

INFINITY PROPERTY & CASUALTY CORP  
Form S-1/A  
December 01, 2003  
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As filed with the Securities and Exchange Commission on December 1, 2003

Registration No. 333-110564

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# SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

## Amendment No. 1

to

## Form S-1

## REGISTRATION STATEMENT

*UNDER*

*THE SECURITIES ACT OF 1933*

## Infinity Property and Casualty Corporation

*(Exact Name of Registrant as Specified in Its Charter)*

**Ohio**  
*(State or other jurisdiction of  
incorporation or organization)*

**6331**  
*(Primary Standard Industrial  
Classification Code Number)*

**03-0483872**  
*(IRS Employer Identification  
Number)*

**2204 Lakeshore Drive**  
**Birmingham, Alabama 35209**

**(205) 870-4000**

*(Address, Including Zip Code, and Telephone Number, Including Area Code, of Registrant's Principal Executive Offices)*

**Samuel J. Simon, Esq.**

**Senior Vice President, General Counsel and Secretary**

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**Infinity Property and Casualty Corporation**

**2204 Lakeshore Drive**

**Birmingham, Alabama 35209**

**Telephone: (205) 870-4000**

**Facsimile: (205) 803-8585**

*(Name, Address, Including Zip Code, Telephone and Facsimile Numbers, Including Area Code, of Agent For Service)*

*With copies to:*

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**Approximate date of commencement of proposed sale to the public:** As soon as practicable after the effective date of this Registration Statement.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box.   "

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.   "

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.   "

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.   "

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.   "

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**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, or until the Registration Statement shall become effective on such date as the**

Commission, acting pursuant to said Section 8(a), may determine.

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The information in this prospectus is not complete and may be changed. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

**SUBJECT TO COMPLETION, DATED DECEMBER 1, 2003**

PROSPECTUS

**7,850,465 Common Shares**

**Infinity Property and Casualty Corporation**

**Common Stock**

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A wholly-owned subsidiary of American Financial Group, Inc. is selling all of the shares of common stock in this offering other than the shares subject to the over-allotment option described below. Infinity will not receive any of the proceeds from the sale of the shares by the selling shareholder. Our common stock is quoted on the Nasdaq National Market under the symbol IPCC. On November 25, 2003, the last quoted price of the shares of common stock as reported on the Nasdaq National Market was \$34.00 per share.

**Investing in our common stock involves risks that are described in the Risk Factors section beginning on page 10 of this prospectus.**

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	<u>Per Share</u>	<u>Total</u>
Public offering price	\$	\$
Underwriting discount	\$	\$
Proceeds, before expenses, to selling shareholder	\$	\$

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The underwriters may also purchase up to an additional 1,177,569 shares of common stock from us at the public offering price, less the underwriting discount, within 30 days from the date of this prospectus to cover over-allotments. If the underwriters exercise that option in full, the total public offering price, underwriting discount and proceeds to us would be \$ , \$ , and \$ , respectively.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The shares of common stock will be ready for delivery on or about , 2003.

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**Credit Suisse First Boston**

**Merrill Lynch & Co.**

**UBS Investment Bank**

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**Banc of America Securities LLC**

**Bear, Stearns & Co. Inc.**

**Morgan Keegan & Company, Inc.**

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The date of this prospectus is , 2003.

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You should rely only on the information contained in this document or to which we have referred you. We have not authorized anyone to provide you with information that is different. This document may only be used where it is legal to sell these securities. The information in this document may only be accurate on the date of this document.

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**PROSPECTUS SUMMARY**

*This summary highlights information about Infinity Property and Casualty Corporation and the offering. Because this is a summary, it may not contain all the information you should consider before investing in our common stock. You should carefully read this entire prospectus.*

*References in this prospectus to Infinity, we, us and our, unless the context requires otherwise, refer to Infinity Property and Casualty Corporation and its combined operations, including the Assumed Agency Business. Unless otherwise noted in this prospectus, we assume that the underwriters will not exercise their over-allotment option. Unless otherwise indicated, all financial information in this prospectus is presented on a pro forma basis for periods prior to December 31, 2002 (see Our Formation and Separation from AFG and Unaudited Pro Forma Financial Information). In this prospectus, all share and per share data assumes that the stock split we declared in January 2003 had already occurred. Unless otherwise indicated, insurance industry data and our market share or ranking in the industry were derived from data compiled by A.M. Best Company Inc.*

**Infinity**

**What We Do**

We are a national provider of personal automobile insurance with an emphasis on nonstandard auto insurance. Nonstandard auto insurance provides coverage to drivers who, due to their driving record, age or vehicle type, represent higher than normal risks and pay higher rates for comparable coverage. We also write standard and preferred personal auto insurance, nonstandard commercial auto insurance and complementary personal lines insurance products.

Our products are offered primarily through a network of approximately 14,000 independent agencies and strategic partnerships. Based on data published by A.M. Best, we believe we are the second largest provider of nonstandard auto coverage through independent agents in the United States, behind only The Progressive Corporation. While licensed to write insurance in every state, we focus on 15 states which we believe provide the greatest opportunity for profitable growth.

In 2002, we generated, on a pro forma basis, \$988.9 million in gross premiums written, \$687.3 million in net premiums written and had net earnings of \$36.3 million. For the nine months ended September 30, 2003, we generated \$734.8 million in gross premiums written, \$622.8 million in net premiums written and had net earnings of \$38.8 million. For the year ended December 31, 2002 and the nine months ended September 30, 2003, approximately 95% of our business was personal auto and the remaining 5% was homeowners, umbrella liability, boat owners and nonstandard commercial auto coverages. While there is no precise, industry-recognized definition of nonstandard auto insurance, we estimate that, for the year ended December 31, 2002 and the nine months ended September 30, 2003, approximately four-fifths of our personal auto business was nonstandard coverage. At September 30, 2003, we had total assets of \$2.0 billion, total liabilities of \$1.5 billion and shareholders' equity of \$442 million.

The following table compares our statutory combined ratio in past years with those of the personal lines insurance industry as a whole. See Business Our Strengths for a description of how the combined ratio is calculated, the use of the combined ratio as a measure of underwriting profitability and the source of the industry combined ratios presented.

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	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1998-2002</u>	<u>1993-2002</u>
Infinity	95.9%(1)	92.7%	104.6%	108.7%	98.7%	97.0%	100.9%	101.4%
Industry	99.7%(2)	105.3%	110.9%	109.9%	104.5%	102.7%	106.6%	105.2%
Percentage Points Better Than Industry	3.8%	12.6%	6.3%	1.2%	5.8%	5.7%	5.7%	3.8%

(1) Combined ratio through September 30, 2003.

(2) Combined ratio through June 30, 2003, from A.M. Best. Industry data through September 30, 2003 are not yet available.



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### **Our Strengths**

We believe that we are well positioned to compete in today's market through various strengths that should enable us to build upon our history of favorable underwriting results. These strengths include:

**Our product focus** on nonstandard auto insurance with a selected presence in the standard and preferred segments.

**Our expertise in risk segmentation**, including our detailed evaluation of risks and use of sophisticated proprietary data bases and risk models.

**Our claims handling capability**, including our emphasis on employee claims personnel and our 24-hour, seven days per week toll-free claims service.

**Our agency relationships** with approximately 14,000 independent agents.

**Our low cost structure**, resulting in our ratio of underwriting expenses to premiums being better than the personal lines industry average by 4.4 points for the calendar years 1998 through 2002.

**Our experienced management team** with extensive experience in the personal automobile insurance business and with us.

**Our financial strength**, including our conservative investment portfolio and the A (Excellent) ratings of our insurance subsidiaries from A.M. Best.

### **Our Strategy**

Our goal is to maximize shareholder value by focusing on underwriting profitability and long-term return on equity. We pursue this goal through a strategy of:

**Product focus** on personal automobile insurance.

**Geographic focus** on the states that we believe offer us the greatest opportunity for profitable growth.

**Controlled operating expenses** to achieve a competitive cost structure.

**Disciplined pricing** so as to achieve adequate and accurate rates.

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**Field claim handling** emphasizing prompt response to claims, continued good service to our customers and effective control of the claims process.

**Distribution focus** on independent agent channel.

### Certain Risks We Face

Our ability to capitalize on our strengths and implement our strategy entails risks. For example, we have a limited operating history as an independent public company. Further, the process of consolidating the operations of our insurance subsidiaries poses managerial, strategic and technological challenges. Adverse developments in the market for personal automobile insurance, or the personal automobile insurance industry in general, could cause our results of operations to suffer. Our reliance on the independent agency market makes us vulnerable to a reduction in the amount of business written by independent agents, and if we are not able to attract and retain independent agents, our revenues could be negatively affected. For further discussion of these and other risks we face, see Risk Factors .

Our principal executive offices are located at 2204 Lakeshore Drive, Birmingham, Alabama, 35209. Our telephone number is (205) 870-4000.

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**The Offering**

Common stock offered by selling shareholder	7,850,465 shares, representing all of the remaining shares owned by American Financial Group, Inc. ( AFG ).
Common stock to be outstanding after this offering (1)	20,483,958 shares
Use of proceeds	We will receive no proceeds from the sale of shares by the selling shareholder. Proceeds from the sale of shares, if any, from the exercise of the underwriters' over-allotment option will be used to pay down debt under our term loan and for general corporate purposes.
<u>Nasdaq National Market Symbol</u>	IPCC

- (1) The number of shares of common stock excludes 2.5 million shares reserved for issuance under various employee and director compensation plans.

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**Our Formation and Separation from AFG**

Infinity was formed in September 2002 as an indirect wholly-owned subsidiary of American Financial Group, Inc. to acquire and conduct, as a separate public company, AFG's personal lines insurance business written through independent agents. Prior to the initial public offering of common stock, AFG transferred to Infinity all of the issued and outstanding capital stock of the following personal auto insurance subsidiaries, including their respective subsidiaries, involved primarily in the issuance of nonstandard auto policies: Atlanta Casualty Company, Leader Insurance Company, Infinity Insurance Company and Windsor Insurance Company. We refer to these subsidiaries as the NSA Group. In this prospectus, we refer to our operations and financial results before January 1, 2003 as the operations and financial results of either Infinity or the NSA Group. In exchange for the NSA Group, AFG received all of the issued and outstanding shares of Infinity common stock and a note payable in the amount of \$55 million.

In addition, as of January 1, 2003, AFG's principal property and casualty insurance subsidiary, Great American Insurance Company (Great American), transferred to us its personal insurance business written through independent agents. This is primarily auto insurance for standard and preferred drivers, but also includes other personal lines. Because this business is not a separate legal entity, the transfer was effected through a reinsurance agreement under which we assumed the inforce business, service the policyholders and handle the claims. Great American, in turn, transferred to us assets (primarily investment securities) with a market value of \$125.3 million, which was approximately equal to the net liabilities related to the inforce business, less

\$5 million. We refer to this business as the Assumed Agency Business.

We completed the initial public offering of our common stock in February 2003. In the initial public offering, AFG sold 12.5 million shares of our common stock held by it. We received no proceeds from the initial public offering. AFG is selling its remaining shares in this offering.

The financial assets transferred to us from Great American in connection with our acquisition of Great American's personal insurance business written through independent agents include primarily investment securities which are described in more detail in Note 1 to the Unaudited Pro Forma Financial Information. Other financial assets (primarily agents' balances and deferred policy acquisition costs) and financial liabilities (primarily loss reserves and unearned premiums) transferred are described more fully in the Statement of Assets (excluding investments) and Liabilities to be Transferred for this business which begin on page F-18 of this Prospectus. In addition to the transfer of financial assets and liabilities, we received the operational processes, including policy renewal rights, and employees necessary to conduct the normal operations of this business following the date of transfer. Accordingly, the transfer represented the acquisition of a business under generally accepted accounting principles. Since the transfer was made while Infinity was an AFG subsidiary, the assets and liabilities transferred were recorded at AFG's historical cost.

The companies and business comprising Infinity represented approximately 31% of AFG's entire property and casualty group and approximately 83% of AFG's Personal segment based on earned premiums in 2002. AFG's property and casualty group was engaged primarily in specialty and private passenger automobile insurance businesses. The Specialty group includes a highly diversified group of specialty business units. Some of the more significant areas are inland and ocean marine, California workers' compensation, agricultural-related coverages, executive and professional liability, fidelity and surety bonds, collateral protection, and umbrella and excess coverages. The Personal group wrote nonstandard and preferred/standard private passenger auto and other personal insurance coverage. AFG's annuity and life business markets primarily retirement products as well as life and supplemental health insurance. AFG's businesses operate throughout the United States. In 2002, 2001 and 2000, AFG derived less than 2% of its revenues from the sale of life and supplemental health products in Puerto Rico and less than 1% of its revenues from the sale of property and casualty insurance in Mexico, Canada, Puerto Rico, Europe and Asia.

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The following table (in millions) shows AFG's revenues by significant business segment for the three years preceding our initial public offering of common stock.

	Year ended December 31,		
	2002	2001	2000
<b>Revenues(a)</b>			
Property and casualty insurance:			
Premiums earned:			
Specialty	\$ 1,497	\$ 1,409	\$ 1,223
Personal	905	1,183	1,270
Other lines(b)	1	2	1
	<u>2,403</u>	<u>2,594</u>	<u>2,494</u>
Investment and other income	411	458	451
	<u>2,814</u>	<u>3,052</u>	<u>2,945</u>
Annuities and life(c)	897	856	824
Other	39	16	48
	<u>\$ 3,750</u>	<u>\$ 3,924</u>	<u>\$ 3,817</u>

(a) Revenues include sales of products and services as well as other income earned by the respective segments.

(b) Represents lines in run-off ; AFG has ceased underwriting new business in these operations.

(c) Represents primarily investment income.

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We derived the summary data as of and for each of the three years ended December 31, 2002, from financial statements audited by Ernst & Young LLP. We derived the summary data as of and for the nine months ended September 30, 2003 and 2002, from unaudited financial statements which include all adjustments, consisting of normal recurring accruals, that management considers necessary for a fair presentation of the financial position and results of operations for those periods. Results for the interim periods are not necessarily indicative of results to be expected for the entire year. The Infinity financial data set forth below for all periods prior to December 31, 2002 is the financial data of the NSA Group. The Infinity financial data for the nine months ended September 30, 2003 include the results of the Assumed Agency Business. You should read this summary in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and related notes appearing elsewhere in this prospectus.

	Nine Months Ended				
	September 30,		Year ended December 31,		
	2003	2002	2002	2001	2000
	(unaudited)	(unaudited)			
(dollars in millions, except per share amounts)					
<b>Infinity</b>					
<b>Earnings Statement Data:</b>					
Earned Premiums	\$ 504.2	\$ 496.0	\$ 645.9 (a)	\$ 916.4 (a)	\$ 1,043.3
Net Investment Income	41.9	47.4	61.3	75.2	69.3
Realized Gains (Losses) on Investments	1.3	(6.4)	(6.7)	(5.9)	(5.4)
Other Income	4.0	3.2	4.0	4.3	3.6
	<u>551.3</u>	<u>540.2</u>	<u>704.5</u>	<u>990.0</u>	<u>1,110.8</u>
Total Revenues					
Losses and Loss Adjustment Expenses	399.8	390.7	527.8	752.3	915.8
Commissions and Other Underwriting Expenses	68.1	83.1	79.0	202.1	229.5
Interest Expense	4.4				
Corporate General and Administrative Expenses	5.0				
Other Expenses	15.6	18.5	26.8	19.8	24.4
	<u>492.9</u>	<u>492.3</u>	<u>633.6</u>	<u>974.2</u>	<u>1,169.7</u>
Total Expenses					
Earnings (Loss) before Income Taxes	58.4	47.9	70.9	15.8	(58.9)
Provision (Credit) for Income Taxes	19.7	16.5	25.0	6.1	(20.3)
	<u>38.8</u>	<u>31.4</u>	<u>45.9</u>	<u>9.7</u>	<u>(38.6)</u>
Net Earnings (Loss) Before Equity in Affiliates					
Equity in Losses of Affiliates, Net of Tax					(11.5)
	<u>38.8</u>	<u>31.4</u>	<u>45.9</u>	<u>9.7</u>	<u>(50.1)</u>
Net Earnings (Loss)					
Net Earnings (Loss) per Common Share Diluted	\$ 1.89				
<b>Balance Sheet Data:</b>					
Cash and Investments	\$ 1,389.1	\$ 1,189.4	\$ 1,061.3	\$ 1,188.1	\$ 1,216.2
Total Assets	1,987.7	1,752.7	1,550.9	1,760.4	1,787.9
Unpaid Losses and Loss Adjustment Expenses	723.7	631.5	604.0	645.2	640.3
Total Liabilities	1,545.6	1,227.6	1,164.1	1,197.7	1,173.7
Shareholders' Equity	442.1	525.1	386.8	562.8	614.2
Book Value per Common Share	\$ 21.73				

**Statutory Data(b):**

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Loss and LAE Ratio	79.5%	78.7%	81.8%	82.1%	87.8%
Underwriting Expense Ratio	16.4%	15.1%	9.7%	21.3%	21.7%
Combined Ratio	95.9%	93.8%	91.5%	103.4%	109.5%
Policyholders Surplus	\$ 453.2	\$ 400.2	\$ 325.4	\$ 442.8	\$ 425.5

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	Nine Months Ended				
	September 30,		Year ended December 31,		
	2003	2002	2002	2001	2000
	(c)	(unaudited)			
	(dollars in millions)				
<b>Assumed Agency Business</b>					
<b>Earnings Statement Data:</b>					
Earned Premiums		\$ 84.6	\$ 107.2(d)	\$ 149.9	\$ 128.9
Underwriting Gain (Loss)		(8.4)	(10.0)	(14.7)	(3.6)
<b>Balance Sheet Data:</b>					
Assets (excluding Investments) to be Transferred		\$ 61.2	\$ 53.5	\$ 78.8	\$ 65.2
Investments to be Transferred			125.3		
Unpaid Losses and Loss Adjustment Expenses		123.6	125.6	115.9	105.9
Liabilities to be Transferred		176.5	178.8	200.5	173.3

- (a) The decline in earned premiums during 2001 and 2002 is due primarily to a reinsurance agreement pursuant to which we ceded 90% of the automobile physical damage business written by us as more fully discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations.
- (b) While financial data is reported in accordance with generally accepted accounting principles ( GAAP ) for shareholder and other investment purposes, it is reported on a statutory basis for insurance regulatory purposes. An insurer's underwriting profitability, as opposed to overall profitability or net earnings, is measured by the combined ratio. When the combined ratio is under 100%, underwriting results are generally considered profitable; when the ratio is over 100%, underwriting results are generally considered unprofitable. The combined ratio does not reflect investment income, other income or federal income taxes.
- The statutory combined ratio represents the sum of the following ratios: (1) losses and loss adjustment expenses incurred as a percentage of net earned premiums and (2) underwriting expenses incurred as a percentage of net written premiums. Certain statutory expenses differ from amounts reported under GAAP. Specifically, under GAAP, commissions, premium taxes and other variable costs incurred in connection with writing new and renewal business are capitalized and amortized on a pro rata basis over the period in which the related premiums are earned; on a statutory basis these items are expensed as incurred. In addition, costs for computer software developed or obtained for internal use are capitalized under GAAP and amortized over their useful life, rather than expensed as incurred, as required for statutory purposes.
- See Results of Operations Underwriting in Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of GAAP combined ratios for Infinity and the Assumed Agency Business.
- (c) The results of the Assumed Agency Business are included in the Infinity earnings statement data for the nine months ended September 30, 2003.
- (d) The decline in earned premiums during 2002 was due primarily to the reinsurance agreement described in note (a) above.



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**RISK FACTORS**

An investment in the common stock involves a number of risks. You should carefully consider the following information, together with the other information contained in this prospectus, before investing in the common stock.

*We have a limited operating history as a stand-alone entity.*

We became an independent public company in February 2003. Prior to that time, our insurance subsidiaries relied on AFG for assistance with respect to financial, administrative, managerial and other matters. While we have developed our own credit and banking relationships and perform our own financial and investor relations functions, continuing to develop the infrastructure necessary to operate as an independent public company has required and will continue to require a substantial amount of time and resources.

*Our ongoing consolidation of the operations of our insurance subsidiaries may not be successful.*

We are combining the operations of several insurance companies that have operated previously as independent business units. The process of consolidating the operations of our insurance subsidiaries poses managerial, strategic and technological challenges for us as an independent company, particularly with respect to the integration of historically separate information systems to a single system. The prospective costs and benefits of the consolidation may not result in equivalent or greater operating efficiencies and savings than those that have already been achieved. Such consolidation may negatively impact our revenues.

*Because we are primarily a personal automobile insurer, our business may be adversely affected by conditions in that business.*

Approximately 95% of our gross written premiums for the year ended December 31, 2002 and the nine months ended September 30, 2003 were generated from personal automobile insurance policies. Adverse developments in the market for personal automobile insurance, or the personal automobile insurance industry in general, could cause our results of operations to suffer. Our industry is exposed to the risks of severe weather conditions, such as rainstorms, snowstorms, hail and ice storms, hurricanes, tornadoes, earthquakes and, to a lesser degree, explosions, terrorist attacks and riots. The automobile insurance business is also affected by cost trends that impact profitability. Factors which negatively affect cost trends include inflation in automobile repair costs, automobile parts costs, used car prices and medical care. Increased litigation of claims may also negatively affect loss costs.

*Our results may fluctuate as a result of cyclical changes in the personal auto insurance industry.*

The personal auto insurance industry historically is cyclical in nature. The industry has been characterized by periods of price competition and excess capacity followed by periods of high premium rates and shortages of underwriting capacity. These fluctuations in the business cycle would be likely to negatively impact our revenues.

*Intense competition could adversely affect our profitability.*

The personal automobile insurance business is highly competitive and, except for regulatory considerations, there are relatively few barriers to entry. We compete with both large national writers and smaller regional companies. Some of our competitors have more capital and greater resources than we have, and may offer a broader range of products and lower prices than we offer. Some of our competitors that are direct writers, as opposed to agency writers as we are, may have certain competitive advantages, including increased name recognition, direct relationships with policyholders rather than with independent agents and, potentially, lower cost structures.

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*We are vulnerable to a reduction in the amount of business written by independent agents.*

Our reliance on the independent agency market makes us vulnerable to a reduction in the amount of business written by independent agents. Many of our competitors, like us, rely significantly on the independent agency market. Approximately two-thirds of all personal automobile insurance is sold direct or through captive agents (agents employed by the company or selling only one company's products) and approximately one-third is sold by independent agents. A material reduction in the amount of business independent agents sell would negatively impact our revenues.

*If we are not able to attract and retain independent agents, our revenues could be negatively affected.*

We must compete with other insurance carriers for independent agents' business. Some of our competitors offer a larger variety of products, lower prices for insurance coverage or higher commissions. While we believe that the products, pricing, commissions and services we offer agents are competitive, we may not be able to continue to attract and retain independent agents to sell our insurance products, in which case, our revenues could be negatively affected.

*We are subject to comprehensive regulation, and our ability to earn profits may be restricted by these regulations.*

We are subject to comprehensive regulation by government agencies in the states where our insurance company subsidiaries are domiciled (California, Indiana, Ohio, Oklahoma and Texas) and where these subsidiaries issue policies and handle claims. We must comply with regulations involving:

the payment of dividends;

the acquisition or disposition of an insurance company or of any company controlling an insurance company;

approval or filing of premium rates and policy forms;

involuntary assignments of high-risk policies, participation in reinsurance facilities and underwriting associations, assessments and other governmental charges;

minimum amounts of capital and surplus that must be maintained;

limitations on types and amounts of investments;

limitation of the right to cancel or non-renew policies;

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regulation of the right to withdraw from markets or terminate involvement with agencies;

licensing of insurers and agents;

reporting with respect to financial condition; and

transactions between an insurance company and any of its affiliates.

In addition, state insurance department examiners perform periodic financial and market conduct examinations of insurance companies. Such regulation is generally intended for the protection of policyholders rather than securityholders.

*Regulation may become more extensive in the future.*

Existing insurance-related laws and regulations may become more restrictive in the future, and new restrictive laws may be enacted. New or more restrictive regulation in the future could make it more expensive for us to conduct our business, restrict the premiums we are able to charge or otherwise change the way we do business. See Business Regulatory Environment.

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***Our insurance subsidiaries are subject to minimum capital and surplus requirements. Our failure to meet these requirements could subject us to regulatory action.***

Our insurance subsidiaries are subject to minimum capital and surplus requirements imposed under the laws of California, Indiana, Ohio, Oklahoma and Texas. Any failure by one of our insurance subsidiaries to meet the minimum capital and surplus requirements imposed by applicable state law will subject it to corrective action, including requiring the adoption of a comprehensive financial plan, examination and the issuance of a corrective order by the applicable state insurance department, revocation of its license to sell insurance products or placing the subsidiary under state regulatory control. Any new minimum capital and surplus requirements adopted in the future may require us to increase our capital and surplus levels, which we may be unable to do. As of September 30, 2003, each of our insurance company subsidiaries had capital and surplus substantially in excess of the currently required amounts.

***As a holding company, we are dependent on the results of operations of our insurance company subsidiaries to meet our obligations and pay future dividends.***

We are a holding company and a legal entity separate and distinct from our insurance company subsidiaries. As a holding company without significant operations of our own, our principal sources of funds are dividends and other distributions from our insurance company subsidiaries. State insurance laws limit the ability of our insurance companies to pay dividends and require our insurance companies to maintain specified levels of statutory capital and surplus. In addition, for competitive reasons, our insurance companies need to maintain financial strength ratings which requires us to sustain capital levels in those subsidiaries. These restrictions affect the ability of our insurance company subsidiaries to pay dividends and use their capital in other ways. Our rights to participate in any distribution of assets of our insurance company subsidiaries are subject to prior claims of policyholders and creditors (except to the extent that our rights, if any, as a creditor are recognized). Also, the covenants in our term loan require us to maintain minimum levels of capital and surplus which may limit the ability of our insurance company subsidiaries to pay dividends to us. Consequently, our ability to pay debts, expenses and cash dividends to our shareholders may be limited. See Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Sources of Funds and Business—Regulatory Environment.

***Our failure to maintain a commercially acceptable financial strength rating would significantly and negatively affect our ability to implement our business strategy successfully.***

Financial strength ratings are an important factor in establishing the competitive position of insurance companies and may be expected to have an effect on an insurance company's sales. A.M. Best has currently assigned our insurance company subsidiaries a group rating of A (Excellent). According to A.M. Best, A ratings are assigned to insurers which have, on balance, excellent balance sheet strength, operating performance and business profile when compared to the standards established by A.M. Best and, in A.M. Best's opinion, have a strong ability to meet their ongoing obligations to policyholders. A.M. Best bases its ratings on factors that concern policyholders and not upon factors concerning investor protection. Such ratings are subject to change and are not recommendations to buy, sell or hold securities. There can be no assurance that our rating or future changes to our rating will not affect our competitive position. See Business—Ratings.

***We are parties to litigation which, if decided adversely to us, could impact our financial results.***

We are named as a defendant in a number of lawsuits, including several class actions. These lawsuits are described more fully in Business—Legal Proceedings. Litigation, by its very nature, is unpredictable and the outcome of these cases is uncertain. Further, the precise nature of the relief that may be sought or granted in any lawsuits is uncertain and may, if these lawsuits are determined adversely to us, negatively impact our

earnings. See Business Legal Proceedings.

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***New claim and coverage issues are continually emerging, and these new issues could negatively impact our revenues or our method of doing business.***

As automobile insurance industry practices and regulatory, judicial, and consumer conditions change, unexpected and unintended issues related to claims and coverage may emerge. The issues can have a negative effect on our business by either extending coverage beyond our underwriting intent or by increasing the size of claims. Recent examples of emerging claims and coverage issues include:

the use of an applicant's credit rating as a factor in making risk selection and pricing decisions;

the availability of coverages which pay different commission levels to agents depending upon premium level;

a growing trend of plaintiffs targeting automobile insurers, including us, in purported class action litigation relating to the claim-handling practices such as total loss evaluation methodology.

The effects of these and other unforeseen emerging claim and coverage issues could negatively impact our revenues or our methods of doing business. See Business Legal Proceedings.

***Our reserves may be inadequate, which could significantly affect our financial results.***

We record reserve liabilities for the estimated payment of losses and loss adjustment expenses for both reported and unreported claims. Due to the inherent uncertainty of estimating reserves, it has been necessary in the past, and may continue to be necessary in the future, to revise estimated liabilities as reflected in our reserves for claims and related expenses. To the extent that reserves are inadequate and are strengthened, the amount of such increase is treated as a charge to earnings in the period in which the deficiency is recognized. The historic development of reserves for losses and loss adjustment expense may not necessarily reflect future trends in the development of these amounts. Accordingly, it is not appropriate to extrapolate redundancies or deficiencies based on historical information.

***We are dependent on key executives.***

Our success will depend in part upon the continued service of our Chief Executive Officer and President, James R. Gober, our Executive Vice President, John R. Miner, our Senior Vice President and General Counsel, Samuel J. Simon, our Senior Vice President and Chief Financial Officer, Roger Smith and our Senior Vice President, Joseph A. Pietrangelo. We have employment or severance agreements with two of our executives which we describe in Management Agreements with Executives . We do not have key person insurance on the lives of any of these individuals. Our success will also depend on our ability to attract and retain additional executives and personnel. The loss of key personnel could cause disruption in our business. As we grow, we will need to recruit and retain additional qualified personnel, and we may not be able to do so.

***Adverse securities market conditions can have significant and negative effects on our investment portfolio.***

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Our results of operations depend in part on the performance of our invested assets. As of September 30, 2003, 98% of our investment portfolio was invested in fixed maturity securities and 2% in equity securities. Certain risks are inherent in connection with fixed maturity securities including loss upon default and price volatility in reaction to changes in interest rates and general market factors. An increase in interest rates lowers prices on fixed maturity securities, and any sales we make during a period of increasing interest rates may result in losses. Conversely, investment income earned from future investments in fixed maturity securities will decrease if interest rates decrease.

*Our results may be adversely affected by conditions in the states where our business is concentrated.*

For the year ended December 31, 2002 and the nine months ended September 30, 2003, we generated approximately 80% and 87%, respectively, of our gross written premiums in our top 15 states. California,



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our largest market, generated approximately 34% and 46%, respectively, of our gross written premiums in 2002 and the nine months ended September 30, 2003. Our revenues and profitability are therefore subject to prevailing regulatory, legal, economic, demographic, competitive and other conditions in these states. Changes in any of these conditions could make it less attractive for us to do business in those states. Adverse regulatory developments in any of these states, which could include, among others, reductions in the rates permitted to be charged, inadequate rate increases, an inability to reduce the amount of insurance we write in those states, or more fundamental changes in the design or implementation of the automobile insurance regulatory framework, could negatively affect our premium revenue or make it more expensive or less profitable for us to conduct our business.

*We are dependent on certain contractual arrangements with AFG, and we may be unable to replace these arrangements, upon their expiration, with similar or more favorable arrangements.*

In connection with the initial public offering of common stock, we entered into a formation and separation agreement, a registration rights agreement, a noncompetition agreement, an investment advisory agreement, a tax allocation indemnification agreement, a services agreement and other arrangements and agreements with AFG and certain of its affiliates. See **Certain Arrangements and Relationships Between Our Company and AFG**. We negotiated the terms of these agreements with AFG. Our board of directors approved the terms of these agreements, but the agreements were not reviewed or approved by the independent directors who joined our board upon completion of the initial public offering of our common stock. Several of these agreements govern our relationship with AFG and its affiliates with respect to various intercompany services which AFG and its affiliates provide us. After the expiration of these agreements, we may not be able to replace these services and arrangements in a timely manner or on terms and conditions, including cost, as favorable as those we have with AFG.

*Certain provisions contained in our organizational documents and the insurance laws of various states could impede an attempt to replace or remove our management or prevent the sale of our company, which could diminish the value of our common stock.*

Our Articles of Incorporation and Regulations and the insurance laws of various states contain provisions that could impede an attempt to replace or remove our management or prevent the sale of our company that, in either case, shareholders might not consider to be in their best interests. For instance, these provisions may prevent shareholders from receiving the benefit of any premium over the market price of our common stock offered by a bidder in a potential takeover. In addition, the existence of these provisions may adversely affect the prevailing market price of our common stock if they are viewed as discouraging takeover attempts in the future. See **Business Regulatory Environment** and **Description of Capital Stock**.

## **CAUTIONARY STATEMENT CONCERNING FORWARD LOOKING STATEMENTS**

Some of the statements under **Summary**, **Risk Factors**, **Management's Discussion and Analysis of Financial Condition and Results of Operations**, **Business** and elsewhere in this prospectus may include forward-looking statements which reflect our current views with respect to future events and financial performance. These statements include forward-looking statements both with respect to us and the insurance industry. Statements which include the words *believes*, *expects*, *may*, *will*, *should*, *seeks*, *intends*, *plans*, *estimates*, *anticipates* or the negative version or other comparable terminology and similar statements of a future or forward-looking nature identify forward-looking statements.

These are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Examples of such forward-looking statements include statements relating to: expectations concerning market and other conditions, future premiums, revenues, earnings and investment activities, expected losses, rate increases, improved loss experience and expected expense savings



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resulting from consolidation of the operations of our subsidiaries. Actual results could differ materially from those we expect depending on certain risks and uncertainties including but not limited to:

changes in economic conditions and financial markets (including interest rates);

the adequacy or accuracy of our pricing methodologies;

the presence of competitors with greater financial resources and the impact of competitive pricing;

the ability to obtain timely approval for requested rate changes;

judicial and regulatory developments adverse to the automobile insurance industry;

the outcome of pending litigation against us;

weather conditions (including the severity and frequency of storms, hurricanes, snowfalls, hail and winter conditions);

changes in driving patterns and loss trends;

acts of war and terrorist activities; and

the challenges posed by consolidating the operations of its insurance subsidiaries.

All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in these statements. We believe that these factors include but are not limited to those described under "Risk Factors" above. We undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

## **USE OF PROCEEDS**

We will receive no proceeds from the sale of common stock by the selling shareholder. Fifty percent of any proceeds that we receive from the exercise of the underwriters' over-allotment option will be used to repay debt as required under provisions of the term loan we secured in July 2003. The remaining proceeds will be used for general corporate purposes. Our term loan matures on June 30, 2010 and currently bears interest at 3.6%. Proceeds of \$110 million from the term loan were contributed to our insurance subsidiaries to support future growth of their business and reduce our reliance on reinsurance, and the remaining proceeds were used to repay a \$55 million promissory note issued to AFG in connection with our formation and for general corporate purposes.

## **CAPITALIZATION**

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The following table shows our capitalization at September 30, 2003. This information should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and related notes appearing elsewhere in this prospectus.

	September 30, 2003
	(dollars in millions, except per share amounts)
Term loan	\$ 197.8
Shareholders' equity:	
Preferred stock; 10,000,000 shares authorized; no shares issued or outstanding	0
Common stock and paid-in capital; 50,000,000 shares authorized; 20,483,958 shares issued and outstanding	346.1
Unrealized gain on marketable securities	39.5
Retained earnings	56.5
<b>Total shareholders' equity</b>	<b>442.1</b>
<b>Total capitalization</b>	<b>\$ 639.8</b>
<b>Book value per common share</b>	<b>\$ 21.73</b>

**Table of Contents****PRICE RANGE FOR COMMON STOCK AND DIVIDENDS**

Our common stock began trading on February 18, 2003 on the Nasdaq National Market under the symbol IPCC. The following table sets forth, for the periods indicated, the high and low sales prices per share of common stock as reported on the Nasdaq National Market and the dividends paid per share of common stock during such period.

	<u>High</u>	<u>Low</u>	<u>Dividend</u>
<b>2003</b>			
First Quarter (beginning February 18)	\$ 18.40	\$ 15.60	\$
Second Quarter	24.55	17.51	0.055
Third Quarter	29.15	22.65	0.055
Fourth Quarter (through November 14)	34.82	27.55	0.055

On November 25, 2003, the last quoted price per share of our common stock on the Nasdaq National Market was \$34.00. As of September 30, 2003, we had 10 shareholders of record and approximately 116 beneficial holders of our common stock.

**DIVIDEND POLICY**

Our board of directors currently intends to declare a dividend on our common stock of \$0.22 per share annually. In 2003, our board of directors declared dividends of \$0.055 per share of common stock which were paid on each of May 25, August 28 and November 14, 2003. The declaration and payment of dividends is subject to the discretion of our board of directors, and will depend on, among other things, our financial condition, results of operations, capital and cash requirements, future prospects, regulatory and contractual restrictions on the payment of dividends by our subsidiaries, and other factors deemed relevant by the board. For a discussion of our cash resources and needs, see Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources.

We are a holding company and a legal entity separate and distinct from our insurance company subsidiaries. As a holding company without significant operations of our own, our principal sources of funds are dividends and other distributions from our insurance company subsidiaries. Our ability to receive dividends from subsidiaries is subject to limits under applicable state insurance laws. See Business - Regulatory Environment.

**Table of Contents****SELECTED HISTORICAL FINANCIAL DATA**

The following tables summarize certain historical financial data of Infinity and of the Assumed Agency Business. We derived the data as of and for each of the four years ended December 31, 2002, from financial statements audited by Ernst & Young LLP. We derived the data as of and for the year ended December 31, 1998, and the nine months ended September 30, 2003 and 2002, from unaudited financial statements which include all adjustments, consisting of normal recurring accruals, that management considers necessary for a fair presentation of the financial position and results of operations for those periods. Results for the interim periods are not necessarily indicative of results to be expected for the entire year. The Infinity financial data set forth below for all periods prior to December 31, 2002 is the financial data of the NSA Group. The Infinity financial data for the nine months ended September 30, 2003 include the results of the Assumed Agency Business. You should read this data in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and related notes appearing elsewhere in this prospectus.

	Nine months ended		Year ended December 31,				
	September 30,						
	2003	2002	2002	2001	2000	1999	1998
	(unaudited)	(unaudited)					(unaudited)
(dollars in millions, except per share amounts)							
<b>Infinity</b>							
<b>Earnings Statement Data:</b>							
Earned Premiums	\$ 504.2	\$ 496.0	\$ 645.9(a)	\$ 916.4(a)	\$ 1,043.3	\$ 944.5	\$ 1,156.7
Net Investment Income	41.9	47.4	61.3	75.2	69.3	74.3	77.6
Realized Gains (Losses) on Investments	1.3	(6.4)	(6.7)	(5.9)	(5.4)	22.6	9.0
Other Income	4.0	3.2	4.0	4.3	3.6	3.5	1.5
<b>Total Revenues</b>	<b>551.3</b>	<b>540.2</b>	<b>704.5</b>	<b>990.0</b>	<b>1,110.8</b>	<b>1,044.9</b>	<b>1,244.8</b>
Losses and Loss Adjustment Expenses	399.8	390.7	527.8	752.3	915.8	730.5	890.7
Commissions and Other Underwriting Expenses	68.1	83.1	79.0	202.1	229.5	213.4	250.1
Interest Expenses	4.4						
Corporate General and Administrative Expenses	5.0						
Other Expenses	15.6	18.5	26.8	19.8	24.4	19.4	9.8
<b>Total Expenses</b>	<b>492.9</b>	<b>492.3</b>	<b>633.6</b>	<b>974.2</b>	<b>1,169.7</b>	<b>963.3</b>	<b>1,150.6</b>
Earnings (Loss) before Income Taxes	58.4	47.9	70.9	15.8	(58.9)	81.6	94.2
Provision (Credit) for Income Taxes	19.7	16.5	25.0	6.1	(20.3)	29.2	29.5
<b>Net Earnings (Loss) Before Equity in Affiliates</b>	<b>38.8</b>	<b>31.4</b>	<b>45.9</b>	<b>9.7</b>	<b>(38.6)</b>	<b>52.4</b>	<b>64.7</b>
Equity in Losses of Affiliates, Net of Tax					(11.5)	(1.5)	(0.7)
<b>Net Earnings (Loss)</b>	<b>\$ 38.8</b>	<b>\$ 31.4</b>	<b>\$ 45.9</b>	<b>\$ 9.7</b>	<b>\$ (50.1)</b>	<b>\$ 50.9</b>	<b>\$ 64.0</b>
Net Earnings (Loss) per Common Share Diluted	\$ 1.89						

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**Balance Sheet Data:**

Cash and Investments	\$ 1,389.1	\$ 1,189.4	\$ 1,061.3	\$ 1,188.1	\$ 1,216.2	\$ 1,095.6	\$ 1,276.7
Total Assets	1,987.7	1,752.7	1,550.9	1,760.4	1,787.9	1,594.9	1,778.4
Unpaid Losses and Loss							
Adjustment Expenses	723.7	631.5	604.0	645.2	640.3	553.3	599.5
Total Liabilities	1,545.6	1,227.6	1,164.1	1,197.7	1,173.7	1,060.9	1,136.7
Shareholders Equity	442.1	525.1	386.8	562.8	614.2	534.0	641.7
Book Value per Common							
Share	\$ 21.73						

**Statutory Data (b):**

Loss and LAE Ratio	79.5%	78.7%	81.8%	82.1%	87.8%	77.4%	77.0%
Underwriting Expense Ratio	16.4%	15.1%	9.7%	21.3%	21.7%	22.6%	21.3%
<hr/>							
Combined Ratio	95.9%	93.8%	91.5%	103.4%	109.5%	100.0%	98.3%
Policyholders Surplus	\$ 453.2	\$ 400.2	\$ 325.4	\$ 442.8	\$ 425.5	\$ 345.4	\$ 434.1

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	Nine months ended					
	September 30,		Year ended December 31,			
	2003	2002	2002	2001	2000	1999
(c)	(unaudited)					(unaudited)
(dollars in millions)						
<b>Assumed Agency Business</b>						
<b>Earnings Statement Data:</b>						
Earned Premiums	\$ 84.6	\$ 107.2(d)	\$ 149.9	\$ 128.9	\$ 138.5	\$ 148.2
Losses and Loss Adjustment Expenses	72.0	91.1	121.8	93.3	73.3	81.6
Commissions and Other Underwriting Expenses	21.0	26.2	42.8	39.2	46.6	47.2
	93.0	117.3	164.6	132.5	119.9	128.8
Underwriting Gain (Loss)	\$ (8.4)	\$ (10.0)	\$ (14.7)	\$ (3.6)	\$ 18.6	\$ 19.4
<b>Balance Sheet Data:</b>						
Assets (excluding Investments) to be Transferred	\$ 61.2	\$ 53.5	\$ 78.8	\$ 65.2	\$ 55.4	\$ 62.1
Investments to be Transferred		125.3				
Unpaid Losses and Loss Adjustment Expenses	123.6	125.6	115.9	105.9	118.3	150.5
Liabilities to be Transferred	176.5	178.8	200.5	173.3	183.1	222.2
<b>Statutory Data (b):</b>						
Loss and LAE Ratio	84.9%	84.8%	81.3%	72.4%	54.8%	55.0%
Underwriting Expense Ratio	20.2%	17.2%	28.7%	30.3%	35.0%	31.4%
Combined Ratio	105.1%	102.0%	110.0%	102.7%	89.8%	86.4%

(a) The decline in earned premiums during 2001 and 2002 is due primarily to a reinsurance agreement pursuant to which the NSA Group ceded 90% of the automobile physical damage business written by it as more fully discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations.

(b) While financial data is reported in accordance with generally accepted accounting principles ( GAAP ) for shareholder and other investment purposes, it is reported on a statutory basis for insurance regulatory purposes. An insurer's underwriting profitability, as opposed to overall profitability or net earnings, is measured by the combined ratio. When the combined ratio is under 100%, underwriting results are generally considered profitable; when the ratio is over 100%, underwriting results are generally considered unprofitable. The combined ratio does not reflect investment income, other income or federal income taxes.

The statutory combined ratio represents the sum of the following ratios: (1) losses and loss adjustment expenses incurred as a percentage of net earned premiums and (2) underwriting expenses incurred as a percentage of net written premiums. Certain statutory expenses differ from amounts reported under GAAP. Specifically, under GAAP, commissions, premium taxes and other variable costs incurred in connection with writing new and renewal business are capitalized and amortized on a pro rata basis over the period in which the related premiums are earned; on a statutory basis these items are expensed as incurred. In addition, costs for computer software developed or obtained for internal use are capitalized under GAAP and amortized over their useful life, rather than expensed as incurred, as required for statutory purposes.

See Results of Operations - Underwriting in Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of GAAP combined ratios for Infinity and the Assumed Agency Business.



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- (c) The results of the Assumed Agency Business are included in the Infinity earnings statement data for the nine months ended September 30, 2003.
- (d) The decline in earned premiums during 2002 was due primarily to the reinsurance agreement described in note (a) above.

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**UNAUDITED PRO FORMA FINANCIAL INFORMATION**

The following pro forma financial information is intended to provide you with information about how the transactions described herein might have affected the historical financial statements of Infinity and the Assumed Agency Business if they had been consummated before 2003. Since the Assumed Agency Business is not a separate legal entity, it does not have complete historical balance sheets reflecting a separate investment portfolio and equity nor complete income statements reflecting investment income and income taxes. The following pro forma information does not necessarily reflect the financial position or results of operations which would have actually resulted had the transactions described occurred as of the dates indicated, nor should they be taken as necessarily indicative of the future financial position or results of operations of Infinity.

The unaudited pro forma financial information is based upon and should be read in conjunction with the separate audited financial statements of both Infinity and the Assumed Agency Business and the related notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this prospectus.

We have prepared the following Unaudited Pro Forma Condensed Combined Balance Sheet assuming that on December 31, 2002 Infinity assumed the Assumed Agency Business through a reinsurance agreement.

Pro forma statements of operations for the years 2000 and 2001 and the nine months ended September 30, 2002, are presented for comparative purposes to show the retroactive combination of Infinity and the Assumed Agency Business. We have prepared the following Unaudited Pro Forma Condensed Combined Statements of Operations assuming that the 8.5% promissory note with a principal amount of \$55 million was put in place on January 1, 2002. Pro forma investment income does not include any earnings on the \$125.3 million in investment securities received by Infinity in connection with the acquisition of the Assumed Agency Business. Annual investment income (based on the overall yield of these securities of 4.4% at December 31, 2002) would be \$5.5 million. The results of interim periods are not necessarily indicative of results for the entire year.

Pro forma amounts do not reflect any charges for the added costs of Infinity operating as a separate public company. We estimate these costs to be approximately \$6 million annually. Pro forma amounts also do not reflect the benefits of Infinity's consolidation of its claims, underwriting, product management and other functions in 2002. Management estimates that this consolidation will result in annualized savings of approximately \$13 million, about \$4 million of which was realized in 2002.

We ceased amortizing goodwill beginning January 1, 2002, in accordance with Statement of Financial Accounting Standards No. 142. Goodwill amortization expensed for the year 2001 was \$2.2 million.

Pro forma amounts reflect the acquisition of the Assumed Agency Business as a transfer of assets among entities under common control. Further discussion of pro forma adjustments is contained in the accompanying notes.

**Table of Contents****Infinity Property and Casualty Corporation****Unaudited Pro Forma Condensed Combined Balance Sheet****December 31, 2002**

	Assumed			Infinity Pro Forma Combined
	Infinity Historical	Agency Business Historical	Combining Adjustments	
(in millions, except per share amounts)				
<b>Assets:</b>				
Investments	\$ 973.2	\$	\$ 125.3(1)	\$ 1,098.5
Cash	88.1			88.1
Agents' balances and premiums receivable	206.8	37.0		243.8
Prepaid reinsurance premiums	91.9			91.9
Goodwill	70.3	5.0		75.3
Other assets	120.6	11.5		132.1
	<u>\$ 1,550.9</u>	<u>\$ 53.5</u>	<u>\$ 125.3</u>	<u>\$ 1,729.7</u>
<b>Liabilities and Capital:</b>				
Unpaid losses and loss adjustment expenses	\$ 604.0	\$ 125.6	\$	\$ 729.6
Unearned premiums	302.6	48.0		350.6
Payable to affiliates	4.8			4.8
Long-term debt payable to affiliate	55.0			55.0
Other liabilities and accrued expenses	197.7	5.2		202.9
	<u>1,164.1</u>	<u>178.8</u>		<u>1,342.9</u>
Excess of liabilities over assets of Assumed Agency Business		(125.3)	125.3(1)	
Shareholders' equity	386.8			386.8
	<u>\$ 1,550.9</u>	<u>\$ 53.5</u>	<u>\$ 125.3</u>	<u>\$ 1,729.7</u>
Book value per common share				\$ 19.01

**Table of Contents****Infinity Property and Casualty Corporation****Unaudited Condensed Combined Statement of Operations**

	Three months ended September 30,		Nine months ended September 30,		Year ended December 31,		
	2003 <u>(Actual)</u>	2002 <u>(pro forma)*</u>	2003 <u>(Actual)</u>	2002 <u>(pro forma)*</u>	2002 <u>(pro forma)*</u>	2001 <u>(pro forma)*</u>	2000 <u>(pro forma)*</u>
<b>(in millions, except per share amounts)</b>							
<b>Income:</b>							
Earned premiums	\$ 172.8	\$ 163.9	\$ 504.2	\$ 580.6	\$ 753.1	\$ 1,066.3	\$ 1,172.2
Net investment income	14.2	14.8	41.9	47.4	61.3	75.2	69.3
Realized gains (losses) on investments	0.8	5.4	1.3	(6.4)	(6.7)	(5.9)	(5.4)
Other income	2.2	1.1	4.0	3.2	4.0	4.3	3.6
	<u>190.0</u>	<u>185.3</u>	<u>551.3</u>	<u>624.8</u>	<u>811.7</u>	<u>1,139.9</u>	<u>1,239.7</u>
<b>Costs and Expenses:</b>							
Loss and loss adjustment expenses	136.7	132.4	399.8	462.7	618.9	874.1	1,009.1
Commissions and other underwriting expenses	22.4	20.8	68.1	104.1	105.2	244.9	268.7
Interest expense	2.0	1.2	4.4	3.6	4.7		
Corporate General & Administrative Expense	1.9		5.0				
Other expenses	4.9	9.0	15.6	18.5	26.8	19.8	24.4
	<u>167.9</u>	<u>163.4</u>	<u>492.9</u>	<u>588.9</u>	<u>755.6</u>	<u>1,138.8</u>	<u>1,302.2</u>
Earnings (loss) before income taxes	22.1	21.9	58.4	35.9	56.1	1.1	(62.5)
Provision (credit) for income taxes	7.2	7.5	19.7	12.3	19.8	1.0	(21.6)
	<u>15.0</u>	<u>14.4</u>	<u>38.8</u>	<u>23.6</u>	<u>36.3</u>	<u>0.1</u>	<u>(40.9)</u>
Net earnings (loss) before equity in affiliates	15.0	14.4	38.8	23.6	36.3	0.1	(40.9)
Equity in net losses of affiliates, net of tax							(11.5)
	<u>\$ 15.0</u>	<u>\$ 14.4</u>	<u>\$ 38.8</u>	<u>\$ 23.6</u>	<u>\$ 36.3</u>	<u>\$ 0.1</u>	<u>\$ (52.4)</u>
<b>Net Earnings (Loss)</b>							
Net earnings per common share basic	\$ 0.73	\$ 0.71	\$ 1.90	\$ 1.16	\$ 1.78	\$ 0.00	\$ (2.58)
Net earnings per common share diluted	\$ 0.72	\$ 0.71	\$ 1.89	\$ 1.16	\$ 1.78	\$ 0.00	\$ (2.58)

\* Combining details for each period presented are shown in the following pages.



**Table of Contents****Infinity Property and Casualty Corporation****Unaudited Pro Forma Condensed Combined Statement of Operations**

	Assumed			Infinity Pro Forma Combined
	Infinity	Business	Combining	
Three Months Ended September 30, 2002	Historical	Historical	Adjustments	Combined
	(in millions, except per share amounts)			
<b>Income:</b>				
Earned premiums	\$ 160.1	\$ 3.8	\$	\$ 163.9
Net investment income	14.8	(2)	(2)	14.8
Realized gains (losses) on investments	5.4			5.4
Other income	1.1			1.1
	<u>181.5</u>	<u>3.8</u>		<u>185.3</u>
<b>Costs and Expenses:</b>				
Loss and loss adjustment expenses	122.8	9.6		132.4
Commissions and other underwriting expenses	22.5	(1.6)		20.8
Interest expense			1.2(3)	1.2
Other expenses	9.0			9.0
	<u>154.2</u>	<u>8.0</u>	<u>1.2</u>	<u>163.4</u>
Earnings (loss) before income taxes	27.3	(4.2)	(1.2)	21.9
Provision (credit) for income taxes	9.4		(1.9)(4)	7.5
	<u>17.9</u>	<u>(4.2)</u>	<u>0.7</u>	<u>14.4</u>
<b>Net earnings (loss)</b>	<b>\$ 17.9</b>	<b>\$ (4.2)</b>	<b>\$ 0.7</b>	<b>\$ 14.4</b>
Net earnings per common share basic and diluted				\$ 0.71(5)

	Assumed			Infinity Pro Forma Combined
	Infinity	Business	Combining	
Nine Months Ended September 30, 2002	Historical	Historical	Adjustments	Combined
	(in millions, except per share amounts)			
<b>Income:</b>				
Earned premiums	\$ 496.0	\$ 84.6	\$	\$ 580.6
Net investment income	47.4	(2)	(2)	47.4
Realized losses on investments	(6.4)			(6.4)
Other income	3.2			3.2
	<u>540.2</u>	<u>84.6</u>		<u>624.8</u>

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**Costs and Expenses:**

Loss and loss adjustment expenses	390.7	72.0		462.7
Commissions and other underwriting expenses	83.1	21.0		104.1
Interest expense			3.6(3)	3.6
Other expenses	18.5			18.5
	<u>492.3</u>	<u>93.0</u>	<u>3.6</u>	<u>588.9</u>
Earnings (loss) before income taxes	47.9	(8.4)	(3.6)	35.9
Provision (credit) for income taxes	16.5		(4.2)(4)	12.3
<b>Net earnings (loss)</b>	<u>\$ 31.4</u>	<u>\$ (8.4)</u>	<u>\$ 0.6</u>	<u>\$ 23.6</u>
Net earnings per common share basic and diluted				\$ 1.16(5)

**Table of Contents****Infinity Property and Casualty Corporation****Unaudited Pro Forma Condensed Combined Statement of Operations**

Year ended December 31, 2002	Assumed			Infinity Pro Forma Combined
	Infinity Historical	Agency Business Historical	Combining Adjustments	
	(in millions, except per share amounts)			
<b>Income:</b>				
Earned premiums	\$ 645.9	\$ 107.2	\$	\$ 753.1
Net investment income	61.3	(2)	(2)	61.3
Realized losses on investments	(6.7)			(6.7)
Other income	4.0			4.0
	<u>704.5</u>	<u>107.2</u>		<u>811.7</u>
<b>Costs and Expenses:</b>				
Loss and loss adjustment expenses	527.8	91.1		618.9
Commissions and other underwriting expenses	79.0	26.2		105.2
Interest expense			4.7(3)	4.7
Other expenses	26.8			26.8
	<u>633.5</u>	<u>117.3</u>	<u>4.7</u>	<u>755.6</u>
Earnings (loss) before income taxes	70.9	(10.1)	(4.7)	56.1
Provision (credit) for income taxes	25.0		(5.2)(4)	19.8
<b>Net Earnings (loss)</b>	<u>\$ 45.9</u>	<u>\$ (10.1)</u>	<u>\$ 0.5</u>	<u>\$ 36.3</u>
Net earnings per common share basic and diluted				\$ 1.78(5)



**Table of Contents****Infinity Property and Casualty Corporation****Unaudited Pro Forma Condensed Combined Statement of Operations**

<u>Year ended December 31, 2001</u>	Assumed			Infinity Pro Forma Combined
	Agency			
	Infinity	Business	Combining	
	Historical	Historical	Adjustments	
	(in millions, except per share amounts)			
<b>Income:</b>				
Earned premiums	\$ 916.4	\$ 149.9	\$	\$ 1,066.3
Net investment income	75.2	(2)	(2)	75.2
Realized losses on investments	(5.9)			(5.9)
Other income	4.3			4.3
	<u>990.0</u>	<u>149.9</u>		<u>1,139.9</u>
<b>Costs and Expenses:</b>				
Loss and loss adjustment expenses	752.3	121.8		874.1
Commissions and other underwriting expenses	202.1	42.8		244.9
Other expenses	19.8			19.8
	<u>974.2</u>	<u>164.6</u>		<u>1,138.8</u>
Earnings (loss) before income taxes	15.8	(14.7)		1.1
Provision (credit) for income taxes	6.1		5.1(4)	1.0
<b>Net earnings (loss)</b>	<u>\$ 9.7</u>	<u>\$ (14.7)</u>	<u>\$ 5.1</u>	<u>\$ 0.1</u>
Net earnings per common share basic and diluted				\$ 0.00(5)

<u>Year ended December 31, 2000</u>	Assumed			Infinity Pro Forma Combined
	Agency			
	Infinity	Business	Combining	
	Historical	Historical	Adjustments	
	(in millions, except per share amounts)			
<b>Income:</b>				
Earned premiums	\$ 1,043.3	\$ 128.9	\$	\$ 1,172.2
Net investment income	69.3	(2)	(2)	69.3
Realized losses on investments	(5.4)			(5.4)
Other income	3.6			3.6
	<u>1,110.8</u>	<u>128.9</u>		<u>1,239.7</u>
<b>Costs and Expenses:</b>				

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Loss and loss adjustment expenses	915.8	93.3		1,009.1
Commissions and other underwriting expenses	229.5	39.2		268.7
Other expenses	24.4			24.4
	<u>1,169.7</u>	<u>132.5</u>		<u>1,302.2</u>
Loss before income taxes	(58.9)	(3.6)		(62.5)
Provision (credit) for income taxes	(20.3)		(1.3)(4)	(21.6)
Net earnings (loss) before equity in affiliates	(38.6)	(3.6)	1.3	(40.9)
Equity in net losses of affiliates, net of tax	(11.5)			(11.5)
<b>Net earnings (loss)</b>	<u>\$ (50.1)</u>	<u>\$ (3.6)</u>	<u>\$ 1.3</u>	<u>\$ (52.4)</u>
Net loss per common share basic and diluted				\$ (2.58)(5)

**Table of Contents****Notes To Unaudited Pro Forma Financial Information**

- (1) Reflects the acquisition of the Assumed Agency Business of Great American which occurred on January 1, 2003. Because the Assumed Agency Business is not a separate legal entity, the acquisition was effected through a reinsurance agreement. Under the agreement, Infinity received the net liabilities of the Assumed Agency Business plus primarily investment securities with a market value equal to \$125.3 million (the excess of liabilities over assets of the Assumed Agency Business at December 31, 2002 less \$5 million). The securities transferred were selected from Great American's portfolio by the AFG subsidiary that manages investments for Great American and Infinity. While the selected investments have not historically been managed as a separate portfolio or matched with the liabilities of the Assumed Agency Business, we consider them representative of Great American's overall portfolio.

The investment securities transferred by Great American consisted of 61 positions, 93% of which were rated investment grade (credit rating of AAA to BBB) by nationally recognized rating agencies at December 31, 2002, with the largest single position having a market value of \$4.0 million or 3% of the total. Industry classifications for these investments were as follows: mortgage-backed securities 11%, municipal bonds 9%, utilities 13%, banks 9% and life insurers 7%; all others were less than 5% each. The table below shows the scheduled maturities of these investments based on market value as of December 31, 2002. Mortgage-backed securities had an average life of approximately five years at December 31, 2002.

<b>Maturity</b>	
One year or less	10%
After one year through five years	30%
After five years through ten years	41%
After ten years	8%
	<hr/>
	89%
Mortgage-backed securities	11%
	<hr/>
	100%
	<hr/>

The overall yield of the transferred portfolio based on December 31, 2002, market prices was 4.4%. For pro forma income statement purposes, no income is assumed to have been earned on these investments.

In addition to the transfer of financial assets and liabilities, Great American transferred to Infinity the operational processes, including policy renewal rights, and employees necessary to conduct the normal operations of this business following the date of transfer. Accordingly, the operations transferred represent a business under Emerging Issues Task Force Issue 98-3. Since the transfer was made while Infinity was an AFG subsidiary, the net liabilities and investment assets were recorded at AFG's historical cost.

- (2) The Assumed Agency Business represents a portion of AFG's Personal Lines segment of operations and does not have a separate investment portfolio. No investment income is assumed earned on the \$125.3 million in investment securities which were received by Infinity as described in note (1) above. As disclosed under Business Investments, the NSA Group's yield on fixed income securities for the first nine months of 2002 and the years 2002, 2001 and 2000 were 6.5%, 6.3%, 6.7% and 6.7%, respectively.
- (3) Represents interest incurred on the \$55 million to repay the promissory note to AFG. The note was repaid in July 2003.

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- (4) The historical Assumed Agency Business was not a separate legal entity, and accordingly, does not have a separate tax provision. The combining adjustment reflects a tax benefit on the historical underwriting loss of the Assumed Agency Business in addition to the tax effects of the adjustments to pretax income at the statutory rate of 35%.
  
- (5) Per share amounts assume 20,347,083 shares were outstanding for all periods presented.

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**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS**

**General**

Following is a discussion and analysis of the historical combined financial statements of the NSA Group and the historical financial statements of the Assumed Agency Business that we have assumed. Together, these businesses comprise Infinity's operations following the initial public offering of our common stock. Following the discussion of the results of operations of these businesses is a discussion of the underwriting results of AFG's Personal segment which includes the NSA Group and the Assumed Agency Business as well as other personal business (substantially all of which is written directly with the customer instead of through independent agents) that is being retained by AFG.

This discussion should be read in conjunction with our financial statements beginning on page F-2 and the financial statements of the Assumed Agency Business that follow our financial statements. See "Unaudited Pro Forma Financial Information" for information about the financial impact of the initial public offering, the acquisition of the NSA Group and the assumption of the Assumed Agency Business.

Infinity was incorporated in the state of Ohio in September 2002, as an indirect wholly-owned subsidiary of AFG. In connection with the initial public offering of our common stock, AFG transferred to Infinity all of the outstanding common stock of certain subsidiaries engaged primarily in nonstandard personal automobile insurance. The accompanying combined statements include the accounts of the following subsidiaries which were transferred to Infinity: Atlanta Casualty Company, Infinity Insurance Company, Leader Insurance Company and Windsor Insurance Company.

Through a reinsurance transaction entered into effective January 1, 2003, we assumed the Assumed Agency Business consisting of the personal lines business written through independent agents by AFG's principal property and casualty subsidiary, Great American. The Assumed Agency Business had net earned premiums of \$107 million in 2002 consisting primarily of standard and preferred private passenger automobile insurance. The Assumed Agency Business is not included in Infinity's historical financial statements for periods before 2003.

We accounted for our acquisition of the NSA Group and the assumption of the Assumed Agency Business at AFG's historical carrying amounts as transfers of net assets between entities under common control in accordance with Statement of Financial Accounting Standards No. 141.

**Critical Accounting Policies**

Our significant accounting policies are described in Note B to the audited financial statements of both Infinity and the Assumed Agency Business as of and for the year ended December 31, 2002. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that can significantly affect amounts reported in the financial statements. As more information becomes known, these estimates and assumptions could change and thus impact amounts reported in the future. Management believes that the establishment of insurance reserves and the determination of other than temporary impairment on investments and accruals for litigation are areas where the degree of judgment required to determine amounts recorded in the financial statements make the accounting policies critical. We discuss these policies below under the headings Liquidity and Capital Resources, Investments and Liquidity and Capital Resources, and Uncertainties.

**Liquidity and Capital Resources**

*Ratios.* The National Association of Insurance Commissioners' model law for risk based capital ( RBC ) provides formulas to determine the amount of capital that an insurance company needs to ensure that it has an acceptable expectation of not becoming financially impaired. At December 31, 2002, the capital ratios of all our insurance companies substantially exceeded the RBC requirements.

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*Sources of Funds.* We are organized as a holding company with all of our operations being conducted by our insurance subsidiaries. Accordingly, we will have continuing cash needs for administrative expenses, the payment of principal and interest on borrowings, shareholder dividends, and taxes. Funds to meet these obligations will come primarily from dividends and distributions from our insurance subsidiaries.

We plan to file a consolidated federal income tax return including all 80%-owned U.S. subsidiaries for periods after our initial public offering. We intend to execute a tax allocation agreement with our eligible subsidiaries under which each company will be allocated its share of the federal consolidated tax liability. The resulting provision or credit will be currently payable to or from the parent company, Infinity Property and Casualty Corporation. We have made the appropriate filing with the insurance departments of Ohio, Indiana, Oklahoma and California seeking approval to use this tax allocation agreement and expect to receive approval before year-end 2003.

In July 2003, we secured a \$200 million, seven-year amortizing term loan, and we expect to add a revolving credit line of \$20 million in the fourth quarter of 2003. Proceeds of \$110 million were contributed to our insurance subsidiaries to support future growth of their business and reduce reliance on reinsurance. The remaining proceeds were used to repay a \$55 million promissory note issued in connection with our initial public offering and for general corporate purposes. The term loan is collateralized by our assets and by a pledge of stock of our insurance subsidiaries. The loan contains various covenants that require us to meet certain minimum net worth and financial ratio standards. Scheduled payments in 2004 are \$9.0 million and increase in subsequent years. Note 7 to our Consolidated Financial Statements as of and for the periods ended September 30, 2003 contains the complete amortization schedule.

In 2003, our operating subsidiaries may pay to us up to \$51 million in ordinary dividends without prior regulatory approval. Through September 2003, these operating subsidiaries have paid no dividends to us. We believe that our cash and investment balances and cash flows generated from operations, including dividends and distributions from our subsidiaries, are adequate to meet our future liquidity needs.

Our insurance subsidiaries generate liquidity primarily by collecting and investing premiums in advance of paying claims. We had positive cash flow from operations of approximately \$52 million for the nine months ended September 30, 2003 and \$45 million in 2002, \$33 million in 2001 and \$25 million in 2000.

*Quota Share Agreement.* We utilize the reinsurance market to manage our capital and surplus levels relative to our reserve liabilities, supporting our capacity for growth (as well as manage our risk). Throughout 2002, our insurance subsidiaries ceded 90% of their personal auto physical damage business on a funds withheld basis to Inter-Ocean Reinsurance Limited. We renewed this agreement for 2003 on terms substantially equivalent to those in effect in 2002 except that we have the flexibility to elect, on a quarterly basis, the percentage of business to be ceded under the reinsurance agreement. The percentage ceded may range from as high as 90% to as low as 20%.

Because we obtained the \$200 million term loan facility, we reduced the amount ceded under this agreement from 90% to 20% for the third quarter 2003. We intend to remain at the 20% level for the rest of the year. We are also currently in negotiations to renew this agreement for 2004 under substantially the same terms, but with a lower minimum ceding threshold. Premiums ceded under this agreement for the third quarter and first nine months of 2003 were \$9.9 million and \$176.2 million, respectively, compared to \$126.6 million and \$297.7 million for the corresponding 2002 periods. These amounts include the business ceded under this agreement for the Great American Assumed Business, as discussed in the following paragraph.

In September 2002, this agreement was amended to include coverage of Great American's personal lines that we assumed as part of the Assumed Agency Business. Accordingly, Great American's participation in the Inter-Ocean reinsurance agreement reduces the size of the Assumed Agency Business. Premiums ceded under this agreement were \$2.6 million and \$21.3 million for the three and nine month periods ended

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September 30, 2003, respectively and \$78.5 million in 2002.

*Investments.* Our investment portfolio at September 30, 2003, contained approximately \$1.3 billion in fixed maturity securities and \$27.8 million in equity securities, all carried at market value with unrealized gains and losses reported as a separate component of shareholders' equity on an after-tax basis. At September 30, 2003,



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we had pretax net unrealized gains of \$60.5 million on fixed maturities and \$0.4 million on equity securities. Combined, these figures increased \$24 million for the nine months ended September 30, 2003 due to the general decrease in interest rates since December 31, 2002.

Approximately 93% of the fixed maturities that we held at September 30, 2003 were rated investment grade, as defined by the National Association of Insurance Commissioners investment rating system. Investment grade securities generally bear lower yields and have lower degrees of risk than those that are unrated or noninvestment grade. We believe that a high quality investment portfolio is more likely to generate a stable and predictable investment return.

Individual portfolio securities are sold creating gains or losses as market opportunities exist. Since all of these securities are carried at market value on the balance sheet, there is virtually no effect on liquidity or financial condition upon the sale and ultimate realization of unrealized gains and losses. The average duration of our fixed maturity portfolio was 4.6 years at September 30, 2003.

Summarized information for our investment portfolio follows:

<b>September 30, 2003</b>	<b>(in millions)</b>				
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Market Value</b>	<b>% of Total</b>
Fixed Maturities	\$ 1,215	\$ 64	\$ 4	\$ 1,275	98%
Preferred Stocks	10			10	1%
Common Stocks	17	1	1	17	1%
<b>Total</b>	<b>\$ 1,242</b>	<b>\$ 65</b>	<b>\$ 5</b>	<b>\$ 1,302</b>	<b>100%</b>

<b>December 31, 2002</b>	<b>(in millions)</b>				
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Market Value</b>	<b>% of Total</b>
Fixed Maturities	\$ 917	\$ 51	\$ 12	\$ 956	98%
Common Stocks	19		2	17	2%
<b>Total</b>	<b>\$ 936</b>	<b>\$ 51</b>	<b>\$ 14</b>	<b>\$ 973</b>	<b>100%</b>

	<b>September 30, 2003</b>	<b>December 31, 2002</b>
Number of positions held with unrealized:		
Gains	449	345
Losses	59	61
Number of positions held that individually exceed unrealized:		
Gains of \$500,000	17	14

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Losses of \$500,000	1	7
Percentage of positions held with unrealized:		
Gains that were investment grade	88%	98%
Losses that were investment grade	56%	44%

Our investment portfolio had gross unrealized losses of \$4.6 million at September 30, 2003. There was no single industry segment concentration that accounted for more than \$1 million of these losses at that date. At December 31, 2002, our investment portfolio included \$14.3 million of gross unrealized losses; \$4.7 million of these losses were in securities issued by companies in the airline industry and \$1.8 million was in securities issued by an electric service industry firm. No other industry segment accounted for more than \$1 million of unrealized losses at December 31, 2002.

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The table below sets forth the scheduled maturities of fixed maturity securities at September 30, 2003 based on their market values in millions. Securities that do not have a single maturity date are reported at average maturity. Actual maturities may differ from contractual maturities because certain securities may be called or prepaid by the issuers.

<u>Maturity</u>	<u>Securities With Unrealized Gains</u>	<u>Securities With Unrealized Losses</u>	<u>Securities With No Unrealized Gain or Loss</u>	<u>All Fixed Maturity Securities</u>
One year or less	\$ 39	\$	\$ 6	\$ 45
After one year through five years	338	19		357
After five years through ten years	458	46	2	506
After ten years	97	13		110
Mortgage-backed securities	189	60	8	257
<b>Total</b>	<b>\$ 1,121</b>	<b>\$ 138</b>	<b>\$ 16</b>	<b>\$ 1,275</b>

We realized aggregate losses of \$103,000 during the nine months ended September 30, 2003 on \$11.8 million in sales of fixed maturity securities (four issues/four issuers) that had individual unrealized losses greater than \$100,000 at December 31, 2002. Market values of all four of the securities increased an aggregate of \$777,000 from December 31, 2002 to the date of sale.

We realized aggregate losses of \$5.9 million for the year ended December 31, 2002 on \$34 million in sales of fixed maturity securities (12 issues; nine issuers) that had unrealized losses greater than \$100,000 at December 31, 2001. The market value of four of our securities did not change from December 31, 2001 to the date of sale. Market values of three of the securities increased an aggregate of \$1.4 million from December 31, 2001 to the sale date. One of the securities was a Qwest Communications bond that decreased in value by \$2.2 million from December 31, 2001 to the date of sale due to the decline in Qwest Communications financial condition. Market values of the remaining four securities decreased an aggregate of \$694,000 from December 31, 2001 to the sale date.

Our pretax impairment charges (in thousands) on securities for the periods indicated were:

	<u>Three months ended September 30,</u>		<u>Nine months ended September 30,</u>	
	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>
Fixed maturities	\$	\$ 1,139	\$ 2,963	\$ 4,932
Equities	486	71	517	2,744
<b>Total</b>	<b>\$ 486</b>	<b>\$ 1,210</b>	<b>\$ 3,480</b>	<b>\$ 7,676</b>

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The impairments recorded during the first nine months of 2003 are primarily due to economic challenges faced by the airline industry. The impairments recorded during the first nine months of 2002 were primarily related to investments in the telecommunications industry.

Based on our analysis, we believe (i) that we will recover its cost basis in these securities and (ii) that we have the ability and intent to hold these securities until they mature or recover in value. Should either of these beliefs change with regard to a particular security, a charge for impairment would likely be required. While it is not possible to accurately predict if or when a specific security will become impaired, charges for other than temporary impairments could be material to results of operations in a future period. We believe it is not likely that future impairment charges will have a significant effect on our liquidity.

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When a decline in the value of a specific investment is considered to be other than temporary, a provision for impairment is charged to earnings (accounted for as a realized loss) and the cost basis of that investment is reduced. The determination of whether unrealized losses are other than temporary requires judgment based on subjective as well as objective factors. Factors we consider and resources we use include:

whether the unrealized loss is credit-driven or a result of changes in market interest rates,

the extent to which market value is less than cost basis,

historical operating, balance sheet and cash flow data contained in issuer SEC filings,

issuer news releases,

near-term prospects for improvement in the issuer and/or its industry,

industry research and communications with industry specialists,

third party research and credit rating reports,

internally generated financial models and forecasts,

discussions with issuer management, and

ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value.

Changes in the market values of investment securities are usually recorded as changes in unrealized gains or losses on investments, a component of shareholders' equity. Net earnings are not affected until the disposition of a given security or if an unrealized loss is deemed to be other than temporary; in the case of the latter, an impairment charge is recorded as a realized capital loss and the cost basis of the security is reduced.

## ***Uncertainties***

***Insurance Reserves.*** Liabilities for the costs of losses and loss adjustment expenses for both reported and unreported claims are estimated based on historical trends adjusted for changes in loss cost trends, underwriting standards, policy provisions, product mix and other factors. Estimating the liability for unpaid losses and loss adjustment expense is inherently judgmental and is influenced by factors which are subject to significant variation. Through the use of analytical reserve development techniques, management monitors items such as the effect of inflation on medical, hospitalization, material repair and replacement costs, general economic trends and the legal environment. Adjustments to reserves are reflected in the results of operations in the periods in which estimates change.

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*Exposure to Market Risk.* Market risk represents the potential economic loss arising from adverse changes in the fair value of financial instruments. Our exposures to market risk relate primarily to our investment portfolio which is exposed to interest rate risk and, to a lesser extent, equity price risk.

*Fixed Maturity Portfolio.* The fair value of our fixed maturity portfolio is directly impacted by changes in market interest rates. Our fixed maturity portfolio is comprised of substantially all fixed rate investments with primarily short-term and intermediate-term maturities. This practice allows us to be flexible in reacting to

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fluctuations of interest rates. We manage the portfolios of our insurance companies to attempt to achieve an adequate risk-adjusted return while maintaining sufficient liquidity to meet policyholder obligations.

The following table provides information about the NSA Group's fixed maturity investments that are sensitive to interest rate risk. The table shows expected principal cash flows and related weighted average interest rates by expected maturity date for each of the five subsequent years and collectively for all years thereafter. We include callable bonds and notes based on call date or maturity date depending upon which date produces the most conservative yield. We include mortgage-backed securities and sinking fund issues based on maturity year adjusted for expected payment patterns. Actual cash flows may differ from those expected.

Year	December 31, 2002		December 31, 2001		December 31, 2000	
	Principal		Principal		Principal	
	Cash Flows	Rate	Cash Flows	Rate	Cash Flows	Rate
	(dollars in millions)					
Subsequent Calendar Year	\$ 105.0	6.7%	\$ 63.7	7.5%	\$ 41.7	7.2%
Second Subsequent Calendar Year	76.6	7.1%	143.9	7.1%	53.4	6.7%
Third Subsequent Calendar Year	122.9	6.4%	89.1	7.0%	135.2	7.1%
Fourth Subsequent Calendar Year	100.3	6.5%	119.4	6.6%	88.7	7.0%
Fifth Subsequent Calendar Year	97.9	6.6%	137.1	6.3%	121.1	6.9%
Thereafter	404.1	6.2%	523.1	6.8%	583.5	7.0%
Total	\$ 906.8	6.4%	\$ 1,076.3	6.8%	\$ 1,023.6	7.0%
Fair Value	\$ 955.6		\$ 1,082.8		\$ 991.4	

*Equity Price Risk.* Equity price risk is the potential economic loss from adverse changes in equity security prices. Although our investment in equity securities is only 2% of the total investments at December 31, 2002, it is concentrated in a relatively limited number of positions; approximately 80% of the total is in three investments. We believe this approach allows us to more closely monitor the companies and industries in which they operate.

*Accruals for Litigation.* We continually evaluate potential liabilities and reserves for them using the criteria established by SFAS No. 5, *Accounting for Contingencies*. We believe the current assumptions and other considerations used to estimate potential liability for litigation are appropriate. While it is not possible to know with certainty the ultimate outcome of these claims or lawsuits, we do not expect them to have a material effect on our financial condition or results of operations.

**Results Of Operations***Underwriting*

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Our insurance subsidiaries sell nonstandard, standard and preferred personal auto insurance and, to a lesser extent, nonstandard commercial auto coverage and a complement of other personal lines insurance products. Nonstandard coverage is a product designed for drivers who, due to their driving record, age or vehicle type, represent higher than normal risks and pay higher rates for comparable coverage.

Underwriting profitability is measured by the combined ratio which is a sum of the ratios of losses, loss adjustment expenses and underwriting expenses to earned premiums. When the combined ratio is under 100%, underwriting results are generally considered profitable; when the ratio is over 100%, underwriting results are generally considered unprofitable. The combined ratio does not reflect investment income, other income or federal income taxes.

While losses on claims reported are generally determinable, the process of determining overall loss and LAE reserves is also highly dependent upon the use of estimates in the case of losses incurred or expected but not yet reported or developed. Actuarial procedures and projections are used to obtain best estimates which are then included in the overall results. These estimates are subject to changes in claim amounts and frequency and are periodically reviewed and adjusted as additional information becomes known. In accordance with industry



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practices, such adjustments are reflected in current year underwriting results. As a result, the ratio of loss and LAE expenses component of the combined ratio includes development of prior year reserves in addition to provision for losses and LAE occurring in the current year.

Underwriting expenses include expenses that vary directly with premium volume (commissions) as well as expenses that are relatively fixed (administrative expenses). Accordingly, underwriting expenses tend to move in the same direction as premiums but at a slower rate. As a result, the underwriting expense ratio tends to decrease when premiums grow and increase when premiums decline.

Since early 2000, Infinity's insurance subsidiaries have been increasing their premium rates with a goal of achieving underwriting profits, even if it entails foregoing volume. We increased personal auto rates by 14% in 2000, again in 2001, 12% in 2002 and 2% for the nine months ended September 30, 2003. As with all property and casualty companies, the beneficial impact of these price increases is reflected in our financial results over time. We implement price increases on our in-force policies as they are renewed, which generally takes between six and twelve months for our entire book of business. We recognize increased premiums on particular policies as the premiums are earned, generally over the course of the six to twelve months after the policy is effective.

Net earned premiums and combined ratios for the NSA Group and the Assumed Agency Business were as follows:

	Three Months Ended		Nine Months Ended		Year Ended December 31,		
	September 30		September 30,		Year Ended December 31,		
	2003	2002	2003	2002	2002	2001	2000
(in millions, except percentages)							
<b>Net Earned Premiums (GAAP)</b>							
NSA Group:							
Gross written premiums	\$ 208.8	\$ 206.0	\$ 667.1	\$ 727.0	\$ 914.6	\$ 962.3	\$ 1,077.7
Ceded reinsurance	(8.8)	(66.6)	(112.0)	(240.2)	(301.6)	(224.7)	(3.8)
Net written premiums	200.0	139.4	507.1	486.8	613.0	737.6	1,073.9
Change in unearned premiums	(48.4)	20.7	(71.7)	9.2	32.9	178.8	(30.6)
Net earned premiums	\$ 151.6	\$ 160.1	\$ 435.4	\$ 496.0	\$ 645.9	\$ 916.4	\$ 1,043.3
Assumed Agency Business:							
Net written premiums(a)	\$ 26.6	\$ (23.9)	\$ 115.7	\$ 54.7	\$ 74.3	\$ 165.3	\$ 133.1
Change in unearned premiums	(5.4)	27.7	(46.9)	29.9	32.9	(15.4)	(4.2)
Net earned premiums	\$ 21.2	\$ 3.8	\$ 68.8	\$ 84.6	\$ 107.2	\$ 149.9	\$ 128.9
<b>Combined Ratios (GAAP)</b>							
NSA Group:							
Loss and LAE ratio	77.7%	76.7%	79.3%	78.8%	81.8%	82.1%	87.8%
Underwriting expense ratio	12.2	14.0	12.0	16.7	12.2	22.1	22.0
Combined ratio	89.9%	90.7%	91.3%	95.5%	94.0%	104.2%	109.8%

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Assumed Agency Business:							
Loss and LAE ratio	88.4%	254.0%	79.4%	85.0%	84.9%	81.2%	72.4%
Underwriting expense ratio	18.3	(43.2)	23.0	24.9	24.4	28.6	30.4
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Combined ratio	106.7%	210.8%	102.4%	109.9%	109.3%	109.8%	102.8%
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Weighted Average of NSA Group and Agency:							
Loss and LAE ratio	79.1%	80.8%	79.3%	79.7%	82.2%	82.0%	86.1%
Underwriting expense ratio	12.9	12.7	13.5	17.9	13.9	22.9	22.9
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Combined ratio	92.0%	93.5%	92.8%	97.6%	96.1%	104.9%	109.0%
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Combined ratio before effects of Inter-Ocean agreement							
	93.5%	96.1%	94.8%	98.3%	97.3%	104.5%	109.0%
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>

- (a) Under a reinsurance agreement entered into with Great American, Infinity's insurance subsidiaries assumed net written premiums from Great American. Accordingly, gross written premiums and net written premiums are the same.

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*Three Months Ended September 30, 2003 compared to Three Months Ended September 30, 2002.* The NSA Group's net earned premiums fell \$8.5 million, or 5.3%, during the three month period ended September 30, 2003. The impact from ceding only 20% of physical damage premiums under the Inter-Ocean reinsurance agreement beginning in the second half of 2003 from 90% in all of 2002 and the first half on 2003 mitigated the decline. Earned premiums excluding the effect of that reinsurance agreement declined \$28.9 million, or 12.2%, due primarily to a planned withdrawal of business in non-focus states partially offset by rate increases. The policies in force declined 6.8% from 658,000 at September 2002 to 613,000 at September 2003. The decline in policy counts was due primarily to actions taken in late 2002 to discontinue writing inadequately priced business in certain focus states as well as decisions by insureds not to renew. Gross written premiums for the NSA Group, which represent premiums from insureds before the effect of reinsurance, increased \$2.8 million, or 1.4%, for the third quarter of 2003 as compared with the same period in 2002 as a result of new programs in several focus states as well as significant growth in volume in California, the state from which Infinity derives the greatest amount of revenue. The loss and LAE ratio increased from 76.7% for the three month period ended September 30, 2002 to 77.7% for the same period in 2003 as a result of the effect of the Inter-Ocean agreement. The loss and LAE ratio excluding the impact of the Inter-Ocean agreement improved 2.1 points for the three month period ended September 30, 2003 as compared with the same period in 2002 as a result of increases in rates, lower frequency of claims per auto insured and moderate increases in the average cost per claim, as well as a reduction of business in non-focus states. The expense ratio improved by 1.8 points in the third quarter of 2003 primarily as a result of the impact of the ceding commission from the Inter-Ocean reinsurance agreement. Excluding this impact, the expense ratio increased .7 points to 21.8%, in the third quarter of 2003 as compared to the same period in 2002. The .7 point increase in the expense ratio was due to charges of \$2.9 million relating to an increase in commissions paid to certain agents based on underwriting results and an increase in amortization of acquisition costs relating to a periodic review of the deferability of acquisition expenses. Excluding these items, the expense ratio actually fell .6 point for the three month period ended September 30, 2003.

The Assumed Agency Business' net earned premiums increased \$17.4 million in the three month period ended September 30, 2003 as compared to the three month period ended September 30, 2002. In the third quarter 2002, we recorded ceded reinsurance to Inter-Ocean retroactive to January 1, 2002. In 2002 and the first half of 2003, we ceded 90% of that business under the reinsurance agreement. Earned premiums excluding the effect of this agreement declined \$9.8 million, or 24.2%, due primarily to a reduction in business volume partially offset by rate increases. The policies in force on personal automobile policies declined 15.0% from 131,000 at September 2002 to 110,000 at September 2003. The decline in policy counts is due primarily to actions taken in late 2002 to discontinue writing inadequately priced business in certain focus states as well as decisions by insureds not to renew. In addition, 14,000 of the decline in policies in force is a result of the non-renewal of business in New Jersey that began in October 2002. The loss and LAE ratios improved compared to the three month period ended September 30, 2002, due primarily to the effects of the Inter-Ocean reinsurance agreement. Excluding the effects of this agreement, the loss and LAE ratios still showed improvement, dropping from 81.6% for the third quarter of 2002 to 80.5% for the same period of 2003, as a result of increases in rates, lower frequency of claims per auto insured and moderate increases in the average cost per claim, as well as a reduction in volume in non-focus states, such as New Jersey, which were typically unprofitable. The expense ratio increased 61.5 points primarily due to the effect of the Inter-Ocean reinsurance agreement. Excluding the effects of this agreement, the expense ratio improved by 6.7 points, dropping from 27.8% in the third quarter of 2002 to 21.1% for the same period in 2003, primarily as a result of expense savings from consolidation efforts.

*Nine Months Ended September 30, 2003 compared to Nine Months Ended September 30, 2002.* The NSA Group's net earned premiums fell \$60.6 million, or 12.2%, in the nine month period ended September 30, 2003 compared to the nine month period ended September 30, 2002 primarily as a result of actions taken to discontinue writing inadequately priced business in certain focus states. Earned premiums excluding the effect of the Inter-Ocean reinsurance agreement declined 13.6% to \$98.8 million, due primarily to a reduction in business volume partially offset by rate increases. The loss and LAE ratio deteriorated for the nine-month period ended September 30, 2002 from the same period in 2002 by 0.5 points due to the Inter-Ocean reinsurance agreement. Excluding the effects of the Inter-Ocean reinsurance agreement, the loss and LAE ratio improved 2.2 points. The

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expense ratio improved by 4.8 points in the first nine months of 2003 compared to the nine months ended September 30, 2003 as a result of the impact of the ceding commission from the Inter-Ocean reinsurance agreement, as well as savings from consolidation efforts taken. Excluding the effect of the Inter-Ocean agreement, the expense ratio improved 1.0 point from 22.2% in the nine months ended September 30, 2002 to 21.2% in the same period in 2003.

The Assumed Agency Business net earned premiums decreased \$15.8 million, or 18.7%, for the nine month period ended September 30, 2003 compared to the nine month period ended September 30, 2002 primarily as a result of a reduction in business volume. Earned premiums excluding the effect of the Inter-Ocean reinsurance agreement declined \$18.7 million, or 15.4%, due primarily to a reduction in business volume partially offset by rate increases. The loss and LAE ratios for the Assumed Agency Business improved from 85.0% in the first nine months of 2002 to 79.4% for the same period in 2003, as a result of increases in rates, lower frequency of claims per auto insured and moderate increases in the average cost per claim as well as a reduction in business in the non-focus states. Excluding the effects of the Inter-Ocean reinsurance agreement, the loss and LAE ratio improved from 78.6% to 74.1%, as a result of increases in rates, lower claim frequency and moderate increases in average claim costs. The expense ratio decreased 1.9 points from 24.9% for the first nine months of 2002 to 23.0% for the same period in 2003. Excluding the effects of the Inter-Ocean reinsurance agreement, the expense ratio improved by 1.4 points, dropping from 27.9% in the first nine months of 2002 to 26.5% from the same period in 2002. The reduction in the expense ratio is due substantially to expense savings from consolidation efforts.

*2002 compared to 2001.* Our net earned premiums decreased \$271 million (30%) during 2002 due primarily to the Inter-Ocean reinsurance agreement, effective April 1, 2001, under which we ceded 90% of the personal automobile physical damage business written by our insurance subsidiaries during 2002. Excluding the effect of this agreement, net earned premiums declined approximately 9%, reflecting lower business volume partially offset by the impact of rate increases. Policies in force declined 16% from approximately 734,000 on December 31, 2001 to 616,000 on December 31, 2002. The decline in policy counts is due to rate increases and actions taken to reduce business in certain non-focus or non-profitable states as well as decisions by insureds not to renew. During 2002, we increased personal auto rates about 12% over rates in effect at year end 2001. Underwriting expenses in 2002 include the effect of \$130.4 million in ceding commissions earned under the Inter-Ocean reinsurance agreement. Commissions earned under this agreement generally vary directly with the loss and LAE ratio on the business ceded. Accordingly, Infinity's expense ratio reflects the benefit of strong underwriting results in the business ceded to Inter-Ocean. Overall, our combined ratio improved 10.2 points over 2001 due primarily to recent rate increases. Excluding the effect of the Inter-Ocean agreement, our combined ratio for 2002 was 95.9% compared to 103.7% in 2001.

Net earned premiums of the Assumed Agency Business decreased \$43 million (28%) in 2002 reflecting the impact of the Inter-Ocean reinsurance agreement, effective January 1, 2002, under which 90% of Great American's personal automobile physical damage business written through independent agents was ceded. Excluding the effect of this agreement, net earned premiums increased \$12.1 million (8%) reflecting rate increases implemented in the later part of 2001, partially offset by a reduction in volume from certain unprofitable business. The combined ratio was flat as an increase in prior year development was offset by the shift away from underperforming business and the increase in rates over the past year. Underwriting expenses fell \$16.6 million in 2002 compared to 2001 reflecting Great American's \$19.7 million ceding commission earned on premiums ceded under the Inter-Ocean reinsurance agreement.

*2001 compared to 2000.* The NSA Group's net earned premiums decreased \$127 million (12%) in 2001 due primarily to the automobile physical damage reinsurance agreement discussed above. Excluding the effect of the agreement, net earned premiums were flat in 2001. Policies in force declined 19% as some customers decided not to renew policies at higher rates. The NSA Group increased personal auto rates approximately 15% in 2001. The 2001 combined ratio improved 5.6 points compared to 2000 as the effect of rate increases in 2001 and 2000 more than offset a \$5.1 million charge to write-off policy-processing software that was not in use. The NSA Group's underwriting expenses decreased \$27 million (12%) during 2001 as the \$38 million ceding commission earned on the reinsurance agreement more than offset increased salaries and employee-related expenses.

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The \$21 million (16%) increase in net earned premiums for the Assumed Agency Business was due primarily to volume growth across numerous states stemming from a 10% increase in new agents. The increase in the combined ratio resulted from insufficient pricing on new business. The Assumed Agency Business's underwriting expenses increased \$3.6 million (9%) in 2001 primarily due to increased commissions on higher premiums.

### ***Investment Income***

Changes in Infinity's net investment income reflect fluctuations in market rates and changes in average invested assets. Fluctuations in average invested assets reflect primarily the timing of dividends and capital contributions as the NSA Group's capital requirements and the cash needs of the holding company for the NSA Group change.

*September 30, 2003 compared to September 30, 2002.* Net investment income decreased \$610,000 and \$5.5 million for the third quarter and first nine months ended September 30, 2003 versus the comparable periods in 2002 due to lower yields available for newly invested funds, and to a lesser extent due to a reallocation to tax advantaged securities, partially offset by an increase in average invested assets of 5% and 12%, respectively, for the three and nine month periods ended September 30, 2003. Average invested assets increased as a result of the transfer at January 1, 2003 of \$125.3 million of securities and cash in conjunction with Infinity's assumption of insurance liabilities of the Assumed Agency Business, as well as proceeds received in July 2003 from the term loan.

*2002 compared to 2001.* Net investment income decreased \$14.0 million in 2002 compared to 2001 due primarily to (i) a \$4.6 million increase in interest expense (included in net investment income) on funds held from the aforementioned automobile reinsurance agreement, (ii) a decrease in interest rates and (iii) an 8% decrease in average invested assets. Average invested assets decreased due primarily to dividends paid in the fourth quarter of 2001 and the last three quarters of 2002.

*2001 compared to 2000.* Net investment income increased \$5.9 million in 2001 due primarily to a 12% increase in average invested assets in fixed maturity securities, partially offset by \$3.1 million in interest expense on funds held from the Inter-Ocean reinsurance agreement discussed above. Average invested assets increased due primarily to a capital contribution received in the fourth quarter of 2000.

**Table of Contents****Realized Gains (Losses) on Investments.**

September 2003 compared to September 2002. Infinity recorded impairments for unrealized losses deemed other-than-temporary and realized gains on sales and disposals as follows (before tax, in thousands):

	Three months ended		
	September 30, 2003		
	Impairments on securities	Realized gains	Total realized gains
	held	on sales	(losses)
Fixed maturities	\$	\$ 1,058	\$ 1,058
Equities	(486)	189	(297)
<b>Total</b>	<b>\$ (486)</b>	<b>\$ 1,247</b>	<b>\$ 761</b>

  

	Nine months ended		
	September 30, 2003		
	Impairments on securities	Realized gains	Total realized gains
	held	on sales	(losses)
Fixed maturities	\$ (2,963)	\$ 4,693	\$ 1,730
Equities	(517)	70	(447)
<b>Total</b>	<b>\$ (3,480)</b>	<b>\$ 4,763</b>	<b>\$ 1,283</b>

Total realized gains (losses) on investments include provisions for other-than-temporary impairment of securities still held of \$1.2 million and \$7.7 million for the three and nine months ended September 30, 2002, respectively. The impairments in the 2002 period related primarily to fixed income securities from firms in the telecommunications and airline industries. The impairments in the 2003 period were primarily for fixed income securities from firms in the airline industry.

Until September 2003, we owned warrants to buy common stock of a publicly traded company. Under generally accepted accounting principles, these investments are considered derivatives and are marked to market resulting in realized gains and losses. Realized gains (losses) on investments included a gain of \$111,000 and a loss of \$84,000 for the first nine months of 2003 and 2002, respectively to adjust the carrying value of these warrants to their market value. These warrants were sold in the third quarter of 2003 with no additional gain or loss incurred.

*2002 compared to 2001.* Realized gains (losses) on investments include provisions for other than temporary impairment of securities still held of \$9.4 million in 2002 and \$16.2 million in 2001. Increased impairment charges in recent years reflect, among other things, a rise in corporate defaults in the marketplace.

Realized gains (losses) on investments include a loss of \$281,000 in 2002 to adjust the carrying value of warrants considered derivatives to their market value of \$883,000 at December 31, 2002.

*2001 compared to 2000.* Realized gains (losses) on investments include provisions for other than temporary impairment of securities still held of \$16.2 million in 2001 and \$3.0 million in 2000.

### ***Interest Expense***

Interest expense was accrued at a fixed rate of 8.5% on the \$55 million note due to AFG until its repayment in mid-July, 2003 using a portion of the proceeds of the \$200 million term loan. This debt instrument accrues

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interest at a variable rate, which averaged 3.6% from the date of issue through September 30, 2003. The risk of variability in future interest expense is partially hedged by the interest rate swap described in Note 7 to our September 30, 2003 consolidated financial statements included in this prospectus.

Interest expense was (in thousands):

	<b>Three months ended September 30, 2003</b>	<b>Nine months ended September 30, 2003</b>
\$55 million note due to AFG	\$ 196	\$ 2,546
\$200 million term loan	1,600	1,600
Interest rate swap	249	249
<b>Total</b>	<b>\$ 2,045</b>	<b>\$ 4,395</b>

**Other Operating and General Expenses**

*September 2003 compared to September 2002.* Corporate general and administrative expenses for the three and nine month periods ended September 30, 2003 include costs associated with the new public parent company beginning in February 2003.

*2002 compared to 2001.* Other operating and general expenses for 2001 include goodwill amortization of \$2.2 million. Under SFAS No. 142, which was implemented January 1, 2002, goodwill is no longer amortized. Excluding 2001 goodwill amortization, other operating and general expenses increased \$9.2 million due primarily to a \$5.3 million litigation settlement.

*2001 compared to 2000.* Other operating and general expenses for the NSA Group decreased \$4.6 million (19%) due primarily to a \$3.7 million reduction in corporate litigation expenses.

**Income Taxes**

Our effective tax rate was 34% in the nine months ended September 30, 2003, 35% in 2002, 38% in 2001 and 35% in 2000. See Note H to our historical audited financial statements for an analysis of items affecting our effective tax rate.

**Equity in Affiliate Losses**



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Equity in net losses of affiliates for 2000 represents our proportionate share of the results of Chiquita Brands International, an affiliate of AFG during those periods. Chiquita reported net losses attributable to common shareholders of \$112 million in 2000. In 2001, we suspended accounting for Chiquita under the equity method due to Chiquita's pending restructuring.

Equity in net losses of affiliates for 2000 also includes a \$14.2 million pretax charge to writedown of our investment in Chiquita to quoted market value at December 31, 2000.

### *Recent Accounting Standards*

In July 2001, the Financial Accounting Standards Board issued SFAS No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets. Under SFAS No. 141, business combinations initiated after June 30, 2001 are required to be accounted for using the purchase method of accounting. Under SFAS No. 142, goodwill is no longer amortized beginning January 1, 2002, but is subject to an impairment test at least annually. We completed the transitional test for impairment in 2002 and 2003 with no writedown required. Other operating and general expenses for the NSA Group include goodwill amortization of \$2.2 million in both 2001 and 2000. The carrying value of goodwill at December 31, 2001, was \$70.3 million for the NSA Group and \$5 million for the Assumed Agency Business.

**Table of Contents****Operations of AFG Personal Segment**

The following information concerning AFG's Personal segment has been supplied to us by AFG. The NSA Group and the Assumed Agency Business comprised approximately 83% of AFG's Personal segment based on earned premiums in 2002. AFG's segment also included personal lines businesses that sell directly to consumers, as well as certain foreign personal lines businesses, neither of which were transferred to Infinity. The results of operations of the AFG Personal segment are different from our results of operations. The following discussion of the underwriting results of AFG's Personal reporting segment is presented to provide the historical financial performance for this AFG segment.

GAAP premiums and underwriting ratios for AFG's Personal segment were as follows (dollars in millions) for the three-year period preceding our initial public offering of common stock:

	<b>Year Ended December 31,</b>		
	<b>2002</b>	<b>2001</b>	<b>2000</b>
Net Written Premiums	\$ 836	\$ 1,040	\$ 1,311
Net Earned Premiums	905	1,183	1,270
Loss and LAE Ratio	83.1%	82.1%	83.6%
Underwriting Expense Ratio	16.7%	25.8%	25.0%
Combined Ratio	99.8%	107.9%	108.6%

*2002 compared to 2001.*

The AFG Personal segment's net written premiums decreased 20% due primarily to the Inter-Ocean reinsurance agreement, effective April 1, 2001, under which 90% of the auto physical damage insurance written through the agency channel is ceded. Excluding the effect of this agreement, net written premiums declined about 4% due primarily to intentional reductions in new business volume in certain non-core markets and through the direct channel, partially offset by the effect of continuing rate increases and volume growth in target markets. Rate increases implemented in 2002 were approximately 10%. Due primarily to rate increases and a \$12.6 million reduction in marketing and media costs of the direct business, the Personal group's combined ratio improved by 8.1 points compared to 2001.

*2001 compared to 2000*

The AFG Personal segment's 21% decline in net written premiums in 2001 reflects the impact of the Inter-Ocean reinsurance agreement effective April 1, 2001. Excluding the effect of this agreement, the Personal segment's net written premiums declined about 4% in 2001 as lower business volume was partially offset by the impact of rate increases.

The segment implemented rate increases of about 14% in 2001. As a result of these rate increases, the loss and LAE ratio improved 1.5 points reflecting a 4.1 point improvement in the agency businesses, partially offset by deterioration in the loss and LAE of the direct business. The deterioration in the loss and LAE ratio of the direct business was the result of the absence of favorable development that occurred in 2000.



**Table of Contents****BUSINESS**

We are a national provider of personal automobile insurance with an emphasis on nonstandard auto insurance. Nonstandard auto insurance provides coverage to drivers who, due to their driving record, age or vehicle type, represent higher than normal risks and pay higher rates for comparable coverage. We also write standard and preferred personal auto insurance, nonstandard commercial auto insurance and complementary personal lines insurance products.

Our products are offered primarily through a network of approximately 14,000 independent agencies and strategic partnerships. Based on data published by A.M. Best, we believe we are the second largest provider of nonstandard auto coverage through independent agents in the United States, behind only The Progressive Corporation. While licensed to write insurance in every state, we focus on 15 states which we believe provide the greatest opportunity for profitable growth.

In 2002, we generated, on a pro forma basis, \$988.9 million in gross premiums written, \$687.3 million in net premiums written and had net earnings of \$36.3 million. For the nine months ended September 30, 2003, we generated \$734.8 million in gross premiums written, \$622.8 million in net premiums written and had net earnings of \$38.8 million. For the year ended December 31, 2002 and the nine months ended September 30, 2003, approximately 95% of our business was personal auto and the remaining 5% was homeowners, umbrella liability, boat owners and nonstandard commercial auto coverages. While there is no precise, industry-recognized definition of nonstandard auto insurance, we estimate that, for the year ended December 31, 2002 and the nine months ended September 30, 2003, approximately four-fifths of our personal auto business was nonstandard coverage. At September 30, 2003, we had total assets of \$2.0 billion, liabilities of \$1.5 billion and shareholders equity of \$442 million.

**Our Strengths**

We believe that we are well positioned to compete in today's market through various strengths that should enable us to build upon our history of favorable underwriting results. The following table compares our statutory combined ratio in past years with those of the personal lines insurance industry as a whole. The statutory combined ratio is the sum of the loss ratio (the ratio of losses and loss adjustment expenses to net earned premiums) and the expense ratio (when calculated on a statutory accounting basis, the ratio of underwriting expenses to net written premiums). When the combined ratio is under 100%, underwriting results are generally considered profitable; when the ratio is over 100%, underwriting results are generally considered unprofitable. The combined ratio does not reflect investment income, other income or federal income taxes.

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1998-2002</u>	<u>1993-2002</u>
Infinity	95.9%(1)	92.7%	104.6%	108.7%	98.7%	97.0%	100.9%	101.4%
Industry	99.7%(2)	105.3%	110.9%	109.9%	104.5%	102.7%	106.6%	105.2%
Percentage Points Better Than Industry	3.8%	12.6%	6.3%	1.2%	5.8%	5.7%	5.7%	3.8%

(1) Combined ratio through September 30, 2003.

(2) Combined ratio through June 30, 2003, from A.M. Best. Industry data through September 30, 2003 are not yet available.

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Statutory combined ratios shown here are obtained from A.M. Best. A.M. Best compiles these insurance industry statistics based on financial statements that are prepared on a statutory accounting basis and filed with the various state insurance departments. We are not aware that similar industry statistics are available on a GAAP basis.

***Our Product Focus.*** We are focused on writing personal automobile insurance through independent agents. We believe this focus has helped us become one of the largest writers of nonstandard auto insurance with a

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selected presence in the standard and preferred segments. Our low cost, value added and premier policies are tailored to meet a customer's particular needs and enable us to service niche markets across the entire range from nonstandard to preferred. For example, we have developed programs to focus on the Southern California Latino market, which we believe have given us an important position in a growth market.

***Our Expertise in Risk Segmentation.*** We believe that appropriate risk segmentation is the primary way in which we can maximize underwriting performance. We evaluate risks in great detail and use sophisticated proprietary databases and risk models to offer each driver the appropriate rate. For example, while many insurers evaluate drivers' ages based on broad groupings, we look at exact age to reflect differences in risk more accurately. In addition to varying rates, we offer coverage terms tailored to unique market needs.

***Our Claims Handling Capability.*** We believe that properly handling claims controls the amounts we pay to settle claims and increases customer and agent satisfaction. We employ approximately 1,200 claims personnel located throughout the United States, and we provide a 24-hour, seven days per week toll-free service for our customers to report claims. We use predominantly our own local adjusters who typically respond to claims within 24 hours of a report. This approach allows us to consistently apply our philosophy of paying valid claims promptly while denying non-meritorious claims.

***Our Agency Relationships.*** We have a long-term commitment to independent agencies and see them as a very effective, variable cost distribution channel for personal automobile insurance. We have active relationships with approximately 14,000 independent agencies whom we support with competitive compensation programs, agency interface technology and an array of support programs.

***Our Low Cost Structure.*** Controlling expenses allows us to price competitively and achieve better underwriting returns. From 1998 through 2002, our ratio of underwriting expenses to premiums has averaged 23.2%, which is 4.4 points better than the personal lines industry average of 27.6% for the same period. Ongoing consolidation of our historically separate business units has generated savings during 2003 and, with the further planned integration in 2004 of our separate information systems, is expected to generate additional expense reductions and efficiencies in future years.

***Our Management Experience.*** We have an experienced management team. James R. Gober, Chief Executive Officer and President, has been with our companies for 25 years. Since 1991, Mr. Gober had been the principal operating officer of some or all of the companies within the NSA Group. John R. Miner, Executive Vice President, spent five years with Chubb and had been with Great American for 14 years and served as President of Great American's Personal Lines Division. Roger Smith, Senior Vice President and Chief Financial Officer, has served in various executive capacities in the financial and corporate development areas with Great American for over 15 years. Joseph A. Pietrangelo, Senior Vice President - Claims, has over 16 years of experience in personal automobile insurance, including as head of our claims division for the past two years and service in various capacities with Zurich/Farmers Personal Insurance and The Progressive Corporation.

***Our Financial Strength.*** We have a conservative investment portfolio. At September 30, 2003, the portfolio consisted of 98% fixed maturity securities, 93% of which are investment grade. A.M. Best has assigned our insurance subsidiaries an A (Excellent) rating which, according to A.M. Best, reflects our solid capitalization, favorable overall operating performance, adequacy of loss reserves and strong nonstandard auto market presence. A (Excellent) is the third highest of A.M. Best's 16 ratings behind A++ and A+ (Superior). These ratings do not represent a recommendation to buy, sell or hold securities. We can give no assurance that we will maintain our current ratings.

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### **Our Strategy**

Our goal is to maximize shareholder value by focusing on underwriting profitability and long-term return on equity. We will pursue this goal through a strategy of:

**Product focus.** We will focus on personal automobile insurance where we expect the nonstandard business to benefit from an improved price environment and where we will have a selected presence in standard and preferred segments.

**Geographic focus.** We will focus on the states that we believe offer us the greatest opportunity for profitable growth. Target states will be distinguished by their personal auto insurance market size and legal and regulatory environments that we view as conducive to the profitability of our business.

**Controlled operating expenses.** We will manage our cost structure to be competitive and will remain committed to reducing costs further through consolidation designed to eliminate redundancies and achieve greater efficiencies.

**Disciplined pricing.** We will demand adequate rates to achieve underwriting profitability and are willing to forego volume if necessary to achieve our profit objectives. We will remain committed to setting individual rates more accurately than our competitors.

**Field claim handling.** We will emphasize prompt response to claims by our own local claim adjusters in a manner that will continue to deliver good service to our customers and provide effective control of the claim resolution process.

**Distribution focus.** We will focus on the independent agent channel as a cost-effective system to access the personal auto insurance market and provide us a flow of customers.

### **The Personal Automobile Market**

Personal auto insurance is the largest line of property and casualty insurance accounting for approximately 37% or \$140 billion of the total \$377 billion of annual industry premiums in 2002. Personal auto insurance provides coverage to drivers for liability to others for both bodily injury and property damage and for physical damage to an insured's own vehicle from collision and other perils. Personal auto insurance is comprised of preferred, standard and nonstandard risks. Nonstandard insurance is intended for drivers who, due to their driving record, age or vehicle type, represent a higher than normal risk. As a result, customers that purchase nonstandard auto insurance generally pay higher premiums for similar coverage than drivers qualifying for standard or preferred policies. While there is no established industry-recognized demarcation between nonstandard policies and all other personal auto policies, we believe that nonstandard auto risks generally constitute between 15% and 20% of the personal automobile insurance market, with this range fluctuating according to competitive conditions in the market. Approximately one-third of all personal automobile insurance is sold by independent agents.

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The personal auto insurance industry is cyclical, characterized by periods of price competition and excess capacity followed by periods of high premium rates and shortages of underwriting capacity. In the late 1990s, many automobile insurers attempted to capture more business by reducing rates. We believe that these industry-wide rate reductions combined with increased severity trends during the period contributed to the deterioration of industry loss ratios in the years 1999 through 2001. We began implementing rate increases in early 2000. Since that time, most of the industry, including some of the largest companies, have begun to raise rates and tighten underwriting standards in order to address poor results. Other insurance companies have recently withdrawn from the market because of their inability to compete successfully, impaired capital positions, or because of a decrease in the availability of reinsurance.



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### **Our Products**

*Personal Automobile* is our primary insurance product. It provides coverage to individuals for liability to others for bodily injury and property damage and for physical damage to an insured's own vehicle from collision and various other perils. In addition, many states require policies to provide for first party personal injury protection, frequently referred to as no-fault coverage. We offer personal automobile insurance to nonstandard, standard and preferred customers. Personal automobile insurance accounted for approximately 95% of our gross written premiums for the year ended December 31, 2002 and the nine months ended September 30, 2003.

*Nonstandard Commercial Automobile* provides coverage to businesses for liability to others for bodily injury and property damage and for physical damage to businesses' vehicles from collision and various other perils. We offer nonstandard commercial automobile insurance to businesses who employ one or more nonstandard risk drivers. We target businesses with fleets of 12 or fewer vehicles and generally avoid businesses which are involved in what we consider to be hazardous operations or interstate commerce. Nonstandard commercial automobile insurance accounted for approximately 4% of our gross written premiums for the year ended December 31, 2002 and the nine months ended September 30, 2003.

*Homeowners and Other* includes homeowners insurance and several other personal lines insurance products. We write homeowners insurance for dwellings, condominiums and rental property contents on a limited basis in selected markets. Homeowners insurance provides protection against losses from a wide variety of perils, as well as coverage for liability arising from ownership or occupancy. We also write coverage on a limited basis for personal watercraft, personal articles, such as jewelry, and umbrella liability protection. Homeowners and other insurance accounted for less than 1% of our gross written premiums for the year ended December 31, 2002 and the nine months ended September 30, 2003.

### **Pricing and Product Management**

The pricing segmentation approach that we utilize requires the extensive involvement of product managers who are responsible for the underwriting profitability of a specific state or region with the direct oversight of rate level structure by our most senior managers. Product managers work closely with our pricing and product development departments to generate rate level indications and other relevant data. This data enables our product managers to change the rate structure by evaluating detailed information, such as loss experience based on driver characteristics, financial responsibility scores and make/model of vehicles. Product managers are also responsible for obtaining approval of our rate filings from state insurance departments. We believe this approach has permitted us to respond more quickly than our competitors to adverse loss trends such as those experienced in 1999 and 2000 and to obtain faster approval for our filings. Unlike many of our competitors, we reacted by increasing personal auto rates across the NSA Group and Assumed Agency Business by 14% in 2000, again in 2001, 12% in 2002 and 2% in the nine months ended September 30, 2003. We have benefited from our rate actions and the price firming taking place in the market given the more recent rate actions by many of our competitors.

Beyond the detailed pricing analysis, product managers are responsible for developing innovative products which meet the needs of our customers and provide us a competitive advantage in the marketplace. We have had success in designing products that provide the basic required coverage for our nonstandard customers, and products that include expanded coverage for our preferred customers.

### **Distribution and Marketing**

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We distribute our products primarily through a network of approximately 14,000 independent agencies and strategic partnerships. Independent agencies were responsible for approximately 97% of our gross written premiums for the year ended December 31, 2002 and the nine months ended September 30, 2003. In those

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periods, no one independent agency accounted for more than 2% of our gross written premiums, and only two agencies accounted for more than 1% of our gross written premiums. Another mode of distribution includes relationships, or strategic partnerships, with some non-affiliated property and casualty insurers that have their own captive agency forces. These companies usually provide standard and preferred auto coverage through one of their own companies while utilizing our companies for their nonstandard risks. We believe these are mutually beneficial relationships since our partners gain access to our nonstandard auto expertise and we gain access to a new distribution channel. This channel represented approximately 3% of gross written premiums for the year ended December 31, 2002 and the nine months ended September 30, 2003.

We hold licenses to write auto insurance in all 50 states, but we are committed to growth in 15 focus states that we believe provide the greatest opportunity for profit considering the market size and the current legal and regulatory environment. We classify the states in which we operate into four categories:

**Franchise States** We believe these states provide us with the best opportunity for profitable growth. They are California, Florida, Georgia, Connecticut and Pennsylvania.

**Resource States** We intend to strengthen operations in these ten states and implement the operating model currently in place in California which stresses our strategies discussed above. Combined with our Franchise States, these states represent our Focus States.

**Maintenance States** We are seeking to maintain our renewal business in these seven states while we increase rates to achieve underwriting profitability. We are accepting no new business in these states due to what we perceive to be the current lack of opportunity for profitable growth.

**Exit States** We have discontinued or intend to discontinue writing insurance in these 28 states.

The following table sets forth the distribution of our gross premiums written by state for the Franchise states, as well as the other categories, as a percent of total gross written premiums for the periods indicated:

	Nine Months Ended September 30, 2003	Year Ended		
		December 31,		
		2002	2001	2000
<b>Franchise States:</b>				
California	46%	34%	25%	23%
Florida	9%	10%	10%	10%
Connecticut	7%	8%	8%	7%
Pennsylvania	7%	7%	7%	6%
Georgia	6%	7%	8%	8%
<b>Sub-Total Franchise States</b>	<b>75%</b>	<b>66%</b>	<b>58%</b>	<b>54%</b>
Next 10 Resource States	12%	14%	17%	17%
<b>Sub-Total 15 Focus States</b>	<b>87%</b>	<b>80%</b>	<b>75%</b>	<b>71%</b>
Maintenance States	10%	13%	14%	17%

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Exit States	3%	7%	11%	12%
All States	100%	100%	100%	100%

Over the last several years in California, we have been successful in growing our business profitably at very attractive combined ratios. It is this California business model that we are expanding into our other Franchise States in 2003 and Resource States in 2004 and beyond through a one state at a time implementation plan. For example, in late 2002, we determined that the rates charged for several of our programs in Florida and Georgia were

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inadequate to generate satisfactory underwriting results. We therefore took action to discontinue writing new business in those states and others until we could put in place programs with rates we believed to be adequate. As a result, the premium volume in these two states was reduced during the first three quarters of 2003, as shown in the following table:

	<b>Change in Gross Premiums from Comparable Period in Prior Year</b>			
	<b>Three Months</b>	<b>Three Months</b>	<b>Three Months</b>	<b>Twelve Months</b>
	<b>Ended</b>	<b>Ended</b>	<b>Ended</b>	<b>Ended</b>
	<b>September 30, 2003</b>	<b>June 30, 2003</b>	<b>March 31, 2003</b>	<b>December 31, 2002</b>
Franchise States:				
California	39%	17%	21%	26%
Florida	(1)%	(24)%	(25)%	(2)%
Connecticut	(5)%	(10)%	(24)%	(11)%
Pennsylvania	(18)%	(22)%	(22)%	6%
Georgia	(16)%	(18)%	(14)%	(15)%
<b>Subtotal Franchise</b>	<b>14%</b>	<b>1%</b>	<b>0%</b>	<b>8%</b>
Resource States	(18)%	(30)%	(32)%	(19)%
<b>Subtotal Focus States</b>	<b>9%</b>	<b>(5)%</b>	<b>(7)%</b>	<b>2%</b>
Maintenance States	(36)%	(34)%	(29)%	(15)%
Exit States	(69)%	(66)%	(59)%	(36)%
<b>All States</b>	<b>(3)%</b>	<b>(13)%</b>	<b>(14)%</b>	<b>(5)%</b>

During the second and third quarters of 2003, new rates and insurance policy forms were filed and approved in Florida, Georgia and Pennsylvania. The rate of premium volume shrinkage has decreased for Florida and Pennsylvania in the three month period ended September 30, 2003 as compared to the previous two quarters. For Florida, Georgia and Pennsylvania, premiums for the third quarter of 2003 have increased from those of the second quarter of 2003. For the Resource States the business continued to decline in 2003 as a result of rate actions taken to achieve rate adequacy. For the Maintenance States, no new business is currently being written, and we do not plan to write new business until we believe we can achieve adequate rates. For the Exit States, which represent only 3% of the total gross written premiums for the nine month period ended September 30, 2003, we are taking action to continue to reduce the premium volume further.

For the nine month period ended September 30, 2003, excluding the effects of the Inter-Ocean reinsurance agreement the combined ratio in our Franchise and Resource States was 86% while our overall combined ratio was 95%.

Our business development department is responsible for the distribution and sale of our products through our independent agencies and strategic partners. This department is split into two key areas, field operations and corporate business development. The responsibilities of our field business development representatives include selecting agencies and strategic partners for appointment, training them to sell our products, and monitoring their operations to ensure compliance with our production and profitability standards. While most of the field activity occurs face-to-face in the producer's office, we have had success with other approaches such as group seminars that focus on promoting our products and conducting training for our agents.

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Our corporate business development staff is responsible for our branding initiatives, cooperative advertising with our independent agents, sales promotions and agents incentives. In addition, this team is actively engaged in building agency relationships via telephone, e-mail, fax and direct mail.

We believe that our ability to develop strong and mutually beneficial relationships with our agents is paramount to our success. We foster our agent relationships by providing them our software applications along with programs and services designed to strengthen and expand their marketing, sales and service capabilities. Our internet-based software applications provide many of our agents with real-time underwriting, claims and

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policy information. We believe the array of services that we offer to our agents adds significant value to their businesses. For example, our PASS Program (Providing Agents Service and Support) is an incentive-based program through which our agents earn savings on service and support needs including technology, training, financial services, office supplies, advertising, promotion and travel. In addition, our Infinity University offers education courses to our agents to assist them in achieving growth and success in their businesses.

We focus particular attention on developing relationships with Latino agents, especially in Southern California. Over the past decade, Latinos have been the fastest growing segment of the United States population according to U.S. Census Bureau data. For example, Latinos constitute an estimated 47% of the population in Los Angeles County. Over the past decade, we have actively developed close relationships with Latino agents by supporting their businesses and customers in their local communities. We have developed products and services that support their special needs and interests such as translating important documents to Spanish and providing bilingual customer service and claims personnel. We consider our position in this unique niche of the market, including our Infinity brand, to be a significant competitive advantage.

## **Claims Handling**

Our claims organization employs approximately 1,200 people and has 40 field branch offices and three regional offices. We provide a 24-hour, seven days per week toll-free service for our customers to report claims. We use predominantly our own local adjusters who typically respond to claims within 24 hours of a report.

We are committed to the field handling of claims and believe it provides better service to our customers and better control of the claim resolution process than alternative methods. We open claims branch offices in areas where we believe the volume of business will support them. Customer interactions can occur with generalists (multi-line claim representatives) and specialists (staff appraisers, field casualty representatives and special investigators) based on local market volume, density and performance. Nationally, over 65% of our claims are handled face-to-face. We strive for accuracy, consistency and fairness in our claim resolutions. We have an auditing program which measures performance in investigations, damage documentation and other relevant areas.

Our claims organization is committed to defending against non-meritorious claims. This is done through referrals to our special investigations team. This team, made up of claims and former law enforcement professionals, works in concert with field operations to resolve questionable claims.

The recent consolidation of our separate claims departments has allowed us to gain economies of scale and to eliminate redundancies. This provides us greater consistency in the claims handling process. The consolidation of our claims departments has reduced annual claims handling costs by approximately \$6.5 million since the consolidation began in 2002.

## **Loss and Loss Adjustment Expense Reserves**

We estimate liabilities for the costs of losses and loss adjustment expenses for both reported and unreported claims based on historical trends adjusted for changes in loss cost trends, underwriting standards, policy provisions, product mix and other factors. Estimating the liability for unpaid losses and loss adjustment expense is inherently judgmental and is influenced by factors which are subject to significant variation. We monitor items such as the effect of inflation on medical, hospitalization, material repair and replacement costs, general economic trends and the legal environment. While the ultimate liability may be greater or lower than recorded loss reserves, the reserve tail for personal auto coverage is

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shorter than that associated with many other property and casualty coverages and can, therefore, be established with less uncertainty than coverages having longer reserve tails.

We review loss reserve adequacy quarterly. Our independent auditors also review the adequacy of our loss reserves as part of their audit procedures. Our reserves are also certified to state regulators annually. Reserves are adjusted as additional information becomes known. Such adjustments are reflected in current year operations.



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The following tables present the development of Infinity's and the Assumed Agency Business' loss reserves, net of reinsurance, on a GAAP basis for calendar years 1992 through 2002. The top line of each table shows the estimated liability for unpaid losses and loss adjustment expense recorded at the balance sheet date for the indicated years. The next line, captioned Liability for Unpaid Losses and Loss Adjustment Expenses as re-estimated at December 31, 2002, shows the re-estimated liability as of December 31, 2002. The remainder of the table presents intervening development as percentages of the initially estimated liability. The development results from additional information and experience in subsequent years. The middle line shows a cumulative deficiency (redundancy) which represents the aggregate percentage increase (decrease) in the liability initially estimated. The lower portion of the table indicates the cumulative amounts paid as of successive periods as a percentage of the original loss reserve liability.

**INFINITY**

	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>
Liability for unpaid losses and loss adjustment expenses (in millions):											
As originally estimated	\$ 262	\$ 385	\$ 489	\$ 569	\$ 511	\$ 525	\$ 589	\$ 543	\$ 627	\$ 608	\$ 571
As re-estimated at December 31, 2002	230	347	494	567	532	534	544	508	634	609	N/A
<b>Liability re-estimated:</b>											
One year later	89.0%	89.6%	96.8%	97.8%	99.5%	100.8%	95.0%	95.3%	98.5%	100.2%	
Two years later	87.0%	89.3%	100.4%	98.6%	101.9%	103.3%	93.6%	92.9%	101.1%		
Three years later	87.5%	89.7%	101.1%	99.2%	104.7%	102.5%	91.0%	93.6%			
Four years later	87.3%	90.2%	100.9%	100.3%	104.3%	100.9%	92.5%				
Five years later	87.8%	90.1%	101.5%	100.0%	103.5%	101.7%					
Six years later	88.0%	90.4%	101.3%	99.5%	103.9%						
Seven years later	88.3%	90.6%	100.9%	99.7%							
Eight years later	88.4%	90.1%	101.0								