STEWART INFORMATION SERVICES CORP
Form 10-Q
May 04, 2011

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2011

or

o **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 001-02658

STEWART INFORMATION SERVICES CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	**74-1677330**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1980 Post Oak Blvd., Houston TX	**77056**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(713) 625-8100**

(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 þ No o

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 o No o

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

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

On April 30, 2011, the following shares of each of the issuer s classes of common stock were outstanding:

Common, $1 par value	18,196,983
Class B Common, $1 par value	1,050,012

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QUARTER ENDED MARCH 31, 2011
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As used in this report, we, us, our, the Company and Stewart mean Stewart Information Services Corporation an subsidiaries, unless the context indicates otherwise.

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

	For the Three Months Ended March 31,	
	2011	2010
	($000 omitted, except per share)	
Revenues		
Title insurance:		
Direct operations	139,230	129,505
Agency operations	191,809	202,571
Real estate information	31,385	11,542
Investment income	3,861	4,782
Investment and other gains net	132	2,913
	366,417	351,313
Expenses		
Amounts retained by agencies	158,447	168,735
Employee costs	117,926	114,103
Other operating expenses	59,129	64,387
Title losses and related claims	31,200	26,337
Depreciation and amortization	4,830	5,936
Interest	1,278	1,558
	372,810	381,056
Loss before taxes and noncontrolling interests	(6,393)	(29,743)
Income tax expense (benefit)	3,131	(1,538)
Net loss	(9,524)	(28,205)
Less net earnings attributable to noncontrolling interests	769	758
Net loss attributable to Stewart	(10,293)	(28,963)
Comprehensive loss:		
Net loss	(9,524)	(28,205)
Other comprehensive (loss) earnings, net of taxes of $1,161 and $1,484	(389)	1,990
Comprehensive loss	(9,913)	(26,215)
Less comprehensive earnings attributable to noncontrolling interests	769	758
Comprehensive loss attributable to Stewart	(10,682)	(26,973)

Basic and diluted average shares outstanding (000)	18,829	18,257
Basic and dilutive loss per share attributable to Stewart	(0.55)	(1.59)

See notes to condensed consolidated financial statements.

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CONDENSED CONSOLIDATED BALANCE SHEETS

	As of March 31,2011	As of December 31, 2010
	($000 omitted)	
Assets		
Cash and cash equivalents	103,842	144,564
Cash and cash equivalents statutory reserve funds	8,028	9,926
	111,870	154,490
Short-term investments	32,789	33,457
Investments in debt and equity securities available-for-sale, at fair value:		
Statutory reserve funds	392,174	396,317
Other	60,174	54,007
	452,348	450,324
Receivables:		
Notes	10,332	10,747
Premiums from agencies	40,151	45,399
Income taxes	6,778	651
Other	53,716	41,323
Allowance for uncollectible amounts	(20,038)	(19,438)
	90,939	78,682
Property and equipment, at cost		
Land	6,469	6,445
Buildings	23,844	23,769
Furniture and equipment	251,414	250,355
Accumulated depreciation	(221,437)	(219,000)
	60,290	61,569
Title plants, at cost	77,450	77,397
Real estate, at lower of cost or net realizable value	2,433	3,266
Investments in investees, on an equity method basis	16,979	17,608
Goodwill	206,861	206,861
Intangible assets, net of amortization	7,967	8,228
Other assets	54,396	49,324
	1,114,322	1,141,206
Liabilities		
Notes payable	9,117	8,784
Convertible senior notes	64,382	64,338
Accounts payable and accrued liabilities	70,495	95,666

Estimated title losses	493,240	495,849
Deferred income taxes	31,426	28,236
	668,660	692,873
Contingent liabilities and commitments		
Stockholders equity		
Common and Class B Common Stock and additional paid-in capital	151,711	143,264
Retained earnings	272,373	282,666
Accumulated other comprehensive earnings	13,221	13,610
Treasury stock 476,227 common shares, at cost	(4,330)	(4,330)
Stockholders equity attributable to Stewart	432,975	435,210
Noncontrolling interests	12,687	13,123
Total stockholders equity (19,122,929 and 18,375,058 shares outstanding)	445,662	448,333
	1,114,322	1,141,206

See notes to condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Three Months Ended March 31,	
	2011	2010
	($000 omitted)	
Reconciliation of net loss to cash (used) provided by operating activities:		
Net loss	(9,524)	(28,205)
Add (deduct):		
Depreciation and amortization	4,830	5,936
Provision for bad debt	996	1,445
Investment and other gains net	(132)	(2,913)
Payments for title losses in excess of provisions	(5,099)	(11,718)
Insurance recoveries of title losses	1,581	4,823
(Increase) decrease in receivables net	(8,677)	57,444
Increase in other assets net	(2,501)	(736)
Decrease in payables and accrued liabilities net	(23,742)	(13,664)
Increase (decrease) in net deferred income taxes	2,030	(809)
Net (earnings) loss from equity investees	(69)	238
Dividends received from equity investees	717	470
Other net	958	1,292
Cash (used) provided by operating activities	(38,632)	13,603
Investing activities:		
Proceeds from investments available-for-sale matured and sold	22,267	58,042
Purchases of investments available-for-sale	(21,531)	(44,949)
Proceeds from redemptions of investments pledged		9,275
Purchases of property and equipment and title plants net	(4,249)	(2,914)
Increases in notes receivable	(180)	(73)
Collections on notes receivable	538	166
Change in cash and cash equivalents due to sale and deconsolidation of subsidiaries (see below)		(1,844)
Cash paid for acquisitions of subsidiaries and other net		(8)
Net cash received for other assets, cost-basis investments, equity investees and other	58	
Cash (used) provided by investing activities	(3,097)	17,695
Financing activities:		
Payments on notes payable	(1,143)	(2,161)
Payments on line of credit		(9,628)
Proceeds from notes payable	500	114
Distributions to noncontrolling interests	(1,251)	(1,003)
Cash used by financing activities	(1,894)	(12,678)
Effects of changes in foreign currency exchange rates	1,003	65
(Decrease) increase in cash and cash equivalents	(42,620)	18,685

Cash and cash equivalents at beginning of period	154,490	116,100
Cash and cash equivalents at end of period	111,870	134,785
Supplemental information:		
Settlement of wage and hour litigation through issuance of Common Stock	7,582	
Changes in financial statement amounts due to sale and deconsolidation of subsidiaries:		
Note receivable		2,500
Investments in investees, on an equity method basis		5,316
Goodwill		(5,831)
Title plants		(1,048)
Property and equipment, net of accumulated depreciation		(1,560)
Intangible asset, net of amortization		2,827
Other net		(878)
Liabilities		1,344
Noncontrolling interests		336
Investment and other gains net		(1,162)
Change in cash and cash equivalents due to sale and deconsolidation of Subsidiaries		1,844

See notes to condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1

Interim financial statements. The financial information contained in this report for the three months ended March 31, 2011 and 2010, and as of March 31, 2011, is unaudited. This report should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

A. Management s responsibility. The accompanying interim financial statements were prepared by management, who is responsible for their integrity and objectivity. These financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP), including management s best judgments and estimates. In the opinion of management, all adjustments necessary for a fair presentation of this information for all interim periods, consisting only of normal recurring accruals, have been made. The Company s results of operations for interim periods are not necessarily indicative of results for a full year and actual results could differ from those estimates.

B. Consolidation. The condensed consolidated financial statements include all subsidiaries in which the Company owns more than 50% voting rights in electing directors. All significant intercompany amounts and transactions have been eliminated and provisions have been made for noncontrolling interests. Unconsolidated investees, in which the Company typically owns 20% through 50% of the equity, are accounted for by the equity method.

C. Reclassifications. Certain amounts in the 2010 interim financial statements have been reclassified for comparative purposes. Net losses, as previously reported, were not affected.

NOTE 2

Investments in debt and equity securities. The amortized costs and fair values follow:

	March 31, 2011		December 31, 2010	
	Amortized costs	Fair values	Amortized costs	Fair values
	($000 omitted)			
Debt securities:				
Municipal	36,582	37,109	39,589	40,185
Corporate and utilities	228,068	228,080	228,270	229,972
Foreign	160,350	161,376	155,977	157,745
U.S. Government	19,414	20,841	20,792	22,422
Equity securities	5,005	4,942		
	449,419	452,348	444,628	450,324

Gross unrealized gains and losses were:

	March 31, 2011		December 31, 2010	
	Gains	Losses	Gains	Losses
	($000 omitted)			
Debt securities:				
Municipal	1,016	489	1,235	639
Corporate and utilities	3,972	3,961	4,574	2,872
Foreign	1,469	443	1,861	93
U.S. Government	1,428	2	1,634	4
Equity securities	17	78		
	7,902	4,973	9,304	3,608

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Debt securities as of March 31, 2011 mature, according to their contractual terms, as follows (actual maturities may differ due to call or prepayment rights):

	Amortized costs	Fair values
	($000 omitted)	
In one year or less	37,179	37,394
After one year through five years	187,883	189,547
After five years through ten years	174,752	175,247
After ten years	44,600	45,218
	444,414	447,406

As of March 31, 2011, gross unrealized losses on investments and the fair values of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were:

	Less than 12 months		More than 12 months		Total	
	Losses	Fair values	Losses	Fair values	Losses	Fair values
			($000 omitted)			
Debt securities:						
Municipal	489	13,804			489	13,804
Corporate and utilities	3,956	114,973	4	233	3,961	115,206
Foreign	443	103,610			443	103,610
U.S. Government	1	3,177	1	120	2	3,297
Equity securities	79	3,676			78	3,676
	4,968	239,240	5	353	4,973	239,593

The unrealized loss positions were primarily caused by interest rate fluctuations. The number of investments in an unrealized loss position as of March 31, 2011 was 94. Since the Company does not intend to sell and will more-likely-than-not maintain each debt security until its anticipated recovery, and no significant credit risk is deemed to exist, these investments are not considered other-than-temporarily impaired.

As of December 31, 2010, gross unrealized losses on investments and the fair values of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were:

	Less than 12 months		More than 12 months		Total	
	Losses	Fair values	Losses	Fair values	Losses	Fair values
			($000 omitted)			
Debt securities:						
Municipal	638	14,391	1	25	639	14,416
Corporate and utilities	2,868	95,354	4	235	2,872	95,589
Foreign	93	55,773			93	55,773
U.S. Government	4	3,711			4	3,711
	3,603	169,229	5	260	3,608	169,489

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The Company believes its investment portfolio is diversified and expects no material loss to result from the failure to perform by issuers of the debt securities it holds. Investments made by the Company are not collateralized. Foreign debt securities primarily include Canadian government bonds and United Kingdom treasury bonds.

NOTE 3

Fair value measurements. The Fair Value Measurements and Disclosures Topic of the FASB ASC defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal, or most advantageous, market for the asset or liability in an orderly transaction between market participants at the measurement date. The Fair Value Measurements Topic establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs when possible. The three levels of inputs used to measure fair value are as follows:

Level 1 quoted prices in active markets for identical assets or liabilities;

Level 2 observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data; and

Level 3 unobservable inputs that are supported by little or no market activity and that are significant to the fair values of the assets or liabilities, including certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

As of March 31, 2011, financial instruments measured at fair value on a recurring basis are summarized below:

	Level 1	Level 2	Fair value measurements
		($000 omitted)	
Short-term investments	32,789		32,789
Investments available-for-sale:			
Debt securities:			
Municipal		37,109	37,109
Corporate and utilities		228,080	228,080
Foreign	161,376		161,376
U.S. Government	20,841		20,841
Equity securities	4,942		4,942
	219,948	265,189	485,137

As of March 31, 2011, Level 1 financial instruments consist of short-term investments, U.S. and foreign government bonds and equity securities. Level 2 financial instruments consist of municipal and corporate bonds. The municipal bonds are valued using a third-party pricing service, and the corporate bonds are valued using actual transaction levels, independent broker/dealer quotes or information, or a combination thereof. When no relevant broker/dealer information can be obtained, the third-party service price will be used. The third-party pricing service for both municipal and corporate bonds determines a consensus price derived from prices provided by various broker/dealers that meet certain statistical requirements within a predefined statistical deviation. If a consensus price cannot be determined, then, by using a recognized pricing model, a theoretical value, based on where similar bonds, as defined by credit quality and market sector have traded, is used.

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NOTE 4

Investment income. Gross realized investment and other gains and losses follows:

	For the Three Months Ended March 31,	
	2011	2010
	($000 omitted)	
Realized gains	851	3,194
Realized losses	(719)	(281)
	132	2,913

Expenses assignable to investment income were insignificant. There were no significant investments as of March 31, 2011 that did not produce income during the year.

Proceeds from the sales of investments available-for-sale follows:

	For the Three Months Ended March 31,	
	2011	2010
	($000 omitted)	
Proceeds from sales of investments available-for-sale	15,789	50,743

For the three months ended March 31, 2010, investment and other gains net included realized gains of $1.2 million from the sale of debt and equity investments available-for-sale, $1.2 million from the sale of interests in subsidiaries and $0.5 million from the change in fair value for the cash settlement option related to the convertible senior notes.

NOTE 5

Share-based incentives. The Company accounts for its stock option plan in accordance with the Compensation Stock Compensation Topic of the FASB ASC and uses the modified prospective method under which share-based compensation expense is recognized for new share-based awards granted, and any outstanding awards that are modified, repurchased or canceled subsequent to January 1, 2006. Compensation expense is based on the fair value of the options, which is estimated using the Black-Scholes Model. All options expire 10 years from the date of grant and are granted at the closing market price of the Company s Common Stock on the date of grant. There are no unvested awards since all options are immediately exercisable.

There were no options granted for option awards during the three months ended March 31, 2011 and 2010 and, accordingly, no compensation expense has been reflected in the accompanying condensed consolidated financial statements.

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A summary of the Company s stock option plan follows:

	Options	Weighted-average exercise prices ($)
December 31, 2010	183,700	23.80
Forfeited	(25,000)	20.01
March 31, 2011	158,700	24.39

As of March 31, 2011, the weighted-average remaining contractual life of options outstanding was 2.4 years and there was no aggregate intrinsic value of dilutive options.

During the three months ended March 31, 2011, the Company granted 51,000 shares of fully vested, unrestricted Common Stock with a fair value of $0.6 million, which was recorded as compensation expense. During the same period, the Company also granted 37,000 shares of restricted Common Stock with a fair value of $0.4 million. The restricted Common Stock awards will vest at 20% over five years beginning March 10, 2012. Compensation expense associated with restricted stock awards will be recognized over this vesting period.