supply to other affiliated entities if they made full use of their existing lines of credit during 2002 with the Company s finance subsidiary, Alfa Financial Corporation. Other commercial commitments of the Company shown below include commercial paper outstanding, scheduled fundings of partnerships, and loans sold to members of the Alfa Mutual Group through which recourse against the finance subsidiary is available if repayment by the customer fails to occur.

Amount of Commitment Expiration Per Period

		Total Amounts Committed		Less than 1 year		1 - 3 years	4 - 5 years	After 5 years
Lines of	ф	20.015.000	Φ.	21.015.000	Ф	0.000.000	Φ.	d
Credit	\$	29,015,000	\$	21,015,000	\$	8,000,000	\$	\$
Standby								
Letters of								
Credit								
Guarantees								
Standby								
Repurchase								
Obligations								
Other								
Commercial								
Commitments		177,095,610		174,618,528		2,447,082		

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Commercial Commitments \$ 206,110,610 \$ 195,633,528 \$ 10,477,082 \$ \$	Total				
Commitments \$ 206,110,610 \$ 195,633,528 \$ 10,477,082 \$ \$	Commercial				
	Commitments	\$ 206,110,610	\$ 195,633,528	\$ 10,477,082	\$ \$

Assessment of credit risk is a critical factor in the Company s consumer loan and commercial leasing subsidiary. All credit decisions are made by personnel trained to limit loss exposure from unfavorable risks. In attempting to manage risk, the Company regularly reviews delinquent accounts and adjusts reserves for potential

loan losses and potential lease losses. To the extent these reserves are inadequate at the time an account is written off, income would be negatively impacted. In addition, the Company monitors interest rates relative to the portfolio duration.

Rising interest rates on commercial paper issued, a major source of funding portfolio growth, could reduce the interest rate spread if the Company failed to adequately adjust interest rates charged to customers.

Total borrowings increased approximately \$49.6 million in the first nine months of 2002 to \$252.1 million. The majority of the short-term debt is commercial paper issued by the Company. At September 30, 2002, the Company had approximately \$133.5 million in commercial paper at rates ranging from 1.77% to 2.03% with maturities ranging from October 1, 2002 to November 26, 2002. The Company intends to continue to use the commercial paper program as a major source to fund the consumer loan portfolio, commercial lease portfolio and other corporate short-term needs. Backup lines of credit are in place up to \$220 million. The backup lines agreements contain usual and customary covenants requiring the Company to meet certain operating levels. The Company has maintained full compliance with all such covenants. The Company has A-1+ and P-1 commercial paper ratings from Standard & Poor s and Moody s Investors Service, respectively. The commercial paper is guaranteed by two affiliates, Alfa Mutual Insurance Company and Alfa Mutual Fire Insurance Company. In addition, the Company had \$48.6 million in short-term debt outstanding to affiliates at September 30, 2002.

Included in total borrowings is a variable rate note issued by the Company during the second quarter of 2002 in the amount of \$70 million. This note is payable in its entirety at the end of fifteen years with interest payments due monthly. The Company is using the proceeds of this note to partially fund the consumer loan and commercial lease portfolios of its finance subsidiary. The Company has entered into an interest rate swap contract in order to achieve its objective of economically hedging 100 percent of its variable-rate long-term interest payments over the first five years of the note. Under the interest rate swap, the Company receives variable interest payments and makes fixed interest rate payments, thereby fixing the rate on such debt at 4.945%.

On October 25, 1993, the Company established a Stock Option Plan, pursuant to which a maximum aggregate of 4,000,000 shares of common stock were reserved for grant to key personnel. On April 26, 2001, the plan was amended to increase the maximum aggregate number of shares available for grant to 6,400,000 shares. Under the plan, options ratably become exercisable annually over three years and may not be exercised after ten years from the date of the award. During March 2002, the Company issued 423,000 options.

The Company s Board of Directors has approved stock repurchase programs authorizing the repurchase of up to 12,000,000 shares of its outstanding common stock in the open market or in negotiated transactions in such quantities and at such times and prices as management may decide. During the first nine months of 2002, the Company repurchased 271,962 shares at a cost of \$3,331,785. At September 30, 2002, the total repurchased was 6,718,062 shares at a cost of \$44,984,511. The Company has reissued 1,465,230 treasury shares as a result of option exercises. In May 2002, the Company began selling treasury shares to its mutual affiliates as a means of meeting provisions under their participation in the Company s dividend reinvestment plan. At September 30, 2002, the total sold was 476,481 shares at a cost of \$896,379.

Due to the sensitivity of the products offered by the life subsidiary to interest rates fluctuations, the Company must assess the risk of surrenders exceeding expectations factored into its pricing program. Internal actuaries are used to determine the need for modifying the Company s policies on surrender charges and assessing the Company s competitiveness with regard to rates offered.

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Cash surrenders paid to policyholders on a statutory basis totaled \$11.0 million in the first nine months of 2002 and \$11.7 million for the first nine months of 2001. This level of surrenders is within the Company's pricing expectations. Historical persistency rates indicate a normal pattern of surrender activity. The structure of the surrender charges is such that persistency is encouraged. The majority of the policies in force have surrender charges which grade downward over a 12 to 15 year period. In addition, the majority of the in-force business is interest sensitive type policies which generally have lower rates of surrender. At September 30, 2002, the total amount of cash that would be required to fund all amounts subject to surrender was approximately \$485.8 million.

The Company s business is concentrated geographically in Alabama, Georgia and Mississippi. Accordingly, unusually severe storms or other disasters in these contiguous states might have a more significant effect on the Company than on a more geographically diversified insurance company. Unusually severe storms, other natural disasters and other events could have an adverse impact on the Company s financial condition and operating results. However, the Company s current catastrophe protection program, which began November 1, 1996, reduced the earnings volatility caused by such catastrophe exposures.

The Company s management uses estimates in determining loss reserves for inclusion in its financial statements. Periodic reviews are conducted with the assistance of both internal and external actuaries to determine a range of reasonable loss reserves. In addition, the Company s current catastrophe protection program, which began November 1, 1996, was established to address the economics of catastrophe finance. This plan limits the Company s exposure to catastrophes which might otherwise deplete the Company s surplus through the combination of shared catastrophe exposure within the Alfa Group and the purchase of reinsurance coverage from external reinsurers.

Reinsurance contracts do not relieve the Company from its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Company; therefore, allowances are established if amounts are determined to be uncollectible. The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurance to minimize exposure to significant losses from reinsurer insolvencies. At September 30, 2002, the Company does not believe there to be a significant concentration of credit risk related to its reinsurance program.

Lawsuits brought by policyholders or third-party claimants can create volatility in the Company s earnings. The Company maintains in-house legal staff and, as needed, secures the services of external legal firms to present and protect its position. Certain legal proceedings are in process at September 30, 2002. These proceedings involve alleged breaches of contract, torts, including bad faith and fraud claims, and miscellaneous other causes of action. These lawsuits involve claims for mental anguish and punitive damages. Costs for these and similar proceedings, including accruals for outstanding cases, are included in the financial statements of the Company. Management periodically reviews reserves established to cover potential costs of litigation including legal fees and potential damage assessments and adjusts them based on their best estimates. It should be noted that in Alabama, where the Company has substantial business, the likelihood of a judgment in any given suit, including a large mental anguish and/or punitive damage award by a jury, bearing little or no relation to actual damages, continues to exist, creating the potential for unpredictable material adverse financial results.

Increased public interest in the availability and affordability of insurance has prompted legislative, regulatory and judicial activity in several states. This includes efforts to contain insurance prices, restrict underwriting practices and risk classifications, mandate rate reductions and refunds, eliminate or reduce exemptions from antitrust laws and generally expand regulation. Because of Alabama s low automobile rates as compared to rates in

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most other states, the Company does not expect the type of punitive legislation and initiatives found in some states to be a factor in its primary market in the immediate future. In 1999, the Alabama legislature passed a tort reform package that should help to curb some of the excessive litigation experienced in recent years. In addition, a mandatory insurance bill was passed to require motorists to obtain insurance coverage beginning in June 2000. While this requirement will affect both the revenues and losses incurred by the Company in the future, the full extent or impact is not possible to predict and the Company believes any impact on future results will not be significant.

CRITICAL ACCOUNTING POLICIES

The Company s Summary of Significant Accounting Policies is presented in the notes to its audited consolidated financial statements for the fiscal year ended December 31, 2001. As the Company operates in the property and casualty and life insurance industries, its accounting policies are well defined with industry-specific accounting literature governing the recognition of insurance-related revenues and expenses. The exercise of management judgment is, however, a critical aspect governing the application of such accounting guidance. Management believes that the significant assumptions used in the determination of its insurance assets and liabilities are supported by actuarial studies conducted in accordance with generally accepted actuarial standards and that the resulting insurance assets and liabilities fall within a reasonable range of actuarial estimates given current trends and the nature of the Company s coverages. Significant assumptions used in the determination of actuarially determined assets and liabilities are also contained within the notes to its audited consolidated financial statements for the fiscal year ended December 31, 2001.

FINANCIAL ACCOUNTING DEVELOPMENTS

The Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities in June 1998. This Statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in investment securities and other contracts, and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The accounting for changes in the fair value of a derivative will be included in either earnings or other comprehensive income depending on the intended use of the derivative instrument. This standard, as amended by SFAS No. 137, became effective for the Company January 1, 2001. At this time, the Company does not anticipate this standard having a significant impact on the Company s financial position or income as it does not use derivative instruments in the normal course of business. On January 1, 2001, the Company recorded approximately \$229,000, net of tax, as the effect upon adoption of this standard.

The FASB also issued SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (a replacement of SFAS No. 125) in September 2000. This standard became effective April 1, 2001. At this time, the Company does not anticipate this standard having a significant impact on the Company s financial position or income.

The FASB issued SFAS No. 141, Business Combinations, and SFAS No. 142, Goodwill and Other Intangible Assets, in September 2001. These standards became effective July 1, 2001 and January 1, 2002, respectively. Based on current information available and the fact that the Company has not engaged in material transactions covered by these standards, the Company does not anticipate these standards having a significant

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impact on the Company s financial position or income.

In June 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. Subsequently, in August 2001, the FASB issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. These standards became effective for fiscal years beginning after June 15, 2002 and December 15, 200, respectively. At this time, the Company does not anticipate either of these standards having a significant impact on the Company s financial position or income.

The FASB also issued SFAS No. 145, Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections, in April 2002. At this time, the Company does not anticipate this standard having a significant impact on the Company s financial position or income.

In August 2002, The FASB also issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities. The Company does not anticipate this standard having a significant impact on the Company s financial position or income.

In October 2002, the FASB issued SFAS No. 147, Acquisitions of Certain Financial Institutions. The Company does not anticipate this standard having a significant impact on the Company s financial position or income.

INFORMATION ABOUT FORWARD-LOOKING STATEMENTS

Any statement contained in this report which is not a historical fact, or which might otherwise be considered an opinion or projection concerning the Company or its business, whether expressed or implied, is meant as and should be considered a forward-looking statement as that term is defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements are based on assumptions and opinions concerning a variety of known and unknown risks, including but not necessarily limited to changes in market conditions, natural disasters and other catastrophic events, increased competition, changes in availability and cost of reinsurance, changes in governmental regulations, technological changes, political and legal contingencies and general economic conditions, as well as other risks and uncertainties more completely described in the Company s filings with the Securities and Exchange Commission. If any of these assumptions or opinions prove incorrect, any forward-looking statements made on the basis of such assumptions or opinions may also prove materially incorrect in one or more respects and may cause actual future results to differ materially from those contemplated, projected, estimated or budgeted in such forward-looking statements.

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Item 3.

MARKET RISK DISCLOSURES

The Company s objectives in managing its investment portfolio are to maximize investment income and investment returns while minimizing overall credit risk. Investment strategies are developed based on many factors including underwriting results, overall tax position, regulatory requirements, and fluctuations in interest rates. Investment decisions are made by management and approved by the Board of Directors. Market risk represents the potential for loss due to adverse changes in the fair value of securities. The market risk related to the Company s fixed maturity portfolio are primarily interest rate risk and prepayment risk. The market risk related to the Company s equity portfolio is equity price risk. For further information, reference is made to Management s Discussion and Analysis of Results of Operations in Alfa Corporation s Annual Report on Form 10-K for the year ended December 31, 2001.

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<u>Item 4.</u>

CONTROLS AND PROCEDURES

The Company has evaluated the effectiveness of its disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. The evaluation was performed under the supervision and with the participation of the Company s Disclosure Committee and Management, including the Chief Executive Officer and the Chief Financial Officer, within 90 days prior to the date of the filing of this quarterly report. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the disclosure controls and procedures are effective in ensuring that all material information required to be filed in this quarterly report has been made known to them in a timely fashion.

Subsequent to the date of their evaluation, there were no significant changes in internal controls or other factors that could significantly affect internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

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PART II. OTHER INFORMATION

Item 1.

LEGAL PROCEEDINGS

Certain legal proceedings are in process at September 30, 2002. Costs for these and similar legal proceedings, including accruals for outstanding cases, totaled \$3.4 million in the first nine months of 2002, \$930,000 in 2001, and \$3.0 million in 2000. These proceedings involve alleged breaches of contract, torts, including bad faith and fraud claims, and miscellaneous other causes of action. These lawsuits involve claims for mental anguish and punitive damages. Approximately 17 legal proceedings against Alfa Life Insurance Corporation (Life) were in process at September 30, 2002. Of the 17 proceedings, eight were filed in 2002, two were filed in 2001, one was filed in 2000, four were filed in 1999, one was filed in 1997, and one was filed in 1996. In a case tried in January 2001, in Barbour County, Alabama, the jury returned a verdict for the plaintiff against Life for \$500,000 in compensatory damages and \$5,000,000 in punitive damages. After Life filed post-trial motions, the trial court reduced the punitive damage award to \$1,500,000. Life has appealed the award to the Alabama Supreme Court. In a case tried in December 2001, in Bullock County, Alabama, the jury returned a verdict for the plaintiffs against Life for \$300,000 in compensatory damages and \$3,000,000 in punitive damages. After Life filed post-trial motions, the trial court reduced the punitive damage award to \$900,000. Life has appealed the award to the Alabama Supreme Court. Two of the 17 pending legal proceedings against Life have been certified as class actions by the trial court in each case. After the trial court certified the first class action against Life, Life appealed the class certification order to the Alabama Supreme Court. In November 2001, the Alabama Supreme Court reversed the trial court, decertified the class, and remanded the case to the trial court for further proceedings. The trial court has again certified the class and Life has appealed the certification to the Alabama Supreme Court. The trial court order certifying the second class action has also been appealed to the Alabama Supreme Court. In addition, one purported class action lawsuit is pending against both Alfa Builders, Inc. and Alfa Mutual Fire Insurance Company. Additionally, five purported class action lawsuits are pending against the property and casualty mutual companies involving a number of issues and allegations which could affect the Company because of a pooling agreement between the companies. No class has been certified in any of these six purported class action cases. In addition, Alfa Insurance Corporation and Alfa General Insurance Corporation have been served with a purported class action in the State of Georgia, alleging the two corporations improperly refused to evaluate and refused to pay diminution in value respecting automobile first-party physical damage claims. It should be noted that in Alabama, where the Company has substantial business, the likelihood of a judgment in any given suit, including a large mental anguish and/or punitive damage award by a jury, bearing little or no relation to actual damages, continues to exist, creating the potential for unpredictable material adverse financial results.

Based upon information presently available, contingent liabilities arising from any other threatened litigation are not presently considered by management to be material.

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Item 6.

EXHIBITS AND REPORTS ON FORM 8-K

- (a) Exhibits:
 - 11 Statement of Computation of Per Share Earnings
 - 15 Letter Regarding Unaudited Interim Financial Information
 - 99 Miscellaneous
- 99.1 Certification of Chief Executive Officer
- 99.2 Certification of Chief Financial Officer
- 99.3 Certification of Chief Executive Officer
- 99.4 Certification of Chief Financial Officer
- (b) Reports on Form 8-K:

There were no reports on Form 8-K filed during the quarter ended September 30, 2002.

Items other than those listed above are omitted because they are not required or are not applicable.

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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.

ALFA CORPORATION

Date 11/13/02 By: /S/ JERRY A. NEWBY

Jerry A. Newby President

(Chief Executive Officer)

Date 11/13/02 By: /S/ STEPHEN G. RUTLEDGE

Stephen G. Rutledge Senior Vice President

(Chief Financial Officer and Chief Investment Officer)

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