

Edgar Filing: State Auto Financial CORP - Form 10-Q

State Auto Financial CORP

Form 10-Q

November 07, 2016

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**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 September 30, 2016

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 000-19289

## STATE AUTO FINANCIAL CORPORATION

(Exact name of Registrant as specified in its charter)

**Ohio**

(State or other jurisdiction of  
incorporation or organization)

**31-1324304**

(I.R.S. Employer  
Identification No.)

**518 East Broad Street, Columbus, Ohio 43215-3976**

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (614) 464-5000

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 definition of "large accelerated filer", "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

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

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

On October 28, 2016, the Registrant had 41,742,438 Common Shares outstanding.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

**PART I – FINANCIAL STATEMENTS****Item 1. Condensed Consolidated Balance Sheets**

(\$ and shares in millions, except per share amounts)

	<b>September 30, 2016</b>	December 31, 2015
	(unaudited)	
<b>Assets</b>		
Fixed maturities, available-for-sale, at fair value (amortized cost \$2,061.0 and \$1,972.9, respectively)	<b>\$ 2,143.3</b>	\$2,000.7
Equity securities, available-for-sale, at fair value (cost \$246.1 and \$265.2, respectively)	<b>297.5</b>	310.6
Other invested assets, available-for-sale, at fair value (cost \$57.1 and \$56.9, respectively)	<b>89.7</b>	85.1
Other invested assets	<b>5.4</b>	5.3
Notes receivable from affiliate	<b>70.0</b>	70.0
<i>Total investments</i>	<b>2,605.9</b>	2,471.7
Cash and cash equivalents	<b>69.5</b>	58.1
Accrued investment income and other assets	<b>39.0</b>	35.7
Deferred policy acquisition costs (affiliated net assumed \$52.8 and \$49.3, respectively)	<b>133.8</b>	129.1
Reinsurance recoverable on losses and loss expenses payable	<b>4.1</b>	5.9
Prepaid reinsurance premiums	<b>6.1</b>	6.8
Due from affiliate	<b>21.2</b>	5.9
Current federal income taxes	<b>6.4</b>	4.9
Net deferred federal income taxes	<b>76.6</b>	102.5
Property and equipment, at cost	<b>7.4</b>	7.6
<b>Total assets</b>	<b>\$ 2,970.0</b>	\$2,828.2
<b>Liabilities and Stockholders' Equity</b>		
Losses and loss expenses payable (affiliated net assumed \$606.7 and \$532.4, respectively)	<b>\$ 1,165.6</b>	\$1,053.0
Unearned premiums (affiliated net assumed \$227.0 and \$214.2, respectively)	<b>634.2</b>	616.3
Notes payable (affiliates \$15.2 and \$15.2, respectively)	<b>122.1</b>	100.5
Postretirement and pension benefits (affiliated net ceded \$38.4 and \$56.0, respectively)	<b>71.4</b>	104.0
Other liabilities (affiliated net assumed \$10.5 and affiliated net ceded \$8.4, respectively)	<b>68.9</b>	69.8
<b>Total liabilities</b>	<b>2,062.2</b>	1,943.6
Stockholders' equity:		
Class A Preferred stock (nonvoting), without par value. Authorized 2.5 shares; none issued	—	—
Class B Preferred stock, without par value. Authorized 2.5 shares; none issued	—	—
Common stock, without par value. Authorized 100.0 shares; 48.4 and 48.1 shares issued, respectively, at stated value of \$2.50 per share	<b>121.1</b>	120.4
Treasury stock, 6.8 and 6.8 shares, respectively, at cost	<b>(116.5)</b>	(116.3)
Additional paid-in capital	<b>156.0</b>	153.5
Accumulated other comprehensive income (affiliated net ceded \$53.3 and \$56.7, respectively)	<b>81.7</b>	37.6
Retained earnings	<b>665.5</b>	689.4
<b>Total stockholders' equity</b>	<b>907.8</b>	884.6
<b>Total liabilities and stockholders' equity</b>	<b>\$ 2,970.0</b>	\$2,828.2

See accompanying notes to condensed consolidated financial statements.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

**Condensed Consolidated Statements of Income**

	Three months ended September 30	
	<b>2016</b>	2015
<i>(\$ in millions, except per share amounts)</i>		
(unaudited)		
Earned premiums (affiliated net assumed \$121.4 and \$112.2, respectively)	<b>\$325.8</b>	\$319.7
Net investment income (affiliates \$1.3 and \$1.3, respectively)	<b>17.6</b>	18.7
Net realized gains on investments:		
Total other-than-temporary impairment losses	<b>(1.1 )</b>	(3.5 )
Portion of loss recognized in other comprehensive income	—	—
Other net realized investment gains	<b>9.9</b>	14.3
Total net realized gains on investments	<b>8.8</b>	10.8
Other income from affiliates	<b>0.6</b>	0.5
<b>Total revenues</b>	<b>352.8</b>	349.7
Losses and loss expenses (affiliated net assumed \$100.9 and \$67.4, respectively)	<b>232.3</b>	207.5
Acquisition and operating expenses (affiliated net assumed \$73.9 and \$52.8, respectively)	<b>109.9</b>	109.4
Interest expense (affiliates \$0.2 and \$0.1, respectively)	<b>1.4</b>	1.3
Other expenses	<b>1.8</b>	1.6
<b>Total expenses</b>	<b>345.4</b>	319.8
<b>Income before federal income taxes</b>	<b>7.4</b>	29.9
Federal income tax (benefit) expense:		
Current	<b>(1.5 )</b>	2.7
Deferred	<b>(1.2 )</b>	6.5
<b>Total federal income tax (benefit) expense</b>	<b>(2.7 )</b>	9.2
<b>Net income</b>	<b>\$10.1</b>	\$20.7
Earnings per common share:		
Basic	<b>\$0.24</b>	\$0.50
Diluted	<b>\$0.24</b>	\$0.50
Dividends paid per common share	<b>\$0.10</b>	\$0.10

See accompanying notes to condensed consolidated financial statements.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

**Condensed Consolidated Statements of Income**

	Nine months ended September 30	
	<b>2016</b>	2015
<i>(\$ in millions, except per share amounts)</i>		
(unaudited)		
Earned premiums (affiliated net assumed \$352.4 and \$320.5, respectively)	<b>\$968.1</b>	\$946.5
Net investment income (affiliates \$3.7 and \$3.7, respectively)	<b>54.1</b>	53.9
Net realized gains on investments:		
Total other-than-temporary impairment losses	<b>(5.4 )</b>	(4.8 )
Portion of loss recognized in other comprehensive income	—	—
Other net realized investment gains	<b>22.0</b>	24.8
Total net realized gains on investments	<b>16.6</b>	20.0
Other income from affiliates	<b>1.7</b>	1.6
<b>Total revenues</b>	<b>1,040.5</b>	1,022.0
Losses and loss expenses (affiliated net assumed \$281.4 and \$200.9, respectively)	<b>720.2</b>	627.1
Acquisition and operating expenses (affiliated net assumed \$217.0 and \$188.9, respectively)	<b>324.6</b>	318.7
Interest expense (affiliates \$0.6 and \$0.5, respectively)	<b>4.1</b>	4.0
Other expenses	<b>5.5</b>	5.7
<b>Total expenses</b>	<b>1,054.4</b>	955.5
<b>(Loss) income before federal income taxes</b>	<b>(13.9 )</b>	66.5
Federal income tax (benefit) expense:		
Current	<b>(1.5 )</b>	3.3
Deferred	<b>(0.9 )</b>	15.1
<b>Total federal income tax (benefit) expense</b>	<b>(2.4 )</b>	18.4
<b>Net (loss) income</b>	<b>\$(11.5)</b>	\$48.1
(Loss) earnings per common share:		
Basic	<b>\$(0.28)</b>	\$1.17
Diluted	<b>\$(0.28)</b>	\$1.16
Dividends paid per common share	<b>\$0.30</b>	\$0.30

See accompanying notes to condensed consolidated financial statements.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

**Consolidated Statements of Comprehensive Income**

	Three months ended	
	September 30	
(unaudited)	<b>2016</b>	2015
Net income	<b>\$10.1</b>	\$20.7
Other comprehensive loss, net of tax:		
Net unrealized holding gains (losses) on investments:		
Unrealized holding gains (losses)	<b>6.3</b>	(24.5 )
Reclassification adjustments for gains realized in net income	<b>(8.8 )</b>	(10.8 )
Income tax benefit	<b>0.8</b>	12.4
<i>Total net unrealized holding losses on investments</i>	<b>(1.7 )</b>	(22.9 )
Net unrecognized benefit plan obligations:		
Reclassification adjustments for amortization to statements of income:		
Negative prior service cost	<b>(1.3 )</b>	(1.3 )
Net actuarial loss	<b>2.4</b>	2.8
Income tax expense	<b>(0.4 )</b>	(0.6 )
<i>Total net unrecognized benefit plan obligations</i>	<b>0.7</b>	0.9
<i>Other comprehensive loss</i>	<b>(1.0 )</b>	(22.0 )
<b>Comprehensive income (loss)</b>	<b>\$9.1</b>	\$(1.3 )

See accompanying notes to condensed consolidated financial statements.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

**Consolidated Statements of Comprehensive Income**

	Nine months ended September 30	
	2016	2015
<i>(\$ in millions, except per share amounts)</i>		
(unaudited)		
Net (loss) income	<b>\$(11.5)</b>	\$48.1
Other comprehensive income (loss), net of tax:		
Net unrealized holding gains (losses) on investments:		
Unrealized holding gains (losses)	<b>81.5</b>	(46.1 )
Reclassification adjustments for gains realized in net income	<b>(16.6 )</b>	(20.4 )
Income tax (expense) benefit	<b>(22.8 )</b>	23.3
<i>Total net unrealized holding gains (losses) on investments</i>	<b>42.1</b>	(43.2 )
Net unrecognized benefit plan obligations:		
Reclassification adjustments for amortization to statements of income:		
Negative prior service cost	<b>(4.1 )</b>	(4.1 )
Net actuarial loss	<b>7.1</b>	8.6
Income tax expense	<b>(1.0 )</b>	(1.6 )
<i>Total net unrecognized benefit plan obligations</i>	<b>2.0</b>	2.9
<i>Other comprehensive income (loss)</i>	<b>44.1</b>	(40.3 )
<b>Comprehensive income</b>	<b>\$32.6</b>	\$7.8

See accompanying notes to condensed consolidated financial statements.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

**Condensed Consolidated Statements of Cash Flows**

	Nine months ended September 30	
	2016	2015
<i>(\$ in millions)</i>		
(unaudited)		
<b>Cash flows from operating activities:</b>		
Net (loss) income	<b>\$(11.5)</b>	\$48.1
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization, net	<b>11.5</b>	10.8
Share-based compensation	<b>3.2</b>	5.1
Net realized gains on investments	<b>(16.6)</b>	(20.0)
Changes in operating assets and liabilities:		
Deferred policy acquisition benefits	<b>(4.7)</b>	(7.5)
Accrued investment income and other assets	<b>(3.4)</b>	(4.5)
Postretirement and pension benefits	<b>(30.6)</b>	(5.8)
Other liabilities and due to/from affiliates, net	<b>(17.4)</b>	(63.5)
Reinsurance recoverable on losses and loss expenses payable and prepaid reinsurance premiums	<b>2.5</b>	1.2
Losses and loss expenses payable	<b>112.6</b>	38.3
Unearned premiums	<b>17.9</b>	25.1
Excess tax benefits on share-based awards	<b>(0.1)</b>	0.1
Federal income taxes	<b>(1.4)</b>	17.6
Cash provided from December 31, 2014 unearned premium transfer related to the homeowners quota share arrangement	<b>—</b>	63.5
<b><i>Net cash provided by operating activities</i></b>	<b>62.0</b>	108.5
<b>Cash flows from investing activities:</b>		
Purchases of fixed maturities available-for-sale	<b>(414.6)</b>	(459.8)
Purchases of equity securities available-for-sale	<b>(77.9)</b>	(131.8)
Purchases of other invested assets	<b>(1.0)</b>	(6.5)
Maturities, calls and pay downs of fixed maturities available-for-sale	<b>177.1</b>	203.4
Sales of fixed maturities available-for-sale	<b>138.0</b>	142.7
Sales of equity securities available-for-sale	<b>113.9</b>	117.4
Sales of other invested assets available-for-sale	<b>0.7</b>	0.5
Net additions of property and equipment	<b>—</b>	(0.1)
<b><i>Net cash used in investing activities</i></b>	<b>(63.8)</b>	(134.2)
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of common stock	<b>4.2</b>	2.9
Payments to acquire treasury stock	<b>(0.2)</b>	(0.3)
Payment of dividends	<b>(12.4)</b>	(12.3)
Excess tax benefits on share-based awards	<b>0.1</b>	—
Proceeds from long-term debt	<b>21.5</b>	—
<b><i>Net cash provided by (used in) financing activities</i></b>	<b>13.2</b>	(9.7)
Net increase (decrease) in cash and cash equivalents	<b>11.4</b>	(35.4)
Cash and cash equivalents at beginning of period	<b>58.1</b>	86.3
<b>Cash and cash equivalents at end of period</b>	<b>\$69.5</b>	\$50.9
<u>Supplemental disclosures:</u>		
Interest paid (affiliates \$0.6 and \$0.5, respectively)	<b>\$4.0</b>	\$3.9

Federal income taxes paid

\$— \$2.4

See accompanying notes to condensed consolidated financial statements.

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STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

Notes to Condensed Consolidated Financial Statements (Unaudited)

**1. Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements of State Auto Financial Corporation and Subsidiaries (“State Auto Financial” or the “Company”) have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles (“GAAP”) for complete financial statements. In the opinion of the Company, all adjustments (consisting of normal, recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine month period ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. The balance sheet at December 31, 2015 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by GAAP for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2015 (the “2015 Form 10-K”). Capitalized terms used herein and not otherwise defined shall have the meaning ascribed to them in the 2015 Form 10-K.

**Adoption of Recent Accounting Pronouncements**

*Simplifying the Presentation of Debt Issuance Costs*

The amendments in this guidance simplify the presentation of debt issuance costs by requiring them to be presented in the balance sheet as a direct deduction from the carrying amount of the related recognized debt liability, consistent with debt discounts. The Company adopted this guidance at January 1, 2016 on a retrospective basis and it resulted in a \$0.3 million decrease to notes payable and accrued investment income and other assets at December 31, 2015.

*Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*

The amendments in this guidance remove the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. The amendments also remove the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using that practical expedient. The amendments in this update are effective for public business entities for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years and should be applied retrospectively to all periods presented. The Company adopted this guidance at January 1, 2016 and it did not have a material impact on the condensed consolidated financial statements.

**Pending Adoption of Recent Accounting Pronouncements**

*Improvements to Employee Share-Based Payment Accounting*

The amendments in this guidance simplify the accounting for share-based payment award transactions including: income tax consequences, classification of awards as either equity or liabilities, classification of excess tax benefits, and classification on the statement of cash flows. The guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and early adoption is permitted. The Company is currently evaluating the requirements of the guidance and has not yet determined its effect on the Company’s results of operations, financial position or liquidity.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

Notes to Condensed Consolidated Financial Statements, Continued (Unaudited)

**2. Investments**

The following tables set forth the cost or amortized cost and fair value of available-for-sale securities by lot at September 30, 2016 and December 31, 2015:

(\$ millions)

	Cost or amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
<b>September 30, 2016</b>				
Fixed maturities:				
U.S. treasury securities and obligations of U.S. government agencies	\$316.8	\$14.3	\$(0.2)	\$330.9
Obligations of states and political subdivisions	664.1	34.5	—	698.6
Corporate securities	510.4	13.1	(0.6)	522.9
U.S. government agencies mortgage-backed securities	569.7	22.4	(1.2)	590.9
<i>Total fixed maturities</i>	<b>2,061.0</b>	<b>84.3</b>	<b>(2.0)</b>	<b>2,143.3</b>
Equity securities:				
Large-cap securities	193.1	37.1	(4.6)	225.6
Small-cap securities	53.0	18.9	—	71.9
<i>Total equity securities</i>	<b>246.1</b>	<b>56.0</b>	<b>(4.6)</b>	<b>297.5</b>
Other invested assets	57.1	32.6	—	89.7
<i>Total available-for-sale securities</i>	<b>\$2,364.2</b>	<b>\$172.9</b>	<b>\$(6.6)</b>	<b>\$2,530.5</b>

(\$ millions)

December 31, 2015

	Cost or amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
December 31, 2015				
Fixed maturities:				
U.S. treasury securities and obligations of U.S. government agencies	\$219.8	\$6.6	\$(2.0)	\$224.4
Obligations of states and political subdivisions	804.0	22.5	(1.7)	824.8
Corporate securities	500.3	5.8	(11.7)	494.4
U.S. government agencies mortgage-backed securities	448.8	11.5	(3.2)	457.1
<i>Total fixed maturities</i>	<b>1,972.9</b>	<b>46.4</b>	<b>(18.6)</b>	<b>2,000.7</b>
Equity securities:				
Large-cap securities	211.9	34.2	(5.1)	241.0
Small-cap securities	53.3	16.5	(0.2)	69.6
<i>Total equity securities</i>	<b>265.2</b>	<b>50.7</b>	<b>(5.3)</b>	<b>310.6</b>
Other invested assets	56.9	28.3	(0.1)	85.1
<i>Total available-for-sale securities</i>	<b>\$2,295.0</b>	<b>\$125.4</b>	<b>\$(24.0)</b>	<b>\$2,396.4</b>

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

Notes to Condensed Consolidated Financial Statements, Continued (Unaudited)

The following tables set forth the Company's gross unrealized losses and fair value on its investments by lot, aggregated by investment category and length of time for individual securities that have been in a continuous unrealized loss position at September 30, 2016 and December 31, 2015:

(\$ millions, except # of positions)

	Less than 12 months			12 months or more			Total		
	Fair value	Unrealized losses	Number of positions	Fair value	Unrealized losses	Number of positions	Fair value	Unrealized losses	Number of positions
<b>September 30, 2016</b>									
Fixed maturities:									
U.S. treasury securities and obligations of U.S. government agencies	\$107.6	\$(0.2)	8	\$—	\$—	—	\$107.6	\$(0.2)	8
Corporate securities	33.8	(0.3)	5	37.3	(0.3)	5	71.1	(0.6)	10
U.S. government agencies mortgage-backed securities	95.6	(0.6)	11	21.1	(0.6)	9	116.7	(1.2)	20
<i>Total fixed maturities</i>	<b>237.0</b>	<b>(1.1)</b>	<b>24</b>	<b>58.4</b>	<b>(0.9)</b>	<b>14</b>	<b>295.4</b>	<b>(2.0)</b>	<b>38</b>
Equity securities:									
Large-cap equity securities	39.9	(3.6)	11	6.9	(1.0)	5	46.8	(4.6)	16
<i>Total temporarily impaired securities</i>	<b>\$276.9</b>	<b>\$(4.7)</b>	<b>35</b>	<b>\$65.3</b>	<b>\$(1.9)</b>	<b>19</b>	<b>\$342.2</b>	<b>\$(6.6)</b>	<b>54</b>

(\$ millions, except # of positions)

	Less than 12 months			12 months or more			Total		
	Fair value	Unrealized losses	Number of positions	Fair value	Unrealized losses	Number of positions	Fair value	Unrealized losses	Number of positions
<b>December 31, 2015</b>									
Fixed maturities:									
U.S. treasury securities and obligations of U.S. government agencies	\$68.6	\$(1.6)	15	\$13.5	\$(0.4)	4	\$82.1	\$(2.0)	19
Obligations of states and political subdivisions	137.5	(1.7)	16	—	—	—	137.5	(1.7)	16
Corporate securities	246.9	(5.3)	36	63.9	(6.4)	11	310.8	(11.7)	47
U.S. government agencies mortgage-backed securities	132.2	(2.3)	18	33.0	(0.9)	11	165.2	(3.2)	29
<i>Total fixed maturities</i>	<b>585.2</b>	<b>(10.9)</b>	<b>85</b>	<b>110.4</b>	<b>(7.7)</b>	<b>26</b>	<b>695.6</b>	<b>(18.6)</b>	<b>111</b>
Equity securities:									
Large-cap equity securities	65.8	(5.1)	24	—	—	—	65.8	(5.1)	24
Small-cap equity securities	3.4	(0.2)	1	—	—	—	3.4	(0.2)	1
<i>Total equity securities</i>	<b>69.2</b>	<b>(5.3)</b>	<b>25</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>69.2</b>	<b>(5.3)</b>	<b>25</b>
Other invested assets	8.1	(0.1)	1	—	—	—	8.1	(0.1)	1
<i>Total temporarily impaired securities</i>	<b>\$662.5</b>	<b>\$(16.3)</b>	<b>111</b>	<b>\$110.4</b>	<b>\$(7.7)</b>	<b>26</b>	<b>\$772.9</b>	<b>\$(24.0)</b>	<b>137</b>

The Company reviewed its investments at September 30, 2016, and determined that no additional other-than-temporary impairment existed in the gross unrealized holding losses other than those listed in the table below. The following table sets forth the realized losses related to other-than-temporary impairments on the Company's investment portfolio recognized for the three and nine months ended September 30, 2016 and 2015:

	Three months ended		Nine months ended	
	September 30 2016	September 30 2015	September 30 2016	September 30 2015
Equity securities:				
Large-cap securities	\$—	\$—	\$(0.2)	\$—
Small-cap securities	(1.1)	(3.5)	(2.9)	(4.8)

Fixed maturities:	—	—	(2.3)	—
<i>Total other-than-temporary impairments</i>	<b>\$(1.1)</b>	<b>\$(3.5)</b>	<b>\$(5.4)</b>	<b>\$(4.8)</b>

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

(a majority-owned subsidiary of State Automobile Mutual Insurance Company)

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The Company regularly monitors its investments that have fair values less than cost or amortized cost for signs of other-than-temporary impairment, an assessment that requires significant management judgment regarding the evidence known. Such judgments could change in the future as more information becomes known, which could negatively impact the amounts reported. Among the factors that management considers for fixed maturity securities are the financial condition of the issuer including receipt of scheduled principal and interest cash flows, and intent to sell, including if it is more likely than not that the Company will be required to sell the investments before recovery. When a fixed maturity has been determined to have an other-than-temporary impairment, the impairment charge is separated into an amount representing the credit loss, which is recognized in earnings as a realized loss, and the amount related to non-credit factors, which is recognized in accumulated other comprehensive income. Future increases or decreases in fair value, if not other-than-temporary, are included in accumulated other comprehensive income.

Among the factors that management considers for equity securities and other invested assets are the length of time and/or the significance of decline below cost, the Company's ability and intent to hold these securities through their recovery periods, the current financial condition of the issuer and its future business prospects, and the ability of the market value to recover to cost in the near term. When an equity security or other invested asset has been determined to have a decline in fair value that is other-than-temporary, the cost basis of the security is adjusted to fair value. This results in a charge to earnings as a realized loss, which is not reversed for subsequent recoveries in fair value. Future increases or decreases in fair value, if not other-than-temporary, are included in accumulated other comprehensive income.

The following table sets forth the amortized cost and fair value of available-for-sale fixed maturities by contractual maturity at September 30, 2016:

<i>(\$ millions)</i>	Amortized Fair	
	cost	value
Due in 1 year or less	<b>\$ 67.1</b>	<b>\$68.1</b>
Due after 1 year through 5 years	<b>564.0</b>	<b>579.4</b>
Due after 5 years through 10 years	<b>275.3</b>	<b>286.1</b>
Due after 10 years	<b>584.9</b>	<b>618.8</b>
U.S. government agencies mortgage-backed securities	<b>569.7</b>	<b>590.9</b>
<i>Total</i>	<b>\$ 2,061.0</b>	<b>\$2,143.3</b>

Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay the obligations with or without call or prepayment penalties.

At September 30, 2016, State Auto P&C had U.S. government agencies mortgage-backed fixed maturity securities, with a carrying value of approximately \$106.5 million, that were pledged as collateral for the FHLB Loans (as defined in Note 3). In accordance with the terms of the FHLB Loans, State Auto P&C retains all rights regarding these pledged securities.

Fixed maturities with fair values of \$9.2 million and \$8.8 million were on deposit with insurance regulators as required by law at September 30, 2016 and December 31, 2015, respectively. The Company retains all rights regarding these securities.

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## STATE AUTO FINANCIAL CORPORATION AND SUBSIDIARIES

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Notes to Condensed Consolidated Financial Statements, Continued (Unaudited)

The following table sets forth the components of net investment income for the three and nine months ended September 30, 2016 and 2015:

(\$ millions)	Three months ended September 30		Nine months ended September 30	
	2016	2015	2016	2015
Fixed maturities	\$15.4	\$16.1	\$47.0	\$46.4
Equity securities	1.3	1.4	4.3	4.7
Cash and cash equivalents, and other	1.4	1.6	4.1	4.3
<i>Investment income</i>	<b>18.1</b>	19.1	<b>55.4</b>	55.4
Investment expenses	0.5	0.4	1.3	1.5
<i>Net investment income</i>	<b>\$17.6</b>	\$18.7	<b>\$54.1</b>	\$53.9

The Company's current investment strategy does not rely on the use of derivative financial instruments.

Proceeds on sales of available-for-sale securities were \$252.6 million and \$260.6 million for the nine months ended September 30, 2016 and 2015, respectively.

The following table sets forth the realized and unrealized holding gains (losses) on the Company's investment portfolio for the three and nine months ended September 30, 2016 and 2015:

(\$ millions)	Three months ended September 30		Nine months ended September 30	
	2016	2015	2016	2015
Realized gains:				
Fixed maturities	\$—	\$2.9	\$2.1	\$4.4
Equity securities	9.9	11.8	20.6	21.8
Other invested assets	—	—	0.1	0.1
<i>Total realized gains</i>	<b>9.9</b>	14.7	<b>22.8</b>	26.3
Realized losses:				
Equity securities:				
Sales	—	(0.4 )	(0.8 )	(1.1 )
OTTI	(1.1 )	(3.5 )	(3.1 )	(4.8 )
Fixed maturities:				
OTTI	—	—	(2.3 )	—
<i>Total realized losses</i>	<b>(1.1 )</b>	(3.9 )	<b>(6.2 )</b>	(5.9 )
<i>Net realized gains on investments</i>	<b>\$8.8</b>	\$10.8	<b>\$16.6</b>	\$20.4
Change in unrealized holding (losses) gains, net of tax:				
Fixed maturities	\$ (11.2 )	\$		