

First American Financial Corp
Form 10-Q
April 23, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2015

OR

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

For the transition period from _____ to _____

Commission file number 001-34580

FIRST AMERICAN FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

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Incorporated in Delaware (State or other jurisdiction of incorporation or organization)	26-1911571 (I.R.S. Employer Identification No.)
1 First American Way, Santa Ana, California (Address of principal executive offices)	92707-5913 (Zip Code)

(714) 250-3000

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer 1

Non-accelerated filer 1 (Do not check if a smaller reporting company) Smaller reporting company 1

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY

PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

On April 17, 2015, there were 108,397,408 shares of common stock outstanding.

FIRST AMERICAN FINANCIAL CORPORATION

AND SUBSIDIARY COMPANIES

INFORMATION INCLUDED IN REPORT

PART I: FINANCIAL INFORMATION

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Items 2 through 5 of Part II have been omitted because they are not applicable with respect to the current reporting period.

CERTAIN STATEMENTS IN THIS QUARTERLY REPORT ON FORM 10-Q, INCLUDING BUT NOT LIMITED TO THOSE RELATING TO:

• THE EFFECT OF PENDING ACCOUNTING PRONOUNCEMENTS ON THE COMPANY'S FINANCIAL STATEMENTS;
• EXPECTED PENSION PLAN AND SUPPLEMENTAL BENEFIT PLAN CONTRIBUTIONS AND RETURNS;
• THE EFFECT OF LAWSUITS, REGULATORY EXAMINATIONS AND INVESTIGATIONS AND OTHER LEGAL PROCEEDINGS ON THE COMPANY'S FINANCIAL CONDITION, RESULTS OF OPERATIONS OR CASH FLOWS;
• FUTURE PAYMENT OF DIVIDENDS;
• THE SUFFICIENCY OF THE COMPANY'S RESOURCES TO SATISFY OPERATIONAL CASH REQUIREMENTS;
• THE EFFECTS OF THE CONSUMER FINANCIAL PROTECTION BUREAU'S INTEGRATED DISCLOSURE RULES;
• THE LIKELIHOOD OF CHANGES IN EXPECTED ULTIMATE LOSSES AND CORRESPONDING LOSS RATES AND CLAIM RESERVES;
• THE LIKELIHOOD AND EFFECTS OF CYBER ATTACKS AND SIMILAR INCIDENTS;
• FUTURE ACQUISITIONS; AND
• CANADIAN EXCISE TAXES FOR SERVICES PROVIDED TO LENDERS,
ARE FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF SECTION 27A OF THE SECURITIES ACT OF 1933, AS AMENDED, AND SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED. THESE FORWARD-LOOKING STATEMENTS MAY CONTAIN THE WORDS "BELIEVE," "ANTICIPATE," "EXPECT," "PLAN," "PREDICT," "ESTIMATE," "PROJECT," "WILL BE," "WILL CONTAIN," "WILL LIKELY RESULT," OR OTHER SIMILAR WORDS AND PHRASES.

RISKS AND UNCERTAINTIES EXIST THAT MAY CAUSE RESULTS TO DIFFER MATERIALLY FROM THOSE SET FORTH IN THESE FORWARD-LOOKING STATEMENTS. FACTORS THAT COULD CAUSE THE ANTICIPATED RESULTS TO DIFFER FROM THOSE DESCRIBED IN THE FORWARD-LOOKING STATEMENTS INCLUDE:

• INTEREST RATE FLUCTUATIONS;
• CHANGES IN THE PERFORMANCE OF THE REAL ESTATE MARKETS;
• VOLATILITY IN THE CAPITAL MARKETS;
• UNFAVORABLE ECONOMIC CONDITIONS;
• IMPAIRMENTS IN THE COMPANY'S GOODWILL OR OTHER INTANGIBLE ASSETS;
• FAILURES AT FINANCIAL INSTITUTIONS WHERE THE COMPANY DEPOSITS FUNDS;
• CHANGES IN APPLICABLE GOVERNMENT REGULATIONS;
• HEIGHTENED SCRUTINY BY LEGISLATORS AND REGULATORS OF THE COMPANY'S TITLE INSURANCE AND SERVICES SEGMENT AND CERTAIN OTHER OF THE COMPANY'S BUSINESSES;
• THE CONSUMER FINANCIAL PROTECTION BUREAU'S EXERCISE OF ITS BROAD RULEMAKING AND SUPERVISORY POWERS;
• COMPLIANCE WITH THE CONSUMER FINANCIAL PROTECTION BUREAU'S INTEGRATED DISCLOSURE RULES;
• REGULATION OF TITLE INSURANCE RATES;
• REFORM OF GOVERNMENT-SPONSORED MORTGAGE ENTERPRISES;
• LIMITATIONS ON ACCESS TO PUBLIC RECORDS AND OTHER DATA;
• CHANGES IN RELATIONSHIPS WITH LARGE MORTGAGE LENDERS AND GOVERNMENT-SPONSORED ENTERPRISES;

•

CHANGES IN MEASURES OF THE STRENGTH OF THE COMPANY'S TITLE INSURANCE UNDERWRITERS, INCLUDING RATINGS AND STATUTORY CAPITAL AND SURPLUS;
LOSSES IN THE COMPANY'S INVESTMENT PORTFOLIO;
EXPENSES OF AND FUNDING OBLIGATIONS TO THE PENSION PLAN;
MATERIAL VARIANCE BETWEEN ACTUAL AND EXPECTED CLAIMS EXPERIENCE;
DEFALCATIONS, INCREASED CLAIMS OR OTHER COSTS AND EXPENSES ATTRIBUTABLE TO THE COMPANY'S USE OF TITLE AGENTS;
ANY INADEQUACY IN THE COMPANY'S RISK MITIGATION EFFORTS;

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SYSTEMS DAMAGE, FAILURES, INTERRUPTIONS AND INTRUSIONS, WIRE TRANSFER ERRORS OR UNAUTHORIZED DATA DISCLOSURES;
INABILITY TO REALIZE THE BENEFITS OF THE COMPANY'S OFFSHORE STRATEGY;
INABILITY OF THE COMPANY'S SUBSIDIARIES TO PAY DIVIDENDS OR REPAY FUNDS;
INABILITY TO REALIZE THE BENEFITS OF, AND CHALLENGES ARISING FROM, THE COMPANY'S ACQUISITION STRATEGY; AND
OTHER FACTORS DESCRIBED IN PART II, ITEM 1A OF THIS QUARTERLY REPORT ON FORM 10-Q. THE FORWARD-LOOKING STATEMENTS SPEAK ONLY AS OF THE DATE THEY ARE MADE. THE COMPANY DOES NOT UNDERTAKE TO UPDATE FORWARD-LOOKING STATEMENTS TO REFLECT CIRCUMSTANCES OR EVENTS THAT OCCUR AFTER THE DATE THE FORWARD-LOOKING STATEMENTS ARE MADE.

PART I: FINANCIAL INFORMATION

Item 1. Financial Statements.

FIRST AMERICAN FINANCIAL CORPORATION

AND SUBSIDIARY COMPANIES

Condensed Consolidated Balance Sheets

(in thousands, except par values)

(unaudited)

	March 31,	December 31,
	2015	2014
Assets		
Cash and cash equivalents	\$878,397	\$ 1,190,080
Accounts and accrued income receivable, net	259,327	276,610
Income taxes receivable	2,682	5,547
Investments:		
Deposits with banks	17,679	21,445
Debt securities, includes pledged securities of \$121,784 and \$120,742	4,039,816	3,450,252
Equity securities	286,329	402,412
Other investments	157,586	159,783
	4,501,410	4,033,892
Property and equipment, net	396,353	395,287
Title plants and other indexes	535,814	530,589
Deferred income taxes	19,712	19,712
Goodwill	983,707	959,945
Other intangible assets, net	52,629	55,812
Other assets	189,461	198,626
	\$7,819,492	\$ 7,666,100
Liabilities and Equity		
Deposits	\$2,612,350	\$ 2,332,714
Accounts payable and accrued liabilities	782,062	854,105
Deferred revenue	189,232	202,764
Reserve for known and incurred but not reported claims	946,847	1,011,780
Income taxes payable	5,509	6,228
Deferred income taxes	91,371	95,128
Notes and contracts payable	585,551	587,337
	5,212,922	5,090,056
Commitments and contingencies (Note 13)		
Stockholders' equity:		
Preferred stock, \$0.00001 par value; Authorized—500 shares;		
Outstanding—none	—	—
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Common stock, \$0.00001 par value; Authorized—300,000 shares;
Outstanding—108,367 shares and 107,541 shares

Additional paid-in capital	2,124,751	2,109,712
Retained earnings	672,275	662,310
Accumulated other comprehensive loss	(193,091)	(199,106)
Total stockholders' equity	2,603,936	2,572,917
Noncontrolling interests	2,634	3,127
Total equity	2,606,570	2,576,044
	\$7,819,492	\$ 7,666,100

See notes to condensed consolidated financial statements.

FIRST AMERICAN FINANCIAL CORPORATION

AND SUBSIDIARY COMPANIES

Condensed Consolidated Statements of Income

(in thousands, except per share amounts)

(unaudited)

	For the Three Months Ended March 31,	
	2015	2014
Revenues		
Direct premiums and escrow fees	\$ 518,504	\$ 433,872
Agent premiums	426,327	420,924
Information and other	146,648	137,642
Net investment income	20,558	17,767
Net realized investment (losses) gains	(953)	2,594
	1,111,084	1,012,799
Expenses		
Personnel costs	358,000	326,518
Premiums retained by agents	342,460	336,665
Other operating expenses	208,557	188,367
Provision for policy losses and other claims	101,554	89,883
Depreciation and amortization	20,854	19,972
Premium taxes	13,469	12,290
Interest	7,242	3,851
	1,052,136	977,546
Income before income taxes	58,948	35,253
Income taxes	21,152	13,401
Net income	37,796	21,852
Less: Net income attributable to noncontrolling interests	164	128
Net income attributable to the Company	\$ 37,632	\$ 21,724
Net income per share attributable to the Company's stockholders (Note 8):		
Basic	\$ 0.35	\$ 0.20
Diluted	\$ 0.34	\$ 0.20
Cash dividends declared per share	\$ 0.25	\$ 0.36
Weighted-average common shares outstanding (Note 8):		
Basic	107,744	106,166
Diluted	109,444	108,276

See notes to condensed consolidated financial statements.

FIRST AMERICAN FINANCIAL CORPORATION

AND SUBSIDIARY COMPANIES

Condensed Consolidated Statements of Comprehensive Income

(in thousands)

(unaudited)

	For the Three Months Ended March 31,	
	2015	2014
Net income	\$ 37,796	\$ 21,852
Other comprehensive income (loss), net of tax:		
Unrealized gain on securities	20,073	12,200
Foreign currency translation adjustment	(18,660)	(6,040)
Pension benefit adjustment	4,600	3,891
Total other comprehensive income (loss), net of tax	6,013	10,051
Comprehensive income	43,809	31,903
Less: Comprehensive income attributable to noncontrolling interests	162	131
Comprehensive income attributable to the Company	\$ 43,647	\$ 31,772

See notes to condensed consolidated financial statements.

FIRST AMERICAN FINANCIAL CORPORATION

AND SUBSIDIARY COMPANIES

Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	For the Three Months Ended March 31,	
	2015	2014
Cash flows from operating activities:		
Net income	\$37,796	\$21,852
Adjustments to reconcile net income to cash used for operating activities:		
Provision for policy losses and other claims	101,554	89,883
Depreciation and amortization	20,854	19,972
Amortization of premiums and accretion of discounts on debt securities, net	6,676	6,680
Excess tax benefits from share-based compensation	(5,588)	(4,036)
Net realized investment losses (gains)	953	(2,594)
Share-based compensation	10,858	9,397
Equity in earnings of affiliates, net	(1,130)	2,031
Dividends from equity method investments	2,433	205
Changes in assets and liabilities excluding effects of acquisitions and noncash transactions:		
Claims paid, including assets acquired, net of recoveries	(135,692)	(123,039)
Net change in income tax accounts	(7,052)	9,625
(Increase) decrease in accounts and accrued income receivable	(600)	3,837
Decrease in accounts payable and accrued liabilities	(98,704)	(133,600)
Decrease in deferred revenue	(13,033)	(13,419)
Other, net	14,358	8,585
Cash used for operating activities	(66,317)	(104,621)
Cash flows from investing activities:		
Net cash effect of acquisitions/dispositions	(25,860)	(165,858)
Net decrease in deposits with banks	3,354	611
Purchases of debt and equity securities	(806,547)	(202,519)
Proceeds from sales of debt and equity securities	255,643	142,938
Proceeds from maturities of debt securities	104,070	74,716
Net change in other investments	1,784	909
Net paydowns on loans receivable	—	4,276
Capital expenditures	(31,881)	(21,158)
Proceeds from sale of property and equipment	4,197	—
Cash used for investing activities	(495,240)	(166,085)
Cash flows from financing activities:		
Net change in deposits	279,636	69,185
Net proceeds from issuance of debt	—	150,000
Repayment of debt	(1,123)	(3,210)
Net activity related to noncontrolling interests	(655)	(624)

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Excess tax benefits from share-based compensation	5,588	4,036
Net payments in connection with share-based compensation plans	(2,093)	(402)
Cash dividends		