MEADOWBROOK INSURANCE GROUP INC
Form 10-K
March 15, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2011

OR

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

Commission File Number: 1-14094

MEADOWBROOK INSURANCE GROUP, INC.
(Exact name of Registrant as specified in its charter)

Michigan	38-2626206
(State of Incorporation)	(IRS Employer Identification No.)
26255 American Drive, Southfield, MI	48034-6112
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (248) 358-1100
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Exchange on Which Registered
Common Stock, $.01 par value per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes o No x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes o No x

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Website, 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 x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 x Non-accelerated filer o 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 x

The aggregate market value of the voting and non-voting common stock held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of June 30, 2011 was $523,993,272. As of March 5, 2012, there were 50,920,511 shares of the Company's common stock ($.01 par value) outstanding.

Documents Incorporated by Reference

Certain portions of the Registrant's Proxy Statement for the 2012 Annual Shareholders' Meeting scheduled for May 17, 2012 are incorporated by reference into Part III of this report.

MEADOWBROOK INSURANCE GROUP, INC.

PART I

ITEM 1. BUSINESS

Legal Organization

As used in this Form 10-K, references to the “Company”, “we”, “us”, or “our” refer to Meadowbrook Insurance Group, Inc. (“Meadowbrook”) and its subsidiaries: Star Insurance Company (“Star”), ProCentury Corporation (“ProCentury”), Meadowbrook Inc., and Crest Financial Corporation. References to Meadowbrook also includes Star’s wholly-owned subsidiaries Ameritrust Insurance Corporation (“Ameritrust”), Savers Property and Casualty Insurance Company (“Savers”), and Williamsburg National Insurance Company (“Williamsburg”) and ProCentury’s wholly-owned subsidiaries Century Surety Company (“Century”), ProCentury Insurance Company (“PIC”), and ProCentury Risk Partners Insurance Company (“Propic”).

Star, Savers, Williamsburg, Ameritrust, Century, and PIC are collectively referred to as the Insurance Company Subsidiaries.

Meadowbrook was founded in 1955 as Meadowbrook Insurance Agency and was subsequently incorporated in Michigan in 1965. Meadowbrook Insurance Group, Inc. (“We,” “Our,” “Us,” or “Meadowbrook”) (NYSE: MIG) is a holding company organized as a Michigan corporation in 1985. Our principal executive offices are located at 26255 American Drive, Southfield, Michigan 48034-6112 (telephone number: (248) 358-1100).

Business Overview

We are a specialty niche focused commercial insurance underwriter and insurance administration services company. We market and underwrite specialty property and casualty insurance programs and products on both an admitted and non-admitted basis through a broad and diverse network of independent retail agents, wholesalers, program administrators and general agents, who value service, specialized knowledge, and focused expertise. Program business refers to an aggregation of individually underwritten risks that have some unique characteristic and are distributed through a select group of agents. We seek to combine profitable underwriting, income from our net commissions and fees, investment returns and efficient capital management to deliver consistent long-term growth in shareholder value.

Through our retail property and casualty agencies, we also generate commission revenue. Our agencies are located in Michigan, California, and Florida and produce commercial, personal lines, life and accident and health insurance that is placed primarily with unaffiliated insurance carriers. Our agencies are a minimal source of business for our Insurance Company Subsidiaries.

We recognize revenue related to the services and coverages within the following categories: net earned premiums, management fees, claims fees, loss control fees, reinsurance placement, investment income, commission revenue, and net realized gains (losses).

We compete in the specialty insurance market. Our wide range of specialty niche insurance expertise allows us to accommodate a diverse distribution network ranging from specialized program agents to insurance brokers. In the specialty market, competition tends to place considerable focus on availability, service and other tailored coverages in addition to price. Moreover, our broad geographical footprint enables us to function with a local presence on both a regional and national basis. We also have the capacity to write specialty insurance in both the admitted and non-admitted markets. These unique aspects of our business model enable us to compete on factors other than price.

The Meadowbrook Approach

We have built our business in a manner that enables us to adapt to changing market conditions and deliver consistent, profitable results. The following highlights key aspects of our model that contribute to our balanced approach:

Diverse Revenue Sources: We generate the vast majority of our revenues from net earned premiums. To grow our premiums, we have developed specialty niche expertise relative to a wide range of underwriting risks. Consequently, our premium base is broadly diversified by line of business, customer, type of distribution and geography. We also generate fee-for-service revenues from risk management services and commission revenue from our agency that are not related to our insurance underwriting operations. Our range of capabilities provides flexibility for our long-term business development efforts as we seek to continue to generate profitable growth. We also believe revenue diversification reduces our risk profile and enables us to deliver more predictable results.

Positioned to Manage Insurance Cycles: We serve markets that operate on different cycles; this diversification enhances the stability of our earnings. Our admitted market capabilities generally provide a consistent source of revenues as this market generally has less pronounced cycles, higher renewal retentions, and more stable pricing than the non-admitted markets. Our non-admitted capabilities enable us to respond opportunistically to the unavailability of insurance and volatile pricing environment. We believe our mix of admitted and non-admitted capabilities enhances our profitability without increasing our risk profile.

MEADOWBROOK INSURANCE GROUP, INC.

Conservative Investment Philosophy: We seek to generate consistent investment income through a low-risk, high-quality investment portfolio. We manage overall credit, interest rate, and liquidity risks when making investment decisions. We invest in highly rated, investment grade securities. We manage the duration of our investment portfolio to match our liabilities and ensure that we have sufficient liquidity to fund our cash needs without having to sell securities prior to maturity. This approach reinforces our focus on underwriting profitability and reduces our overall risk-return profile.

Ability to Attract and Retain Talented Insurance Professionals throughout U.S.: We have assembled a team of talented insurance professionals with a wide range of expertise across all functions and lines of business. Moreover, our regional structure enables our associates to deliver strong and responsive local service to our clients. We believe this is a unique aspect of our business model that enables us to better serve our agency network.

Culture of Disciplined Underwriting, Claims Handling & Reserving: Our associates have significant experience across all functions of our business including underwriting, claims handling, and reserving. New business opportunities undergo a vigourous due diligence process with input provided from key functional areas. Our underwriters are focused on generating profitable underwriting results, rather than top line premium growth. Our main street excess and surplus lines business includes binding authority and brokerage production sources. We re-underwrite the binding authority produced files for accuracy and completeness through our dedicated binding authority teams and further control the risks assumed by issuing all the policies to assure compliance with our policy and underwriting protocols. Further, the vast majority of this business can be handled within our CenturyOnLine ("COL") online quote and bind system used by our general agents. Our non-admitted programs business employs dedicated undewriting specialists in the particular class of business being considered. These professionals review policy files for completeness and compliance with our terms, conduct on site audits, and when necessary send and enforce underwriting notifications on files found to be out of compliance. However this business is generally issued by the program manager. With regard to property coverages, we limit exposures to catastrophe prone areas and purchase excess of loss and catastrophe insurance. Additionally, our actuarial associates support underwriting with pricing and loss analysis. We have also built a robust control environment where underwriting trends are closely monitored on a very granular level, which enables us to proactively manage our business and deliver consistent, profitable results. Finally, we have built a strong claims handling function internally and play a substantial role in claims management and handling activities.

Strong Capital and Liquidity Position: We believe the Company is currently operating from a strong capital position. Our Insurance Company Subsidiaries are rated “A-” (Excellent) by A.M. Best Company (“A.M. Best”). A.M. Best’s ratings represent an independent third-party evaluation that provides an opinion of an insurer’s financial strength and ability to meet ongoing obligations to policyholders. We believe our Insurance Company Subsidiaries are well capitalized and have adequate surplus to support meaningful future premium growth. We generate cash flows from both regulated and non-regulated sources, which provides us with the flexibility to grow profitably during different market cycles. Additionally, our debt levels are very manageable and we have access to a $35 million line of credit that is available for general business purposes ($4.5 million outstanding balance as of December 31, 2011). See “Management’s Discussion and Analysis” for a further discussion of our liquidity position.

Our approach has delivered results over time. Between 2007 and 2011, net operating income has grown at a compound annual growth rate (CAGR) of 10.0% from $27.9 million to $40.9 million. Over the same period, our book value per share has grown at a CAGR of 9.2% and from $8.16 to $11.60. The Board has declared quarterly dividends starting in first quarter of 2008. On February 9, 2012 the Board declared the most recent dividend of $0.05 per share for shareholders of record as of March 21, 2012 and payable on April 5, 2012.

Objective and Strategy

Our objective is to generate predictable results across the market cycle, with a target return on average equity range ("ROAE") of 10%-17%. We view this objective relative to the risk free, reinvestment rate. If the current, low interest rate environment persists, our ability to achieve a 10% ROAE in the short term may be adversely impacted. To achieve these results we seek to leverage the unique characteristics of our balanced business model to generate:

- Consistent, profitable underwriting results
- Predictable investment income in a low-risk, high-quality, fixed income portfolio
- Profitable growth both organically and through acquisitions
- Strong cash flow from our Insurance Company Subsidiaries and non-regulated fee-based services to leverage invested assets to equity and manage debt service
- Steady fee and commission income

We monitor our objectives and strategy in the context of the interest rate environment, insurance market cycle conditions, and general economic conditions. As we seek to maximize long-term shareholder value, our priorities may be influenced by these factors.

MEADOWBROOK INSURANCE GROUP, INC.

Significant Mergers, Acquisitions, and Strategic Investments

Meadowbrook actively reviews merger, acquisition and strategic investment prospects and these transactions play a significant role in our growth strategy. We consider a range of strategic factors when looking at acquisitions including:

- High probability that revenue and cost synergies such as the ability to leverage our diverse revenue platform, expansion of current distribution network, enhancement of servicing capabilities, and complimentary product lines and classes.
- Opportunity to both expand an existing specialty into new markets and expand into new specialty areas.
- Ability to attract and retain talented insurance professionals that blend with our culture.
- Opportunity to create “win-win” situations by mitigating our downside risk and providing sellers with opportunity to obtain fair value through deal structure, including adjustments to the purchase price based upon actual results.

The following is a summary of significant transactions we have entered into during the last five years:

Midwest Financial Holdings, LLC (“MFH”): In July 2009, our subsidiary, Star, purchased a 28.5% ownership interest in MFH. MFH is a limited liability holding company with the primary purpose of providing workers’ compensation insurance coverage for a variety of businesses. MFH’s holding company system consists of a managing general agency and an insurance company. We serve as the primary market for MFH’s managing general agent and we have a quota share agreement in place with MFH’s insurance company. We performed an analysis under ASC 810 – Consolidations and determined that we are not MFH’s primary beneficiary. Therefore, we are not required to consolidate this investment. Accordingly, we account for this investment under the equity method of accounting. Under this accounting method we recognize 28.5% of MFH’s profits and losses.

ProCentury Corporation (“ProCentury”): In July 2008, we completed the ProCentury Corporation (“ProCentury”) merger (“Merger”). ProCentury is a specialty insurance company that primarily underwrites general liability, commercial property, environmental, garage, commercial multi-peril, commercial auto, surety, and marine insurance primarily. This business is primarily in the excess and surplus lines or “non-admitted” market and is distributed through a select group of general agents. Since the completion of the merger, we have been able to leverage our existing infrastructure and increased size.

U.S. Specialty Underwriters, Inc. (“USSU”): In April 2007, we acquired the business of USSU. USSU is a specialty program manager that produces fee based income by underwriting targeted classes within excess workers’ compensation coverage for a select group of insurance companies through its national network of agents and brokers. This acquisition enhanced our existing specialty niche capabilities and expanded our distribution network. During the fourth quarter of 2010 this program was converted into an insured program within the Company’s underwriting subsidiary. Consequently, the Company now generates underwriting profits from this business, as well as investment income. As this book matures on our paper, we should also generate an increasing amount of net investment income. Prior to the conversion, Meadowbrook generated fee income through USSU.

Description of Programs, Products, and Services

We market and underwrite specialty property and casualty insurance programs and products on both an admitted and non-admitted basis. We categorize our products into the following four categories:

Admitted Programs and Standard Market Products: The admitted programs that we write are characterized by risks that are homogeneous or similar within programs but have a diverse geographic profile. We also write a range of standard market products that are distributed through specialty agents. Generally, the average account premium for our admitted programs and standard market products is within a range of $1,000 to $7,000 and due to the specialized nature of the program and distribution style, our admitted programs have high premium retention levels. This helps create stability in our business amid the cyclicality of the insurance industry. Examples of admitted programs we write are coverages for the food service industry, educators, and auto re-possessors. The largest line of business for our standard market products is workers' compensation.

Main Street Excess and Surplus Lines: The excess and surplus lines business we write is characterized by broad classes of "Main Street" commercial risks that are ineligible for coverage by the standard market. Similar to our admitted programs and standard market products, the average account premium is within a range of $1,000 to $7,000 for the excess and surplus lines risks we write. The excess and surplus lines regulatory environment allows rate and form freedom, which gives us the flexibility to design tailored coverage forms that are often more restrictive than those available in the admitted market. The high degree of flexibility contributes to heightened competition during soft markets and creates the potential for rapid expansion during hard markets. Examples of our excess and surplus lines business we underwrite are coverages for restaurants, bars/taverns, apartments, hotels/motels, convenience stores and contractors' liability.

MEADOWBROOK INSURANCE GROUP, INC.

Non-Admitted Programs: The non-admitted programs we write have characteristics that are similar to our admitted programs; however, the commercial risks we provide coverage for are ineligible for coverage by the standard or admitted market. With this focus on non-admitted program underwriting, we are able to provide coverage for start-up organizations and relatively low volume programs that other markets are unable or unwilling to serve. Examples of non-admitted programs we offer include coverages for pet-sitters, oil and gas contractors, professional liability and package delivery.

Specialty Market Products: We also offer specialty market products, where specific and unique underwriting expertise is required. We develop solutions for specific market segments that may leverage either our admitted market or non-admitted market product capabilities, or both, depending on the market need. The specific and unique underwriting expertise that is required to write business profitably in the segments we serve creates barriers to entry for new competitors. Examples of specialty markets we serve are the excess workers' compensation, environmental, agriculture and marine.

As part of delivering our insurance programs and products we are actively involved in a range of activities as described below.

Program and Product Design. Before implementing a new program on behalf of a client, we generally review: (1) financial projections for the contemplated program, (2) historical loss and actuarial experience, (3) actuarial studies of the underlying risks, (4) the credit worthiness of the potential agent or client, and (5) the availability of reinsurance. Our senior management team and associates representing each of the risk-management disciplines work together to design, market, and implement new programs. Our due diligence process is structured to provide an underwriting risk assessment of the program and how the program fits within our client's entity wide business plan and our overall risk profile.

Underwriting Risk Selection and Policy Issuance. Our underwriting personnel help develop the proper criteria for selecting risks, while actuarial and reinsurance personnel evaluate and recommend the appropriate levels of rate and risk retention. The program is then tailored according to the requirements and qualifications of each client. With managed programs, we may also perform underwriting services based upon the profile of the specific program for a fee.

Claims Administration and Handling. We provide substantially all claims management and handling services for workers' compensation and most other lines, such as property, auto liability, professional liability, and general liability. Our claims handling is managed by our field offices. Corporate claims monitors the results through self-audits, corporate claim audits, internal controls, and other executive oversight reports. With the exception of MFH, whom we have direct access to their paid and case reserve loss data and perform corporate claims audits, we handle substantially all claims functions for the majority of the programs we manage. Our involvement in claims administration and handling provides benchmarks and valuable feedback to program managers in assessing the client's risk environment and the overall structure of the program.

Loss Prevention and Control. We provide loss control services, which are designed to help clients prevent or limit the impact of certain loss events. Through an evaluation of the client's workplace environment, our loss control specialists assist the client in planning and implementing a loss prevention program and, in certain cases, provide educational and training programs. With our managed programs, we provide these same services for a fee based upon the profile of the specific program.

We also provide the following services to our fee-for-service and agency clients:

Administration of Risk-Bearing Entities. We generate fee revenue by assisting in the formation and administration of risk-bearing entities for clients and agents. Through our subsidiaries in Bermuda and Washington D.C., we provide administrative services for certain captives and/or rent-a-captives.

Agency. We earn commission revenue through the operation of our retail property and casualty insurance agencies, located in Michigan, California and Florida. These agencies produce commercial, personal lines, life and accident and health insurance with more than fifty unaffiliated insurance carriers.

MEADOWBROOK INSURANCE GROUP, INC.

Distribution

We market our specialty property and casualty insurance products on both an admitted and non-admitted basis through a broad and diverse network of independent retail agents, wholesalers, program administrators and general agents (referred to as, “agents” or “producers”). On a limited basis, some of our producers provide certain policy issuance functions on our behalf.

Unlike typical standard market companies that sell a menu of capabilities to their distribution network, we selectively determine distribution and target agents that meet the individual admitted program and standard market product focus and needs.

Our largest producer in 2011 was Midwest General Insurance Agency, LLC, which, in combination with its affiliates, accounted for 14.7% of our gross written premium. We have a 28.5% equity interest in Midwest General Agency’s parent, MFH. No other producer was responsible for more than 10% of our gross written premium.

We seek to incentivize our distribution network in a manner that aligns their financial interests with our continued profitability. Our experience has been that the number of claims and the cost of losses tend to be lower in risk-sharing programs than with traditional forms of insurance. We believe that risk-sharing motivates participants to focus on underwriting selection, loss prevention, risk control measures and adherence to stricter underwriting guidelines. Risk sharing structures are designed based on the particular risk management goals of our clients, market conditions and our assessment of the opportunity for operating profit. We categorize risk sharing into two categories: profit sharing and quota sharing.

Profit-Sharing: In addition to the initial commission allowed to the producing agent, we at times offer various program dependent, profit-sharing commission contracts. These are tailored to the specific product and its attributes.

Quota Sharing: A second way we incentivize our producers is through quota sharing reinsurance structures. In these scenarios, producers of the business determine which risks to submit to us for underwriting. For risks submitted, Meadowbrook underwrites individual primary insurance policies for members of a group or association, or a specific industry. We share in the operating results with the producer through a quota share reinsurance agreement with an insurance company (owned by the producer) or a captive or rent-a-captive.

We believe our selective approach to distribution also serves to align the agents’ financial interests with our continued profitability. Our selective approach reduces channel conflict and allows our agencies to generate franchise value. This is a mutually beneficial approach to enhancing the value of our distribution relationships.

Technology

We seek to leverage our business technology platform in order to achieve a high level of customer service and enhance operating efficiencies. We provide a select set of internet-based business processing systems to our producers to automate their capability to rate, quote, bind and service insurance policies in a timely and efficient manner. Advantage is a processing system for quoting and binding workers’ compensation insurance policies. COL is a processing system for quoting, binding, and issuing policies for general liability, property and garage insurance policies underwritten by our excess and surplus lines company, Century. Further, we provide additional systems on a network-accessible basis for processing select package and commercial auto programs. In addition to reducing our internal administrative processing costs, these systems enhance underwriting practices by automating risk selection criteria.

Competition and Pricing

As a provider of specialty niche programs, products and risk management services, we are part of a highly competitive industry that is cyclical and historically characterized by periods of high premium rates and shortages of underwriting capacity followed by periods of intense competition and excess underwriting capacity. We compete with other providers of specialty insurance programs, products, and risk management services, as well as, with traditional providers of commercial insurance. Some of our competitors may have greater financial resources than we do.

Pricing is a primary means of competition in the commercial insurance market. Competition is also based on the availability and quality of products, quality and speed of service (including claims service), financial strength, ratings, distribution systems and technical expertise. In addition to the factors noted above, the insurance industry also competes on commission rates. As noted above, we have a selective approach to distribution. Consequently, our distribution channel partners are highly focused and have a limited appetite, which enables them to generate business that results in better than industry average loss results. This allows us to be competitive on commission rates where needed for profitable business.

Principal competitive factors for providing risk management services include the costs of self-insuring relative to the cost of purchasing insurance from an insurance carrier, the availability and pricing of excess reinsurance coverage, cash flow needs, and the expected quality and consistency of the services to be provided.

We believe that we are able to compete based on our experience, the quality of our products and services, our processing technology platforms, and our program-oriented approach. However, our ability to successfully compete is dependent upon a number of factors, including market and competitive conditions, many of which are outside of our control.

Geographic Diversity and Mix of Business

Our revenues are diversified geographically, by class and line of business, type of insured and distribution. Our corporate strategy emphasizes a regional focus and diverse source of revenues between underwriting premiums, fee-for-service revenue and commissions. We believe our approach balances an effective local touch with efficient national coordination. Additionally, this allows us to leverage fixed costs over a larger revenue base and opportunistically take advantage of new opportunities. Within the workers' compensation line of business, we have a regional focus in California and New England. Within the other liability, commercial auto liability, excess worker's compensation, and commercial multiple peril liability lines of business, we have a regional focus in the Southeast and California. Within the commercial multiple property line of business we have a focus in Texas. Our fee-for-service business is managed on a regional basis with an emphasis in the Midwest, New England, and southeastern regions of the United States.

The following table summarizes our gross written premium distribution by state for the years ended December 31, 2011, 2010, and 2009 (in thousands). We include only states that were top ten gross written premium production states in 2011:

Gross Written Premium	2011	%		2010	%		2009	%	
California	300,539	33.2	%	285,771	35.6	%	209,293	30.4	%
Florida	89,068	9.9	%	80,876	10.1	%	74,639	10.8	%
Texas	58,760	6.5	%	51,621	6.4	%	51,506	7.5	%
New Jersey	39,972	4.4	%	38,198	4.8	%	41,095	6.0	%
New York	33,455	3.7	%	25,366	3.2	%	21,704	3.2	%
Illinois	24,644	2.7	%	18,772	2.3	%	15,432	2.2	%
Missouri	23,709	2.6	%	23,882	3.0	%	23,711	3.4	%
Michigan	22,030	2.4	%	23.074	2.9	%	17,445	2.5	%
Pennsylvania	19,970	2.2	%	15,143	1.9	%	14,771	2.1	%
Louisiana	18,531	2.0	%	16,878	2.1	%	15,937	2.3	%
All Other States	273,351	30.4	%	222,319	27.7	%	203,154	29.6	%
Total	904,029	100.0	%	801,900	100.0	%	688,687	100.0	%

Our most significant geographic concentration is in the state of California. After studying the California market for several years and concluding that profitable growth could be achieved in select niche areas, we decided to enter the California workers' compensation market in 2009. Our current book of business in this state is largely related to our relationship with a general agent who specializes in non-contractor workers' compensation, as well as a program, which includes a general agent that primarily focuses on the food service industry. It is important to note the business we added has a history of underwriting profitability. Moreover, indications are that rate increases have been keeping up with the underlying loss trends and overall the business remains profitable.

As part of our growth strategy, we manage our business to reduce geographic concentration of risk that could increase our exposure to losses from natural or intentionally caused catastrophic events. We also monitor the regulatory environment within our concentrated regions. We believe we have been able to strategically increase our California exposure, while maintaining a geographically diverse premium base.

MEADOWBROOK INSURANCE GROUP, INC.

The following table summarizes gross written premiums, net earned premiums, and net written premiums by line of business for the years ended December 31, 2011, 2010, and 2009 (in thousands):

Gross Written Premium	2011	%		2010	%		2009	%	
Workers' Compensation	$345,402	38.21	%	$320,348	39.95	%	$233,269	33.87	%
Other Liability	150,751	16.67	%	129,876	16.19	%	140,541	20.41	%
Commercial Auto Liability	99,409	11.00	%	101,096	12.61	%	92,632	13.45	%
Commercial Multi-Peril Property	68,745	7.60	%	62,769	7.83	%	54,901	7.97	%
Excess Worker's Compensation	68,058	7.53	%	34,235	4.27	%	29,427	4.27	%
Commercial Multi-Peril Liability	51,133	5.66	%	47,493	5.92	%	43,428	6.31	%
All Other Lines	120,528	13.33	%	106,083	13.23	%	94,489	13.72	%
Total	$904,026	100.00	%	$801,900	100.00	%	$688,687	100.00	%

Net Earned Premium	2011	%		2010	%		2009	%	
Workers' Compensation	$314,825	42.11	%	$275,585	41.76	%	$163,834	30.36	%
Other Liability	112,610	15.07	%	105,024	15.92	%	121,324	22.49	%
Commercial Auto Liability	91,576	12.24	%	89,215	13.52	%	79,802	14.79	%
Commercial Multi-Peril Property	57,138	7.64	%	$48,956	7.42	%	$45,660	8.46	%
Excess Worker's Compensation	35,471	4.74	%	$17,690	2.68	%	$19,162	3.55	%
Commercial Multi-Peril Liability	48,738	6.52	%	41,697	6.32	%	37,133	6.88	%
All Other Lines	87,277	11.68	%	81,673	12.38	%	72,687	13.47	%
Total	$747,635	100.00	%	$659,840	100.00	%	$539,602	100.00	%

Net Written Premium	2011	%		2010	%		2009	%	
Workers' Compensation	$314,168	40.47	%	$291,670	42.05	%	$206,246	35.56	%
Other Liability	123,651	15.93	%	103,350	14.90	%	113,004	19.49	%
Commercial Auto Liability	91,948	11.85	%	91,860	13.24	%	82,499	14.22	%
Commercial Multi-Peril Property	59,908	7.72	%	54,667	7.88	%	45,462	7.84	%
Excess Worker's Compensation	44,234	5.70	%	21,839	3.15	%	18,917	3.26	%
Commercial Multi-Peril Liability	49,333	6.36	%	45,620	6.58	%	38,825	6.69	%
All Other Lines	93,011	11.97	%	84,593	12.20	%	75,065	12.94	%
Total	$776,253	100.00	%	$693,599	100.00	%	$580,018	100.00	%

In 2011, we increased our premium writings within the excess workers' compensation line of business. This increase was driven primarily by the conversion of an existing fee-based program into an insured program where we now write the underwriting risk on our paper. The conversion of this business began in the fourth quarter of 2010 and was completed in 2011 and increased gross written premium by approximately $34.0 million in 2011.

We also experienced a moderate increase in our workers' compensation line of business during 2011. This increase primarily reflects the maturation of existing programs, as well as rate increases achieved during the year. For the year, our workers' compensation rates increased 3.4%.

Our other liability line of business is comprised of both shorter tail lines of business, such as habitational risks (i.e., hotels, motels and apartments, mercantile operations, etc.), and longer tail lines of business, such as, public entity excess and environmental. Growth in this line of business has been primarily driven by maturation of existing specialties.

We reduced our commercial auto premium writings during 2011. This primarily reflects underwriting pricing actions intended to improve the profitability of a program that was not meeting our expected targets.

Overall, we believe we have achieved controlled, profitable growth.

MEADOWBROOK INSURANCE GROUP, INC.

Reserves

The following table shows the development of reserves for unpaid losses and loss adjustment expenses (“LAE”) from 2002 through 2011 for our Insurance Company Subsidiaries, and the deconsolidation impact of American Indemnity Insurance Company, Ltd (“American Indemnity”). American Indemnity is a wholly-owned subsidiary that is not consolidated pursuant to ASC 810 – Consolidations. Prior to 2004, we consolidated American Indemnity.

Development on the ProCentury acquired reserves is not included for the years prior to 2008, because our merger was not effective until August 1, 2008. The lower portion of the table reflects the impact of reinsurance for the years 2002 through 2011 reconciling the net reserves shown in the upper portion of the table to gross reserves.

Additional information relating to our reserves is included within the Losses and Loss Adjustment Expenses and Reinsurance Recoverables section of Note 1 ~ Summary of Significant Accounting Policies and Note 4 ~ Liability for Losses and Loss Adjustment Expenses of the Notes to the Consolidated Financial Statements, as well as to the Critical Accounting Policies section and the Reserves section of Item 7, Management’s Discussion and Analysis.

MEADOWBROOK INSURANCE GROUP, INC.

Analysis of Loss and Loss Adjustment Expense Development (1)

	Years Ended December 31,								
	2002	2003	2004	2005	2006	2007	2008	2009	20
	(in thousands)								
Reserves for losses and LAE at end of period	$193,116	$192,019	$226,996	$271,423	$302,655	$341,541	$625,331	$682,376	$784
Deconsolidation of subsidiary	(2,973)	(2,989)							
Adjusted reserves for losses and LAE at end of period	$190,143	$189,030	$226,996	$271,423	$302,655	$341,541	$625,331	$682,376	$784
Cumulative paid as of									
1 year later	78,023	71,427	79,056	83,271	81,779	95,393	173,525	187,818	269
2 years later	122,180	118,729	124,685	133,809	140,308	155,745	279,221	338,925	
3 years later	151,720	145,279	153,780	170,226	207,227	197,558	369,313		
4 years later	167,288	159,220	171,946	210,110	204,802	233,421			
5 years later	174,778	169,980	195,328	210,993	228,284				
6 years later	180,489	184,663	195,691	226,048					
7 years later	190,133	183,961	204,939						
8 years later	187,692	190,965							
9 years later	191,268								
Reserves re-estimated as of end of year:									
1 year later	193,532	193,559	231,880	268,704	295,563	330,416	596,661	651,373	791
2 years later	196,448	203,394	227,462	263,069	286,647	327,862	566,878	654,641	
3 years later	202,126	205,650	226,437	261,319	283,583	331,034	568,751		
4 years later	203,738	202,748	226,492	260,373	293,897	339,931			
5 years later	202,028	202,716	229,746	268,007	303,948				
6 years later	201,786	203,727	233,560	276,374					
7 years later	201,355	207,401	238,547						
8 years later	203,867	209,606							
9 years later	204,332								
Net cumulative redundancy (deficiency):									
Dollars	$(14,189)	$(20,575)	$(11,552)	$(4,951)	$(1,294)	$1,610	$56,580	$27,736	$(7,3
Percentage	-7.5 %	-10.9 %	-5.1 %	-1.8 %	-0.4 %	0.5 %	9.0 %	4.1 %	-0.9

Net reserves	190,143	189,030	226,996	271,423	302,655	341,541	625,331	682,376	784
Ceded reserves	181,817	147,446	151,161	187,254	198,422	198,461	260,366	266,801	280
Gross reserves	371,960	336,476	378,157	458,677	501,077	540,002	885,697	949,177	1,06
Net re-estimated	204,332	209,606	238,547	276,374	303,948	339,931	568,751	654,641	791
Ceded re-estimated	257,016	245,826	207,893	207,915	203,039	200,220	242,105	255,081	284
Gross re-estimated	461,347	455,432	446,440	484,289	506,988	540,151	810,856	909,721	1,07
Gross cumulative redundancy (deficiency)	$(89,387)	$(118,955)	$(68,284)	$(25,612)	$(5,911)	$(150)	$74,840	$39,456	$(10

(1) In accordance with ASC 810 - Consolidations, we performed an evaluation of our business relationship and determined that our wholly owned subsidiary, American Indemnity, did not meet the tests for consolidation, as neither us, nor our subsidiary Star, are the primary beneficiaries of American Indemnity. Therefore, effective January 1, 2004, we deconsolidated American Indemnity on a prospective basis in accordance with the provisions of ASC 810. Accordingly, we have adjusted the reserves and development within the above table. The adoption of ASC 810 and the deconsolidation of American Indemnity did not have a material impact on our consolidated balance sheet or consolidated statement of income.

MEADOWBROOK INSURANCE GROUP, INC.

The following table sets forth the difference between GAAP reserves for loss and loss adjustment expenses and statutory reserves for loss and loss adjustment expenses at December 31, (in thousands):

	2011	2010
GAAP reserves for loss and LAE	$1,194,977	$1,065,056
Reinsurance recoverables for unpaid losses	(315,884)	(280,854)
ASC 944 adjustment*	(8,322)	-
Statutory reserves for loss and LAE	$870,771	$784,202

* 100% Quota Share reinsurance agreement related to a worker's compensation replacement policy, with reinsurance provisions recognized as retroactive reinsurance on a GAAP basis in accordance with ASC 944 - Financial Services - Insurance.

For the year ended December 31, 2011, we reported an increase of $10.6 million in gross ultimate loss estimates for accident years 2010 and prior, or 1.0% of $1,065.1 million of gross loss and LAE reserves at January 1, 2011. We reported a $7.3 million increase in net ultimate loss and LAE estimates for accident years 2010 and prior, or 0.9% of $784.2 million of net loss & LAE reserves at January 1, 2011.

For the year ended December 31, 2010, we reported a decrease of $41.3 million in gross ultimate loss estimates for accident years 2009 and prior, or 4.4% of $949.2 million of gross loss and LAE reserves at January 1, 2010. We reported a $31.0 million decrease in net ultimate loss and LAE estimates for accident years 2009 and prior, or 4.5% of $682.4 million of net loss & LAE reserves at January 1, 2010.

Reinsurance

Information relating to our reinsurance structure and treaty information is included within Note 6 ~ Reinsurance of the Notes to the Consolidated Financial Statements.

Investments

Information relating to our investment portfolio is included within Note 3 ~ Investments of the Notes to the Consolidated Financial Statements and the Investments section of Item 7, Management's Discussion and Analysis, as well as Item 7A Quantitative and Qualitative Disclosures about Market Risk.

Regulation

Insurance Company Regulation

Our Insurance Company Subsidiaries are subject to regulation in the states where they conduct business. State insurance regulations generally are designed to protect the interests of policyholders, state insurance consumers or claimants rather than shareholders or other investors. The nature and extent of such state regulation varies by jurisdiction, but generally involves:

- prior approval of the acquisition of control of an insurance company or of any company controlling an insurance company;
- regulation of certain transactions entered into by an insurance company with any of its affiliates;
- approval of premium rates, forms and policies used for many lines of insurance;

- standards of solvency and minimum amounts of capital and surplus that must be maintained;
- establishment of reserves required to be maintained for unearned premium, loss and loss adjustment expense, or for other purposes;
- limitations on types and amounts of investments;
- underwriting and claims settlement practices;
- restrictions on the size of risks that may be insured by a single company;
- licensing of insurers and agents;
- deposits of securities for the benefit of policyholders; and
- the filing of periodic reports with respect to financial condition and other matters.

In addition, state regulatory examiners perform periodic examinations of insurance companies. The results of these examinations can give rise to regulatory orders requiring remedial, injunctive or other corrective action.

Insurance Holding Company Regulation

We operate as an insurance holding company system and are subject to regulation in the jurisdictions in which we conduct business. These regulations require that each insurance company in the system register with the insurance department of its state of domicile and furnish information concerning the operations of companies within the holding company system that may materially affect the operations, management or financial condition of the insurers within the system domiciled in that state. The insurance laws similarly provide that all transactions among members of a holding company system must be fair and reasonable. Transactions between insurance subsidiaries and their parents and affiliates generally must be disclosed to the state regulators, and prior approval of the applicable state insurance regulator generally is required for any material or extraordinary transaction. In addition, a change of control of a domestic insurer or of any controlling person requires the prior approval of the state insurance regulator. Generally, any person who acquires ten percent or more of the outstanding voting securities of the insurer or its parent company is presumed to have acquired control of the domestic insurer.

Various State and Federal Regulation

Insurance companies are also affected by a variety of state and federal legislative and regulatory measures and judicial decisions that define and extend the risks and benefits for which insurance is sought and provided. These include redefinition of risk exposure in areas such as product liability, environmental damage, and workers’ compensation. In addition, individual state insurance departments may prevent premium rates for some classes of insureds from reflecting the level of risk assumed by the insurer for those classes. Such developments may adversely affect the profitability of various lines of insurance. In some cases, these adverse effects on profitability can be minimized through repricing, if permitted by applicable regulations, of coverages or limitations or cessation of the affected business.

Reinsurance Intermediary

Our reinsurance intermediary is also subject to regulation. Under applicable regulations, the intermediary is responsible, as a fiduciary, for funds received on account of the parties to the reinsurance transaction and is required to hold such funds in appropriate bank accounts subject to restrictions on withdrawals and prohibitions on commingling.

Licensing and Agency Contracts

We, or certain of our designated employees, must be licensed to act as agents by state regulatory authorities in the states in which we conduct business. Regulations and licensing laws vary in individual states and are often complex.

Insurance licenses are issued by state insurance regulators upon application and may be of perpetual duration or may require periodic renewal. We must apply for and obtain appropriate new licenses before we can expand into a new state on an admitted basis or offer new lines of insurance that require separate or additional licensing.

Insurers operating on an admitted basis must file premium rate schedules and policy or coverage forms for review and approval by the insurance regulators. In many states, rates and policy forms must be approved prior to use, and insurance regulators have broad discretion in judging whether an insurer’s rates are adequate, not excessive and not unfairly discriminatory.

The applicable licensing laws and regulations in all states are subject to amendment or reinterpretation by state regulatory authorities, and such authorities are vested in most cases with relatively broad discretion as to the granting, revocation, suspension and renewal of licenses. We, or our employees, could be excluded, or temporarily suspended, from continuing with some or all of our activities in, or otherwise subjected to penalties by, a particular state.

Insurance Regulation Concerning Change or Acquisition of Control

Star, Williamsburg, and Ameritrust are domestic property and casualty insurance companies organized under the insurance laws (the “Insurance Codes”) of Michigan, while Savers, Century, PIC, and Propic are organized under the Insurance Codes of Missouri, Ohio, Texas, and Washington D.C., respectively. The Insurance Codes provide that acquisition or change of control of a domestic insurer or of any person that controls a domestic insurer cannot be consummated without the prior approval of the relevant insurance regulatory authority. A person seeking to acquire control, directly or indirectly, of a domestic insurance company or of any person controlling a domestic insurance company must generally file with the relevant insurance regulatory authority an application for change of control (commonly known as a “Form A”) containing information required by statute and published regulations and provide a copy of such Form A to the domestic insurer. In Michigan and Missouri, control is generally presumed to exist if any person, directly or indirectly, owns, controls, holds with the power to vote or holds proxies representing ten percent or more of the voting securities of the company.

In addition, many state insurance regulatory laws contain provisions that require pre-notification to state agencies of a change in control of a non-domestic admitted insurance company in that state. While such pre-notification statutes do not authorize the state agency to disapprove the change of control, such statutes do authorize issuance of a cease and desist order with respect to the non-domestic admitted insurer if certain conditions exist, such as undue market concentration.

Any future transactions that would constitute a change in control would also generally require prior approval by the Insurance Departments of Michigan, Missouri, Ohio, Texas, and Washington D.C. and would require pre-acquisition notification in those states that have adopted pre-acquisition notification provisions and in which the insurers are admitted. Such requirements may deter, delay or prevent certain transactions that could be advantageous to our shareholders.

Membership in Insolvency Funds and Associations and Mandatory Pools

Most states require admitted property and casualty insurers to become members of insolvency funds or associations, which generally protect policyholders against the insolvency of such insurers. Members of the fund or association must contribute to the payment of certain claims made against insolvent insurers. Maximum contributions required by law in any one year vary between 1% and 2% of annual premium written by a member in that state. For 2011, 2010, and 2009, assessments from insolvency funds were $8.6 million, $5.1 million, and $491,000, respectively. Most of these payments are recoverable through future policy surcharges and premium tax reductions. Except for New Jersey, business written on a surplus lines basis is not subject to state guaranty fund assessments.

Our Insurance Company Subsidiaries are also required to participate in various mandatory insurance facilities or in funding mandatory pools, which are generally designed to provide insurance coverage for consumers who are unable to obtain insurance in the voluntary insurance market. Among the pools participated in are those established in certain states to provide windstorm and other similar types of property coverage. These pools typically require all companies writing applicable lines of insurance in the state for which the pool has been established to fund deficiencies experienced by the pool based upon each company’s relative premium writings in that state, with any excess funding typically distributed to the participating companies on the same basis. To the extent that reinsurance treaties do not cover these assessments, they may adversely affect us. For 2011, 2010, and 2009, total assessments paid to all such facilities were $5.0 million, $3.5 million, and $2.7 million, respectively.

Restrictions on Dividends and Risk-Based Capital

For information on Restrictions on Dividends and Risk-based Capital that affect us please refer to Note 8 ~ Regulatory Matters and Rating Issues of the Notes to the Consolidated Financial Statements and the Regulatory and Rating Issues section within Item 7, Management’s Discussion and Analysis.

NAIC-IRIS Ratios

The National Association of Insurance Commissioners’ (“NAIC”) Insurance Regulatory Information System (“IRIS”) was developed by a committee of state insurance regulators and is primarily intended to assist state insurance departments in executing their statutory mandates to oversee the financial condition of insurance companies operating in their respective states. IRIS identifies thirteen industry ratios and specifies “usual values” for each ratio. Departure from the usual values on four or more ratios generally leads to inquiries or possible further review from individual state insurance commissioners. Refer to the Regulatory and Rating Issues section of Item 7, Management’s Discussion and Analysis.

Effect of Federal Legislation

The Terrorism Risk Insurance Act of 2002 (“TRIA”) established a program under which the United States federal government will provide governmental support for businesses that suffer damages from certain acts of international terrorism. In 2007, TRIA was extended through December 31, 2014. The terms of the legislation enacted now also include domestic terrorist acts. TRIA serves as an additional high layer of reinsurance against losses that may arise from a terrorist incident. The impact upon us resulting from TRIA is minimal as we generally do not underwrite risks that are considered targets for terrorism, avoid concentration of exposures in both property and workers’ compensation and have terrorism coverage included in our reinsurance treaties to cover the most likely exposure.

MEADOWBROOK INSURANCE GROUP, INC.

Employees

At March 5, 2012, we employed 1,054 associates to service our clients and provide management services to our Insurance Company Subsidiaries as described below. We believe we have good relationships with our associates.

Available Information

Our Internet address is www.meadowbrook.com. There we make available, free of charge, our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, Statements of Beneficial Ownership (Forms 3, 4, and 5), and any amendments to those reports, as soon as reasonably practicable after we electronically file such material with, or furnish to, the SEC. You may read and copy materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington D.C., 20549. You may obtain information about the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet site that contains reports, proxy statements, and other information that we file at www.sec.gov. Our SEC reports can also be accessed through the investor relations section of our website. The information found on our website is not part of this or any other report we file with, or furnished to the SEC. The Charters of the Nominating and Governance Committee, the Compensation Committee, the Audit Committee, Risk Management and Finance Committee , and Investment Committee, as well as the Board of Directors Governance Guidelines are also available on our website, or available in print to any shareholder who requests this information. In addition, our Compliance Code of Conduct and Business Ethics Policy are available on our website, or in print to any shareholder who requests this information.

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the following risk factors, categorized by "Our Business" and "Our Industry", which could materially affect our business, financial condition or results of operations in future periods.

Risks Related to Our Business

We face competitive pressures in our business that could cause our revenues to decline and adversely affect our profitability.

We compete with a large number of other companies in our selected lines of business. Many of our competitors have greater financial and marketing resources. A number of new, proposed or potential legislative or industry developments could further increase competition in our industry including:

- the formation of new insurers and an influx of new capital in the marketplace as existing companies attempt to expand their business as a result of better pricing and/or terms;
- programs in which state-sponsored entities provide property insurance in catastrophe-prone areas, other alternative market types of coverage; or other non-property insurance; and
- changing practices created by the Internet, which has increased competition within the insurance business.

New competition from these developments could make the property and casualty insurance marketplace more competitive by increasing the supply of insurance capacity. In that event, the current market softens further, and it may negatively influence our ability to maintain or increase rates. Consequently, our profitability could be adversely impacted by increased competition.

Actual loss and loss adjustment expenses may exceed our reserve estimates, which would negatively impact our profitability and financial position.

In many cases, several years may elapse between the occurrence of an insured loss, the reporting of the loss to us and our payment of the loss. To recognize liabilities for unpaid losses, we establish reserves as balance sheet liabilities representing estimates of amounts needed to pay reported and unreported losses and the related loss adjustment expenses. Loss reserves are an estimate of what we anticipate the ultimate costs to be and therefore do not represent an exact calculation of liabilities. Estimating loss reserves is a difficult and complex process involving many variables and subjective judgments. As part of the reserving process, we review historical data and consider the impact of various factors such as:

- Loss emergence patterns;
- Emerging economic and social trends;
- Inflation; and
- Changes in the regulatory and litigation environments.

This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for predicting future results. It also assumes that adequate historical or other data exists upon which to make these judgments. There is no precise method, however, for evaluating the impact of any specific factor on the adequacy of reserves and actual results are likely to differ from original estimates. If the actual amount of insured losses is greater than our reserve estimates, our profitability and financial position could suffer.

In addition, an increase in reserves may also require us to write off a portion of our deferred acquisition costs asset, which would also negatively impact our operating results and financial position.

The failure of any of the loss limitation methods we employ could have a material adverse effect on our results of operations and financial condition.

Various provisions of our policies, such as limitations or exclusions from coverage or choice of forum, have been negotiated to limit our risks. It is possible that a court or regulatory authority could nullify or void an exclusion, or legislation could be enacted that modifies or voids the use of such endorsements and limitations in a way that could have a materially adverse impact on our financial condition and operating results. We also seek to limit our loss exposure by geographic diversification. One or more catastrophic or other events could result in claims that substantially exceed our expectations, which could have an adverse effect on our results of operations or financial condition. Likewise, for catastrophe events and for per-risk events we buy a limited amount of reinsurance coverage that we believe is adequate to reimburse us for our large losses with a very high degree of probability. Should an unlikely event occur that exceeds our reinsurance coverage, then the amounts in excess of our reinsurance coverage could adversely impact our financial condition or results of operations.

Our geographic concentration ties our performance to the business, economic, natural perils, man made perils, and regulatory conditions within our concentrated regions.

One of our predominate lines of business is workers' compensation (42.1% of net earned premiums in 2011), which is concentrated in California. Accordingly, unfavorable business, economic or regulatory conditions in this state could negatively impact our business. California is also exposed to climate and environmental changes, natural perils such as earthquakes, water supplies, and the possibility of pandemics or terrorist acts. Because our business is concentrated in this manner, we may be exposed to economic and regulatory risks or risk from natural perils that are greater than the risks associated with greater geographic diversification. Refer to Note 5 ~ Reinsurance for further information regarding our reinsurance structure related to workers' compensation business.

Our success depends on our ability to appropriately price the risks we underwrite.

Our financial results depend on our ability to underwrite and collect adequate premium rates for a wide variety of risks. Rate adequacy is necessary to generate sufficient premiums to pay losses, loss expenses, and underwriting expenses and to earn a profit. To price our products accurately, we must collect and properly analyze a substantial amount of data, develop, test and apply appropriate rating formulas, monitor and react to changes in trends and project both severity and frequency of losses with reasonable accuracy. These activities are subject to a number of risks and uncertainties that are outside our control, including:

- availability of sufficient reliable data and our ability to properly analyze available data;
- uncertainties that inherently characterize estimates and assumptions;
- selection and application of appropriate rating and pricing techniques;
- changes in legal standards, claim settlement practices, medical care expenses and restoration costs;
- changes in mandated rates or benefits set by the state regulators; and
- legislative actions.

Consequently, we could underprice risks, which would negatively affect our profit margins, or we could overprice risks, which could reduce our sales volume and competitiveness. In either event, our profitability could be materially and adversely affected.

If market conditions cause our reinsurance to be more costly or unavailable, we may be required to bear increased risks or reduce the level of our underwriting commitments.

As part of our overall risk and capacity management strategy, we purchase reinsurance for significant amounts of risk underwritten by our Insurance Company Subsidiaries, especially for the excess-of-loss and severity risks. Market conditions beyond our control determine the availability and cost of the reinsurance we purchase, which may affect the level of our business and profitability. Our reinsurance facilities are generally subject to annual renewal. We may be unable to maintain our current reinsurance facilities or to obtain other reinsurance in adequate amounts and at favorable rates. Increases in the cost of reinsurance would adversely affect our profitability. In addition, if we are unable to renew our expiring facilities or to obtain new reinsurance on favorable terms, either our net exposure to risk would increase or, if we are unwilling to bear an increase in net risk exposures, we would have to reduce the amount of risk we underwrite.

Our reinsurers may not pay on losses in a timely fashion, or at all, which may cause a substantial loss and increase our costs.

We purchase reinsurance by transferring part of the risk we have assumed (known as ceding) to a reinsurance company in exchange for part of the premium we receive in connection with the risk under pro-rata and excess-of-loss contracts. These reinsurance arrangements diversify our business and reduce our exposure to large losses or from hazards of an unusual nature. Although reinsurance makes the reinsurer liable to us to the extent the risk is transferred, the ceding of insurance does not discharge us of our primary liability to our policyholder. Therefore, we are subject to credit risk with respect to the obligations of our reinsurers. If our reinsurers fail to pay us or fail to pay on a timely basis, our financial results and financial condition could be adversely affected. In order to minimize our exposure to significant losses from reinsurer insolvencies, we evaluate the financial condition of our reinsurers and monitor the economic characteristics of the reinsurers on an ongoing basis and, if appropriate, we may require trust agreements to collateralize reinsurers' financial obligation to us.

We may be adversely affected by interest rate changes.

Our investment portfolio is predominantly comprised of fixed income securities. These securities are sensitive to changes in interest rates. An increase in interest rates typically reduces the fair market value of fixed income securities. In addition, if interest rates decline, investment income earned from future investments in fixed income securities will be lower.

We generally hold our fixed income securities to maturity, so our interest rate exposure does not usually result in realized losses. However, as noted above, rising interest rates could result in a significant reduction of our book value. While, a low investment yield environment could adversely impact our net earnings, as a result of fixed income securities maturing and being replaced with lower yielding securities which impact investing results.

Interest rates are highly sensitive to many factors beyond our control including general economic conditions, governmental monetary policy, and political conditions. As discussed above, fluctuations in interest rates may adversely impact our business. See "Item 7A. Qualitative and Quantitative Disclosures About Market Risk" for further discussion on interest rate risk.

Our investment portfolio is subject to market and credit risks, which could affect our financial results and ability to conduct business.

Our investment portfolio is subject to overall market risk and credit risk of the individual issuers of securities. The value of investments in marketable securities is subject to impairment as a result of deterioration in the creditworthiness of the issuer. Although we try to manage this risk by diversifying our portfolio and emphasizing credit quality, our investments are subject to losses as a result of a general downturn in the economy. A severe economic downturn could have a material adverse impact on our results from operations and our financial condition.

We could be forced to sell investments to meet our liquidity requirements.

We invest the premiums we receive from customers until they are needed to pay policyholder claims or until they are recognized as profits. Consequently, we seek to match the duration of our investment portfolio with the duration of our loss and loss adjustment expense reserves to ensure strong liquidity and avoid having to liquidate securities to fund claims. As an example, we ladder the maturities of our investment portfolio to ensure we have adequate liquidity to fund anticipated liabilities that are coming due. We believe that we are currently well positioned from a liquidity perspective. That said, risk factors such as inadequate loss and loss adjustment reserves or unfavorable trends in litigation could potentially result in the need to sell investments to fund these liabilities. This could result in significant realized losses depending on the conditions of the general market, interest rates and credit issues with individual securities.

A decrease in our A.M. Best rating could negatively affect our business.

Insurance companies are subject to financial strength ratings produced by external rating agencies. Higher ratings generally indicate greater financial stability and a stronger ability to pay claims. Ratings are assigned by rating agencies to insurers based upon factors they believe are important to policyholders. Ratings are not recommendations to buy, hold, or sell our securities.

Our ability to write business is most influenced by our rating from A.M. Best. A.M. Best ratings are designed to assess an insurer's financial strength and ability to meet continuing obligations to policyholders. Currently, our financial strength rating from A.M. Best is "A−" (Excellent) for our Insurance Company Subsidiaries. There can be no assurance that A.M. Best will not change this rating in the future. A rating downgrade from A.M. Best could materially adversely affect the business we write and our results of operations.

Provisions of the Michigan Business Corporation Act, our articles of incorporation and other corporate governing documents and the insurance laws may discourage takeover attempts.

The Michigan Business Corporation Act contains "anti-takeover" provisions. Chapter 7A (the "Fair Price Act") of the Business Corporation Act applies to us and may have an anti-takeover effect and may delay, defer or prevent a tender offer or takeover attempt that a shareholder might consider in their best interest, including those attempts that might result in shareholders receiving a premium over market price for their shares.

The Fair Price Act provides that a supermajority vote of ninety percent of the shareholders and no less than two-thirds of the votes of non interested shareholders must approve a "business combination." The Fair Price Act defines a "business combination" to encompass any merger, consolidation, share exchange, sale of assets, stock issue, liquidation, or reclassification of securities involving an "interested shareholder" or certain "affiliates." An "interested shareholder" is generally any person who owns ten percent or more of the outstanding voting shares of the company. An "affiliate" is a person who directly or indirectly controls, is controlled by, or is under common control with, a specified person. The supermajority vote required by the Fair Price Act does not apply to business combinations that satisfy certain conditions. These conditions include, among others: (i) the purchase price to be paid for the shares of the company in the business combination must be at least equal to the highest of either (a) the market value of the shares or (b) the highest per share price paid by the interested shareholder within the preceding two-year period or in the transaction in which the shareholder became an interested shareholder, whichever is higher; and (ii) once becoming an interested shareholder, the person may not become the beneficial owner of any additional shares of the company except as part of the transaction that resulted in the interested shareholder becoming an interested shareholder or by virtue of proportionate stock splits or stock dividends.

Our articles of incorporation allow our Board of Directors to issue one or more classes or series of preferred stock with voting rights, preferences and other privileges as the Board of Directors may determine. The possible issuance of preferred shares could adversely affect the holders of our common stock and could prevent, delay, or defer a change of control.

We are also subject to the laws of Michigan, Ohio, Texas, California, Washington D.C., Missouri, and other states, which govern insurance holding companies. Under these laws, a person generally must obtain the applicable Insurance Department's approval to acquire, directly or indirectly, five to ten percent or more of the outstanding voting securities of our Insurance Company Subsidiaries. An Insurance Department's determination of whether to approve an acquisition would be based on a variety of factors, including an evaluation of the acquirer's financial stability, the competence of its management, and whether competition in that state would be reduced. These laws may prevent, delay or defer a change of control of us or our Insurance Company Subsidiaries.

Our ability to meet ongoing cash requirements and pay dividends may be limited by our holding company structure and regulatory constraints.

We are a holding company that transacts the majority of our business through our Insurance Company Subsidiaries. Our ability to meet our obligations on our outstanding debt, and to pay our expenses and shareholder dividends, may depend upon the dividend paying capacity of our Insurance Company Subsidiaries. Payments of dividends to us by our Insurance Company Subsidiaries are restricted by state insurance laws, including laws establishing minimum solvency and liquidity thresholds, and could be subject to revised restrictions in the future. As a result, at times, we may not be able to receive dividends from our Insurance Company Subsidiaries and we may not receive dividends in amounts necessary to meet our debt obligations or to pay shareholder dividends on our capital stock.

Although we have paid cash dividends in the past, we may not pay cash dividends in the future.

The declaration and payment of dividends is subject to the discretion of our Board of Directors and will depend on our financial condition, results of operations, cash flows, cash requirements, future prospects, regulatory and contractual restrictions on the payment of dividends by our Insurance Company Subsidiaries and other factors deemed relevant by our Board of Directors. There is no requirement that we must, and we cannot assure you that we will, declare and pay any dividends in the future. Our Board of Directors may determine to retain such capital for general corporate or other purposes.

We may require additional capital in the future, which may not be available or may only be available on unfavorable terms.

Our future capital requirements depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover losses. To the extent that our present capital is insufficient to meet future operating requirements and/or cover losses, we may need to raise additional funds through financings. If we had to raise additional capital, equity or debt financing may not be available or may be on terms that are not favorable to us. In the case of equity financings, dilution to our shareholders could result, and in any case such securities may have rights, preferences and privileges that are senior to those of the shares currently outstanding. If we cannot obtain adequate capital on favorable terms or at all, our business, operating results and financial condition could be adversely affected.

We are exposed to goodwill impairment risk as part of our growth strategy.

Goodwill represents the excess of the amounts we paid to acquire subsidiaries and other businesses over the fair value of their net assets at the date of acquisition. We are required to perform a goodwill impairment analysis at least annually and whenever events or circumstances indicate that the carrying value of a reporting unit may not be recoverable from estimated future cash flows. If it is determined that the goodwill has been impaired, we would be required to write down the goodwill by the amount of the impairment, with a corresponding charge to net income. Such impairments could have a material adverse effect on our results of operations and our financial position.

Acquisitions and integration of acquired businesses may result in operating difficulties, which may prevent us from achieving the expected benefits.

At times, we may investigate and pursue acquisition opportunities if we believe such opportunities are consistent with our long-term objectives and that the expected benefits exceed the risks. Achieving such benefits is subject to a number of uncertainties, including whether the combined businesses are integrated in an efficient and effective manner, as well as general competitive factors in the marketplace. We believe we have a robust due diligence process; however, integrating an acquired company or business can be a complex and costly endeavor. Sometimes we can be confronted with unexpected issues that may present significant risks, which could materially impact our business, financial condition, results of operations, and cash flows.

Our reliance upon producers subjects us to their credit risk.

With respect to agency-billed premiums and premiums generated by brokers, producers collect premiums from the policyholders and forward them to us. In certain jurisdictions, when the insured pays premium for these policies to producers for payment, the premium might be considered to have been paid under applicable insurance laws and the insured will no longer be liable to us for those amounts, whether or not we have actually received the premium from the producer. Consequently, we assume a degree of credit risk associated with producers. Although producers' failures to remit premiums to us have not caused a material adverse impact on us to date, there may be instances where producers collect premium but do not remit it to us and we may be required under applicable law to provide the coverage set forth in the policy despite the actual lack of collection of the premium by us. Because the possibility of these events is dependent in large part upon the financial condition, cash flows, and internal operations of our producers, we may not be able to quantify any potential exposure presented by the risk. If we are unable to collect premium from our producers in the future, our financial condition and results of operations could be materially and adversely affected.

MEADOWBROOK INSURANCE GROUP, INC.

One of our core selected producers accounts for a large portion of our premium volume, loss of business provided by this entity could adversely affect us.

Our largest producer in 2011 was Midwest Insurance General Agency, LLC, which in combination with its affiliates, accounted for 14.7% of our gross written premium. No other producer was responsible for more than 10% of our gross written premium. A significant decrease in business from this producer could have an adverse impact on our operating results.

Our performance is dependent on the continued services and performance of our senior management and other key personnel.

The success of our business is dependent on our ability to retain and motivate our senior management and key management personnel and their efforts. The loss of the services of any of our executive officers or other key employees could have a material adverse effect on our business, financial condition, results of operations, and cash flows. We have existing employment or severance agreements with Robert S. Cubbin, Christopher J. Timm, Karen M. Spaun, Michael G. Costello, and other senior executives. We maintain a “key person” life insurance policy on Robert S. Cubbin, our President and CEO. The loss of any of these officers or other key personnel could cause our ability to implement our business strategies to be delayed or hindered.

Our future success also will depend on our ability to attract, train, motivate and retain other highly skilled technical, managerial, marketing, and customer service personnel. Competition for these employees is strong and we may not be able to successfully attract, integrate or retain sufficiently qualified personnel. In addition, our future success depends on our ability to attract, retain and motivate our agents and other producers. Our failure to attract and retain the necessary personnel and producers could have a material adverse effect on our business, financial condition, results of operations, and cash flows.

We rely on our information technology and telecommunications systems to conduct our business.

Our business is dependent upon the uninterrupted functioning of our information technology and telecommunication systems. We rely upon our systems, as well as the systems of our vendors, to underwrite and process our business; make claim payments; provide customer service; provide policy administration services, such as endorsements, cancellations and premium collections; comply with insurance regulatory requirements; and perform actuarial and other analytical functions necessary for pricing and product development. Our operations are dependent upon our ability to timely and efficiently process our business and protect our information and telecommunications systems from physical loss, telecommunications failure or other similar catastrophic events, as well as from security breaches. While we have implemented business contingency plans and other reasonable and appropriate internal controls to protect our systems from interruption, loss or security breaches, a sustained business interruption or system failure could adversely impact our ability to process our business, provide customer service, pay claims in a timely manner or perform other necessary business functions. Likewise, a security breach of our computer systems could also interrupt or damage our operations or harm our reputation in the event confidential customer information is disclosed to third–parties. We could also be subject to fines and penalties from a security breach. The cost to remedy a severe security breach could also be substantial. These circumstances could have a material adverse effect upon our financial condition, results of operations, cash flows, and reputation.

Managing technology initiatives and obtaining the efficiencies anticipated with technology implementation may present significant challenges.

While technological enhancements and initiatives can streamline several business processes and ultimately reduce the costs of operations, these initiatives can present short-term costs and implementation risks. Projections of associated costs, implementation timelines, and the benefits of those results may be inaccurate and such inaccuracies could increase over time. In addition, there are risks associated with not achieving the anticipated efficiencies from technology implementation that could impact our financial condition, results of operations, and cash flows.

Risks Related to Our Industry

The property and casualty insurance industry is cyclical in nature, which may affect our overall financial performance.

Historically, the financial performance of the property and casualty insurance industry has tended to fluctuate in cyclical periods of price competition, excess capacity and lower levels of profitability (known as a soft market) followed by periods of high premium rates, shortages of underwriting capacity, and higher levels of profitability (known as a hard market). Although an individual insurance company’s financial performance is dependent on its own specific business characteristics, the profitability of most property and casualty insurance companies tends to follow this cyclical market pattern. Specific factors that can drive the industry’s profitability include:

MEADOWBROOK INSURANCE GROUP, INC.

- rising levels of actual costs that are not known by companies at the time they price their products;
- volatile and unpredictable developments, including man-made, weather-related and other natural catastrophes or terrorist attacks;
- changes in loss reserves resulting from the general claims and legal environments as different types of claims arise and judicial interpretations relating to the scope of insurer's liability develop;
- fluctuations in interest rates, inflationary pressures and other changes in the investment environment, which affect returns on invested assets and may impact the ultimate payout of losses; and
- increases in medical costs beyond historic or expected annual inflationary levels.

Because the cyclicality of our industry is due in large part to the actions of competitors and general economic conditions, we cannot predict with certainty the timing or duration of changes in the market cycle.

Severe weather conditions and other catastrophes are inherently unpredictable and could cause us to suffer material financial losses.

The majority of our property business is exposed to the risk of severe weather conditions and other catastrophes. Catastrophes can be caused by various events, including natural events, such as hurricanes, winter weather, tornadoes, windstorms, earthquakes, hailstorms, severe thunderstorms and fires, and other events, such as explosions, terrorist attacks and riots. The incidence and severity of catastrophes and severe weather conditions are inherently unpredictable. Generally these losses result in an increase in the number of claims incurred as well as the amount of compensation sought by claimants. In 2011, we experienced an unusual frequency of storm activity, although none of the storms were severe enough to trigger our catastrophe reinsurance program. We did not have any significant catastrophic-related losses in 2010. Currently, we purchase catastrophe reinsurance to cover for a potential catastrophe. However, it is possible that a catastrophic event or multiple catastrophic events could cause our loss and loss adjustment expense reserves to increase and our liquidity and financial condition to decline. Refer to Note 5 ~ Reinsurance for a detailed description of our reinsurance treaties and structure.

Litigation may have an adverse effect on our business

We are subject at times to various claims, lawsuits and proceedings relating principally to alleged errors or omissions in the placement of insurance, claims administration, consulting services and other business transactions arising in the ordinary course of business. Where appropriate, we vigorously defend such claims, lawsuits and proceedings. Some of these claims, lawsuits and proceedings seek damages, including consequential, exemplary, or punitive damages, in amounts that could, if awarded, be significant. Most of the claims, lawsuits and proceedings arising in the ordinary course of business are covered by the policy at issue, errors and omissions insurance or other appropriate insurance. In terms of deductibles associated with such insurance, we have established provisions against these items, which are believed to be adequate in light of current information and legal advice. With the assistance of outside counsel, we adjust such provisions according to new developments or changes in the strategy in dealing with such matters. On the basis of current information, we do not expect the outcome of the claims, lawsuits and proceedings to which we are subject to, either individually, or in the aggregate, will have a material adverse effect on our financial condition. However, it is possible that future results of operations or cash flows for any particular quarter or annual period could be materially affected by an unfavorable resolution of any such matters.

Because we are heavily regulated by the states in which we operate, we may be limited in the way we operate.

We are subject to extensive supervision and regulation in the states in which we operate. The supervision and regulation relate to numerous aspects of our business and financial condition. The primary purpose of the supervision and regulation is to maintain compliance with insurance regulations and to protect policyholders. The extent of regulation varies, but generally is governed by state statutes. These statutes delegate regulatory, supervisory and administrative authority to state insurance departments. This system of regulation covers, among other things:

- standards of solvency, including risk-based capital measurements;
- restrictions on the nature, quality and concentration of investments;
- restrictions on the types of terms that we can include in the insurance policies we offer;
- required methods of accounting;
- required reserves for unearned premiums, losses and other purposes;
- permissible underwriting and claims settlement practices; and
- assessments for the provision of funds necessary for the settlement of covered claims under certain insurance policies provided by impaired, insolvent or failed insurance companies.

MEADOWBROOK INSURANCE GROUP, INC.

The regulations of the state insurance departments may affect the cost or demand for our products and may impede us from obtaining rate increases or taking other actions we might wish to take to increase our profitability. Furthermore, we may be unable to maintain all required licenses and approvals and our business may not fully comply with the wide variety of applicable laws and regulations or the relevant authority's interpretation of the laws and regulations. Also, regulatory authorities have relatively broad discretion to grant, renew or revoke licenses and approvals. If we do not have the requisite licenses and approvals, or do not comply with applicable regulatory requirements, the insurance regulatory authorities could stop or temporarily suspend us from conducting some or all of our activities or monetarily penalize us.

Although the United States federal government does not directly regulate the insurance business, changes in federal legislation, regulation, and/or administrative policies in several areas, including changes in financial services regulation and federal taxation, can significantly harm the insurance industry.

Most states assess our Insurance Company Subsidiaries to provide funds for failing insurance companies and those assessments could be material.

Our Insurance Company Subsidiaries are subject to assessments in most states where we are licensed for the provision of funds necessary for the settlement of covered claims under certain policies provided by impaired, insolvent or failed insurance companies. Maximum contributions required by law in any one year vary by state, and have historically been less than one percent of annual premiums written. We cannot predict with certainty the amount of future assessments. Significant assessments could have a material adverse effect on our financial condition and results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We own the land and an approximately 72,000 square feet corporate headquarters building in Southfield, Michigan. We expect that our corporate headquarters building will be adequate for our current and expected future operations.

With the ProCentury merger, we assumed the lease of their corporate headquarters, an approximately 44,000 square foot office building located in Westerville, Ohio. The lease agreement for this building has an initial term of ten years that expires in 2013.

We are also a party to various leases for other locations in which we have offices. We do not consider any of these leases to be material.

ITEM 3. LEGAL PROCEEDINGS

We are subject at times to various claims, lawsuits and proceedings relating principally to alleged errors or omissions in the placement of insurance, claims administration, consulting services and other business transactions arising in the ordinary course of business. Where appropriate, we vigorously defend such claims, lawsuits and proceedings. Some of these claims, lawsuits and proceedings seek damages, including consequential, exemplary or punitive damages, in amounts that could, if awarded, be significant. Most of the claims, lawsuits and proceedings arising in the ordinary course of business are covered by the policy at issue, errors and omissions insurance or other appropriate insurance. In terms of deductibles associated with such insurance, we have established provisions against these items, which are believed to be adequate in light of current information and legal advice. In accordance with accounting guidance, if it is probable that an asset has been impaired or a liability has been incurred as of the date of the financial statements and the amount of loss is estimable, an accrual for the costs to resolve these claims is recorded in our consolidated financial statements. Period expenses related to the defense of such claims are included in the accompanying consolidated statements of income. With the assistance of outside counsel, we adjust such provisions according to new developments or changes in the strategy in dealing with such matters. On the basis of current information, we do not expect the outcome of the claims, lawsuits and proceedings to which we are subject to, either individually, or in the aggregate, will have a material adverse effect on our financial condition. However, it is possible that future results of operations or cash flows for any particular quarter or annual period could be materially affected by an unfavorable resolution of any such matters.

ITEM 4. RESERVED

MEADOWBROOK INSURANCE GROUP, INC.

PART II

ITEM 5. MARKET PRICE