SAFETY INSURANCE GROUP INC
Form 10-Q
May 07, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2010

OR

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

For the transition period from to

Commission File Number: 000-50070

SAFETY INSURANCE GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**13-4181699**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20 Custom House Street, Boston, Massachusetts 02110
(Address of principal executive offices including zip code)

(617) 951-0600
(Registrant s telephone number, including area code)

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

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

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

As of May 5, 2010, there were 15,170,879 shares of common stock with a par value of $0.01 per share outstanding.

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Safety Insurance Group, Inc. and Subsidiaries

Consolidated Balance Sheets

(Unaudited)

(Dollars in thousands, except share data)

	March 31, 2010	December 31, 2009
Assets		
Investment securities available for sale:		
Fixed maturities, at fair value (amortized cost: $1,014,040 and $989,444)	$ 1,049,551	$ 1,018,329
Equity securities, at fair value (cost: $12,174 and $9,736)	12,430	9,876
Total investment securities	1,061,981	1,028,205
Cash and cash equivalents	39,060	74,470
Accounts receivable, net of allowance for doubtful accounts	141,175	137,238
Accrued investment income	9,919	10,044
Receivable from reinsurers related to paid loss and loss adjustment expenses	7,427	6,851
Receivable from reinsurers related to unpaid loss and loss adjustment expenses	60,634	64,874
Ceded unearned premiums	13,385	13,698
Deferred policy acquisition costs	50,068	47,900
Deferred income taxes	5,798	8,335
Equity and deposits in pools	24,813	23,840
Other assets	12,376	12,382
Total assets	$ 1,426,636	$ 1,427,837
Liabilities		
Loss and loss adjustment expense reserves	$ 430,440	$ 439,706
Unearned premium reserves	296,052	282,434
Accounts payable and accrued liabilities	35,407	59,869
Taxes payable	2,279	3,916
Payable for securities purchased	7,617	
Payable to reinsurers	5,068	4,674
Other liabilities	16,911	16,803
Total liabilities	793,774	807,402
Commitments and contingencies (Note 7)		
Shareholders equity		
Common stock: $0.01 par value; 30,000,000 shares authorized; 16,734,132 and 16,624,220 shares issued	167	166
Additional paid-in capital	146,108	144,814
Accumulated other comprehensive income, net of taxes	23,248	18,866
Retained earnings	513,051	506,301
Treasury stock, at cost; 1,564,548 shares	(49,712)	(49,712)
Total shareholders equity	632,862	620,435
Total liabilities and shareholders equity	$ 1,426,636	$ 1,427,837

The accompanying notes are an integral part of these financial statements.

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Safety Insurance Group, Inc. and Subsidiaries

Consolidated Statements of Operations

(Unaudited)

(Dollars in thousands, except per share data)

	Three Months Ended March 31, 2010	2009
Net earned premiums	$ **133,157**	$ 135,350
Net investment income	**10,792**	10,422
Net realized gains (losses) on investments	**110**	(318)
Finance and other service income	**4,296**	4,088
Total revenue	**148,355**	149,542
Losses and loss adjustment expenses	**88,674**	92,882
Underwriting, operating and related expenses	**41,868**	41,072
Interest expenses	**22**	22
Total expenses	**130,564**	133,976
Income before income taxes	**17,791**	15,566
Income tax expense	**5,017**	3,722
Net income	$ **12,774**	$ 11,844
Earnings per weighted average common share:		
Basic	$ **0.85**	$ 0.73
Diluted	$ **0.85**	$ 0.73
Cash dividends paid per common share	$ **0.40**	$ 0.40
Number of shares used in computing earnings per share:		
Basic	**15,085,096**	16,167,850
Diluted	**15,102,105**	16,188,609

The accompanying notes are an integral part of these financial statements.

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Safety Insurance Group, Inc. and Subsidiaries

Consolidated Statements of Changes in Shareholders Equity

(Unaudited)

(Dollars in thousands)

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive (Loss) Income, Net of Taxes	Retained Earnings	Treasury Stock	Total Shareholders Equity
Balance at December 31, 2008	$ 165	$ 140,261	$ (6,528)	$ 476,989	$ (7,516)	$ 603,371
Net income, January 1 to March 31, 2009				11,844		11,844
Other comprehensive income, net of deferred federal income taxes			9,923			9,923
Exercise of options and unearned compensation on restricted stock, net of deferred federal income taxes	1	981				982
Dividends paid				(6,474)		(6,474)
Acquisition of treasury stock					(14,114)	(14,114)
Balance at March 31, 2009	$ 166	$ 141,242	$ 3,395	$ 482,359	$ (21,630)	$ 605,532

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income, Net of Taxes	Retained Earnings	Treasury Stock	Total Shareholders Equity
Balance at December 31, 2009	**$ 166**	**$ 144,814**	**$ 18,866**	**$ 506,301**	**$ (49,712)**	**$ 620,435**
Net income, January 1 to March 31, 2010				**12,774**		**12,774**
Other comprehensive income, net of deferred federal income taxes			**4,382**			**4,382**
Exercise of options and unearned compensation on restricted stock, net of deferred federal income taxes	**1**	**1,294**				**1,295**
Dividends paid				**(6,024)**		**(6,024)**
Balance at March 31, 2010	**$ 167**	**$ 146,108**	**$ 23,248**	**$ 513,051**	**$ (49,712)**	**$ 632,862**

The accompanying notes are an integral part of these financial statements.

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Safety Insurance Group, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income

(Unaudited)

(Dollars in thousands)

	Three Months Ended March 31, 2010		2009	
Net income	**$**	**12,774**	$	11,844
Other comprehensive income, net of tax:				
Unrealized holding gains during the period, net of tax expense of $2,398 and $5,231		**4,453**		9,716
Reclassification adjustment for (gains) losses included in net income, net of tax (expense) benefit of ($39) and $111		**(71)**		207
Unrealized gains on securities available for sale		**4,382**		9,923
Comprehensive income	**$**	**17,156**	$	21,767

The accompanying notes are an integral part of these financial statements.

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Safety Insurance Group, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Unaudited)

(Dollars in thousands)

	Three Months Ended March 31, 2010	2009
Cash flows from operating activities:		
Net income	**$ 12,774**	$ 11,844
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization, net	**3,104**	3,144
Provision for deferred income taxes	**178**	187
Net realized (gains) losses on investments	**(110)**	318
Changes in assets and liabilities:		
Accounts receivable	**(3,937)**	713
Accrued investment income	**125**	130
Receivable from reinsurers	**3,664**	4,632
Ceded unearned premiums	**313**	417
Deferred policy acquisition costs	**(2,168)**	(969)
Other assets	**(1,437)**	(2,334)
Loss and loss adjustment expense reserves	**(9,266)**	(10,802)
Unearned premium reserves	**13,618**	5,188
Accounts payable and accrued liabilities	**(24,462)**	(19,362)
Payable to reinsurers	**394**	(560)
Other liabilities	**(1,467)**	(564)
Net cash used for operating activities	**(8,677)**	(8,018)
Cash flows from investing activities:		
Fixed maturities purchased	**(97,256)**	(37,229)
Equity securities purchased	**(3,239)**	(2,462)
Proceeds from sales, paydowns and calls of fixed maturities	**53,564**	22,003
Proceeds from maturities of fixed maturities	**25,500**	322
Proceed from sales of equity securities	**800**	1,064
Proceed from maturities of short-term securities		15,000
Fixed assets purchased	**(146)**	(60)
Net cash used for investing activities	**(20,777)**	(1,362)
Cash flows from financing activities:		
Proceeds and excess tax benefits from exercise of stock options	**68**	121
Dividends paid to shareholders	**(6,024)**	(6,474)
Acquisition of treasury stock		(14,114)
Net cash used for financing activities	**(5,956)**	(20,467)
Net decrease in cash and cash equivalents	**(35,410)**	(29,847)
Cash and cash equivalents at beginning of year	**74,470**	60,451
Cash and cash equivalents at end of period	**$ 39,060**	$ 30,604

The accompanying notes are an integral part of these financial statements.

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Safety Insurance Group, Inc. and Subsidiaries

Notes to Unaudited Consolidated Financial Statements

(Dollars in thousands except per share and share data)

1. Basis of Presentation

The consolidated financial statements have been prepared on the basis of accounting principles generally accepted in the United States of America (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates.

The consolidated financial statements include Safety Insurance Group, Inc. and its subsidiaries (the Company). The subsidiaries consist of Safety Insurance Company, Safety Indemnity Insurance Company, Safety Property and Casualty Insurance Company, Whiteshirts Asset Management Corporation (WAMC), and Whiteshirts Management Corporation, which is WAMC s holding company. All intercompany transactions have been eliminated. Prior period amounts have been reclassified to conform to the current period presentation.

The financial information as of March 31, 2010 and for the three months ended March 31, 2010 and 2009 is unaudited; however, in the opinion of the Company, the information includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the financial condition and results of operations for the periods. These unaudited consolidated financial statements may not be indicative of financial results for the full year and should be read in conjunction with the audited financial statements included in the Company s annual report on Form 10-K filed with the U.S. Securities and Exchange Commission (SEC) on March 15, 2010.

The Company is a leading provider of personal lines property and casualty insurance focused on the Massachusetts and New Hampshire markets. The Company s principal product line is private passenger automobile insurance, which accounted for 69.2% of its direct written premiums in 2009. The Company operates through its insurance company subsidiaries, Safety Insurance Company, Safety Indemnity Insurance Company, and Safety Property and Casualty Insurance Company (together referred to as the Insurance Subsidiaries).

2. Recent Accounting Pronouncements

In June 2009, the Financial Accounting Standards Board (the FASB) issued Accounting Standards Codification (ASC) 105, *Generally Accepted Accounting Principles*. ASC 105 is now the single source of authoritative nongovernmental GAAP. ASC 105 reorganizes the thousands of GAAP pronouncements into roughly 90 accounting topics and displays them using a consistent structure. Also included is relevant SEC guidance organized using the same topical structure in separate sections. ASC 105 was effective for financial statements issued for reporting periods that ended after September 15, 2009. As of September 30, 2009, all of the Company s disclosures in its consolidated financial statements were referenced in accordance with ASC 105. The implementation of ASC 105 did not have an impact on the Company s consolidated results of operations or financial position as it did not change authoritative guidance.

ASC 320, *Investments Debt and Equity Securities* requires entities to separate an other-than-temporary impairment of a debt security into two components when there are credit related losses associated with the impaired debt security for which management asserts that it does not have the intent to sell the security, and it is more likely than not that it will not be required to sell the security before recovery of its cost basis. The amount of the other-than-temporary impairment related to a credit loss is recognized in earnings, and the amount of the other-than-temporary impairment related to other factors is recorded in other comprehensive loss. The Company adopted ASC 320 effective April 1, 2009. The adoption of ASC 320 did not have an impact on the Company s consolidated results of operations or financial position. For further information, see Note 5, Investments.

ASC 825*, Financial Instruments* requires disclosures about fair value of financial instruments in interim and annual financial statements and is effective for periods ending after June 15, 2009. The Company adopted ASC 825 effective for its interim reporting period ending June 30, 2009, and its adoption did not have an impact on the Company s consolidated financial condition or results of operations. For further information, see Note 5, Investments.

ASC 820, *Fair Value Measurements and Disclosures* expands certain disclosure requirements and is effective for periods ending after June 15, 2009. The Company adopted ASC 820 effective for its interim period ending June 30, 2009, and its adoption did not have an impact on the Company s consolidated financial condition or results of operations.

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(Dollars in thousands except per share and share data)

ASC 855, *Subsequent Events* establishes principles and requirements for subsequent events. ASC 855 is effective for interim and annual financial periods ending after June 15, 2009, and was applied prospectively. In February 2010, the FASB issued updated guidance which amended the subsequent events disclosure requirements to eliminate the requirement for SEC filers to disclose the date through which it has evaluated subsequent events, clarify the period through which conduit bond obligors must evaluate subsequent events and refine the scope of the disclosure requirements for reissued financial statements. The updated guidance was effective upon issuance. The adoption of the guidance had no impact on the Company s consolidated financial condition or results of operations.

In January 2010, the FASB issued ASC Update No. 2010-06 (Topic 820), *Improving Disclosures about Fair Value Measurements* which amends and clarifies existing guidance related to fair value measurements and disclosures. This guidance requires new disclosures for (1) transfers in and out of Level 1 and Level 2 and reasons for such transfers; and (2) the separate presentation of purchases, sales, issuances and settlement in the Level 3 reconciliation. It also clarifies guidance around disaggregation and disclosures of inputs and valuation techniques for Level 2 and Level 3 fair value measurements. The Company adopted this guidance effective the quarter ended March 31, 2010, except for the new disclosures in the Level 3 reconciliation. The Level 3 disclosures are effective for periods ending after December 15, 2010. The adoption of the guidance did not have and is not expected to have an impact on the Company s consolidated financial condition or results of operations when fully adopted.

3. Earnings per Weighted Average Common Share

Basic earnings per weighted average common share (EPS) is calculated by dividing net income by the weighted average number of basic common shares outstanding during the period including unvested restricted shares which are considered participating securities. Diluted earnings per share amounts are based on the weighted average number of common shares including unvested restricted shares and the net effect of potentially dilutive common shares outstanding. At March 31, 2010 and 2009, the Company s potentially dilutive instruments were common shares under options of 212,375 and 233,046, respectively.

The following table sets forth the computation of basic and diluted EPS for the periods indicated.

	Three Months Ended March 31, 2010		2009	
Net income as reported	**$**	**12,774**	$	11,844
Less dividends:				
Distributed to common shareholders		**5,912**		6,390
Distributed to participating security holders		**112**		84
Total undistributed earnings	**$**	**6,750**	$	5,370

Undistributed earnings to common shareholders	**$**	**6,626**	$	5,290
Undistributed earnings to participating security holders	**$**	**124**	$	80
Net income available to common shareholders for basic and diluted earnings per share	**$**	**12,774**	$	11,844
Weighted average number of common shares outstanding		**14,809,087**		15,928,586
Common equivalent shares- restricted stock		**276,009**		239,264
Weighted average common and common equivalent shares outstanding used to calculate basic earnings per share		**15,085,096**		16,167,850
Common equivalent shares- stock options		**17,009**		20,759
Weighted average common and common equivalent shares outstanding used to calculate diluted earnings per share		**15,102,105**		16,188,609
Basic earnings per share	**$**	**0.85**	$	0.73
Diluted earnings per share	**$**	**0.85**	$	0.73

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Diluted EPS excludes stock options with exercise prices and exercise tax benefits greater than the average market price of the Company s common stock during the period because their inclusion would be anti-dilutive. There were 119,725 and 168,925 anti-dilutive stock options for the three months ended March 31, 2010 and 2009, respectively.

4. Stock-Based Compensation

Management Omnibus Incentive Plan

Long-term incentive compensation is provided under the Company s 2002 Management Omnibus Incentive Plan (the Incentive Plan) which provides for a variety of stock-based compensation awards, including nonqualified stock options, incentive stock options, stock appreciation rights and restricted stock (RS) awards.

The maximum number of shares of common stock with respect to which awards may be granted is 2,500,000. Shares of stock covered by an award under the Incentive Plan that are forfeited will again be available for issuance in connection with future grants of awards under the plan. At March 31, 2010, there were 813,484 shares available for future grant. The Board of Directors and the Compensation Committee intend to issue more awards under the Incentive Plan in the future.

A summary of stock based awards granted under the Incentive Plan during the three months ended March 31, 2010 is as follows:

Type of Equity Awarded	Effective Date	Number of Awards Granted		Fair Value per Share (1)	Vesting Terms
RS	**March 9, 2010**	**77,360**	**$**	**38.78**	**3 years, 30%-30%-40%**
RS	**March 9, 2010**	**4,000**	**$**	**38.78**	**No vesting period (2)**
RS	**March 23, 2010**	**25,590**	**$**	**38.09**	**5 years, 20% annually**

(1) The fair value per share of the restricted stock grant is equal to the closing price of our common stock on the grant date.

(2) The shares cannot be sold, assigned, pledged, or otherwise transferred, encumbered or disposed of until the recipient is no longer a member of our Board of Directors.

Accounting and Reporting for Stock-Based Awards

ASC 718, *Compensation Stock Compensation* requires the Company to measure and recognize the cost of employee services received in exchange for an award of equity instruments. The Company adopted ASC 718 effective January 1, 2006. Under the provisions of ASC 718, share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant).

As permitted by ASC 718, the Company elected the modified prospective transition method. Under the modified prospective transition method, (i) compensation expense for share-based awards granted prior to January 1, 2006 is recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under ASC 718 as adjusted to incorporate forfeiture assumptions under ASC 718, and (ii) compensation expense for all share-based awards granted subsequent to December 31, 2005 is based on the grant date fair value estimated in accordance with the provisions of ASC 718.

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(Dollars in thousands except per share and share data)

Stock Options

The fair value of stock options used to compute net income and earnings per share for the three month periods ended March 31, 2010 and 2009 is the estimated fair value at grant date using the Black-Scholes option-pricing model with the following assumptions:

	Three Months Ended March 31, 2010	2009
Expected dividend yield	**1.36% - 1.68%**	1.36% - 2.16%
Expected volatility	**0.31 - 0.36**	0.28 - 0.36
Risk-free interest rate	**4.35% - 4.76%**	3.23% - 4.76%
Expected holding period	**6.5 - 7 years**	6.5 - 7 years

Expected dividend yield is the Company s dividend yield on the measurement date and is based on the assumption that the current yield will continue in the future. Expected volatility is based on historical volatility of the Company s common stock as well as the volatility of a peer group of property and casualty insurers measured for a period equal to the expected holding period of the option. The risk-free interest rate is based upon the yield on the measurement date of a zero-coupon U.S. Treasury bond with a maturity period equal to the expected holding period of the option. The expected holding period is based upon the simplified method provided in SEC Staff Accounting Bulletin No. 107, *Share-Based Payment*, which utilizes the mid-points between the vesting dates and the expiration date of the option award to calculate the overall expected term. There were no stock options granted during the three month periods ended March 31, 2010 and 2009.

The following table summarizes stock option activity under the Incentive Plan for the three months ended March 31, 2010.

	Shares Under Option	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at beginning of year	**215,337**	**$ 35.40**		
Exercised	**(2,962)**	**$ 16.74**		
Outstanding at end of period	**212,375**	**$ 35.66**	**5.2 years**	**$ 1,047**
Exercisable at end of period	**188,430**	**$ 34.75**	**5.1 years**	**$ 1,047**

The aggregate intrinsic value in the preceding table represents the total pretax intrinsic value, based upon the Company s closing stock price of $37.67 on March 31, 2010, which would have been received by the option holders had all option holders exercised their options as of that date. The range of exercise prices on stock options outstanding under the Incentive Plan was $12.00 to $42.85 at March 31, 2010 and 2009. The total intrinsic value of options exercised during the three months ended March 31, 2010 and 2009 was $62 and $98, respectively.

A summary of the status of non-vested options as of March 31, 2010 is presented below.

	Number of Shares		Weighted Average Grant Date Exercise Price
Non-vested at beginning of year	**60,490**	**$**	**41.26**
Vested	**(36,545)**	**$**	**40.22**
Non-vested at end of period	**23,945**	**$**	**42.85**

As of March 31, 2010, there was $317 of unrecognized compensation expense related to non-vested option awards that is expected to be recognized over a weighted average period of 0.8 years. Cash received from options exercised was $50 and $77 for the three months ended March 31, 2010, and 2009, respectively.

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Safety Insurance Group, Inc. and Subsidiaries

Notes to Unaudited Consolidated Financial Statements

(Dollars in thousands except per share and share data)

Restricted Stock

Restricted stock awarded to employees in the form of unvested shares is recorded at the market value of the Company s common stock on the grant date and amortized ratably as expense over the requisite service period.

The following table summarizes restricted stock activity under the Incentive Plan during the three months ended March 31, 2010.

	Shares Under Restriction		Weighted Average Fair Value
Outstanding at beginning of the year	**298,834**	**$**	**34.28**
Granted	**106,950**	**$**	**38.61**
Vested and unrestricted	**(104,283)**	**$**	**36.27**
Outstanding at end of period	**301,501**	**$**	**35.13**

As of March 31, 2010, there was $9,489 of unrecognized compensation expense related to non-vested restricted stock awards that is expected to be recognized over a weighted average period of 1.9 years. The total fair value of the shares that were vested and unrestricted during the three months ended March 31, 2010 and 2009 was $3,782 and $3,412, respectively. For the three months ended March 31, 2010 and 2009, the Company recorded compensation expense related to restricted stock of $681 and $647 net of income tax benefits of $367 and $349, respectively.

5. Investments

The gross unrealized gains and losses on investments in fixed maturity securities and equity securities, including interests in mutual funds, were as follows for the periods indicated:

	As of March 31, 2010									
					Gross Unrealized Losses (3)					
		Cost or Amortized Cost		Gross Unrealized Gains		Non-OTTI Unrealized Losses		OTTI Unrealized Losses (4)		Estimated Fair Value
U.S. Treasury securities and obligations of U.S. Government agencies(1)	**$**	**315,311**	**$**	**15,030**	**$**	**(409)**	**$**		**$**	**329,932**

Obligations of states and political subdivisions	**445,800**	**15,421**	**(960)**		**460,261**
Asset-backed securities (1)	**81,302**	**2,630**	**(1,361)**		**82,571**
Corporate and other securities	**171,627**	**5,434**	**(274)**		**176,787**
Subtotal, fixed maturity securities	**1,014,040**	**38,515**	**(3,004)**		**1,049,551**
Equity securities (2)	**12,174**	**256**			**12,430**
Totals	**$ 1,026,214**	**$ 38,771**	**$ (3,004)**	**$**	**$ 1,061,981**

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Safety Insurance Group, Inc. and Subsidiaries

Notes to Unaudited Consolidated Financial Statements

(Dollars in thousands except per share and share data)

	As of December 31, 2009				
			Gross Unrealized Losses (3)		
	Cost or Amortized Cost	Gross Unrealized Gains	Non-OTTI Unrealized Losses	OTTI Unrealized Losses (4)	Estimated Fair Value
U.S. Treasury securities and obligations of U.S. Government agencies (1)	$ 315,992	$ 12,341	$ (955)	$	$ 327,378
Obligations of states and political subdivisions	468,319	16,218	(1,116)		483,421
Asset-backed securities (1)	82,694	606	(2,469)		80,831
Corporate and other securities	122,439	4,737	(477)		126,699
Subtotal, fixed maturity securities	989,444	33,902	(5,017)		1,018,329
Equity securities (2)	9,736	140			9,876
Totals	$ 999,180	$ 34,042	$ (5,017)	$	$ 1,028,205

(1) Obligations of U.S. Government agencies include collateralized mortgage obligations issued, guaranteed and/or insured by the following issuers: Government National Mortgage Association (GNMA), Federal Home Loan Mortgage Corporation (FHLMC), Federal National Mortgage Association (FNMA) and Small Business Administration (SBA). The total of these fixed maturity securities was $294,489 and $294,648 at amortized cost and $309,022 and $306,077 at fair value as of March 31, 2010 and December 31, 2009, respectively. As such, the asset-backed securities presented exclude such issuers already presented under U.S. Treasury securities and obligations of U.S. Government Agencies.

(2) Equity securities includes interests in mutual funds of $10,879 and $9,736 at cost and $11,090 and $9,876 at fair value as of March 31, 2010 and December 31, 2009, respectively, held to fund the Company s executive deferred compensation plan.

(3) The Company s investment portfolio included 80 and 89 securities in an unrealized loss position at March 31, 2010 and December 31, 2009, respectively.

(4) Amounts in this column represent OTTI recognized in accumulated other comprehensive income.

The amortized cost and the estimated fair value of fixed maturity securities, by maturity, are shown below for the periods indicated. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	As of March 31, 2010	
	Amortized Cost	**Estimated Fair Value**
Due in one year or less	**$ 44,041**	**$ 44,701**
Due after one year through five years	**263,317**	**273,019**
Due after five years through ten years	**189,231**	**195,907**
Due after ten years through twenty years	**131,973**	**134,420**

Due after twenty years		**9,687**		**9,911**
Asset-backed securities		**375,791**		**391,593**
Totals	**$**	**1,014,040**	**$**	**1,049,551**

The gross realized gains (losses) on sales of fixed maturity and equity securities were as follows for the periods indicated:

	Three Months Ended March 31,			
		2010		**2009**
Gross realized gains				
Fixed maturity securities	**$**	**242**	$	
Gross realized losses				
Fixed maturity securities		**(132)**		
Equity securities				(318)
Net realized gains (losses) on investments	**$**	**110**	$	(318)

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Proceeds from fixed maturities maturing were $25,500 and $322 for the three months ended March 31, 2010 and 2009, respectively.

In the normal course of business, the Company enters into transactions involving various types of financial instruments, including investments in fixed maturities and equity securities. Investment transactions have credit exposure to the extent that a counter party may default on an obligation to the Company. Credit risk is a consequence of carrying, trading and investing in securities. To manage credit risk, the Company focuses on higher quality fixed income securities, reviews the credit strength of all companies in which it invests, limits its exposure in any one investment and monitors the portfolio quality, taking into account credit ratings assigned by recognized statistical rating organizations.

The following tables as of March 31, 2010 and December 31, 2009 illustrate the gross unrealized losses included in the Company s investment portfolio and the fair value of those securities aggregated by investment category. The tables also illustrate the length of time that they have been in a continuous unrealized loss position.

	As of March 31, 2010					
	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government agencies	**$ 20,692**	**$ 378**	**$ 503**	**$ 31**	**$ 21,195**	**$ 409**
Obligations of states and political subdivisions	**49,414**	**263**	**11,949**	**697**	**61,363**	**960**
Asset-backed securities			**14,465**	**1,361**	**14,465**	**1,361**
Corporate and other securities	**46,116**	**254**	**1,776**	**20**	**47,892**	**274**
Total temporarily impaired securities	**$ 116,222**	**$ 895**	**$ 28,693**	**$ 2,109**	**$ 144,915**	**$ 3,004**

	As of December 31, 2009					
	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government agencies	$ 43,585	$ 932	$ 566	$ 23	$ 44,151	$ 955
Obligations of states and political subdivisions	47,585	257	13,483	859	61,068	1,116
Asset-backed securities	4,940	67	45,165	2,402	50,105	2,469
Corporate and other securities	26,217	315	5,143	162	31,360	477
Total temporarily impaired securities	$ 122,327	$ 1,571	$ 64,357	$ 3,446	$ 186,684	$ 5,017

As of March 31, 2010, the Company held insured investment securities of approximately $300,968, which represented approximately 28.3% of the Company s total investment portfolio. Approximately $47,367 of these securities are pre-refunded, meaning that funds have been set aside in escrow to satisfy the future interest and principal obligations of the bond.

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The following table shows the Company s insured investment securities that are backed by financial guarantors including pre-refunded securities as of March 31, 2010. The Company does not have any direct investment holdings in a financial guarantee insurance company.

	As of March 31, 2010		
Financial Guarantor	**Total**	**Pre-refunded Securities**	**Exposure Net of Pre-refunded Securities**
Municipal bonds			
Ambac Assurance Corporation	$ 42,277	$ 3,415	$ 38,862
Financial Guaranty Insurance Company	267	267	
Assured Guaranty Municipal Corporation	107,834	30,430	77,404
National Public Finance Guaranty Corporation	144,014	13,255	130,759
Total municipal bonds	294,392	47,367	247,025
Other asset-backed securities			
Ambac Assurance Corporation	4,071		4,071
Financial Guaranty Insurance Company	2,505		2,505
Total other asset-backed securities	6,576		6,576
Total	$ 300,968	$ 47,367	$ 253,601

The following table shows the Company s insured investments by Moody s rating where it is available both with and without the impact of the insurance guarantee as of March 31, 2010.

	As of March 31, 2010	
Rating	**Rating With Insurance**	**Rating Without Insurance**
Aaa	$ 3,959	$ 3,959
Aa1	10,457	10,457
Aa2	32,429	32,429
Aa3	136,365	82,156
A1	45,084	75,915
A2	7,305	28,241
A3	36,985	33,269
Baa1	267	267
Baa2	4,071	4,071
Ba2		6,158
	$ 276,922	$ 276,922

Other-Than-Temporary Impairments

ASC 320, *Investments Debt and Equity Securities* requires entities to separate an other-than-temporary impairment (OTTI) of a debt security into two components when there are credit related losses associated with the impaired debt security for which the Company asserts that it does not have the intent to sell the security, and it is more likely than not that it will not be required to sell the security before recovery of its cost basis. Prior to April 1, 2009, the Company had to determine whether it had the intent and ability to hold the investment for a sufficient period of time for the value to recover. When the analysis of the above factors resulted in the Company s conclusion that declines in market values were other-than-temporary, the cost of the security was written down to market value and the reduction in value was reflected as a realized loss.

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Effective under ASC 320, the amount of the OTTI related to a credit loss is recognized in earnings, and the amount of the OTTI related to other factors is recorded as a component of other comprehensive income (loss). In instances where no credit loss exists but it is more likely than not that the Company will have to sell the debt security prior to the anticipated recovery, the decline in market value below amortized cost is recognized as an OTTI in earnings. In periods after the recognition of an OTTI on debt securities, the Company accounts for such securities as if they had been purchased on the measurement date of the OTTI at an amortized cost basis equal to the previous amortized cost basis less the OTTI recognized in earnings. For debt securities for which OTTI was recognized in earnings, the difference between the new amortized cost basis and the cash flows expected to be collected will be accreted or amortized into net investment income

The Company holds no subprime mortgage debt securities. All of the Company s holdings in mortgage-backed securities are either U.S. Government or Agency guaranteed or are rated investment grade by either Moody s or Standard & Poor s.

The unrealized losses in the Company s fixed income portfolio as of March 31, 2010 were reviewed for potential other- than-temporary asset impairments. The Company obtained qualitative analysis regarding certain debt securities held at March 31, 2010 with a material (20% or greater) unrealized loss for four or more consecutive quarters. Specific qualitative analysis was also performed for any additional securities appearing on our Watch List. Qualitative analysis considered such factors as the financial condition and the near term prospects of the issuer, whether the debtor is current on its contractually obligated interest and principal payments, changes to the rating of the security by a rating agency and the historical volatility of the fair value of the security.

The qualitative analysis performed by the Company concluded that the unrealized losses recorded on the fixed maturity investment portfolio at March 31, 2010 resulted from fluctuations in market interest rates and other temporary market conditions as opposed to fundamental changes in the credit quality of the issuers of such securities. Therefore, decreases in fair values of the Company s securities are viewed as being temporary.

During the three months ended March 31, 2010 and 2009, there was no significant deterioration in the credit quality of any of the Company s holdings and no OTTI charges were recorded related to the Company s portfolio of investment securities.

Based upon the qualitative analysis performed, the Company s decision to hold these securities, the Company s current level of liquidity and its positive operating cash flows, management believes it is more likely than not that it will not be required to sell any of its securities before the anticipated recovery in the fair value to its amortized cost basis.

ASC 320, *Investments Debt and Equity Securities* requires that the Company record, as of the beginning of the interim period of adoption, a cumulative effect adjustment to reclassify the noncredit component of a previously recognized OTTI from retained earnings to other comprehensive income (loss). At March 31, 2010 and December 31, 2009, there were no amounts included in accumulated other comprehensive income related to securities which were considered by the Company to be other-than-temporarily impaired.

Net Investment Income

The components of net investment income were as follows:

	Three Months Ended March 31, 2010		2009	
Interest and dividends on fixed maturities	**$**	**11,064**	$	10,557
Dividends on equity securities		**42**		39
Interest on short-term securities		**3**		44
Interest on cash and cash equivalents		**16**		106
Total investment income		**11,125**		10,746
Investment expenses		**333**		324
Net investment income	**$**	**10,792**	$	10,422

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Fair Value Measurements

ASC 820, *Fair Value Measurements and Disclosure* provides a revised definition of fair value, establishes a framework for measuring fair value and expands financial statement disclosure requirements for fair value information. Under ASC 820, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants (an exit price). ASC 820 establishes a fair value hierarchy that distinguishes between inputs based on market data from independent sources (observable inputs) and a reporting entity s internal assumptions based upon the best information available when external market data is limited or unavailable (unobservable inputs). The fair value hierarchy in ASC 820 prioritizes fair value measurements into three levels based on the nature of the inputs as follows:

Level 1 Valuations based on quoted prices in active markets for identical assets and liabilities;

Level 2 Valuations based on observable inputs that do not meet the criteria for Level 1, including quoted prices in inactive markets and quoted prices in active markets for similar, but not identical instruments; and

Level 3 Valuations based on unobservable inputs.

Fair values for the Company s fixed maturity securities are based on prices provided by its custodian bank and its investment manager. Both the custodian bank and the investment manager use a variety of independent, nationally recognized pricing services to determine market valuations. If the pricing service cannot provide fair value determinations, the Company obtains non-binding price quotes from broker-dealers. A minimum of two quoted prices is obtained for the majority of fixed maturity securities in the Company s investment portfolio. The Company s custodian bank is its primary provider of quoted prices from third-party pricing services and broker-dealers. To provide reasonable assurance of the validity of each price or quote, a secondary third-party pricing service or broker-dealer quote is obtained from the Company s investment manager. An examination of the pricing data is then performed for each security. If the variance between the primary and secondary price quotes for a security is within an accepted tolerance level, the quoted price obtained from the Company s custodian bank is used in the Company s financial statements for the security. If the variance between the primary and secondary price quotes exceeds an accepted tolerance level, the Company obtains a quote from an alternative source, if possible, and documents and resolves any differences between the pricing sources. In addition, the Company may request that its investment manager and their traders provide input as to which vendor is providing prices that their traders believe are reflective of fair value for the security. Following this process, the Company may decide to value the security in its financial statements using the secondary or alternative source if it believes that pricing is more reflective of the security s value than the primary pricing provided by its custodian bank. The Company analyzes market valuations received to verify reasonableness, to understand the key assumptions used and their sources, and to determine an appropriate ASC 820 fair value hierarchy level based upon trading activity and the observability of market inputs. Based on this evaluation and investment class analysis, each price is classified into Level 1, 2 or 3.

Fair values of instruments are based on (i) quoted prices in active markets for identical assets (Level 1), (ii) quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-derived valuations in which all significant inputs are observable in active markets (Level 2) or (iii) valuations derived from valuation techniques in which one or more significant inputs are unobservable in the marketplace (Level 3).

The Company s Level 1 securities consist of equity securities whose values are based on quoted prices in active markets for identical assets. The Company s Level 2 securities are comprised of fixed maturity securities whose fair value was determined using observable market inputs. Fair values for securities for which quoted market prices were unavailable were estimated based upon reference to observable inputs such as benchmark interest rates, market comparables, and other relevant inputs. Investments valued using these inputs include U.S. Treasury securities and obligations of U.S. Government agencies, obligations of international government agencies, obligations of states and political subdivisions, corporate securities, commercial and residential mortgage-backed securities, and other asset- backed securities. All unadjusted estimates of fair value for fixed maturities priced by the pricing services as described above are included in the amounts disclosed in Level 2 of the hierarchy with the exception of one asset-backed security. On January 1 and March 31, 2010, the Company s Level 3 securities consisted of one asset-backed security whose price was based solely on a single broker quote which was deemed to be obtained through unobservable inputs.

In order to ensure the fair value determination is representative of an exit price (consistent with ASC 820), the Company s procedures for validating quotes or prices obtained from third-parties include, but are not limited to, obtaining a minimum of two price quotes for each fixed maturity security if possible, as discussed above, the periodic testing of sales activity to determine if there are any significant differences between the market price used to value the security as of the balance sheet date and the sales price of the security for sales that occurred around the balance sheet date, and the periodic review of reports

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provided by its investment manager regarding those securities with ratings changes and securities placed on the Company s Watch List. In addition, valuation techniques utilized by pricing services and prices obtained from external sources are reviewed by the Company s external investment manager, whose investment professionals are familiar with the securities being priced and the markets in which they trade to ensure the fair value determination is representative of an exit price (consistent with ASC 820).

Approximately 99.8% of the Company s portfolio was priced based upon quoted market prices or other observable inputs as of March 31, 2010. There were no significant changes to the valuation process during the three months ending March 31, 2010.

As of March 31, 2010 and December 31, 2009, no quotes or prices obtained were adjusted by management. All broker quotes obtained were non-binding.

The following tables summarize our total fair value measurements and the fair value measurements based on Level 3 inputs for investments for the periods indicated.

	As of March 31, 2010			
	Total	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**
U.S. Treasury securities and obligations of U.S. Government agencies	**$ 329,932**	**$**	**$ 329,932**	**$**
Obligations of states and political subdivisions	**460,261**		**460,261**	
Asset-backed securities	**82,571**		**80,065**	**2,506**
Corporate and other securities	**176,787**		**176,787**	
Equity securities	**12,430**	**12,430**		
Total investment securities	**$ 1,061,981**	**$ 12,430**	**$ 1,047,045**	**$ 2,506**

	As of December 31, 2009			
	Total	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**
U.S. Treasury securities and obligations of U.S. Government agencies	$ 327,378	$	$ 327,378	$
Obligations of states and political subdivisions	483,421		483,421	
Asset-backed securities	80,831		78,327	2,504
Corporate and other securities	126,699		126,699	
Equity securities	9,876	9,876		
Total investment securities	$ 1,028,205	$ 9,876	$ 1,015,825	$ 2,504

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The following table summarizes the changes in the Company s Level 3 fair value measurements for the three months ended March 31, 2010.

		Asset-Backed Securities
Balance at January 1, 2010	**$**	**2,504**
Net gains and losses included in earnings		
Net gains included in other comprehensive income		**2**
Purchases and sales		
Transfers in (out) of Level 3		
Balance at March 31, 2010	**$**	**2,506**
Amount of total losses included in earnings attributable to the change in unrealized losses related to assets still held at March 31, 2010	**$**	

Transfers in and out of Level 3 would be attributable to changes in the ability to observe significant inputs in determining fair value exit pricing. As noted in the tables above, no transfers were made in or out of Level 3 inputs during the three months ended March 31, 2010.

6. Loss and Loss Adjustment Expense Reserves

The following table sets forth a reconciliation of beginning and ending reserves for losses and LAE, as shown in the Company s consolidated financial statements for the periods indicated:

	Three Months Ended March 31,			
	2010		**2009**	
Reserves for losses and LAE at beginning of year	**$**	**439,706**	$	467,559
Less reinsurance recoverable on unpaid losses and LAE		**(64,874)**		(76,489)
Net reserves for losses and LAE at beginning of year		**374,832**		391,070
Incurred losses and LAE, related to:				
Current year		**101,214**		101,410
Prior years		**(12,540)**		(8,528)
Total incurred losses and LAE		**88,674**		92,882
Paid losses and LAE related to:				
Current year		**43,083**		40,843
Prior years		**50,617**		58,987
Total paid losses and LAE		**93,700**		99,830
Net reserves for losses and LAE at end of period		**369,806**		384,122
Plus reinsurance recoverables on unpaid losses and LAE		**60,634**		72,635

Reserves for losses and LAE at end of period	**$ 430,440**	$ 456,757

At the end of each period, the reserves were re-estimated for all prior accident years. The Company s prior year reserves decreased by $12,540 and $8,528 for the three months ended March 31, 2010 and 2009, respectively, and resulted from re-estimations of prior years ultimate loss and LAE liabilities. The decrease in prior years reserves during the 2010 period is primarily composed of reductions of $8,832 in the Company s retained automobile reserves, $1,879 in the Company s retained homeowners reserves, and $1,391 in reserves assumed from Commonwealth Automobile Reinsurers (CAR). The decrease in prior year reserves during the 2009 period is primarily composed of reductions of $3,489 in the Company s retained automobile reserves, $3,298 in reserves assumed from CAR, and $1,283 in the Company s retained homeowners reserves.

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The Company s private passenger automobile line of business prior year reserves decreased by $8,497 for the three months ended March 31, 2010. The decrease was primarily due to improved retained private passenger results of $7,190 for the accident years 2005 through 2009, and improved assumed CAR results for the private passenger automobile pool of $898 for accident years 2007 through 2009. The Company s private passenger automobile line of business prior year reserves decreased by $5,642 for the three months ended March 31, 2009. The decrease was primarily due to improved retained private passenger results of $2,390 for accident years 2000 through 2006, and improved assumed CAR results for the private passenger automobile pool of $2,290 for accident years 2005 through 2008. The improved retained private passenger results were primarily due to fewer incurred but not yet reported claims than previously estimated and better than previously estimated severity on the Company s established bodily injury and property damage case reserves. The improved CAR results were due primarily to improved CAR private passenger loss ratios as published and reported by the CAR Loss Reserving Committee.

Due to the nature of the risks that the Company underwrites and has historically underwritten, management does not believe that it has an exposure to asbestos or environmental pollution liabilities.

7. Commitments and Contingencies

Various claims, generally incidental to the conduct of normal business, are pending or alleged against the Company from time to time. In the opinion of management, based in part on the advice of legal counsel, the ultimate resolution of such claims will not have a material adverse effect on the Company s consolidated financial statements. However, if estimates of the ultimate resolutions of those proceedings are revised, liabilities related to those proceedings could be adjusted in the near term.

Massachusetts law requires that insurers licensed to do business in Massachusetts participate in the Massachusetts Insurers Insolvency Fund (Insolvency Fund). Members of the Insolvency Fund are assessed a proportionate share of the obligations and expenses of the Insolvency Fund in connection with an insolvent insurer. It is anticipated that there will be additional assessments from time to time relating to various insolvencies. Although the timing and amounts of any future assessments are not known, based upon existing knowledge, management s opinion is that such future assessments will not have a material effect upon the financial position of the Company.

In addition, on November 21, 2008, the Massachusetts Office of the Attorney General (the AG) delivered a civil investigative demand (the CID) to Safety Insurance Company. The CID directed the Company to produce certain information related to its policies and practices in connection with underwriting insurance policies on motorcycles and adjusting total loss claims under such policies. Other insurance companies are also being investigated by the AG related to their policies and practices related to motorcycle insurance.

The focus of the AG s investigation was on the insured values determined by Safety Insurance Company for purposes of charging premiums for physical damage insurance coverage. In 2008, coverage for motorcycles represented 1.9% of the Company s total private passenger automobile insurance. The Company has been cooperating with the AG and responding to the CID and various related additional requests for information by the AG since that time.

In connection with the matters addressed by the CID, the AG delivered a letter to Safety Insurance Company dated February 2, 2009, in which the AG stated that it has reason to believe that Safety Insurance Company has violated the Massachusetts Consumer Protection Act, G.L. c. 93A, §2, by engaging in unfair and deceptive acts and practices regarding motorcycle insurance. Specifically, the AG stated it has reason to believe that the Company overcharged its customers for motorcycle insurance and engaged in related unfair claims settlement practices. By issuing this letter the AG met a statutory prerequisite to filing a civil complaint under the Massachusetts Consumer Protection Act against the Company.

On January 14, 2010, the Company announced it had reached an agreement with the AG s office to change the way in which the Company calculated motorcycle premiums for certain types of coverage dating back to January 1, 2002. Under the terms of the settlement, the Company has agreed to pay refunds to certain motorcycle policyholders. The Company has deposited $7,217 into a trust fund to be used to pay the amount of those refunds and has paid $330 to the Commonwealth of Massachusetts, which includes reimbursement of costs and expenses related to the implementation of the settlement by the Attorney General. The total amount of $7,547 related to the settlement was recorded as an increase to the Company s Underwriting, operating and other expenses for the year ended December 31, 2009.

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The Company is working with the Attorney General s office to identify the policies on which refunds will be issued and the amount of refunds to be paid to each individual policyholder. The Company expects to notify policyholders of the amount of any refunds to be offered later this year and, upon receipt of appropriate releases from policyholders, to access the trust fund to issue refund checks. The final total of refunds paid may be more or less than initially estimated; however, in management s opinion, any future expenses related to the January 2010 settlement amounts will not have a material adverse effect upon the overall financial position of the Company.

8. Debt

On August 14, 2008, we entered into an Amended and Restated Revolving Credit Agreement (the New Credit Agreement) with RBS Citizens, NA (RBS Citizens). The New Credit Agreement amended and restated the terms of our existing Revolving Credit Agreement with RBS Citizens prior to its expiration date of August 17, 2008. The New Credit Agreement extends the maturity date to August 14, 2013 and provides a $30,000 revolving credit facility with an accordion feature allowing for future expansion of the committed amount up to $50,000. Loans under the credit facility bear interest at the Company s option at either (i) the LIBOR rate plus 1.25% per annum or (ii) the higher of RBS Citizens prime rate or 0.5% above the federal funds rate plus 1.25% per annum. Interest only is payable prior to maturity.

The Company s obligations under the credit facility are secured by pledges of its assets and the capital stock of its operating subsidiaries. The credit facility is guaranteed by the Company s non-insurance company subsidiaries. The credit facility contains covenants including requirements to maintain minimum risk based capital ratios and statutory surplus of Safety Insurance Company as well as limitations or restrictions on indebtedness, liens, and other matters. Among other covenants, the credit facility restricts the Company s payment of dividends (i) if a default under the credit facility is continuing or would result therefrom or (ii) in an amount in excess of 50% of the Company s prior year s net income, as determined in accordance with GAAP. As of March 31, 2010, the Company was in compliance with all such covenants. In addition, the credit facility includes customary events of default, including a cross-default provision permitting the lenders to accelerate the facility if the Company (i) defaults in any payment obligation under debt having a principal amount in excess of $10,000 or (ii) fails to perform any other covenant permitting acceleration of all such debt.

The Company had no amounts outstanding on its credit facility at March 31, 2010 and December 31, 2009. The credit facility commitment fee included in interest expenses was computed at a rate of 0.25% on the $30,000 commitment at March 31, 2010 and 2009.

9. Income Taxes

Federal income tax expense for the three months ended March 31, 2010 and 2009 has been computed using estimated effective tax rates. These rates are revised, if necessary, at the end of each successive interim period to reflect the current estimates of the annual effective tax rates.

ASC 740, *Income Taxes,* was adopted by the Company on January 1, 2007. This interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. ASC 740 requires that the Company determine whether the benefits of its tax positions have a more likely than not chance of being sustained upon audit based upon the technical merits of the tax position. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. As a result of the implementation of ASC 740, the Company recognized no adjustment to its consolidated balance sheet or statement of operations. The Company believes that the positions taken on its income tax returns for open tax years will be sustained upon examination by the Internal Revenue Service (IRS). Therefore, the Company has not recorded a liability under ASC 740.

During the three months ended March 31, 2010, there were no material changes to the amount of the Company s unrecognized tax benefits or to any assumptions regarding the amount of its ASC 740 liability.

As of March 31, 2010 and December 31, 2009, the Company was no longer subject to examination of its U.S. federal tax returns for years prior to 2006. The Company is not currently under examination by the IRS. During the year 2009, the Massachusetts Department of Revenue concluded its review of the 2005 and 2006 tax periods. The resulting audit adjustments were immaterial to the Company s financial position.

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10. Share Repurchase Program

On August 3, 2007, the Board of Directors approved a share repurchase program of up to $30,000 of the Company s outstanding common shares. On March 24, 2009, the Board of Directors increased this existing share repurchase program by authorizing repurchase of up to $60,000 of the Company s outstanding common shares. Under the program, the Company may repurchase shares of its common stock for cash in public or private transactions, in the open market or otherwise, at management s discretion. The timing of such repurchases and actual number of shares repurchased will depend on a variety of factors including price, market conditions and applicable regulatory and corporate requirements. The program does not require the Company to repurchase any specific number of shares and may be modified, suspended or terminated at any time without prior notice.

During the three months ended March 31, 2010, the Company did not purchase any of its common shares on the open market under the program. During the three months ended March 31, 2009, the Company purchased 454,848 of its common shares on the open market under the program at a cost of $14,114. As of March 31, 2010 and December 31, 2009, the Company had purchased 1,564,548 of its common shares on the open market under the program at a cost of $49,712.

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Item 2.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our accompanying consolidated financial statements and notes thereto, which appear elsewhere in this document. In this discussion, all dollar amounts are presented in thousands, except share and per share data.

The following discussion contains forward-looking statements. We intend statements which are not historical in nature to be, and are hereby identified as forward-looking statements to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. In addition, the Company s senior management may make forward-looking statements orally to analysts, investors, the media and others. This safe harbor requires that we specify important factors that could cause actual results to differ materially from those contained in forward-looking statements made by or on behalf of us. We cannot promise that our expectations in such forward-looking statements will turn out to be correct. Our actual results could be materially different from and worse than our expectations. See Forward-Looking Statements below for specific important factors that could cause actual results to differ materially from those contained in forward-looking statements

Executive Summary and Overview

In this discussion, Safety refers to Safety Insurance Group, Inc. and our Company, we, us and our refer to Safety Insurance Group, Inc. and i consolidated subsidiaries. Our subsidiaries consist of Safety Insurance Company (Safety Insurance), Safety Indemnity Insurance Company (Safety Indemnity), Safety Property and Casualty Insurance Company (Safety P&C), Whiteshirts Asset Management Corporation (WAMC), and Whiteshirts Management Corporation, which is WAMC s holding company.

We are a leading provider of private passenger automobile insurance in Massachusetts. In addition to private passenger automobile insurance (which represented 69.2% of our direct written premiums in 2009), we offer a portfolio of other insurance products, including commercial automobile (12.0% of 2009 direct written premiums), homeowners (14.7% of 2009 direct written premiums), dwelling fire, umbrella and business owner policies (totaling 4.1% of 2009 direct written premiums). Operating exclusively in Massachusetts and New Hampshire through our insurance company subsidiaries, Safety Insurance, Safety Indemnity, and Safety P&C, (together referred to as the Insurance Subsidiaries), we have established strong relationships with independent insurance agents, who numbered 861 in 999 locations throughout Massachusetts during 2009. We have used these relationships and our extensive knowledge of the Massachusetts market to become the second largest private passenger automobile and the third largest commercial automobile insurance carrier in Massachusetts, capturing an approximate 11.3% and 11.0% share, respectively, of the Massachusetts private passenger and commercial automobile markets in 2009, according to the Commonwealth Automobile Reinsurers (CAR) Cession Volume Analysis Report of March 3, 2010, based on automobile exposures. These statistics total, for each vehicle insured, the number of months during the year insurance for that vehicle is in effect, to arrive at an aggregate number of car-months for each insurer; this aggregate number, divided by 12, equals the insurer s number of car-years, a measure we refer to in this discussion as automobile exposures.

Our Insurance Subsidiaries began writing private passenger automobile and homeowners insurance in New Hampshire on October 15, 2008. For the year ended December 31, 2009 and the three months ended March 31, 2010, we wrote approximately $978 and $441, respectively, in direct written premiums in New Hampshire.

Massachusetts Automobile Insurance Market

We have been subject to extensive regulation in the private passenger automobile insurance industry in Massachusetts, which represented 69.2% of our direct written premiums in 2009. Owners of registered automobiles in Massachusetts are required to maintain minimum automobile insurance coverage. Prior to April 1, 2008, the Commissioner of Insurance (the Commissioner) had fixed and established the maximum rates that could be charged for private passenger automobile insurance. Prior to April 1, 2008, as a servicing carrier of CAR, we were required to issue a policy to all qualified applicants. CAR operates at an underwriting deficit. This deficit is allocated among every Massachusetts automobile insurance company, including us, based on a complex formula that takes into consideration a company s voluntary market share, the rate at which it cedes business to CAR, and the company s utilization of a credit system CAR designed to encourage carriers to reduce their use of CAR. In addition, based on our market share prior to April 1, 2009, we had been assigned certain licensed producers by CAR that were unable to obtain a voluntary contract with another insurer. We call these agents Exclusive Representative Producers, or ERPs.

On July 16, 2007, the Commissioner issued two decisions that significantly changed how private passenger automobile insurance was regulated in Massachusetts. In the first decision, the Commissioner approved and set a time table for the

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implementation of new CAR rules pursuant to which the current reinsurance program run by CAR has been replaced with an assigned risk plan, the Massachusetts Automobile Insurance Plan (MAIP). Under these new rules, as of April 1, 2009 we no longer were assigned ERPs whose business we must insure (subject to the option of ceding it to CAR) and instead, we were assigned individual policies by CAR. The MAIP began with business effective on or after April 1, 2008 for new business and those risks that have 10 or more Safe Driver Points. Beginning April 1, 2009, all business was eligible for MAIP except those risks that have no violations or accidents in the preceding three year period (so called Clean in three risks). The last policy effective date on which any risk could be ceded to CAR was March 31, 2009.

The Commissioner s decision to implement an assigned risk plan brought to a close a lengthy period of regulatory and judicial consideration of the Massachusetts private passenger residual market.

In the second decision referenced above, the Commissioner announced that she would not fix and establish the maximum premium rates that can be charged for private passenger automobile insurance policies issued or renewed after April 1, 2008. In a letter accompanying the decision, the Commissioner stated that in place of the fixed and established system, she would institute a system that introduces competitive pricing to the Massachusetts private passenger automobile insurance market, which the Commissioner has described as managed competition (Managed Competition). On October 5, 2007, the Commissioner issued a Competitive Rating Regulation; 211 CMR 79.00: Private Passenger Motor Vehicle Insurance Rates that describes the technical details of Managed Competition (the Regulation). The Regulation governs the rate filing that an insurer can file.

In addition, the Regulation prohibits the following rating and underwriting factors:

- *Rating Factors:* Insurers are prohibited from using credit information, sex, marital status, race, creed, national origin, religion, occupation, income, education, home ownership and age (except to produce the reduction in rates for insureds age 65 and over).
- *Underwriting Factors:* Insurers are prohibited from refusing to issue or renew a private passenger auto insurance policy based on credit information, sex, marital status, race, creed, national origin, religion, age, occupation, income, principal place of garaging, education and home ownership.

The Commissioner has issued a number of bulletins addressing issues related to the implementation of Managed Competition (the Rating Bulletins). Rating Bulletins 2008-11 and 2009-13 limits voluntary market rates to a level no higher than the rates in the residual market. Rating Bulletin 2008-17 describes how companies may place risks among company affiliates within an insurer group.

CAR runs a reinsurance pool for commercial automobile policies and beginning January 1, 2006, CAR implemented a Limited Servicing Carrier Program (LSC) for ceded commercial automobile policies. CAR approved Safety Insurance and five other servicing carriers through a Request for Proposal to process ceded commercial automobile business, which is spread equitably among the six servicing carriers. Each Massachusetts commercial automobile insurer must bear a portion of the losses of the commercial reinsurance pool that is serviced by the six servicing carriers in the LSC program. Subject to the Commissioner s review, CAR sets the premium rates for commercial automobile policies reinsured through CAR and this reinsurance pool can generate an underwriting result that is a profit or deficit based upon CAR s rate level. This underwriting result is allocated among every Massachusetts commercial automobile insurance company, including us, based on a company s commercial automobile voluntary market share.

CAR also runs a reinsurance pool for Taxi, Limousine and Car Service risks (the Taxi/Limo Program). On April 25, 2007, Safety submitted through a Request for Proposal a bid to process a portion of the Taxi/Limo Program. CAR approved Safety as one of the two servicing carriers for this program beginning January 1, 2008.

As noted above, in 2007 and previous years, the Commissioner set the maximum premium rates that could be charged and minimum commissions that had to be paid to agents for private passenger automobile insurance. Beginning in 2007, the effective date of the Commissioner s rate decision was April 1st as compared to January 1st of 2006 and prior rate decisions. The 2006 rates were in effect from January 1, 2006 until March 31, 2007. The Commissioner announced on December 15, 2006, an 11.7% statewide average private passenger automobile insurance rate decrease for 2007, compared to an 8.7% decrease for 2006. Coinciding with the 2007 rate decision, the Commissioner also approved a 13.0% commission rate which agents receive for selling private passenger automobile insurance, as a percentage of premiums, compared to a commission rate of 11.8% in 2006.