MAXLINEAR INC
Form DEF 14A
October 01, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A INFORMATION

PROXY STATEMENT PURSUANT TO SECTION 14(a) OF THE

SECURITIES EXCHANGE ACT OF 1934

(Amendment No.   )

Filed by the Registrant x   Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary Proxy Statement

¨ Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

x Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to §240.14a-11(c) or §240.14a-2

MAXLINEAR, INC.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid: $

¨ Fee paid previously with preliminary materials.

¨ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

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2051 Palomar Airport Road, Suite 100

Carlsbad, California 92011

(760) 692-0711

October 1, 2010

Dear Stockholder:

We are pleased to invite you to attend our 2010 Annual Meeting of Stockholders to be held on Friday, October 29, 2010 at 8:30 a.m., Pacific time, at our headquarters at 2051 Palomar Airport Road, Suite 100 in Carlsbad, California 92011. The formal meeting notice and proxy statement are attached.

At this year s annual meeting, our stockholders will be asked to

- elect the two nominees for Class I director named in the proxy statement to hold office until our 2013 annual meeting of stockholders; and

- ratify the selection by the audit committee of our board of directors of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2010.

Your vote is important. Whether or not you plan to attend the annual meeting, it is important that your shares be represented, and we hope you will vote as soon as possible. Please vote promptly by mailing a completed proxy card in the enclosed return envelope (which is postage prepaid if mailed in the United States). Please remember to sign and date your card. If you hold shares of our Class A common stock through a broker, bank, or other nominee holder, please follow the voting instructions provided. You may be able to vote by telephone or over the Internet.

Thank you for your ongoing support of MaxLinear. We look forward to seeing you at our annual meeting.

Sincerely,

Kishore Seendripu, Ph.D.
Chairman of the Board of Directors and Chief Executive Officer

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MAXLINEAR, INC.

2051 Palomar Airport Road, Suite 100

Carlsbad, California 92011

(760) 692-0711

NOTICE OF 2010 ANNUAL MEETING OF STOCKHOLDERS

Time and Date	8:30 a.m., Pacific time, on Friday, October 29, 2010
Place	MaxLinear s headquarters, 2051 Palomar Airport Road, Suite 100, Carlsbad, California 92011
Items of Business	To elect the two nominees for Class I director named in the accompanying proxy statement to hold office until our 2013 annual meeting of stockholders or until their respective successors are duly elected and qualified.
	To ratify the selection by our audit committee of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2010.
	To transact any other business that may properly come before the 2010 annual meeting.
Adjournments and Postponements	Any action on the items of business described above may be considered at the annual meeting at the time and on the date specified above or at any time and date to which the annual meeting may be properly adjourned or postponed.
Record Date	You are entitled to vote only if you were a MaxLinear stockholder of record as of the close of business on the record date, September 15, 2010.
Meeting Admission	**You are entitled to attend the annual meeting only if you were a MaxLinear stockholder as of the close of business on the record date or otherwise hold a valid proxy for the Annual Meeting**. If you are not a stockholder of record but hold shares through a broker, bank, trustee, or nominee (*i.e.*, in street name), you should provide proof of beneficial ownership as of the record date, such as your most recent account statement prior to the record date, a copy of the voting instruction card provided by your broker, bank, trustee, or nominee, or similar evidence of ownership.
	Please let us know if you plan to attend the meeting by marking the appropriate box on the enclosed proxy card or, if you vote by telephone or over the Internet, by indicating your plans when prompted.
Annual Report	

	Our 2009 annual report is enclosed with these materials as a separate booklet. You may also access our 2009 annual report by visiting www.envisionreports.com/MXL, if you are a stockholder of record, or www.edocumentview.com/MXL, if you hold shares through a broker, bank, trustee, or nominee. Our 2009 annual report is not a part of the proxy solicitation materials.
Voting	Your vote is very important. Whether or not you plan to attend the annual meeting, we encourage you to read the proxy statement and submit your proxy or voting instructions as soon as possible. For specific instructions on how to vote your shares, please refer to the instructions in the section entitled Questions and Answers About the Proxy Materials and annual meeting beginning on page 1 of this proxy statement, or your enclosed proxy card.

IMPORTANT NOTICE REGARDING THE PROXY MATERIALS FOR THE STOCKHOLDER MEETING TO BE HELD ON OCTOBER 29, 2010: The notice of annual meeting, proxy statement and 2009 annual report are available by visiting www.envisionreports.com/MXL, if you are a stockholder of record, or www.edocumentview.com/MXL, if you hold shares through a broker, bank, trustee, or nominee.

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PROXY STATEMENT

FOR 2010 ANNUAL MEETING OF STOCKHOLDERS

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MAXLINEAR, INC.

2051 Palomar Airport Road, Suite 100

Carlsbad, California 92011

PROXY STATEMENT

For the Annual Meeting of Stockholders

To Be Held October 29, 2010

QUESTIONS AND ANSWERS

ABOUT THE PROXY MATERIALS AND ANNUAL MEETING

What is a proxy?

A proxy is your legal designation of another person to vote the stock you own. The person you designate is your proxy, and you give the proxy authority to vote your shares by submitting the enclosed proxy card or, if available, voting by telephone or over the Internet. We have designated our Chairman and Chief Executive Officer, Kishore Seendripu, Ph.D., our Vice President, Finance and Treasurer, Joe Campa, and our Chief Accounting Officer and Controller, Patrick McCready, to serve as proxies for the annual meeting.

Why am I receiving these materials?

We are providing these proxy materials in connection with the solicitation by our board of directors of proxies to be voted at our 2010 annual meeting of stockholders, which will take place on Friday, October 29, 2010 at 8:30 a.m., Pacific time, at our headquarters located at 2051 Palomar Airport Road, Suite 100, Carlsbad, California 92011. As a stockholder, you are invited to attend the annual meeting and are requested to vote on the items of business described in this proxy statement.

This proxy statement and the accompanying proxy card, notice of annual meeting, and voting instructions are being mailed starting October 1, 2010 to all stockholders of record entitled to vote at the annual meeting.

What information is contained in this proxy statement?

The information in this proxy statement relates to the proposals to be voted on at the annual meeting,

the voting process, the compensation of our directors and most highly paid executive officers, our corporate governance policies, information on our board of directors, and certain other required information.

How do I get electronic access to the proxy materials?

The notice of annual meeting, proxy statement, and 2009 annual report are available by visiting www.envisionreports.com/MXL, if you are a stockholder of record, or www.edocumentview.com/MXL, if you hold shares through a broker, bank, trustee, or nominee.

What items of business will be voted on at the annual meeting?

The items of business scheduled to be voted on at the annual meeting are as follows:

- The election of the two nominees for Class I director named in this proxy statement to hold office until our 2013 annual meeting of stockholders or until their respective successors are duly elected and qualified.

- The ratification of the selection by our audit committee of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2010.

We will also transact any other business that properly comes before the annual meeting.

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How does the board of directors recommend that I vote?

Our board of directors recommends that you vote your shares:

FOR each of the nominees for Class I director named in the proxy statement.

FOR the ratification of Ernst & Young LLP as our independent registered public accounting firm for the 2010 fiscal year.

What shares can I vote?

Each share of our Class A common stock and Class B common stock issued and outstanding as of the close of business on September 15, 2010, the record date for the 2010 annual meeting of stockholders, is entitled to vote on all items being considered at the 2010 annual meeting. You may vote all shares owned by you as of the record date, including (i) shares held directly in your name as the stockholder of record and (ii) shares held for you as the beneficial owner in street name through a broker, bank, or other nominee. On the record date, we had 31,266,237 shares of common stock issued and outstanding, consisting of 7,410,714 shares of Class A common stock and 23,855,523 shares of Class B common stock.

How many votes am I entitled to per share?

For all matters described in this proxy statement for which your vote is being solicited, each holder of shares of Class A common stock is entitled to one vote for each share of Class A common stock held as of the record date, and each holder of shares of Class B common stock is entitled to one vote for each share of Class B common stock held as of the record date. The Class A common stock and Class B common stock are voting as a single class on all matters described in this proxy statement for which your vote is being solicited.

What is the difference between the voting rights of Class A common stock and Class B common stock?

Holders of our Class A and Class B common stock have identical voting rights, except that holders of our Class A common stock are entitled to one vote per share and holders of our Class B common stock

are entitled to ten votes per share with respect to transactions that would result in a change of control of MaxLinear or, in certain cases, that relate to our equity incentive plans. In addition, holders of our Class B common stock are entitled, voting separately as a class, to elect two members of board of directors. None of the proposals currently being considered at the 2010 annual meeting will implicate the preferential voting rights of our Class B common stock.

What is the difference between holding shares as a stockholder of record and as a beneficial owner?

Many MaxLinear stockholders hold their shares as a beneficial owner through a broker or other nominee rather than directly in their own name. As summarized below, there are some distinctions between shares held of record and those owned beneficially.

Stockholder of Record

If your shares are registered directly in your name with our transfer agent, Computershare Trust Company, N.A., you are considered, with respect to those shares, the *stockholder of record*, and these proxy materials were sent directly to you by MaxLinear. As the *stockholder of record*, you have the right to grant your voting proxy directly to our designated proxies or to vote in person at the annual meeting. We have enclosed or sent a proxy card for you to use with the printed proxy materials delivered to you. You may also vote on the Internet or by telephone, as described below under the heading How can I vote my shares without attending the annual meeting? and on your proxy card.

Beneficial Owner

If your shares are held in an account at a brokerage firm, bank, or other similar organization, you are considered the *beneficial owner* of shares held *in street name*, and the notice of annual meeting, proxy statement, and 2009 annual report were forwarded to you by that organization. As the beneficial owner, you have the right to direct your broker, bank, or other nominee how to vote your shares, and you are also invited to attend

the annual meeting.

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Since a beneficial owner is not the *stockholder of record*, he or she may not vote your shares in person at the annual meeting unless you obtain a legal proxy from the broker, bank, trustee, or nominee that holds your shares giving you the right to vote the shares at the meeting. If you are a beneficial owner and do not wish to vote in person or you will not be attending the annual meeting, you may vote by following the instructions provided by your broker or other nominee.

How can I contact MaxLinear s transfer agent?

Contact our transfer agent by writing Computershare Trust Company, N.A., P.O. Box 43078, Providence, Rhode Island 02940 or telephoning (866) 298-8535 or (781) 575-2879.

How can I attend the annual meeting?

You are entitled to attend the annual meeting only if you were a MaxLinear stockholder as of the record date or you hold a valid proxy for the annual meeting. If you are not a stockholder of record but hold shares as a beneficial owner in street name, you should provide proof of beneficial ownership as of the record date, such as your most recent account statement prior to September 15, 2010, a copy of the voting instruction card provided by your broker, bank, or nominee, or other similar evidence of ownership.

If you do not comply with the procedures outlined above, you may not be admitted to the annual meeting.

Please let us know if you plan to attend the meeting by marking the appropriate box on the enclosed proxy card or, if you vote by telephone or Internet, by indicating your plans when prompted.

Will the annual meeting be webcast?

We do not expect to webcast the annual meeting.

How can I vote my shares in person at the annual meeting?

Shares held in your name as the stockholder of record may be voted by you in person at the annual meeting. Shares held beneficially in street name may

be voted by you in person at the annual meeting only if you obtain a legal proxy from the broker, bank, or nominee that holds your shares giving you the right to vote the shares. Even if you plan to attend the annual meeting, we recommend that you also submit your proxy or voting instructions as described below so that your vote will be counted if you later decide not to attend the meeting.

How can I vote my shares without attending the annual meeting?

By mail

Complete, sign and date the enclosed proxy card or voting instruction card and return it in the return envelope provided (which is postage prepaid if mailed in the United States). *If you are a stockholder of record and you return your signed proxy card but do not indicate your voting preferences, the persons named in the proxy card will vote the shares represented by your proxy card as recommended by our board of directors.*

If you are a stockholder of record and the prepaid envelope is missing, please mail your completed proxy card to MaxLinear, Inc., c/o Computershare Trust Company, N.A., P.O. Box 43078, Providence, Rhode Island 02940.

If you are a beneficial owner of shares, you should have received a proxy card and voting instructions with these proxy materials from your broker, bank or other nominee holder of record. Simply complete and mail the proxy card provided to the address provided by your broker, bank or other nominee holder of record.

You may still attend the annual meeting in person even if you have already voted by proxy.

By telephone or on the Internet

If you are a stockholder of record, you may vote by following the telephone or Internet voting instructions on your proxy card.

If you are a beneficial owner of shares, your broker, bank or other holder of record may make telephone or Internet voting available to you. The availability of telephone and Internet voting for beneficial owners will depend on the voting

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processes of your broker, bank or other nominee holder of record. Therefore, we recommend that you follow the voting instructions in the materials you receive.

Can I change my vote or revoke my proxy?

You may change your vote at any time prior to the taking of the vote at the annual meeting. If you are the stockholder of record, you may change your vote by (i) granting a new proxy bearing a later date (which automatically revokes the earlier proxy) using any of the methods described above (and until the applicable deadline for each method), (ii) providing a written notice of revocation to our corporate secretary at MaxLinear, Inc., 2051 Palomar Airport Road, Suite 100, Carlsbad, California 92011 prior to your shares being voted, or (iii) attending the annual meeting and voting in person. Attendance at the meeting will not cause your previously granted proxy to be revoked unless you specifically so request. For shares you hold beneficially in street name, you may change your vote by submitting new voting instructions to your broker, bank, or nominee following the instructions they provided or, if you have obtained a legal proxy from your broker, bank, or nominee giving you the right to vote your shares, by attending the annual meeting and voting in person.

Is there a list of stockholders entitled to vote at the annual meeting?

The names of stockholders of record entitled to vote at the annual meeting will be available at the annual meeting and for ten days prior to the meeting for any purpose germane to the meeting, between the hours of 9:00 a.m. and 4:30 p.m., at our corporate headquarters at 2051 Palomar Airport Road, Suite 100, Carlsbad, California, 92011, by contacting our corporate secretary.

Is my vote confidential?

Proxy instructions, ballots, and voting tabulations that identify individual stockholders are handled in a manner that protects your voting privacy. Your vote will not be disclosed either within MaxLinear or to third parties, except as necessary to meet applicable legal requirements, to allow for the tabulation of votes and certification of the vote, or to facilitate a successful proxy solicitation.

How many shares must be present or represented to conduct business at the annual meeting?

The quorum requirement for holding the annual meeting and transacting business is that holders of a majority of the voting power of our issued and outstanding Class A and Class B common stock (voting together as a single class) be present in person or represented by proxy. Where a separate vote by a class or classes or series is required, a majority of the voting power of the shares of such class or classes or series must be present in person or represented by proxy to constitute a quorum entitled to take action with respect to that vote on that matter. Abstentions and broker non-votes are counted as present and entitled to vote for purposes of determining a quorum. A broker non-vote occurs when a broker, bank or other holder of record holding shares for a beneficial owner does not vote on a particular proposal because that holder does not have discretionary voting power for that particular item and has not received voting instructions from the beneficial owner. If there is no quorum, a majority of the votes present at the annual meeting may adjourn the meeting to another date.

What is the voting requirement to approve each of the proposals?

Proposal	Vote Required	Discretionary Voting Allowed?
Election of Class I directors	Plurality	No
Ratification of Ernst & Young LLP	Majority of the shares present, represented, and entitled to vote at the meeting	Yes

If you are a beneficial owner, your broker, bank or other nominee holder of record is permitted to vote your shares on the ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm, even if the record holder does not receive voting instructions from you. Due to recent rule changes, however, your broker, bank, or other nominee holder of record does not have discretionary authority to vote on the election of directors without instructions from you, in which case a broker non-vote will occur and your shares will not be voted on this matter. This represents a change from prior years when brokers, banks and

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other nominee holders of record had discretionary voting authority in the election of directors. Accordingly, if you are a beneficial owner, it is particularly important that you provide your instructions for voting your shares on the election of directors to your broker, bank, or other nominee holder of record.

Election of directors

The nominees receiving the highest number of affirmative votes will be elected as Class I directors. You may vote FOR or WITHHOLD for each director nominee. A properly executed proxy marked WITHHOLD with respect to the election of a Class I director will not be voted with respect to such director although it will be counted for purposes of determining whether there is a quorum. Abstentions and broker non-votes will not affect the outcome of the election of directors.

Ratification of Ernst & Young LLP

The affirmative FOR vote of a majority of the shares present, represented, and entitled to vote on the proposal is required to ratify the selection by our audit committee of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2010. You may vote FOR, AGAINST, or ABSTAIN on this proposal. Abstentions are deemed to be votes cast and have the same effect as a vote against the proposal. Broker non-votes are not deemed to be votes cast, are not included in the tabulation of voting results on this proposal, and will not affect the outcome of voting on this proposal.

Is cumulative voting permitted for the election of directors?

No. You may not cumulate your votes for the election of directors.

What happens if additional matters are presented at the annual meeting?

Other than the two items of business described in this proxy statement, we are not aware of any other business to be acted upon at the annual meeting. If you grant a proxy, the persons named as proxy holders, Kishore Seendripu, Ph.D., Joe Campa, and Patrick McCready, or any of them, will have the discretion to vote your shares on any additional

matters properly presented for a vote at the meeting. If for any reason any of the nominees is not available as a candidate for director, the persons named as proxy holders will vote your proxy for such other candidate or candidates as may be nominated by the board of directors.

Who will count the votes?

A representative of our transfer agent, Computershare Trust Company, N.A., will tabulate the votes and act as inspector of election.

Who will bear the cost of soliciting votes for the annual meeting?

We will pay the entire cost of preparing, assembling, printing, mailing, and distributing these proxy materials and soliciting votes. In addition to the mailing of these proxy materials, the solicitation of proxies or votes may be made in person, by telephone, or by electronic communication by our directors, officers, and employees, who will not receive any additional compensation for such solicitation activities. We may also reimburse brokerage firms, banks, and other nominee holders of record for the cost of forwarding proxy materials to beneficial owners.

Where can I find the voting results of the annual meeting?

We will announce preliminary voting results at the annual meeting. We will also disclose voting results on a Current Report on Form 8-K filed with the SEC within four business days after the annual meeting. If final voting results are not available to us in time to file a Current Report on Form 8-K, we will file a Current Report on Form 8-K to publish preliminary results and, within four business days after final results are known, file an additional Current Report on Form 8-K to publish the final results.

What is householding and how does it affect me?

We have adopted a procedure approved by the SEC called householding. Under this procedure, stockholders of record who have the same address and last name and do not participate in electronic delivery of proxy materials will receive only one copy of our notice of annual meeting, proxy

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statement and 2009 annual report, unless one or more of these stockholders notifies us that they wish to continue receiving individual copies. This procedure will reduce our printing costs and postage fees.

Stockholders who wish to participate in householding will continue to receive separate proxy cards.

If you are eligible for householding, but you and other stockholders of record with whom you share an address currently receive multiple copies of the notice of annual meeting, proxy statement, 2009 annual report and accompanying documents, or if you hold stock in more than one account, and, in either case, you wish to receive only a single copy of each of these documents for your household, please contact our transfer agent, Computershare Trust Company, N.A., P.O. Box 43078, Providence, Rhode Island 02940 or by telephone at (866) 298-8535 or (781) 575-2879.

If you participate in householding and wish to receive a separate copy of this notice of annual meeting, proxy statement, 2009 annual report and the accompanying documents, or if you do not wish to continue to participate in householding and prefer to receive separate copies of these documents in the future, please contact Computershare Trust Company, N.A. as indicated above.

Beneficial owners can request information about householding from their banks, brokers or other holders of record.

What is the deadline to propose actions for consideration at next year s annual meeting of stockholders or to nominate individuals to serve as directors?

Stockholder Proposals

Stockholders may present proper proposals for inclusion in our proxy statement and for consideration at the next annual meeting of stockholders by submitting their proposals in writing to our corporate secretary in a timely manner. For a stockholder proposal to be considered for inclusion in our proxy statement for our 2011 annual meeting of stockholders, our corporate secretary must receive the written proposal at our principal executive offices

no later than June 3, 2011; provided, however, that in the event that we hold our 2011 annual meeting of stockholders more than 30 days before or after the one-year anniversary date of the 2010 annual meeting, we will disclose the new deadline by which stockholders proposals must be received under Item 5 of our earliest possible Quarterly Report on Form 10-Q or, if impracticable, by any means reasonably calculated to inform stockholders. In addition, stockholder proposals must otherwise comply with the requirements of Rule 14a-8 of the Securities Exchange Act of 1934, as amended. Such proposals also must comply with SEC regulations under Rule 14a-8 regarding the inclusion of stockholder proposals in company-sponsored proxy materials. Proposals should be addressed to:

MaxLinear, Inc.

Attn: Corporate Secretary

2051 Palomar Airport Road, Suite 100

Carlsbad, California 92011

Fax: (760) 444-8598

Our bylaws also establish an advance notice procedure for stockholders who wish to present a proposal before an annual meeting of stockholders, but do not intend for the proposal to be included in our proxy statement. Our bylaws provide that the only business that may be conducted at an annual meeting is business that is (i) specified in the notice of a meeting given by or at the direction of our board of directors, (ii) otherwise properly brought before the meeting by or at the direction of our board of directors, or (iii) properly brought before the meeting by a stockholder of record entitled to vote at the annual meeting who has delivered timely written notice to our corporate secretary, which notice must contain the information specified in our bylaws. To be timely for our 2011 annual meeting of stockholders, our corporate secretary must receive the written notice at our principal executive offices:

- not earlier than July 18, 2011, and

- not later than the close of business on August 17, 2011.

In the event that we hold our 2011 annual meeting of stockholders more than 30 days before or after the one-year anniversary date of the 2010 annual meeting, then notice of a stockholder proposal that is not intended to be included in our proxy

statement must be received not later than the close of business on the later of the following two dates:

- the 90th day before such annual meeting: or
- the 10th day following the day on which public announcement of the date of such meeting is first made.

If a stockholder who has notified us of his or her intention to present a proposal at an annual meeting does not appear to present his or her proposal at such meeting, we are not required to present the proposal for a vote at such meeting.

Nomination of Directors Candidates

You may propose director candidates for consideration by our Nominating and Corporate Governance Committee. Any such recommendations should include the nominee s name and qualifications for membership on our board of directors, and should be directed to the corporate secretary of MaxLinear at the address set forth above. For additional information regarding stockholder recommendations for director candidates, see Corporate Governance and Board Committees Process for Recommending Candidates to the Board of Directors on page 13.

In addition, our bylaws permit stockholders to nominate directors, other than Class B Directors nominated and elected solely by holders of Class B common stock, for election at an annual meeting of stockholders. To nominate a director, the stockholder must provide the information required by our bylaws. In addition, the stockholder must give timely notice to our corporate secretary in accordance with our bylaws, which, in general, require that the notice be received by our corporate secretary within the time period described above under Stockholder Proposals for stockholder proposals that are not intended to be included in our proxy statement. Also, rules recently adopted by the SEC provide certain stockholders with the right to nominate candidates to our board of directors in our proxy materials (referred to as proxy access), and those rules will be in effect next year for our 2011 annual meeting of stockholders.

Availability of Bylaws

A copy of our bylaws may be obtained by accessing MaxLinear s filings on the SEC s website at www.sec.gov. You may also contact our corporate

secretary at our principal executive offices for a copy of the relevant bylaw provisions regarding the requirements for making stockholder proposals and nominating director candidates.

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CORPORATE GOVERNANCE AND BOARD OF DIRECTORS

MaxLinear Policies on Business Conduct

We are committed to the highest standards of integrity and ethics in the way we conduct our business. In connection with our recently completed initial public offering and the listing of our Class A common stock on the New York Stock Exchange, we adopted a code of ethics and employee conduct that applies to our board of directors and all of our employees, including our chief executive officer, principal financial officer, and principal accounting officer. Our code of conduct establishes our policies and expectations with respect to a wide range of business conduct, including preparation and maintenance of financial and accounting information, compliance with laws, and conflicts of interest.

Under our code of conduct, each of our directors and employees is required to report suspected or actual violations. In addition, we have adopted separate procedures concerning the receipt and investigation of complaints relating to accounting or audit matters. These procedures have been adopted and are administered by our audit committee.

Our code of conduct is available at our website by visiting *www.maxlinear.com* and clicking through Investors, Corporate Governance, and Code of Conduct. When required by the rules of the New York Stock Exchange (NYSE) or the Securities and Exchange Commission (SEC), we will disclose any future amendment to, or waiver of, any provision of the code of conduct for our chief executive officer, principal financial officer, or principal accounting officer or any member or members of our board of directors on our website within four business days following the date of such amendment or waiver.

Corporate Governance Principles

Our board of directors has adopted a set of principles that establish the corporate governance policies pursuant to which our board of directors intends to conduct its oversight of MaxLinear. Among other things, these corporate governance principles address the establishment and operation of board committees, the role of our Lead Director, and matters relating to director independence and performance assessments.

Our corporate governance principles are available at our website by visiting *www.maxlinear.com* and clicking through Investors, Corporate Governance, and Corporate Governance Guidelines.

Role and Composition of the Board

As identified in our corporate governance principles, the role of our board of directors is to oversee the performance of our chief executive officer and other senior management. Our board of directors is responsible for hiring, overseeing, and evaluating management while management is responsible for running our day-to-day operations.

Our board of directors is currently comprised of eight members. Two directors are elected exclusively by the holders of our Class B common stock, voting as a separate class. At least one of these directors must be an executive officer nominated by our nominating and governance committee, with the consent of our founders holding a majority-in-interest of the outstanding Class B common stock over which the founders then exercise voting control. Our founders are executive officers Kishore Seendripu, Ph.D., Curtis Ling, Ph.D., Madhukar Reddy, Ph.D., Kimihiko Imura, Brendan Walsh, and several other employees and former employees named in our amended and restated certificate of incorporation. The current Class B directors are Drs. Ling and Seendripu.

Our remaining directors are elected by the holders of our Class A common stock and Class B common stock, voting together as a single class. Our board of directors is divided into three staggered classes of directors. At each annual meeting of stockholders, a class of directors will be

elected for a three year term to succeed the class whose terms are then expiring. The terms of the directors will expire upon the election and qualification of successor directors at the annual meeting of stockholders to be held during the years 2010 for the Class I directors, 2011 for the Class II directors, and 2012 for the Class III directors.

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2009 Board Meetings

During fiscal 2009, our board of directors held 13 meetings. Each of our directors attended or participated in 75% or more of the meetings of the board of directors and 75% or more of the meetings held by all committees of the board of directors on which he served during the past fiscal year.

Board Leadership Structure

As described below, our board of directors is led by directors Kishore Seendripu, Ph.D. and Thomas E. Pardun. Dr. Seendripu founded MaxLinear and has served as our Chairman, President and Chief Executive Officer since inception. In addition, Mr. Pardun, an independent director with substantial board and executive leadership experience, currently serves as our Lead Director.

Lead Director

Our corporate governance principles require that we designate one independent, non-employee director to serve as Lead Director. In November 2009, prior to our initial public offering, our board of directors appointed Mr. Pardun as our Lead Director, and he continues to serve in that capacity. The Board chose Mr. Pardun as our Lead Director because of his substantial executive experience in the technology and telecommunications industries and his extensive board leadership experience. Mr. Pardun currently serves on the board of directors of four public technology companies, including serving as non-executive chairman of Western Digital Corporation. As Lead Director, Mr. Pardun s responsibilities include:

- coordinating and moderating executive sessions of our independent directors;
- advising the chairman as to the quality, quantity, and timeliness of the flow of information from management that is necessary for the independent directors to effectively and responsibly perform their duties;
- confirming the agenda with the chairman for meetings of our board of directors;
- holding regular update sessions with the chairman of our board of directors;
- acting as the principal liaison between the independent directors and the chairman on sensitive issues; and
- performing such other duties as our board of directors may from time to time delegate to the Lead Director to assist our board of directors in the fulfillment of its responsibilities.

Our board believes that these responsibilities of the Lead Director appropriately and effectively complement MaxLinear s combined chairman and chief executive officer structure as described below.

Chairman of the Board

Our current bylaws provide that the chairman of the board of directors will be our chief executive officer. Our corporate governance principles provide that the board will fill the chairman and chief executive officer positions based upon the board s view of what is in our best interests at any point in time. Our board of directors believes that Dr. Seendripu s service as both chairman and chief executive officer, in combination with Mr. Pardun s service as Lead Director, is in the best interests of MaxLinear and its stockholders.

Given his long tenure with and status within MaxLinear, our board of directors believes Dr. Seendripu possesses detailed and in-depth knowledge of the issues, opportunities, and challenges facing MaxLinear, and we believe he is best positioned to develop agendas that ensure that the board s time and attention are focused on the most critical matters. We also believe his combined role enables decisive leadership,

ensures clear accountability, and enhances MaxLinear s ability to communicate its message and strategy clearly and consistently to its stockholders, employees, and customers.

In addition, we believe the working relationship between Dr. Seendripu and Mr. Pardun, on the one hand, and between Mr. Pardun and the other independent directors, on the other, enhances and facilitates the flow of information between management and our board as well as the ability of our independent directors to evaluate and oversee management and its decision-making.

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Director Independence

As a company listed on the New York Stock Exchange, we are required under NYSE listing requirements to maintain a board comprised of a majority of independent directors, as determined affirmatively by our board. In connection with our listing on the NYSE in March 2010, our board of directors undertook a review of the independence of our directors and considered whether any director has a material relationship with us that could compromise his ability to exercise independent judgment in carrying out his responsibilities. As a result of this review, our board of directors determined that directors Edward E. Alexander, Kenneth P. Lawler, Albert J. Moyer, Thomas E. Pardun, and David Liddle, Ph.D., representing a majority of our directors, are independent directors as defined under the rules of the NYSE. Kishore Seendripu, Ph.D. and Curtis Ling, Ph.D. are not considered independent directors because of their employment as our chief executive officer and chief technical officer, respectively.

Executive Sessions of Independent Directors

In order to promote open discussion among independent directors, our board of directors has a policy of conducting executive sessions of independent directors during each regularly scheduled board meeting. These executive sessions are chaired by our Lead Director. Drs. Ling and Seendripu, as the only two management directors, do not participate in sessions of non-management directors.

Board s Role in Risk Oversight

Our board of directors oversees an enterprise-wide approach to risk management, designed to support the achievement of organizational objectives, including strategic objectives, to improve long-term organizational performance, and to enhance stockholder value. A fundamental part of risk management is not only understanding the most significant risks a company faces and what steps management is taking to manage those risks but also understanding what level of risk is appropriate for a given company. The involvement of our full board of directors in reviewing our business is an integral aspect of its assessment of management s tolerance for risk and also its determination of what constitutes an appropriate level of risk.

While our board of directors has the ultimate oversight responsibility for the risk management process, various committees of the board also have responsibility for risk management. The charter of our audit committee provides that one of the committee s responsibilities is oversight of certain compliance matters. In addition, in setting compensation, our compensation committee strives to create incentives that encourage a level of risk taking consistent with our business strategy and to encourage a focus on building long term value that does not encourage excessive risk-taking.

In connection with its oversight of compensation-related risks, our compensation committee has reviewed our compensation programs and practices for employees, including executive and non-executive programs and practices. In its review, our compensation committee evaluated whether our policies and programs encourage unnecessary or excessive risk taking and controls, and how such policies and programs are structured with respect to risks and rewards, as well as controls designed to mitigate any risks. As a result of this review, our compensation committee determined that any risks that may result from our compensation policies and practices for its employees are not reasonably likely to have a material adverse effect on MaxLinear.

At periodic meetings of the board and its committees and in other meetings and discussions, management reports to and seeks guidance from the board and its committees with respect to the most significant risks that could affect our business, such as legal risks and financial, tax and audit related risks. In addition, among other matters, management provides our audit committee periodic reports on our compliance programs and efforts and investment policy and practices.

Board Committees

Our board of directors has three standing committees: an audit committee, a compensation committee, and a nominating and governance committee.

Audit Committee. Our audit committee currently consists of directors Edward E. Alexander, Albert J. Moyer, and Thomas E. Pardun. Mr. Moyer is the chairman of the audit committee. Our board of directors has determined that each of the members of

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our audit committee is independent and financially literate under the current rules and regulations of the SEC and the New York Stock Exchange and that Mr. Moyer qualifies as an audit committee financial expert within the meaning of the rules and regulations of the SEC. Our board of directors has further determined that Mr. Moyer s simultaneous service on more than three audit committees does not impair the ability of Mr. Moyer to effectively serve as a member and chairman of our audit committee.

In July 2010, Mr. Alexander informed us that he would not stand for reelection at the 2010 annual meeting. Our board has designated Mr. Schrock to replace Mr. Alexander on our audit committee effective as of the annual meeting, and Mr. Schrock has agreed to serve on the audit committee.

Our audit committee oversees our corporate accounting and financial reporting process and assists our board of directors in monitoring our financial systems and our legal and regulatory compliance. Our audit committee also:

- oversees the work of our independent registered public accounting firm;
- approves the hiring, discharge and compensation of our independent registered public accounting firm;
- approves engagements of the independent registered independent public accounting firm to render any audit or permissible non-audit services;
- reviews the qualifications, independence, and performance of the independent registered public accounting firm;
- reviews our financial statements and our critical accounting policies and estimates;
- reviews management s assessment of our internal controls; and
- reviews and discusses with management and the independent auditors the results of our annual audit, our quarterly financial statements, and our publicly filed reports.

We comprised our audit committee in 2009 in connection with preparing for an initial public offering. Mr. Moyer joined our board in October 2009 and was appointed chairman of the audit

committee. Our audit committee held one meeting during fiscal 2009. Our audit committee operates under a written charter approved by our board of directors. The charter is available on our website by visiting *www.maxlinear.com* and clicking through Investors, Corporate Governance, and Audit Committee.

Compensation Committee. Our compensation committee is currently comprised of David Liddle, Ph.D., Thomas E. Pardun, and Donald E. Schrock, each of whom qualifies as an independent director under the applicable rules and regulations of the SEC and the NYSE. Mr. Pardun is the chairman of our compensation committee. Our compensation committee oversees our corporate compensation programs. The compensation committee also:

- reviews and recommends policies relating to compensation and benefits of our executive officers and employees;

- reviews and approves corporate goals and objectives relevant to compensation of our chief executive officer and other executive officers;

- evaluates the performance of our executive officers in light of established goals and objectives;

- recommends compensation of our executive officers based on its evaluations; and

- administers the issuance of stock options and other awards under our equity incentive plans.

See Compensation of Non-Employee Directors and Executive Compensation for a description of our processes and procedures for the consideration and determination of executive and director compensation.

Our compensation committee held five meetings during fiscal 2009. Our compensation committee operates under a written charter approved by the board of directors, which is available on our website by visiting *www.maxlinear.com* and clicking through Investors,   Corporate Governance, and Compensation Committee.

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Nominating and Governance Committee. Our nominating and governance committee is comprised of Kenneth P. Lawler, Albert J. Moyer, and Donald E. Schrock, each of whom qualifies as an independent director under the applicable rules and regulations of the SEC and the NYSE. Mr. Schrock is the chairman of the nominating and governance committee. Our nominating and governance committee oversees and assists our board of directors in reviewing and recommending nominees for election as directors. The nominating and governance committee also:

- evaluates and makes recommendations regarding the organization and governance of the board of directors and its committees;
- assesses the performance of members of the board of directors and makes recommendations regarding committee and chair assignments;
- recommends desired qualifications for board of directors membership and conducts searches for potential members of the board of directors; and
- reviews and makes recommendations with regard to our corporate governance guidelines.

Our nominating and governance committee will consider recommendations of candidates for the board of directors submitted by stockholders of MaxLinear; see *Process for Recommending Candidates for Election to the Board of Directors* below.

Our nominating and governance committee held three meetings during fiscal 2009. Our nominating and governance committee operates under a written charter approved by the board of directors, which is available on our website by visiting *www.maxlinear.com* and clicking through Investors, Corporate Governance, and Nominating and Governance Committee.

Compensation Committee Interlocks and Insider Participation

The members of our compensation committee are Dr. Liddle, Mr. Pardun, and Mr. Schrock. Mr. Pardun is the chairman of our compensation

committee. None of the members of our compensation committee is an officer or employee of our company. None of our executive officers currently serves, or in the past year has served, as a member of the board of directors or compensation committee of any entity that has one or more executive officers serving on our board of directors or compensation committee.

Considerations in Identifying and Evaluating Director Nominees

Our nominating and governance committee has established policies and procedures relating to the consideration of any individual recommended or otherwise introduced, whether by management, another director, stockholders, or third parties, as a prospective director nominee.

The committee will consider candidates recommended by stockholders in the same manner as candidates recommended to the committee from other sources.

In its evaluation of director candidates, including the members of the board of directors eligible for re-election, our committee will consider the following:

- The current size and composition of our board of directors and the needs of the board and it respective committees;
- Factors such as character, integrity, judgment, diversity of experience, independence, area of expertise, corporate experience, length of service, potential conflicts of interest, other commitments and the like. Our committee evaluates these factors, among others, and does not assign any particular weighting or priority to any of these factors; and

- Other factors that our committee may consider appropriate.

Our committee requires the following minimum qualifications to be satisfied by any nominee for a position on the board:

- The highest personal and professional ethics and integrity;
- Proven achievement and competence in the nominee s field and the ability to exercise sound business judgment;

- Skills that are complementary to those of the existing board;

- The ability to assist and support management and make significant contributions to MaxLinear s success; and

- An understanding of the fiduciary responsibilities that are required of a member of the board and the commitment of time and energy necessary to diligently carry out those responsibilities.

If our committee determines that an additional or replacement director is required, the committee may take such measures as it considers appropriate in connection with its evaluation of a director candidate, including candidate interviews, inquiry of the person or persons making the recommendation or nomination, engagement of an outside search firm to gather additional information, or reliance on the knowledge of the members of the committee, board, or management.

Process for Recommending Candidates to the Board of Directors

Our nominating and governance committee is responsible for, among other things, determining the criteria for membership to our board of directors and recommending candidates for election to the board of directors. It is the policy of the nominating and governance committee to consider recommendations for candidates to the board of directors from stockholders holding at least 100,000 shares of our Class A and/or Class B common stock continuously for at least twelve months prior to the date of submission of the recommendation. Stockholder recommendations for candidates to the board of directors must be directed in writing to MaxLinear, Inc., 2051 Palomar Airport Road, Suite 100, Carlsbad, California, 92011, Attention: Vice President, Finance, and must include the candidate s name, home and business contact information, detailed biographical data, relevant qualifications, a signed letter from the candidate confirming willingness to serve, information regarding any relationships between the candidate and MaxLinear, and evidence of the nominating person s ownership of our stock. Such recommendations must also include a statement from the recommending stockholder in support of the candidate, particularly within the context of the criteria for board

membership, including issues of character, judgment, diversity of professional experience, independence, area expertise, corporate experience, length of service, other commitments and the like, and personal references. For details regarding the process to nominate a director, under the section entitled Questions and Answers About the Proxy Materials and Annual Meeting, please see *What is the deadline to propose actions for consideration at next year s annual meeting of stockholders or to nominate individuals to serve as directors? Nomination of Director Candidate.*

Director Attendance at Annual Meetings

Although we do not have a formal policy regarding attendance by members of our board of directors at annual meetings of stockholders, we encourage, but do not require, directors to attend. We have scheduled our 2010 annual meeting of Stockholders on the same day as a regularly scheduled board meeting in order to facilitate attendance.

Communications with the Board of Directors

Stockholders who wish to communicate with our board of directors, Lead Director, committee chairman, any other individual director, or the non-management or independent directors as a group, are welcome to do so in writing, addressed to such person(s) in care of our Vice President, Finance, c/o MaxLinear, Inc., 2051 Palomar Airport Road, Carlsbad, CA 92011, or by fax to (760) 444-8598. Our Vice President, Finance will monitor these communications and will provide a summary of all received messages to our board of directors at each regularly scheduled meeting of our board. Our board of directors generally meets on a quarterly basis. Where the nature of the communication warrants, our Vice President, Finance may determine, in his or her judgment, to obtain the more immediate attention of the appropriate committee or non-management director, of our independent advisors, or of our management.

COMPENSATION OF NON-EMPLOYEE DIRECTORS

Compensation Program Prior to Initial Public Offering

Beginning in mid-2009, prior to filing a registration statement with the Securities and Exchange Commission in connection with an initial public offering, we began the process of recruiting additional independent directors to serve on our board. At that time, we established a policy of paying a $20,000 annual retainer to independent directors not affiliated with our venture capital investors. In addition, we provided for equity incentives in the form of stock options for each of the new directors recruited prior to our initial public offering. In connection with these recruitment efforts, Thomas E. Pardun joined our board in July 2009, and Albert J. Moyer and Donald E. Schrock joined our board in October 2009.

In July 2009, we granted an option to purchase 34,575 shares of Class B common stock at an exercise price of $4.26 per share to Mr. Pardun; in October 2009, we granted an option to purchase 34,575 shares of Class B common stock at an exercise price of $6.55 per share to Mr. Moyer; and in October 2009, we granted an option to purchase 34,575 shares of Class B common stock at an exercise price of $7.45 per share to Mr. Schrock. Each of these options was granted under our 2004 Stock Plan and, assuming the optionee continues as a service provider to us, vests with respect to twenty-five percent of the option one year from the date of grant and then vests in equal monthly installments over the next three years.

Post-IPO Compensation Policy

In connection with our recently completed initial public offering, our compensation committee engaged Compensia, Inc., an independent compensation consulting firm to evaluate our compensation policies for independent directors, including independent directors affiliated with our venture capital investors. Prior to our initial public offering, independent directors affiliated with our venture capital investors received no cash or equity compensation. Compensia reviewed director compensation policies at the same peer group established for purposes of the executive

compensation review described in Compensation Discussion and Analysis beginning on page 26.

Cash Compensation

Following their review of the Compensia data, our compensation committee recommended, and our board of directors approved, the following cash compensation program for non-employee directors:

- $25,000 annual retainer for each non-employee director, payable on a quarterly basis;
- $15,000 additional annual retainer for our Lead Director, Mr. Pardun, payable on a quarterly basis;
- $6,000 annual retainer for each member of the audit committee and $14,000 annual retainer for the chairman of the audit committee, payable on a quarterly basis;

- $4,000 annual retainer for each member of the compensation committee and a $9,000 annual retainer for the chairman of the compensation committee, payable on a quarterly basis; and

- $2,000 annual retainer for each member of the nominating and governance committee and a $6,000 annual retainer for the chairman of the nominating and governance committee, payable on a quarterly basis.

These cash payments became effective for all independent directors in March 2010 upon consummation of our recently completed initial public offering and, with respect to Mr. Moyer, Mr. Pardun and Mr. Schrock, superseded the retainer being paid prior to our recently completed initial public offering.

Initial Director Equity Awards

In addition to the cash compensation structure described above, based in part on the Compensia data, our compensation committee recommended and our board of directors implemented as part of our 2010 Equity Incentive Plan an equity compensation

policy for new independent directors who joined our board after March 2010. Specifically, our policy provides that each individual who is elected or appointed as a non-employee director after the date of our initial public offering will automatically be granted, upon his or her election, an option to purchase an aggregate number shares of our Class A common stock having an estimated fair value on the date of grant of $155,000, with the fair value determined using the Black-Scholes option pricing model on the same basis as used for financial accounting purposes. All of the shares subject to each such grant will vest in equal annual installments over three years, assuming the director continues as a service provider to us. The vesting commencement date of these options will occur when the director first takes office.

Annual Equity Awards

At the time of each of our annual stockholders meetings, beginning in 2011, each non-employee director who continues to serve as a director after that meeting will automatically be granted an option on such date to purchase an aggregate number shares of our Class A common stock having an estimated fair value on the date of grant of $80,000, with the fair value determined using the Black-Scholes option pricing model on the same basis as used for financial accounting purposes. These options will vest one year from the date of grant, assuming the director continues as a service provider to us.

IPO Grants

Under the director equity compensation policy established as part of our initial public offering, each of our non-employee directors was granted an option on the effective date of our initial public offering to purchase an aggregate number shares of our Class A common stock having an estimated fair value on the date of grant of $80,000, with the fair value determined using the Black-Scholes option pricing model on the same basis as used for financial accounting purposes. These options were granted to each of our non-employee directors on March 23, 2010. The number of shares subject to the options was 10,857, and the exercise price of the options was $14.00, the price per share determined in our initial public offering. These options will vest one year from the date of grant, assuming the director continues as a service provider to us.

Waiver of Cash Compensation and Equity Awards

Kenneth P. Lawler has executed an irrevocable waiver for receipt of cash compensation fees for service on our board of directors and nominating and governance committee and the stock option granted under our director compensation policy in connection with our initial public offering. He has also waived the right to receive any future cash compensation and equity incentive awards to which he would otherwise be entitled under our director compensation policies. In addition, the waiver with respect to past cash compensation and equity awards may not be revoked, but may be revoked with respect to future cash compensation and equity awards that have not yet been granted.

2009 Director Compensation

The following table sets forth information concerning compensation paid or accrued for services rendered to us by members of our board of directors for the year ended December 31, 2009. The table excludes Kishore Seendripu, Ph.D., and Curtis Ling, Ph.D., who are executive officers and who did not receive any compensation from us in their roles as directors in the year ended December 31, 2009.

Name	Fees Earned or Paid in Cash ($)	Option Awards ($)(1)	All Other Compensation ($)	Total ($)
Edward E. Alexander				
Kenneth P. Lawler				
David Liddle, Ph.D.				
Albert J. Moyer	5,000	6,464		11,464
Thomas E. Pardun	10,000	8,570		18,570
Donald E. Schrock	5,000	6,287		11,287

(1) Represents the aggregate expense recognized for financial statement reporting purposes for the fiscal year ended December 31, 2009, calculated in accordance with ASC 718 without regard to estimated forfeitures. See Note 2 to our consolidated financial statements included in our audited financial statements included with our 2009 annual report for a discussion of assumptions made in determining the

grant date fair value and compensation expense of our stock options.

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Director Equity Awards

The following table lists all outstanding equity awards held by non-employee directors as of the year ended December 31, 2009.

Name	Number of Securities Under-lying Unexer-cised Options Exer-cisable	Number of Securities Under-lying Unexer-cised Options Unexer-cisable	Option Exercise Price ($)	Option Expi-ration Date	Grant Date Fair Value of Option Awards ($)(1)
Edward E. Alexander					
Kenneth P. Lawler					
David Liddle, Ph.D.					
Albert J. Moyer(2)		34,575	6.55	10/16/19	124,270
Thomas E. Pardun(3)		34,575	4.26	7/28/19	80,257
Donald E. Schrock(4)		34,575	7.45	10/27/19	141,311

(1) Fair values of the option awards on the respective grant dates are computed in accordance with ASC 718. See Note 2 to our consolidated financial statements included in our audited financial statements included with our 2009 annual report for a discussion of assumptions made in determining the grant date fair value and compensation expense of our stock options.

(2) These stock options were granted on October 16, 2009 and vest over four years. 25% of the shares subject to the stock options vest one year after grant. 2.08% of the shares vest at the end of each monthly period thereafter.

(3) These stock options were granted on July 28, 2009 and vest over four years. 25% of the shares subject to the stock options vest one year after grant. 2.08% of the shares vest at the end of each monthly period thereafter.

(4) These stock options were granted on October 27, 2009 and vest over four years. 25% of the shares subject to the stock options vest one year after grant. 2.08% of the shares vest at the end of each monthly period thereafter.

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PROPOSAL NUMBER 1

ELECTION OF CLASS I DIRECTORS

Board Structure

Our board of directors is currently composed of eight members. Our amended and restated certificate of incorporation and bylaws provide that the number of our directors shall be at least two and will be fixed from time to time by a resolution of the majority of our board of directors.

Two members of our board of directors are elected exclusively by the holders of the Class B common stock, voting as a separate class. At least one of these directors must be an executive officer nominated by our nominating and governance committee, with the consent of the founders holding a majority-in-interest of the outstanding Class B common stock over which the founders then exercise voting control. Our founders are Kishore Seendripu, Ph.D., Curtis Ling, Ph.D., Madhukar Reddy, Kimihiko Imura, Brendan Walsh, and several other employees and former employees named in our amended and restated certificate of incorporation. The Class B Directors are Drs. Ling and Seendripu. No Class B directors are being elected at the 2010 annual meeting.

The remaining directors are elected by the holders of our Class A common stock and Class B common stock, voting together as a single class. Our board of directors is divided into three staggered classes of directors. At each annual meeting of stockholders, a class of directors will be elected for a three-year term to succeed the class whose terms are then expiring. The terms of the directors will expire upon the election and qualification of successor directors at the annual meetings of stockholders to be held during the years 2010 for the Class I directors, 2011 for the Class II directors and 2012 for the Class III directors.

Nominees for Class I Director (Terms Expiring in 2013)

At the 2010 annual meeting, two Class I directors will be elected to the board of directors. Our nominating and governance committee recommended, and our board of directors nominated,

Kenneth P. Lawler and David Liddle, Ph.D. as nominees for election as Class I directors at the 2010 annual meeting.

Each of Mr. Lawler and Dr. Liddle has agreed to serve if elected, and management has no reason to believe that either nominee will be unavailable to serve. In the event one of the nominees is unable or declines to serve as a director at the time of the 2010 annual meeting, proxies will be voted for any nominee who may be proposed by the nominating and governance committee and designated by the present board of directors to fill the vacancy.

Biographical Information Concerning the Class I Director Nominees

Kenneth P. Lawler, age 51, has served as a member of our board of directors since November 2006. Since February 1995, Mr. Lawler has served as a general partner of the Battery Ventures fund organization, a venture capital investment firm. Mr. Lawler is a managing member of Battery Partner Ventures VII, L.L.C., which is the sole general partner of Battery Ventures VII, L.P. and the sole managing member of Battery Investment Partners VII, L.L.C. Prior to working at Battery Ventures, Mr. Lawler held various positions, including vice president, at Patricof & Co. Ventures, now known as Apax Partners, and also held various positions, including principal, at Berkeley International Capital Corporation, both venture capital firms. Prior to 1985, he worked in product management at Advanced Micro Devices, Inc. and in engineering management at Teradyne, Inc. and Fairchild Semiconductor International, Inc., all semiconductor companies. Mr. Lawler also serves on the Venture Capital Advisory Board for the Global Semiconductor Alliance. Mr. Lawler received a B.S. and an M.S. in Industrial Engineering from Stanford University and an M.B.A. from the University of California, Los Angeles.

We believe that Mr. Lawler s focus on the semiconductor and technology sectors during his time at Battery Ventures, as well as his many years of technical and operating experience with a number of

companies, bring valuable industry and operational knowledge to our board and qualify him to serve as one of our directors.

David Liddle, Ph.D., age 65, has served as a member of our board of directors since November 2004. Since January 2000, Dr. Liddle has been associated with U.S. Venture Partners, a venture capital investment firm. Dr. Liddle is a managing member of Presidio Management Group VIII, L.L.C., or PMG VIII, the general partner of U.S. Venture Partners VIII, L.P. and certain other venture partner investment funds which together with PMG VIII are collectively referred to as U.S. Venture Partners, or USVP. From March 1992 to December 1999, Dr. Liddle co-founded and served as the President and Chief Executive Officer of Interval Research Corporation, a computer-related research laboratory based in Palo Alto, California. From November 1991 to March 1992, he served as Vice President of New Systems Business Development, Personal Systems, for International Business Machines Corporation, a computer and office equipment manufacturer. Dr. Liddle also serves on the board of the New York Times Company, a publishing company. Dr. Liddle received a B.S. in Electrical Engineering from the University of Michigan and a Ph.D. in Electrical Engineering and Computer Science from the University of Toledo.

We believe that Dr. Liddle s focus on the semiconductor and technology sectors during his time at U.S. Venture Partners, as well as his several years of technical and operating experience with a number of companies, bring valuable industry and operational knowledge to our board and qualify him to serve as one of our directors.

Required Vote

Our Class I directors will be elected by a plurality of the votes of the holders of Class A common stock and Class B common stock (voting together as a single class) present in person or represented by proxy and entitled to vote on the election of directors. In other words, the two nominees receiving the highest number of FOR votes will be elected as directors. Shares represented by executed proxies will be voted, if authority to do so is not expressly withheld (as indicated on the proxy card), for the election of Mr. Lawler and Dr. Liddle.

Recommendation

Our board of directors recommends a vote FOR the election to the board of directors of each of Kenneth P. Lawler and David Liddle as a Class I director.

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Class I Director Not Standing for Re-election

In July 2010, *Edward E. Alexander*, age 46 and currently a Class I director, announced that he would not stand for re-election at our 2010 annual meeting. Mr. Alexander has served as a member of our board of directors since November 2004, when he led Mission Ventures investment in our first venture capital financing. Our board of directors, management, and founders wish to thank Mr. Alexander for his support and dedication to MaxLinear. Since January 2000, Mr. Alexander has served as a Managing Partner of Mission Ventures, a venture capital investment firm focused on early stage technology investments throughout Southern California. He joined Mission Ventures as an associate in August 1997. Previously, Mr. Alexander was a platoon commander in the U.S. Navy SEALs and a division officer aboard a U.S. Navy destroyer. Mr. Alexander received a B.S. in Engineering from the United States Naval Academy and an M.B.A. from Duke University.

We believe that Mr. Alexander s focus on technology companies as a Managing Partner of Mission Ventures has brought valuable industry and operational knowledge to our board and qualified him to serve as one of our directors.

Class II Directors Continuing in Office until the 2011 Annual Meeting

Curtis Ling, Ph.D., age 44, is a co-founder and has served as our Chief Technical Officer since April 2006. He serves as a director representing our Class B common stock. From March 2004 to July 2006, Dr. Ling served as our Chief Financial Officer, and from September 2003 to March 2004, as a co-founder, he consulted for us. From July 1999 to July 2003, Dr. Ling served as a principal engineer at Silicon Wave, Inc. From August 1993 to May 1999, Dr. Ling served as a professor at the Hong Kong University of Science and Technology. Dr. Ling received a B.S. in Electrical Engineering from the

California Institute of Technology and an M.S. and Ph.D. in Electrical Engineering from the University of Michigan, Ann Arbor.

We believe Dr. Ling s more than ten years of technical and operational experience in the semiconductor industry brings valuable industry knowledge and practical experience to our board and qualifies him to serve as one of our directors.

Albert J. Moyer, age 66, has served as a member of our board of directors since October 2009. Since 2000, Mr. Moyer has served as a private financial consultant. From March 1998 to February 2000, Mr. Moyer served as Executive Vice President and Chief Financial Officer of QAD Inc., a publicly held software company that is a provider of enterprise resource planning software applications, and he subsequently served as a consultant to QAD Inc., assisting in the Sales Operations of the Americas Region. From August 1995 to March 1998, Mr. Moyer served as Chief Financial Officer of Allergan Inc., a specialty pharmaceutical company. Previously, Mr. Moyer served as Chief Financial Officer of National Semiconductor Corporation, a semiconductor company. Mr. Moyer also served as Chief Financial Officer of Western Digital Corporation, a manufacturer of hard-disk drives for the personal computer and home entertainment markets. Mr. Moyer also serves on the board of each of CalAmp Corp., a provider of wireless communications solutions; Collectors Universe, Inc., a third-party grading and authentication service for high-value collectibles; Virco Manufacturing Corporation, a manufacturer of educational furniture; LaserCard Corporation, a provider of secure identification solutions; and Occam Networks, Inc., a developer of broadband networking equipment. Mr. Moyer received his B.S. in finance from Duquesne University and graduated from the Advanced Management Program at the University of Texas, Austin. In November 2008, Mr. Moyer earned a Professional Director Certification from the Corporate Directors Group, an accredited provider of RiskMetrics ISS director education.

We believe Mr. Moyer s several years experience as chief financial officer for other public companies and his service on the board of directors of several other companies bring substantial financial, accounting, and operational knowledge to our board and qualify him to serve as one of our directors.

Donald E. Schrock, age 65, has served as a member of our board of directors since October 2009. Mr. Schrock retired as Executive Vice President and President of Qualcomm Incorporated s CDMA Technologies Group in 2003. Mr. Schrock began his career with Qualcomm in January 1996 as Corporate Vice President. Prior to joining Qualcomm, Mr. Schrock was Group Vice President and Division Manager with GM Hughes Electronics. Prior to working at Hughes, Mr. Schrock was Vice President of Operations with Applied Micro Circuit Corporation. Mr. Schrock also held positions as Vice President / Division Manager at Burr-Brown Corporation and spent 15 years with Motorola Semiconductor. Mr. Schrock has served on the board of directors of Patriot Scientific Corporation, a public intellectual property licensing company since April 2008, as well as the board of directors of Integrated Devices Technology Inc., a designer and fabricator of semiconductor components, since October 2009. He also previously served on the board of directors of the Fabless Semiconductor Association. Mr. Schrock holds a BSEE with honors from the University of Illinois, has completed the coursework for an MSEE from Arizona State University and has an Advanced Business Administration degree from the Arizona State University Center for Executive Development.

We believe Mr. Schrock s business leadership, operational and financial experience as a result of his experience serving for several years in executive positions for large technology companies, his long history in the technology industry, and his experience serving as a director for other public companies bring valuable industry knowledge and practical experience to our board and qualify him to serve as one of our directors.

Class III Directors Continuing in Office until the 2012 Annual Meeting

Kishore Seendripu, Ph.D., age 41, is a co-founder and has served as our Chairman, President and Chief Executive Officer since our inception in September 2003. He serves as a director representing our Class B common stock. From July 1998 to July 2002, Dr. Seendripu served in senior engineering roles, most recently as the director of RF & Mixed-Signal IC Design at Silicon Wave, Inc., a designer and developer of radio frequency systems-on-chip for use in wireless and broadband communication systems and products. From

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December 1997 to July 1998, Dr. Seendripu served as a member of the technical staff at Broadcom Corporation, a manufacturer of networking and communications integrated circuits for data, voice and video applications. From 1996 to December 1997, Dr. Seendripu served as a radio frequency integrated circuit, or RFIC, design engineer at Rockwell Semiconductor Systems, a provider of semiconductor system solutions for personal communications electronics. From 1990 to 1992 Dr. Seendripu served as a research assistant at the Lawrence Berkeley National Laboratories. Dr. Seendripu received an M.S. in Materials Sciences Engineering and a Ph.D. in Electrical Engineering from the University of California at Berkeley, a B. Tech degree from the Indian Institute of Technology, Bombay, India, and an M.B.A. from the Wharton School, University of Pennsylvania.

We believe Dr. Seendripu s more than 15 years of technical and management experience in the semiconductor industry brings valuable industry knowledge and practical experience to our board and qualifies him to serve as one of our directors.

Thomas E. Pardun, age 66, has served as a member of our board of directors since July 2009. Since April 2007, Mr. Pardun has served as non-executive chairman of the board of directors of Western Digital Corporation. Mr. Pardun has served as a director of Western Digital Corporation since January 1993, and from January 2000 to November 2001, he previously served as chairman of the board of directors of Western Digital Corporation. From May 1996 to July 2000, Mr. Pardun served as president of MediaOne International, Asia-Pacific (formerly US West Asia-Pacific), an owner/operator of international properties in cable television, telephone services and wireless communications. From May 1993 to April 1996, Mr. Pardun served as president and chief executive officer of US West Multimedia Communications, Inc., a communications company, and from June 1988 to April 1993 held numerous other executive positions with US West, Inc. From June 1986 to May 1988, Mr. Pardun was president of the Central Group for Sprint, Inc. as well as president of Sprint s West Division. From September 1984 to May 1986, he also served as senior vice president of United Telecommunications, a predecessor company to Sprint. From June 1965 to August 1984, he held various positions at International Business Machines

Corporation. In addition to Western Digital Corporation, Mr. Pardun also serves on the boards of each of CalAmp Corp., Finisar Corporation, and Occam Networks, Inc. Mr. Pardun received a B.B.A. in Economics and Marketing from the University of Iowa and Management School Certificates from Harvard Business School, Stanford University and The Tuck School of Business at Dartmouth College.

We believe Mr. Pardun s experience serving for several years in executive positions for large technology companies, his long history in the technology industry, and his experience serving as a director and non-executive chairman for other public companies bring valuable industry knowledge and practical experience to our board and qualify him to serve as one of our directors.

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PROPOSAL NUMBER 2

RATIFICATION OF SELECTION OF INDEPENDENT

REGISTERED PUBLIC ACCOUNTING FIRM

Our audit committee has selected Ernst & Young LLP as the independent registered public accounting firm to audit our consolidated financial statements for the fiscal year ending December 31, 2010. During 2009, Ernst & Young LLP served as our independent registered public accounting firm and also provided certain tax and audit-related services.

Notwithstanding its selection and even if stockholders ratify the selection, our audit committee, in its discretion, may appoint another independent registered public accounting firm at any time during the year if the audit committee believes that such a change would be in the best interests of MaxLinear and its stockholders. Our audit committee is submitting the selection of Ernst & Young LLP to our stockholders because we value our stockholders views on our independent registered public accounting firm and as a matter of good corporate governance. If the appointment is not ratified by our stockholders, our audit committee may reconsider whether it should appoint another independent registered public accounting firm.

Representatives of Ernst & Young LLP are expected to attend the annual meeting, where they will be available to respond to appropriate questions and, if they desire, to make a statement.

Required Vote

Ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2010 requires the affirmative FOR vote of a majority of the shares present, represented, and entitled to vote on the proposal. Unless marked to the contrary, executed proxies received will be voted FOR ratification of the appointment of Ernst & Young LLP.

Recommendation

Our board of directors recommends a vote FOR the selection of the appointment of Ernst &

Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2010.

* * * * *

Principal Accounting Fees and Services

The following table presents fees billed for professional audit and other services rendered to MaxLinear by Ernst & Young LLP for the years ended December 31, 2009 and December 31, 2008.

	2009	2008
Audit Fees(1)	$ 877,701	$ 72,648
Audit-Related Fees(2)	1,995	
Tax Fees(3)	149,945	

All Other Fees				
Total	$	1,029,641	$	72,648

(1) Audit fees for 2009 include $786,832 related to services in connection with our initial public offering, including comfort letters, consents and review of documents filed with the SEC.
(2) Audit-related fees relate to an online subscription for accounting information.
(3) Tax fees include analysis of research and development tax credits and net operating loss carryforwards and general tax consulting.

Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services

Consistent with the requirements of the SEC and the Public Company Accounting Oversight Board, or PCAOB, regarding auditor independence, our audit committee has responsibility for appointing, setting compensation, and overseeing the work of our independent registered public accounting firm. In recognition of this responsibility, our audit committee has established a policy for the pre-approval of all audit and permissible non-audit services provided by the independent registered public accounting firm.

Prior to the engagement of the independent registered public accounting firm for the next year s audit, management submits a list of services falling within the four categories below expected to be rendered by the firm during that year and the related fees to the audit committee for approval.

*1. **Audit*** services include audit work performed on the financial statements, as well as work, including information systems and procedural review and testing, that is required to be performed by the independent registered public accounting firm to allow the firm to form an opinion on our financial statements. Audit services also include services that only the independent registered public accounting firm can reasonably be expected to provide, including comfort letters and statutory audits.

*2. **Audit-related*** services are for assurance and related services that are reasonably related to the performance of the audit or review of our financial statements and/or internal control over financial reporting or that are traditionally performed by the independent registered public accounting firm and include due diligence related to mergers and acquisitions, audits of employee benefit plans and special procedures required to meet certain regulatory requirements.

*3. **Tax*** services include services such as tax compliance, tax planning and tax advice, as long as such services do not impair the independence of the independent registered public accounting firm and are consistent with the SEC s rules on auditor independence.

*4. **All other*** services are those services not captured in the audit, audit-related, or tax categories.

Prior to engagement, the audit committee pre-approves the independent registered public accounting firm s services within each of the four categories described above and the fees for each category are budgeted. The audit committee requires the independent registered public accounting firm and management to report actual fees versus the budgeted amount periodically throughout the year by category of services. During the year, circumstances may arise when it may become necessary to engage the independent registered public accounting firm for additional services not contemplated in the original pre-approval categories. In those instances, the audit

committee requires specific pre-approval before engaging the independent registered public accounting firm.

The audit committee may delegate pre-approval authority to one or more of its members provided that such member must report, for informational purposes only, any pre-approval decisions to the audit committee at its next scheduled meeting.

The audit committee has determined that the rendering of services other than audit services by Ernst & Young LLP is consistent with maintaining Ernst & Young LLP s independence.

Report of the Audit Committee

The audit committee assists the board in fulfilling its oversight responsibility over MaxLinear s financial reporting process. It is not the duty of the committee to plan or conduct audits or to prepare MaxLinear s financial statements. Management has the primary responsibility for preparing the financial statements and assuring their accuracy, effectiveness, and completeness. Management is also responsible for the reporting process, including the system of internal controls. The independent registered public accounting firm is responsible for auditing MaxLinear s financial statements and internal control over financial reporting and expressing its opinion as to whether the statements present fairly, in accordance with accounting principles generally accepted in the United States, MaxLinear s financial condition, results of operations, and cash flows. However, the audit committee does consult with management and the independent registered public accounting firm prior to the presentation of financial statements to stockholders and, as appropriate, initiates inquiries into various aspects of MaxLinear s financial affairs.

Unless the committee has reason to question its reliance on management or the independent registered public accounting firm, the members of the committee necessarily rely on information provided to them by and on the representations made by management and the independent registered public accounting firm. Accordingly, the audit committee s oversight does not provide an independent basis to determine that management has applied appropriate accounting and financial reporting principles. Furthermore, the audit committee s authority and

oversight responsibilities do not independently assure that the audits of MaxLinear s financial statements have been carried out in accordance with the standards of the PCAOB or that the financial statements are presented in accordance with accounting principles generally accepted in the United States.

In this context, the committee has met and held discussions with management and the independent registered public accounting firm regarding MaxLinear s audited 2009 consolidated financial statements (including the quality of MaxLinear s accounting principles). Management represented to the committee that MaxLinear s consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States, and the committee consulted with management and the independent registered public accounting firm prior to approving the presentation of the audited 2009 consolidated financial statements to stockholders. The committee discussed with the independent registered public accounting firm the matters required to be discussed by Statement on Auditing Standards No. 61, as amended (*AICPA, Professional Standards*, Vol. 1, AU Section 380), as adopted by the PCAOB in Rule 3200T.

The audit committee has received and discussed with the independent registered public accounting firm the auditor s independence from MaxLinear and its management. As part of that review, the committee received the written disclosures and letter required by the applicable requirements of the PCAOB regarding the independent accountant s communications with the audit committee concerning independence. The committee has also considered whether the provision of non-audit services by the independent registered public accounting firm is compatible with, or has compromised, the auditor s independence. The committee has concluded that the independent registered public accounting firm is independent from MaxLinear and its management.

Based on the reviews and discussions referred to above, the audit committee recommended to the board, and the board approved, MaxLinear s audited consolidated financial statements for the year ended December 31, 2009 for filing with the Securities and Exchange Commission as part of the Company s Registration Statement on Form S-1 (No. 333-162947). The committee has selected Ernst &

Young LLP as the Company s independent registered public accounting firm for the fiscal year ending December 31, 2010.

The Audit Committee

Albert J. Moyer (Chair)

Edward E. Alexander

Thomas E. Pardun

The Report of the Audit Committee does not constitute soliciting material, and shall not be deemed to be filed or incorporated by reference into any other filing by MaxLinear under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent MaxLinear specifically incorporates the Report of the Audit Committee by reference therein.

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EXECUTIVE OFFICERS

The names of our executive officers, their ages, their positions with MaxLinear, and other biographical information as of September 1, 2010, are set forth below. There are no family relationships among any of our directors or executive officers.

Name	Age	Position
Kishore Seendripu, Ph.D.(1)	41	Chairman, President and Chief Executive Officer
Joe D. Campa	53	Vice President, Finance and Treasurer
Patrick E. McCready	52	Chief Accounting Officer and Controller
John M. Graham	48	Vice President, Marketing
Kimihiko Imura	53	Vice President, Semiconductor Technology and Operations
Michael C. Kastner	48	Vice President, Sales
Curtis Ling, Ph.D.(1)	44	Chief Technical Officer and Director
Madhukar Reddy, Ph.D.	40	Vice President, IC and RF Systems Engineering
Brendan Walsh	36	Vice President, Business Development

(1) Class B common stock director

Kishore Seendripu, Ph.D. *For a brief biography of Dr. Seendripu, please see Proposal One Election of Class I Directors Class III Directors continuing in office until the 2012 Annual Meeting.*

Joe D. Campa has served as our Vice President, Finance and Treasurer since January 2010. From March 2008 to January 2010, Mr. Campa served as our Chief Financial Officer. From October 2007 to March 2008, Mr. Campa served as a consultant for us. From September 2002 to June 2007, Mr. Campa served as the chief financial officer of Jaalaa, Inc., a wireless semiconductor company. From August 2000 to July 2002, Mr. Campa served as the Chief Financial Officer and Vice President of Corporate Strategy of Transillica, Inc., a Bluetooth wireless semiconductor company. Prior to August 2000, Mr. Campa served as chief investment officer and portfolio manager for institutional investment management firms. Mr. Campa received a B.A. in Economics and an M.B.A. from Stanford University.

Patrick E. McCready has served as our Chief Accounting Officer and Controller since January 2010. He joined us as our corporate controller in December 2009. From December 2008 to August 2009, Mr. McCready served as Chief Financial Officer of RAD Electronics, Inc., a manufacturing services company specializing in electronic equipment. From September 2006 to November 2008, he served as Chief Financial Officer of Channell Commercial Corporation, a designer and manufacturer of telecommunications equipment.

From April 1991 to April 2006, Mr. McCready was employed with Pulse Engineering, Inc., a designer and manufacturer of magnetics-based electronic components, serving as their corporate controller from 1991 to 1995 and as their Vice President of Finance from 1995 to 2006. Mr. McCready received a Bachelor of Business Administration degree from the University of Notre Dame.

John M. Graham has served as our Vice President, Marketing since November 2008. From March 2005 to November 2008, Mr. Graham served as Vice President of Marketing at Entropic Communications, a provider of silicon and software solutions to enable home networking of digital entertainment. From October 2003 to March 2005, Mr. Graham served as the Vice President of World Wide Sales at picoChip Designs Limited, a supplier of processor array chips for wireless infrastructure applications. From January 2003 to June 2003, he served as Executive Vice President for Transitive Technologies Inc., a central processing unit emulation software company, and from September 2000 to December 2002, Mr. Graham served as the President and Chief Executive Officer of the company. From June 1996 to September 2000, he served as General Manager and Vice President of Marketing for Conexant Systems, Inc., a semiconductor company. From January 1993 to June 1996, Mr. Graham served as the General Manager of the Graphics Business Unit and a Sales Manager at Brooktree Corporation, a producer of integrated circuits

for consumer products, including networking,

digital video, cordless technology, fax machines, modems and set top boxes. Mr. Graham received a B.S. in Electrical and Electronic Engineering from the University of Nottingham, England and an M.B.A. from the University of San Diego.

Kimihiko Imura is a co-founder and has served as our Vice President, Semiconductor Technology and Operations since January 2004. From April 1985 to March 1995, Mr. Imura served as a senior member of technical staff of Compound Semiconductor Device Development at Japan Energy Corporation, a producer and distributor of crude oil. From April 1995 to July 2001, he served as the Technology Development Manager at AMI Semiconductors (now ON Semiconductor). From August 2001 to December 2003, he served as a senior member of technical staff at Silicon Wave, Inc., a semiconductor company (now RF Micro Devices, a Qualcomm Bluetooth Division). Mr. Imura received a B.S. in Engineering from Tokushima University and an M.S. in Materials Science from Hiroshima University in Japan.

Michael C. Kastner has served as our Vice President, Sales since September 2008. From July 2004 to April 2008, Mr. Kastner served as Vice President of Worldwide Sales for Impinj, Inc., a radio-frequency identification systems solutions and semiconductor company. From June 2002 to July 2004, Mr. Kastner served as the Director of Sales, Global Account Management for Skyworks Solutions, Inc., a wireless handset chip supplier. From September 1996 to January 1999, Mr. Kastner held various positions in sales management at Conexant Systems, Inc., a semiconductor company and Rockwell International, a manufacturing company. From June 1987 to September 1996, Mr. Kastner was a Product Line Manager at Brooktree Corporation. Mr. Kastner received a B.S. in Electrical Engineering from Cleveland State University and has completed executive programs at the University of California, San Diego and the University of California, Irvine.

Curtis Ling, Ph.D. *For a brief biography of Dr. Ling, please see* *Proposal One Election of Class I Directors Class II Directors Continuing in Office Until the 2011 Annual Meeting.*

Madhukar Reddy, Ph.D. has served as our Vice President, IC and RF Systems Engineering since November 2006. From January 2005 to November

2006, Dr. Reddy served as our Director, RF/Mixed-Signal IC Design. From July 2002 to January 2005, he served as Manager, RFIC Design at Skyworks Solutions. From January 1999 to July 2002, he served as RFIC Design Engineer and Group Leader at Conexant Systems. From January 1997 to December 1998, he served as RFIC Designer at Rockwell Semiconductor Systems. Since 2005, Dr. Reddy has been a member of the Technical Program Committee of the IEEE RFIC Symposium. Dr. Reddy received a B. Tech degree from the Indian Institute of Technology, Madras, India, and an M.S. and Ph.D. in Electrical Engineering from the University of California, Santa Barbara.

Brendan Walsh has served as our Vice President, Business Development since November 2008. From September 2004 to October 1, 2007, he served as our Vice President of Sales, Marketing and Business Development. From October 2008 to November 2008, he served as our Vice President of Marketing and Business Development. From October 2000 to August 2004, Mr. Walsh was the Director of Business Development and Venture Investment in the corporate mergers and acquisitions department of Philips Electronics N.V., an electronics company. From August 1999 to October 2000, he served as a strategic investment manager for Hikari Tsushin Inc., a retailer of mobile devices and venture capital firm focusing on mobile technologies. Mr. Walsh received a B.A. from the University of California, Davis and an M.B.A. from the Wharton School, University of Pennsylvania.

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EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

This compensation discussion and analysis reviews and discusses our compensation programs and policies for our principal executive officer, principal financial officer, and three additional executive officers who were our most highly compensated executive officers as determined by the rules of the Securities and Exchange Commission. For 2009, these executive officers were Kishore Seendripu, Ph.D., our chairman, president and chief executive officer; Joe D. Campa, our current vice president, finance and treasurer and our principal financial officer; Kimihiko Imura, our vice president, semiconductor technology and operations; Madhukar Reddy, Ph.D., our vice president, IC and RF systems engineering; and Brendan Walsh, our vice president, business development. As a group, we refer to these five executive officers as our named executive officers, and they are identified in the summary compensation table provided below.

Objectives of Executive Compensation Programs

The principal objectives of our executive compensation programs are the following:

- to attract and retain talented and experienced executives;
- to motivate and reward executives whose knowledge, skills and performance are critical to our success;
- to ensure fairness among the executive management team by recognizing the contributions each executive makes to our success; and
- to incentivize our executives to manage our business to meet our long-term objectives and the long-term objectives of our stockholders.

Since we were founded in 2003, our compensation programs have reflected our status as a start-up company, and their principal objective has been to preserve cash resources while attracting and retaining executive talent, largely through the grant of equity incentives consisting of stock options that vest over time. As a result of the heavy equity

weighting in our overall compensation program, our current compensation programs are, when compared to a public company peer group, in the lower ranges with respect to cash compensation and in the higher ranges with respect to equity compensation. By focusing our executive compensation program on equity incentive awards, we have sought to align the interests of our executive officers and stockholders by motivating executive officers to increase the value of our stock over time.

Historically, our compensation programs have been administered by our board of directors, as we did not have an active compensation committee. In connection with our recently completed initial public offering, we formed a compensation committee, which engaged Compensia, an independent executive compensation consulting firm, to evaluate our executive compensation programs relative to those of a public company peer group and to make recommendations with respect to appropriate levels and forms of compensation. The objective of this evaluation and the resulting compensation adjustments was to ensure that we remain competitive as a newly public company and that our named executive officers have meaningful incentives to remain employed with us. As discussed in greater detail below, in October 2009, our compensation committee approved various adjustments in our compensation programs, including base salary adjustments that became effective upon completion of our

initial public offering and implementation of a cash bonus plan for fiscal 2010. These adjustments were intended to begin the process of bringing our cash compensation programs in line with those of public peers, to link short-term cash compensation to achievement of financial milestones, and to ensure that unvested equity awards held by our executive officers create appropriate long-term retention and performance incentives.

Our compensation committee intends to determine allocations of compensation between cash and equity compensation or among different forms of non-cash compensation based on its review of typical allocations within our compensation peer group. The committee has not adopted, however, and has no current plans to adopt, any policy requiring a specific

allocation between cash and equity compensation or between short-term and long-term compensation. In the course of its deliberations, the committee will review each component of compensation, how they relate to each other, and in particular, how they relate to and affect total compensation. The compensation committee s philosophy is that a substantial portion of an executive officer s compensation should be performance-based, whether in the form of equity or cash compensation. In that regard, we also expect to continue to use options or other equity incentive awards as a significant component of compensation because we believe that they best align individual compensation with the creation of stockholder value. To the extent we use cash incentive plans in the future, we anticipate that cash bonuses will be tied to annual financial performance targets.

Role of Our Compensation Committee

As a public company, our compensation committee will assume responsibility for determining the compensation of all executive officers. Our compensation committee operates under a written charter adopted by our board of directors, which establishes the duties and authority of our compensation committee. The fundamental responsibilities of our compensation committee are as follows:

- to oversee our overall compensation philosophy, compensation plans and benefits programs and to make recommendations to our board of directors with respect to improvements or changes to such plans;

- to review and approve all compensation arrangements for our executive officers (including our chief executive officer);

- to review and approve all equity compensation awards to our executive officers (including our chief executive officer); and

- to oversee and administer our equity compensation plans.

Our compensation committee is comprised of the following non-employee members of our board of directors: Thomas E. Pardun, who chairs the committee, David Liddle, Ph.D., and Donald E. Schrock. Each of Mr. Pardun, Dr. Liddle, and

Mr. Schrock is an independent director under the rules of the New York Stock Exchange, an outside director for purposes of Section 162(m) of the Internal Revenue Code, and a non-employee director for purposes of Rule 16b-3 under the Securities Exchange Act of 1934, as amended. Mr. Schrock did not join our board of directors or the compensation committee until October 27, 2009. As a result, he did not participate in the 2010 competitive market review described below or in the development of the committee s recommendations for compensation adjustments made in connection with our recently completed initial public offering. He did, however, participate in the board s consideration and approval of the committee s recommendations on October 27, 2009. Our compensation committee has the authority under its charter to engage the services of outside advisors, experts and others for assistance.

Kishore Seendripu, Ph.D., our chairman, president, and chief executive officer, supports the compensation committee s work by providing information relating to our financial plans, performance assessments of our officers, and other personnel-related data. In particular, as the person to whom our other named executive officers directly report, Dr. Seendripu is responsible for evaluating individual officers contributions to corporate objectives as well as their performance relative to individual objectives. He will, on an annual basis each year beginning in 2011, make recommendations to our compensation committee with respect to base salary adjustments, targets under any annual cash incentive programs, and stock option grants or other equity incentives. Our compensation committee is not required to follow any recommendations of Dr. Seendripu and will exercise its discretion in modifying, accepting or rejecting any recommended adjustments or awards. Without the participation of Dr. Seendripu, we expect our compensation committee, as part of the annual review process, to conduct a similar evaluation of his contribution and individual performance and to make determinations, after the beginning of each fiscal year, with respect to any base salary adjustments, targets under any annual cash incentive programs and stock option grants or other equity incentives.

2010 Competitive Market Review

The market for experienced management is highly competitive in the semiconductor industry.

We seek to attract and retain the most highly qualified executives to manage each of our business functions, and we face substantial competition in recruiting management from companies ranging from established players with multibillion dollar revenue to entrepreneurial, early-stage companies. We are fortunate that many members of our executive management team have long tenures with us, but from time to time we also have been required to recruit new executive officers. As a result, we need to ensure that our executive compensation programs provide sufficient retention incentives as well as incentives to achieve our long-term strategic business and financial objectives. We expect competition for individuals with our required skill sets, particularly technical and engineering skills, to remain intense even in a relatively weak global macroeconomic environment.

In September 2009, our compensation committee initiated a comprehensive review of our executive and director compensation policies. In that regard, the compensation committee engaged Compensia, an independent compensation consulting firm with substantial experience in the technology sector, to evaluate our levels and types of executive compensation and to recommend changes as appropriate. Among other objectives, we engaged Compensia to assist us in identifying a group of peer companies for purposes of benchmarking our levels of compensation; to gather and analyze compensation data from those peer companies as well as from other available compensation data; to advise us on the creation and implementation of a performance-based cash incentive plan, including determining target bonus levels; and to assist us in structuring awards as part of the equity incentive element of our compensation program, including assisting us in establishing appropriate amounts for equity incentive awards. Compensia was retained during fiscal 2009 only for purposes of evaluating and establishing our post-initial public offering executive and director compensation policies. Aggregate fees paid for Compensia s engagement by the compensation committee did not exceed $120,000.

Following Compensia s engagement, a Compensia representative worked with our compensation committee, then comprised of Dr. Liddle and Mr. Pardun, to establish a peer group of companies for comparing our competitive compensation levels with those of relevant peers.

Based on an analysis of companies in our industry and their relative revenue and market capitalizations, Compensia recommended, and our compensation committee approved, two peer sets: a current peer group of semiconductor companies with a range of financial and organizational characteristics, specifically revenue and market capitalization, that we believe establishes an appropriate comparative base for us as a newly public company and an aspirational peer group of larger semiconductor companies. Although our compensation committee s recommendations were based principally on the current peer data, we believe consideration of the larger company data is appropriate, in some cases because of existing or potential overlap in our target product markets and in other cases due to the geographic proximity of our respective operations. For these reasons, we believe we will be competing with our aspirational peer group for available management talent. The current and aspirational peer groups recommended by Compensia and approved by our compensation committee in September 2009 were as follows:

Current Peer Group		**Aspirational Peers**
Cavium Networks, Inc.	Techwell, Inc.	Atheros Communications, Inc.
Conexant Systems, Inc.	Monolithic Power Systems, Inc.	Broadcom Corporation
Entropic Communications, Inc.	Ultratech, Inc.	Marvell Technology Group Ltd.
Exar Corporation	Volterra Semiconductor Corp.	Qualcomm Incorporated
Ikanos Communications, Inc.	Hittite Microwave Corporation	Silicon Laboratories Inc.
Intellon Corporation	MIPS Technologies, Inc.	Skyworks Solutions, Inc.
NetLogic MicroSystems, Inc.	Rambus Inc.	

In directing Compensia s review and analysis of our compensation structure, our compensation committee established, with the approval of our board of directors, a compensation philosophy to guide determinations of compensation adjustments made in connection with our recently completed

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initial public offering. In light of our history as a start-up company and our substantial focus on equity incentives as a recruiting tool, the committee anticipated that our cash compensation would compare less favorably to that of our peer group while the historic size of our equity awards would exceed levels typically available at public companies. The committee also believed that the relative focus of our compensation policy as between cash and equity compensation should shift over time, with an increasing component of compensation being in the form of cash beginning with our recently completed initial public offering and a diminishing focus on equity, on a relative basis with respect to the size of equity awards, after our public offering and as our business grows. Although we expect the cash component of total compensation to increase over time, we nonetheless expect that grants of equity incentives will remain a material element of our overall compensation.

In September 2009, the compensation committee approved the following policies with respect to executive compensation:

- Cash compensation should be heavily weighted toward performance-based compensation;

- Target executive base salaries should approximate the median of our current peer group;

- Target total cash compensation, consisting of base salary and short-term cash incentives, should fall between the 50th to 75th percentiles of our peer group, with a relatively higher percentile target for incentive cash compensation compared to base salary, based on achievement of corporate, financial and/or individual milestones, as may be determined from time to time by the committee; and

- Equity incentive awards should be granted and structured to maximize their long-term retention incentive.

Our compensation committee acknowledged that a transition period will be required to increase our base salary and target total cash compensation levels to these peer group percentile objectives. We currently expect our levels of cash compensation to increase over the next few years, subject to growth

rates in our business and the extent to which our operating plan will support such increases. Our compensation committee is not obligated to increase our cash compensation under any agreements with our executive officers and will exercise its discretion, based on developments in our business and operating results.

In connection with our October 2009 executive compensation assessment, Compensia and our compensation committee concluded that:

- Our current base salary levels are substantially below the 25th percentile of our current peer group;

- Our cash incentive compensation programs and total cash compensation are substantially below the 25th percentile of our current peer group; and

- Our historic long-term equity incentive awards were extremely competitive relative to those of our current peer group, but in the case of several executive officers whose equity incentive awards were largely vested, then-outstanding awards offered limited retention value.

Our compensation committee believes that the loss of any of our key executives would have an adverse effect on the operation and management of our business, particularly in light of the increased management and administrative requirements associated with operating as a public company. The market for executive talent among semiconductor companies is currently very competitive. We believe, and our compensation committee concurs, that we may be vulnerable to a loss of key talent, or an inability to obtain additional talent, if we do not establish a compensation structure that is competitive in our markets and in particular that establishes appropriate performance-based incentives.

In the course of making its October 2009 determinations, the compensation committee consulted with Dr. Seendripu to obtain his input and suggestions concerning proposed compensation adjustments for executive officers reporting to Dr. Seendripu. The committee also discussed with Dr. Seendripu his views concerning his own compensation, but Dr. Seendripu did not participate in any committee deliberations concerning his compensation.

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On October 27, 2009, our board of directors met and approved various adjustments to our compensation structure, which are described in detail below. Dr. Seendripu did not participate in the portion of the meeting where his compensation was discussed and approved. Curtis Ling, Ph.D., a director and our Chief Technology Officer, did not participate in the discussion or approval of any executive s compensation, including his own.

Elements of Executive Compensation

Our executive compensation program currently consists, and is expected to continue to consist, of the following components:

- base salary;
- cash incentive compensation;
- equity-based incentives, principally in the form of stock options;
- benefits (on substantially similar terms as provided to the Company s other employees); and
- severance/termination protection in connection with certain change of control transactions.

The determination of our board of directors and compensation committee as to the appropriate use and weight of each component of executive compensation is subjective, based on their view of the relative importance of each component in meeting our overall objectives and factors relevant to the individual executive. Historically, our compensation structure for executives has consisted principally of a cash-based, short-term salary component and an equity component in the form of stock option grants providing long-term compensation based on company performance. Each of the elements of compensation was determined on an individual basis, and for the year ended December 31, 2009, an increase in one element did not affect decisions regarding the other elements.

Base Salary

The effective base salary for each of our named executive officers for 2007, 2008 and 2009 was and for 2010 will be as follows:

	Annual Base Salary(1)			
Executive Officer	**2007**	**2008**	**2009**	**2010(2)**
Kishore Seendripu, Ph.D.	$ 200,000	$ 250,000	$ 250,000	$ 350,000
Joe D. Campa(3)		$ 175,000	$ 175,000	$ 210,000
Kimihiko Imura	$ 170,000	$ 177,192	$ 170,000	$ 200,000
Madhukar Reddy, Ph.D.	$ 170,000	$ 177,192	$ 170,000	$ 210,000
Brendan Walsh	$ 170,000	$ 177,192	$ 170,000	$ 200,000

(1) Reflects the highest annualized base salary established for the named executive officer during each fiscal year. For Dr. Seendripu, the annual base salary of $200,000 was paid until December 14, 2007, at which time it was increased to $250,000.
(2) Increases in 2010 base salary over 2009 base salary became effective upon our recently completed initial public offering.
(3) Mr. Campa is our Vice President, Finance and Treasurer and serves as our principal financial officer. He also served as our Chief Financial Officer from March 17, 2008 until January 14, 2010.

Our board of directors was historically responsible for setting our executive base salaries. Because we did not recognize any material revenue until 2007, our base salaries reflected our status as a pre-revenue start-up company focused principally on technology and product development and, as a result, efficient use of limited cash resources. In that regard, our board of directors approved, and our management team accepted, base

salaries that were generally acknowledged to be below base salaries available at larger, public companies. All of the named executive officers were founders or early employees who recognized our cash constraints as we focused resources on the development of our business and who agreed to relatively lower base salaries in exchange for substantial initial equity incentive awards.

From the time of incorporation until 2008, we did not make substantial increases in our base salary structure for executive officers. Beginning in 2007, however, our revenue began to increase, and cash compensation became more affordable. Accordingly, for 2008, we increased Dr. Seendripu s base salary by 25% from $200,000 to $250,000. Other than the 2008 increase for Dr. Seendripu, we did not increase base salaries for any other named executive officers between 2007 and 2009. Our board of directors determined that an increase in Dr. Seendripu s base

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salary was appropriate in light of his additional responsibilities as we focused on increased customer and market penetration and revenue growth and as Dr. Seendripu became responsible for managing a larger organization. Our board of directors also determined that these additional responsibilities justified greater differentiation, relative to prior years, between Dr. Seendripu s base salary as Chairman, President and Chief Executive Officer and the base salaries of our other executive officers, who are responsible for specific functional areas. Our board of directors made its determinations of these executive officers base salaries based in part on its view of an appropriate salary level for similarly situated executive officers in their particular roles at a venture-backed company in the early revenue stages and in part to maintain the relative parity in base salaries that existed among our executive officers, other than Dr. Seendripu.

Compensia s October 2009 review of base salary data from our peer group confirmed our board of directors and management s historic views concerning our base salary levels. Relative to our peer group, 2009 base salaries for our named executive officers were uniformly below the 25th percentile for each position. Dr. Seendripu s 2009 base salary was 21.5% below the 25th percentile for chief executive officers at our peer companies, and Mr. Campa s base salary was 26% below the 25th percentile for chief financial officers.

Based on the Compensia data and the compensation committee s objective of gradually transitioning our base salaries to the peer group median, in October 2009, our compensation committee recommended, and our board of directors approved, increases in base salaries for all our executive officers, as indicated in the table above. Increases in base salaries became effective in March 2010 upon the consummation of our initial public offering. The principal objectives of the base salary increases for 2010 were for the named executive officers as a group to approximate the peer group 25th percentile of base salaries and, other than with respect to Dr. Seendripu, to retain the relative parity among our executive officers. We expect gradual increases in our base salaries over the next few years as we adjust salary compensation toward our peer group median, and we expect that base salaries among the various functional areas will become increasingly differentiated.

Cash Incentive Program

Consistent with our historic focus on cash preservation, we did not establish any formal cash incentive programs for our executive officers prior to 2009. From time to time, we paid modest, discretionary bonuses to executive officers. In October 2009, for example, we paid modest discretionary bonuses of $10,000 in recognition of strong performance to Mr. Campa and Dr. Reddy. Specifically, Mr. Campa was rewarded for leading a growing finance department and improving our financial reporting process in preparation for our initial public offering, and Dr. Reddy was rewarded for his increased focus on new product development. We did not pay any bonuses to Dr. Seendripu during 2008 or 2009.

In early 2009, our board of directors approved a bonus structure for 2009 that would result in the payment of bonuses if our 2009 revenue equaled or exceeded an established target, which was $48 million. The bonus threshold was structured to provide for modest award payments if we met a $40 million revenue threshold, gradually increasing as we approached our $48 million target. Our board of directors established the performance threshold in early 2009 based on the approved operating plan. Our board of directors set the revenue target at an amount substantially in excess of 2008 revenues and at a level that it believed to be aggressive in light of the business environment at the time the target was set. In particular, in early 2009, the global economic downturn appeared to be accelerating, equity markets continued to decline substantially and our revenue in the last two quarters of fiscal 2008 had reflected the adverse impact of substantial changes in the Japanese mobile television market as well as the recessionary environment.

In addition, our ability to increase revenue has and will continue to depend upon our ability to develop, market and sell products that address new markets. For example, particularly given growth trends in the Japanese mobile handset market, our board of directors determined that revenue growth for 2009 would be highly dependent on our solutions for the European set top box and Japanese automotive markets. To a lesser extent for 2008 and to an increasing extent in future periods, our revenue growth will depend on our ability to address markets for cable and Internet protocol

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television and personal computers, among others. Our 2009 revenue target was achieved, and, in January 2010, our compensation committee and our board of directors approved bonus awards to our executive officers equal to a percentage of their 2009 base salaries as indicated in the table below. We paid these bonuses during the first quarter of 2010. Our compensation committee and our board of directors maintained discretion to pay bonuses in excess of the targets indicated if we exceeded the established revenue targets and discretion to pay partial bonuses if our revenue was less than the established revenue target.

	Fiscal 2009 Bonus Potential		**Fiscal 2009 Bonus Award(1)**	
Executive Officer	**% Bonus Target**	**$ Bonus Target**	**% Bonus Award**	**$ Bonus Award**
Kishore Seendripu, Ph.D.	50%	$ 125,000	55%	$ 137,500
Joe D. Campa	20%	$ 35,000	13%	$ 22,750
Kimihiko Imura	20%	$ 34,000	15%	$ 25,500
Madhukar Reddy, Ph.D.	20%	$ 34,000	20%	$ 34,000
Brendan Walsh	20%	$ 34,000	17%	$ 28,900

(1) These bonus awards were earned in fiscal 2009 and were paid in early 2010.

With respect to Dr. Seendripu, our compensation committee and our board of directors exercised their discretion and increased Dr. Seendripu s bonus award to 55% of his 2009 base salary from the original bonus target of 50%. Our board of directors and our compensation committee based their determinations on the fact that we exceeded the revenue target by several million dollars and Dr. Seendripu s sole performance objective under the 2009 bonus program was revenue growth.

For our named executive officers other than Dr. Seendripu, payments under the 2009 bonus program were based on achievement of the corporate revenue growth target and individual objectives, with the revenue target receiving a 50% weighting and the individual objectives also receiving a 50% weighting. Specifically, Dr. Reddy s 2009 individual goal related to ensuring that our products for the European set top box market were ready to enter volume production within required time frames; Mr. Campa s individual goals were to ensure timely completion of our 2008 audited financial statements in anticipation of filing the registration statement related to our recently completed initial public offering, to develop our revenue forecasting models, and to expand the

technical expertise in our finance department and to complete our operations planning strategy. Mr. Imura s individual goals related to yield improvements and improving unit costs associated with lower silicon die and manufacturing expenses. Mr. Walsh s individual goals were to expand our business development function and investigate certain business development opportunities. Each of Dr. Reddy, Mr. Imura, Mr. Campa, and Mr. Walsh received full credit under the bonus program for achievement of the corporate revenue objective. Dr. Reddy received full credit for completion of all individual objectives, resulting in a bonus award equal to his full target. Mr. Campa, Mr. Imura, and Mr. Walsh received credit for partial completion of individual objectives, resulting in actual award percentages less than their 20% targets.

In October 2009, our compensation committee reviewed our philosophy and historical practices concerning incentive cash compensation. The committee determined, and our board of directors concurred, that in light of changes in our business, in particular the increased focus on revenue generation and achieving other financial performance metrics, implementation of a more structured performance-based cash incentive plan for executive officers was appropriate. In structuring our plan, the compensation committee reviewed peer group data on cash incentive programs, focusing specifically on how payments under the bonus plans related to total cash compensation targets. Our compensation committee believes that our corporate objectives of increasing market presence and revenue support a cash compensation program that is heavily weighted toward achieving financial objectives.

On November 1, 2009, our compensation committee and, on November 5, 2009, our board of directors approved our 2010 Executive Incentive Bonus Plan, which established target bonus percentages as a percent of base salary and target 2010 total cash compensation for each executive officer as set forth in the following table. As with our base salary levels, the 2010 cash incentive places our named executive officers as a group at approximately the 25th percentile of total cash compensation. Subject to the performance of our business, we expect total cash compensation to increase in future periods as we implement the compensation philosophies adopted as part of the 2010 competitive market review.

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	Bonus Targets		Total Target
Executive Officer	% of Salary	Cash Target	2010 Cash Compensation
Kishore Seendripu, Ph.D.	75%	$ 262,500	$ 612,500
Joe D. Campa	30%	$ 63,000	$ 273,000
Kimihiko Imura	30%	$ 60,000	$ 260,000
Madhukar Reddy, Ph.D.	30%	$ 63,000	$ 273,000
Brendan Walsh	30%	$ 60,000	$ 260,000

Under the 2010 Executive Incentive Bonus Plan, bonus awards will be based on achievement of corporate performance goals, which will carry a seventy percent (70%) weighting, and individual performance, which will carry a thirty percent (30%) weighting. The compensation committee established the categories of performance targets as relating to total revenue and operating income. With respect to the 70% weighting allocated to the corporate performance goals, these two financial targets will each receive a 50% weighting for purposes of determining any payouts under the plan. In making its determination whether financial targets have been achieved, the compensation committee will have authority to make appropriate adjustments to the target for the expected effects of any acquisitions or other approved business plan changes made during the applicable fiscal year. Revenue will also be adjusted by the compensation committee as it determines appropriate to exclude certain non-recurring items under generally accepted accounting principles such as gains or losses on sales of assets. Similarly, the operating income target will reflect our profit from operations excluding extraordinary items. The compensation committee will also adjust our reported operating income to exclude certain charges from our operating expenses, including stock compensation expense, accruals under the 2010 Executive Incentive Bonus Plan, any restructuring and impairment charges and any acquisition related charges. Our compensation committee set the 2010 financial targets at levels moderately in excess of the board-approved 2010 operating plan and at levels our compensation committee believes should be challenging but attainable for management. For purposes of determining the portion of awards payable based on individual performance, the standard will be subjective. For executive officers other than Dr. Seendripu, individual performance will be evaluated by our compensation committee based on Dr. Seendripu s input and recommendations. Our compensation committee will evaluate Dr. Seendripu s performance.

Our board of directors and compensation committee maintain discretion to provide for cash incentive awards under our 2010 Executive Incentive Bonus Plan in excess of the target base salary percentages if it determines appropriate. Awards may be reduced if we do not achieve the targets under the plans. Our compensation committee or our board of directors may also approve payments of bonuses outside these plans, regardless of whether performance targets have been achieved. Our compensation committee may, if permitted by law, make retroactive adjustments to, or seek recovery of, cash bonuses whose payment was predicated on achievement of specified financial results that are subsequently restated. In the case of such a restatement, our Executive Incentive Bonus Plan includes a provision requiring recipients of awards under the plan to repay to us an amount of previously paid bonuses determined appropriate by the administrator of the plan, generally our compensation committee, if the administrator determines that the recipient engaged in an act of embezzlement, fraud, or breach of fiduciary duty during the course of his or her employment that contributed to our obligation to restate our financial statements.

Equity-Based Incentives

We grant equity-based incentives to employees, including our executive officers, in order to create a corporate culture that aligns employee interests with stockholder interests. We have not adopted specific stock ownership guidelines, and other than the issuance of shares to our founders when we were established, our equity incentive plans have provided the principal method for our executive officers to acquire an equity position in our company, whether in the form of shares or options. We have not granted, nor do we intend to grant, equity compensation awards in anticipation of the release of material, nonpublic information that is likely to result in changes to the price of our Class A common stock, such as a significant positive or negative earnings announcement. Similarly, we have not timed, nor do we intend to time, the release of material, nonpublic information based on equity award grant dates.

Prior to our recently completed initial public offering, we granted options and other equity incentives to our officers under the 2004 Stock Plan. In connection with our recently completed initial public offering, our board of directors has adopted

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the 2010 Equity Incentive Plan, which became effective in March 2010 upon the completion of our initial public offering. The 2010 Equity Incentive Plan permits the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, performance units, performance shares and other stock-based awards. Historically, our equity incentive plans were administered by our board of directors. Going forward, all equity incentive plans and awards will be administered by our compensation committee under the delegated authority established in the compensation committee charter.

To date, our equity incentives have been granted principally with time-based vesting. Most new hire option grants, including those for our executive officers, vest over a four-year period with 25% vesting at the end of the first year of employment and the remainder vesting in equal monthly installments over the subsequent three years. Although our practice in recent years has been to provide equity incentives principally in the form of stock option grants that vest over time, our compensation committee may consider alternative forms of equity in the future, such as performance shares, restricted stock units or restricted stock awards with alternative vesting strategies based on the achievement of performance milestones or financial metrics.

	2008 2009 Option Grants					
	March 31, 2008		July 28, 2009		October 27, 2009	
	Shares	Exercise Price	Shares	Exercise Price	Shares	Exercise Price
Kishore Seendripu, Ph.D(1)			86,110	$ 4.69	226,039	$ 8.19
Joe D. Campa	193,748	$ 1.16	43,055	$ 4.26		
Kimihiko Imura					48,437	$ 7.45
Madhukar Reddy, Ph.D.			21,527	$ 4.26	80,728	$ 7.45
Brendan Walsh					48,437	$ 7.45

(1) Under the terms of our 2004 Stock Plan, options granted to any service provider that, at the time of the grant of such option, owns stock representing more than ten percent of the voting power of all classes of our stock, are required to have an exercise price no less than one hundred and ten percent of the of the fair market value on the date of grant. As of the date of the grants to Dr. Seendripu, Dr. Seendripu held stock representing more than ten percent of the voting power of all classes of our stock.

As part of the fiscal 2010 competitive compensation review conducted by the compensation committee, Compensia evaluated the current equity incentive award positions of each of our executive officers, including total potential ownership, vested as compared to unvested positions and the current economic value of outstanding awards. Their analysis compared outstanding equity positions for each executive officer s respective positions with applicable ranges within our peer group. Their analysis indicated that while we were highly competitive overall from an equity incentive perspective, with the current economic value associated with equity incentives held by the named executive officers being substantial, the retentive impact of many outstanding awards was limited because they were substantially vested. Drs. Reddy and Seendripu and Messrs. Imura and Walsh for example, received their initial equity incentives at the time that we were founded or shortly thereafter, and these shares are now fully vested. As of December 31, 2009, Dr. Seendripu was fully vested in 93.25% of the aggregate shares he held or had the right to acquire, including shares subject to options; Dr. Reddy was fully vested in 59.31%.; Mr. Imura was fully vested in 86.54% of the aggregate shares he held or had the right to acquire, including shares subject to options; and Mr. Walsh was fully vested in 83.10% of the aggregate shares he held or had the right to acquire, including shares subject to options. In contrast, Mr. Campa was fully vested in only 38.05% of his shares because he joined us in March of 2008.

As a result of the substantial vested equity position of several of our named executive officers in July 2009 and in October 2009, our compensation committee recommended, and our board of directors approved, new option grants as indicated in the table above for Mr. Campa, Mr. Imura, Mr. Walsh and Drs. Reddy and Seendripu. The relative sizes of these option grants were based on other factors in addition to the individual s vested option position. In particular, the compensation committee and our board of directors considered the equity incentive that would be required to hire and retain an executive officer performing the same responsibilities. The compensation committee and our board of directors also considered the relative competitiveness of the market for each position and the Company s relative performance and contribution requirements from each individual with respect to achieving our short-

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and long-term objectives. Based on that analysis, the compensation committee determined that a relatively larger option grant was appropriate for Dr. Reddy based on the particular importance of maintaining the competitiveness of our engineering and product development efforts. To maximize the retention impact of these option grants, the October 2009 options will vest and become exercisable, assuming continued service with us, on a back-end loaded basis, with 10% of the shares vesting on the one-year anniversary of the date of grant, 20% of the shares vesting on the two-year anniversary of the date of grant, 30% of the shares vesting on the three-year anniversary of the date of grant, and 40% of the shares vesting on the four- year anniversary of the date of grant. Our board of directors had previously approved an option grant for Dr. Seendripu in July 2009 that vests over four years, with 25% vesting on the first anniversary of the date of grant and the balance vesting monthly over the remaining three years.

In determining the size of Dr. Seendripu s October 2009 grant, our compensation committee considered the prior July 2009 grant, which was still unvested. The grant to Dr. Seendripu was based upon his increasing responsibilities as we focus on increasing our customer and market penetration and in ensuring the competitive position of our products and increasing our revenues. In addition, the compensation committee and our board of directors noted Dr. Seendripu s increased leadership responsibility as we become a public company.

In determining the size of Mr. Campa s July 2009 grant, our board of directors considered the prior March 2008 grant, which was largely unvested. The grant to Mr. Campa was based on his increasing responsibilities as we focused on building a larger internal finance team and in ensuring the management of our expenses to enable us to meet our corporate cash objectives.

In approving grants to Mr. Imura and Mr. Walsh in October 2009, our compensation committee considered that neither had received any grants since August 2007 and that these grants were over 50% vested as of October 2009. The committee also considered their relative importance to our ability to achieve our short and long term objectives and the importance of retaining and incentivizing talent in such key functional areas as operations and business development.

Benefits

We provide the following benefits to our executive officers, generally on the same basis provided to all of our employees:

- health, dental and vision insurance;
- life insurance;
- employee stock purchase plan;
- employee assistance plan;
- medical and dependant care flexible spending account;
- short- and long-term disability, accidental death and dismemberment; and
- a 401(k) plan.

We believe that these benefits are consistent with those of companies with which we compete for employees.

Severance and Termination Benefits Upon a Change of Control

In connection with certain terminations of employment upon or following a change of control, our executive officers will be entitled to receive severance payments and benefits pursuant to severance and change in control agreements approved by our compensation committee in November 2009. As part of its compensation review, our compensation committee reviewed competitive data concerning these benefits and made recommendations to our board of directors. In setting the terms of, and determining whether to approve these agreements, our compensation committee or board of directors, as applicable, recognized that executives often face challenges securing new employment following termination, in particular following a change of control, and that distractions created by uncertain job security surrounding potentially beneficial transactions to us and our stockholders may have a detrimental impact on their performance. As a result, the severance benefits identified below are primarily intended to provide these executive officers with post-change of control termination protection of salary and benefits while they seek new employment. We also have agreed to accelerate vesting of certain equity incentives in connection with certain terminations following a change of control, based on our view that these

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executive officers are not likely to be retained in comparable positions by a large acquiror, and the benefit of these equity incentives would otherwise be forfeited upon a termination of employment, including an involuntary termination by an acquiring company.

Chief Executive Officer and Chief Financial Officer

Under the terms of change in control agreements that we entered into with Dr. Seendripu and Mr. Campa, if the executive is a Section 16 officer immediately prior to a change in control (as such terms are defined in the change in control agreement) and upon or within 12 months following a change of control, the executive is involuntarily terminated by us or our successor without cause or he terminates voluntarily for good reason (as such terms are defined in the change in control agreement), we have agreed that the executive will be entitled to receive the following benefits:

- a lump sum cash payment equal to 12 months of his base salary, determined at a rate equal to the greater of (A) his annual salary as in effect immediately prior to the change in control, or (B) his then current annual salary as of the date of such termination;

- a lump sum cash payment equal to a pro-rated amount of his target annual bonus for the year immediately preceding the year of the change in control;

- payment of premiums for continued health benefits under the Company s health plans for 12 months following the executive s termination provided that the executive constitutes a qualified beneficiary under applicable law and timely elects to continue coverage under applicable law; and

- immediate vesting of 100% of the then-unvested portion of any outstanding equity awards held by the executive.

In addition, the change of control agreements with Dr. Seendripu and Mr. Campa provide that in the event that the severance payments and other benefits payable to such executives constitute parachute payments under Section 280G of the Internal Revenue Code of 1986, as amended, and would be subject to the applicable excise tax, then

such executive s severance and other benefits will be either (i) delivered in full or (ii) delivered to such lesser extent which would result in no portion of such benefits being subject to the excise tax, whichever results in the receipt by such executive on an after-tax basis of the greatest amount of benefits.

Payment of the benefits described above is also subject to the executive s timely executing and not revoking a release of claims with us.

Our compensation committee and board of directors approved change in control severance benefits for Dr. Seendripu and Mr. Campa that are greater than the benefits provided to our other executives with respect to vesting acceleration of equity awards after considering factors such as the higher likelihood that a chief executive officer or chief financial officer will be terminated in connection with a change of control transaction as compared to the other executive officers.

Other Executive Officers

In connection with our recently completed initial public offering, we also have entered into change in control agreements with our other executive officers. Under the terms of these agreements, if the executive is a Section 16 officer of us or our successor immediately prior to a change in control (as such terms are defined in the change in control agreement) and upon or within 12 months following a change in control, the executive is involuntarily terminated by us or our successor without cause or the executive voluntarily terminates for good reason (as such terms are defined in the change in control agreement), the executive will be entitled to receive the following benefits:

- a lump sum cash payment equal to 12 months of the executive s base salary, determined at a rate equal to the greater of (A) his annual salary as in effect immediately prior to the change in control, or (B) his then current annual salary as of the date of such

termination;

a lump sum cash payment equal to a pro-rated amount of his target annual bonus for the year immediately preceding the year of the change in control;

payment of premiums for continued health benefits under the Company s health plans

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for 12 months following the executive s termination provided that the executive constitutes a qualified beneficiary under applicable law and timely elects to continue coverage under applicable law; and

immediate vesting of 50% of the then-unvested portion of any outstanding equity awards held by the executive.

In addition, the change of control agreements with each of the executives provide that in the event that the severance payments and other benefits payable to such executives constitute parachute payments under Section 280G of the Internal Revenue Code of 1986, as amended, and would be subject to the applicable excise tax, then such executive s severance and other benefits will be either (i) delivered in full or (ii) delivered to such lesser extent which would result in no portion of such benefits being subject to the excise tax, whichever results in the receipt by such executive on an after-tax basis of the greatest amount of benefits.

Payment of the benefits described above under these change in control agreements is also subject to the executive s executing and not revoking a release of claims with us.

Accounting and Tax Considerations

Internal Revenue Code Section 162(m) limits the amount that we may deduct for compensation paid to our Chief Executive Officer and to each of our four most highly compensated officers to $1,000,000 per person, unless certain exemption requirements are met. Exemptions to this deductibility limit may be made for various forms of performance-based compensation. In addition to salary and bonus compensation, upon the exercise of stock options that are not treated as incentive stock options, the excess of the current market price over the option price, or option spread, is treated as compensation and accordingly, in any year, such exercise may cause an officer s total compensation to exceed $1,000,000. Under certain regulations, option spread compensation from options that meet certain requirements will not be subject to the $1,000,000 cap on deductibility, and in the past, we have granted options that we believe met those requirements. While the compensation committee cannot predict how the deductibility limit may impact our compensation program in future years, the

compensation committee intends to maintain an approach to executive compensation that strongly links pay to performance. While the compensation committee has not adopted a formal policy regarding tax deductibility of compensation paid to our Chief Executive Officer and our four most highly compensated officers, the compensation committee intends to consider tax deductibility under Section 162(m) as a factor in compensation decisions.

Section 409A of the Code imposes additional significant taxes in the event that an executive officer, director, or other service provider receives deferred compensation that does not satisfy the requirements of Section 409A. Although we do not maintain traditional nonqualified deferred compensation plans, Section 409A does apply to certain change of control severance arrangements. Consequently, to assist in avoiding additional tax under Section 409A, we have designed the change of control severance arrangements described above in a manner to avoid the application of Section 409A.

Report of the Compensation Committee

The Compensation Committee oversees MaxLinear s compensation policies, plans, and benefit programs. The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis required by Item 402(b) of Regulation S-K with management. Based on such review and discussions, the Compensation Committee has recommended to the board of directors that the Compensation Discussion and Analysis be included in this proxy statement.

The Compensation Committee

Thomas E. Pardun (Chair)

Donald E. Schrock

David Liddle, Ph.D.

The Report of the Compensation Committee does not constitute soliciting material, and shall not be deemed to be filed or incorporated by reference into any other filing by MaxLinear under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent MaxLinear specifically incorporates the Report of the Compensation Committee by reference therein.

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Summary Compensation Table

The following table provides information regarding the compensation of our principal executive officer, principal financial officer and each of the next three most highly compensated executive officers during our fiscal year ended December 31, 2009, together referred to as our named executive officers for the fiscal years ended December 31, 2009 and December 31, 2008.

Name and Principal Position	Year	Salary ($)	Bonus ($)	Option Awards ($)(1)	Non-Equity Incentive Plan Compensation ($)(2)	All Other Compensation ($)	Total ($)
Kishore Seendripu, Ph.D.	2009	250,000		1,104,518	137,500	23,681(3)	1,515,699
Chairman, President and	2008	260,577					260,577
Chief Executive Officer							
(Principal Executive Officer							
Joe D. Campa(4)	2009	175,000	10,000(5)	99,941	22,750		307,691
Vice President, Finance and	2008	138,542		111,840		42,500(6)	292,882
Treasurer (Principal							
Financial Officer							
Kimihiko Imura	2009	170,000	10,000(5)	203,725	25,500		409,225
Vice President,	2008	177,192					177,192
Semiconductor Technology							
and Operations							
Madhukar Reddy, Ph.D.	2009	170,000	10,000(5)	389,508	34,000	5,794(3)	609,302
Vice President, IC and RF	2008	177,192					177,192
Systems Engineering							
Brendan Walsh	2009	170,000	20,000(5)	203,725	28,900		422,625
Vice President, Business	2008	177,192					177,192
Development							

(1) Amounts shown do not reflect compensation actually received by the named executive officer. Instead, the amounts represent the aggregate grant date fair value related to option awards and performance option awards, and the aggregate grant fair market value related to stock awards, granted in the year indicated, pursuant to Accounting Standards Codification Topic 718. The amounts for stock options and stock awards from prior years were restated to reflect aggregate grant date fair value. For a discussion of the valuation assumptions, see Note 2 to our consolidated financial statements included in our audited financial statements included with the Annual Report. The actual value that may be realized from an award is contingent upon the satisfaction of the conditions to vesting in that award on the date the award is vested. Thus, there is no assurance that the value, if any, eventually realized will correspond to the amount shown.

(2) See Grants of Plan-Based Awards in Fiscal Year 2009 under the column Estimated Future Payouts Under Non-Equity Incentive Plan Awards for the amounts named executive officers were eligible to earn at target in fiscal 2009. Our board of directors retained discretion to approve payments in excess of the target amounts. See also Compensation Discussion and Analysis Cash Incentive Compensation for a discussion of how the bonus program worked in operation.

(3) Includes $23,681 and $5,794, respectively, paid to Drs. Seendripu and Reddy in 2009 for accrued vacation buy-outs.

(4) Mr. Campa became our Vice President, Finance and Treasurer in January 2010. Previously, he served as our Chief Financial Officer.

(5)

Represents payments of $10,000 to each of Mr. Campa, Mr. Imura and Dr. Reddy and $20,000 to Mr. Walsh on October 15, 2009 as discretionary bonuses.

(6) Represents consulting fees paid to Mr. Campa prior to his becoming an employee.

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Grants of Plan-Based Awards

The following table presents information concerning each grant of an award made to a named executive officer in fiscal 2009 under any plan.

Name	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards(1) Threshold ($)	Target ($)	Maximum ($)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards ($/Sh)	Grant Date Fair Value of Stock and Option Awards ($)(2)
Kishore Seendripu, Ph.D.							
Option Award	7/28/09				86,110	4.69	191,333
Option Award	10/27/09				226,039	8.19	913,185
Non-Equity Incentive Cash Payment	5/8/2009	5,000	125,000				
Joe D. Campa							
Option Award	7/28/09				43,055	4.26	99,941
Non-Equity Incentive Cash Payment	5/8/2009	3,500	35,000				
Kimihiko Imura							
Option Award	10/27/09				48,437	7.45	203,725
Non-Equity Incentive Cash Payment	5/8/2009	3,400	34,000				
Madhukar Reddy, Ph.D.							
Option Award	7/28/09				21,527	4.26	49,970
Option Award	10/27/09				80,728	7.45	339,538
Non-Equity Incentive Cash Payment	5/8/2009	3,400	34,000				
Brendan Walsh							
Option Award	10/27/09				48,437	7.45	203,725
Non-Equity Incentive Cash Payment	5/8/2009	3,400	34,000				

(1) Represents awards granted under our 2009 cash incentive bonus program, which were based on achievement of certain levels of performance in fiscal year 2009. These columns show the awards that were possible at the threshold, target and maximum levels of performance. The column titled Non-Equity Incentive Plan Compensation in the Summary Compensation Table shows the actual awards earned in fiscal year 2009 by our named executive officers under the 2009 cash incentive bonus program for 2009. These amounts were paid in early 2010.

(2) Fair values of the option awards on the respective grant dates are computed in accordance with ASC 718. Our assumptions with respect to the calculation of stock-based compensation expense are set forth above in the notes to our consolidated financial statements for the year ended December 31, 2009, included in our Annual Report.

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Outstanding Equity Awards at Fiscal Year-End

The following table presents information concerning unexercised options for each named executive officer outstanding as of the end of fiscal 2009.

	Option Awards			
Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price ($)	Option Expiration Date
Kishore Seendripu, Ph.D.		86,110(1)	4.69	7/28/2019
		226,039(2)	8.19	10/27/2019
Joe D. Campa	84,764(3)	108,984	1.16	3/31/2018
		43,055(1)	4.26	7/28/2019
Kimihiko Imura	449(4)		0.23	10/28/2015
	449(4)		0.23	10/28/2015
	45,208(8)	32,291	1.16	8/7/2017
		48,437(2)	7.45	10/27/2019
Madhukar Reddy, Ph.D.	39,826(5)		0.23	10/28/2015
	36,775(7)	6,279	0.35	7/6/2016
	90,416(8)	64,582	1.16	8/7/2017
		21,527(1)	4.26	7/28/2019
		80,728(2)	7.45	10/27/2019
Brendan Walsh	21,527(6)		0.23	10/28/2015
	21,527(6)		0.23	10/28/2015
	45,208(8)	32,291	1.16	8/7/2017
		48,437(2)	7.45	10/27/2019

(1) This stock option was granted on July 28, 2009 and vests over four years. Subject to the optionee s continuing to provide services, 25% of the shares subject to the stock option vest one year after grant, and 2.08% of the shares vest at the end of each monthly period thereafter.

(2) This stock option was granted on October 27, 2009 and vests over four years. Subject to the optionee s continuing to provide services, 10% of the shares subject to the stock option vest one year after grant, 20% of the shares subject to the stock option vest on the second anniversary of grant date, 30% of the shares subject to the stock option vest on the third anniversary of grant date, and 40% of the shares subject to the stock option vest on the fourth anniversary of grant date.

(3) This stock option was granted on March 31, 2008 and vests over four years. Subject to the optionee s continuing to provide services, 25% of the shares subject to the stock option vest one year after grant, and 2.08% of the shares vest at the end of each monthly period thereafter.

(4) These stock options were granted on October 28, 2005 and fully vested over four years. Mr. Imura previously exercised 42,156 shares subject to the stock options.
(5) This stock option was granted on October 28, 2005 and fully vested over four years. Dr. Reddy previously exercised 16,145 shares subject to the stock options.
(6) This stock option was granted on October 28, 2005 and fully vested over four years.
(7) This stock option was granted on July 6, 2006 and vests over four years. Subject to the optionee s continuing to provide services, 25% of the shares subject to the stock option vest one year after grant, and 2.08% of the shares vest at the end of each monthly period thereafter.
(8) This stock option was granted on August 7, 2007 and vests over four years. Subject to the optionee s continuing to provide services, 25% of the shares subject to the stock option vest one year after grant, and 2.08% of the shares vest at the end of each monthly period thereafter.

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Option Exercises and Stock Vested at Fiscal Year-End 2009

The following table presents information concerning each exercise of stock options during fiscal 2009 for each of the named executive officers.

	Option Awards	
Name	Number of Shares Acquired Underlying on Exercise (#)	Value Realized on Exercise ($)
Kishore Seendripu, Ph.D.		
Joe D. Campa	8,610	45,199
Kimihiko Imura	42,156	221,277
Madhukar Reddy, Ph.D.	16,145	102,000
Brendan Walsh		

Pension Benefits & Nonqualified Deferred Compensation

The Company does not provide a pension plan for its employees and no named executive officers participated in a nonqualified deferred compensation plan during the fiscal year ended December 31, 2009.

Potential Payments Upon Termination or Change of Control

Change in Control Agreements

Chief Executive Officer and Chief Financial Officer

Under the terms of change in control agreements that we have entered into with Dr. Seendripu and Mr. Campa, if the executive is a Section 16 officer immediately prior to a change in control (as such terms are defined in the change in control agreement) and upon or within 12 months following a change of control, the executive is involuntarily terminated by us or our successor without cause or he terminates voluntarily for good reason (as such terms are defined in the change in control agreement), we have agreed that the executive will be entitled to receive the following benefits:

- a lump sum cash payment equal to 12 months of his base salary, determined at a rate equal to the greater of (A) his annual salary as in effect immediately prior to the change in control, or (B) his then current annual salary as of the date of such termination;

- a lump sum cash payment equal to a prorated amount of his target annual bonus for the year immediately preceding the year of the change in control;

- payment of premiums for continued health benefits under the Company s health plans for 12 months following the executive s termination provided that the executive constitutes a qualified beneficiary under applicable law and timely elects to continue coverage under applicable law; and

- immediate vesting of 100% of the then-unvested portion of any outstanding equity awards held by the executive.

In addition, the change of control agreements with Dr. Seendripu and Mr. Campa provide that in the event that the severance payments and other benefits payable to such executives constitute parachute payments under Section 280G of the Internal Revenue Code of 1986, as amended, and

would be subject to the applicable excise tax, then such executive s severance and other benefits will be either (i) delivered in full or (ii) delivered to such lesser extent which would result in no portion of such benefits being subject to the excise tax, whichever results in the receipt by such executive on an after-tax basis of the greatest amount of benefits.

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Other Executive Officers

We have also entered into change in control agreements with Messrs. Imura, Walsh and Dr. Reddy. Under the terms of these agreements, if the executive is a Section 16 officer of us or our successor immediately prior to a change in control (as such terms are defined in the change in control agreement) and upon or within 12 months following a change in control, the executive is involuntarily terminated by us or our successor without cause or the executive voluntarily terminates for good reason (as such terms are defined in the change in control agreement), the executive will be entitled to receive the following benefits:

- a lump sum cash payment equal to 12 months of the executive s base salary, determined at a rate equal to the greater of (A) his annual salary as in effect immediately prior to the change in control, or (B) his then current annual salary as of the date of such termination;

- a lump sum cash payment equal to a prorated amount of his target annual bonus for the year immediately preceding the year of the change in control;

- payment of premiums for continued health benefits under the Company s health plans for 12 months following the executive s termination provided that the executive constitutes a qualified beneficiary under applicable law and timely elects to continue coverage under applicable law; and

- immediate vesting of 50% of the then-unvested portion of any outstanding equity awards held by the executive.

In addition, the change of control agreements with each of the executives provide that in the event that the severance payments and other benefits payable to such executives constitute parachute payments under Section 280G of the Internal Revenue Code of 1986, as amended, and would be subject to the applicable excise tax, then such executive s severance and other benefits will be either (i) delivered in full or (ii) delivered to such lesser extent which would result in no portion of such benefits being subject to the excise tax, whichever results in the receipt by such executive on an after-tax basis of the greatest amount of benefits.

For the purposes of these agreements, change in control is generally defined as: (i) a change in the ownership of the Company (i.e., the date any one person, or more than one person acting as a group, acquires ownership of the stock of the Company that, together with the stock held by such person, constitutes more than 50% of the total voting power of the stock of the Company); (ii) a change in the effective control of the Company which occurs on the date that a majority of members of the board is replaced during any twelve (12) month period by directors whose appointment or election is not endorsed by a majority of the members of the board prior to the date of the appointment or election; and (iii) a change in the ownership of a substantial portion of the Company s assets which occurs on the date that any person acquires (or has acquired during the twelve (12) month period ending on the date of the most recent acquisition by such person or persons) assets from the Company that have a total gross fair market value equal to or more than 50% of the total gross fair market value of all of the assets of the Company immediately prior to such acquisition or acquisitions.

For the purposes of these agreements, good reason is generally defined as: (i) a material reduction of executive s authority, duties or responsibilities; (ii) a material reduction in executive s base compensation; (iii) the relocation of executive to a facility or location more than 50 miles from his or her primary place of employment; (iv) the failure of the Company to obtain the assumption of the agreement by a successor and/or acquirer; or (v) any material breach or material violation of a material provision of the change in control agreement by the Company (or any successor).

For the purposes of these agreements, cause is generally defined as: (i) an executive s willful and continued failure to perform the duties and responsibilities of his or her position; (ii) any material act of personal dishonesty taken by executive; (iii) an executive s conviction of or plea of nolo contendere to a felony; (iv) an executive s willful breach of any fiduciary duty owed to the Company; (v) an executive being found liable in any SEC or other civil or criminal securities law action; (vi) an executive entering any cease and desist order; (vii) an executive obstructing or impeding or endeavoring to obstruct or impede or failing to

materially cooperate with any investigation authorized by the board of directors or any governmental or self-regulatory entity; or (viii) an executive s disqualifications or bars by any governmental or self-regulatory authority from serving in the capacity contemplated by the change in control agreement.

Estimated Termination Payments

The following table provides information concerning the estimated payments and benefits that would be provided in the circumstances described above for each of the named executive officers. Except where otherwise noted, payments and benefits are estimated assuming that the triggering event took place on the last business day of fiscal 2009 (December 31, 2009), and the price per share of MaxLinear s common stock is the initial public offering price of $14.00 per share. MaxLinear completed its initial public offering in March 2010 and its securities were not publicly traded on December 31, 2009. There can be no assurance that a triggering event would produce the same or similar results as those estimated below if such event occurs on any other date or at any other price, of if any other assumption used to estimate potential payments and benefits is not correct. Due to the number of factors that affect the nature and amount of any potential payments or benefits, any actual payments and benefits may be different.

	Change of Control and Involuntary Termination			
Name	**Severance Payments Attributable to Salary ($)(1)**	**Severance Payments Attributable to Bonus ($)(2)**	**Acceleration of Equity Vesting ($)(3)**	**Health Care Benefits ($)(4)**
Kishore Seendripu, Ph.D.	250,000	125,000	2,114,971	14,928
Joe D. Campa	175,000	35,000	1,818,710	5,134
Kimihiko Imura	170,000	34,000	365,972	15,459
Madhukar Reddy, Ph.D.	170,000	34,000	826,691	15,459
Brendan Walsh	170,000	34,000	365,972	15,172

(1) The amounts shown in this column are equal to 12 months of the named executive officer s base salary as of December 31, 2009.

(2) As none of the named executive officers had a target annual bonus amount for 2008 (the year immediately preceding the year of the assumed change of control), the amounts shown in this column for the named executive officers represent a prorated amount of the executive s target annual bonus for 2009 to more accurately reflect the severance payments attributable to their bonus that the named executive officers would be entitled to receive upon such assumed termination of employment.

(3) For Dr. Seendripu and Mr. Campa, the amounts shown in this column are equal to the spread value between (i) the unvested portion of all outstanding stock options held by the named executive officer on December 31, 2009 and (ii) the difference between the initial public offering price of our common stock of $14.00 per share and the exercise price. For all other executives, the amounts shown in this column are equal to the spread value between (i) 50% of the unvested portion of all outstanding stock options held by the named executive officer on December 31, 2009 and (ii) the difference between the initial public offering price of our common stock of $14.00 per share and the exercise price.

(4) The amounts shown in this column are equal to the cost of covering the named executive officer and his or her eligible dependents coverage under our benefit plans for a period of 12 months, assuming that such coverage is timely elected under COBRA.

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Equity Compensation Plan Information

The following table summarizes the number of outstanding options, warrants and rights granted to our employees, consultants, and directors, as well as the number of shares of Class A common stock and Class B common stock remaining available for future issuance, under our equity compensation plans as of September 15, 2010:

Plan category	Class of Common Stock	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted-average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders(1)(2)	Class A	544,323	$ 14.4535	8,918,740
	Class B	4,723,945	3.5170	
Equity compensation plans not approved by security holders	Class A			
	Class B			
Total		5,268,268	$ 4.6470	8,918,740

(1) Consists of 2004 Stock Plan, 2010 Equity Incentive Plan, and 2010 Employee Stock Purchase Plan.

(2) Our 2010 Equity Incentive Plan provides for annual increases in the number of shares available for issuance thereunder on the first day of each fiscal year, beginning with the 2011 fiscal year, equal to the least of (A) 2,583,311 shares of our Class A common stock, (B) four percent (4%) of the outstanding shares of our Class A common stock and Class B common stock on the last day of the immediately preceding fiscal year, or (C) such lesser amount as our board of directors or a designated committee acting as plan administrator may determine. Our 2010 Employee Stock Purchase Plan provides for annual increases in the number of shares available for issuance thereunder on the first day of each fiscal year, beginning with the 2011 fiscal year, equal to the least of (A) 968,741 shares of our Class A common stock, (B) one and a quarter percent (1.25%) of the outstanding shares of our Class A common stock and Class B common stock on the first day of the fiscal year, or (C) such lesser amount as our board of directors or a designated committee acting as administrator of the plan may determine.

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RELATED PERSON TRANSACTIONS AND SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Related Person Transactions

Investor Rights Agreement

We have entered into an investors rights agreement with certain holders of our Class A and/or Class B common stock that provides for certain rights relating to the registration of their shares of Class A and/or Class B common stock, including those issued upon conversion of their previously-held preferred stock.

Customer Relationship with UMC

We purchase processed wafers and pay non-recurring engineering expenses for masks, prototype expenses and expenses for wafer probe to determine good die from United Microelectronics Corporation, or UMC, one of our fabrication suppliers and an affiliate of UMC Capital Corporation, which holds greater than 5% of our outstanding Class B common stock. Our total purchases from UMC were approximately $10.5 million in 2009.

Change in Control Agreements

We have entered into agreements providing termination and change of control benefits to certain of our executive officers as described under the caption Executive Compensation, Potential Payments Upon Termination or Change of Control above.

Indemnification of Officers and Directors

We have entered into indemnification agreements with each of our directors, executive officers, and certain controlling persons. The indemnification agreements and our certificate of incorporation and bylaws require us to indemnify our directors, executive officers and certain controlling persons to the fullest extent permitted by Delaware law.

Policy Concerning Audit Committee Approval of Related Person Transactions

Our board of directors and audit committee has adopted a formal policy that our executive officers, directors, holders of more than 5% of any class of our voting securities, and any member of the immediate family of and any entity affiliated with any of the foregoing persons, are not permitted to enter into a related party transaction with us without the prior consent of our audit committee, or other independent members of our board of directors if it is inappropriate for our audit committee to review such transaction due to a conflict of interest. Any request for us to enter into a transaction with an executive officer, director, principal stockholder, or any of their immediate family members or affiliates, in which the amount involved exceeds $120,000 must first be presented to our audit committee for review, consideration and approval. In approving or rejecting any such proposal, our audit committee is to consider the relevant facts and circumstances available and deemed relevant to the audit committee, including, but not limited to, whether the transaction is on terms no less favorable than terms generally available to an unaffiliated third party under the same or similar circumstances and the extent of the related party s interest in the transaction.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, requires MaxLinear s directors, executive officers, and holders of more than 10% of its Class A and Class B common stock to file with the SEC reports regarding their ownership and changes in

ownership of MaxLinear s securities. MaxLinear believes that, to date during 2010, its directors, executive officers, and 10% stockholders complied with all Section 16(a) filing requirements. MaxLinear was not subject to Exchange Act reporting obligations during 2009.

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SECURITY OWNERSHIP

The following table sets forth information, as of September 1, 2010, concerning, except as indicated by the footnotes below:

- Each person whom we know beneficially owns more than five percent of our Class A common stock or Class B common stock;
- Each of our directors and nominees for the board of directors;
- Each of our named executive officers; and
- All of our directors and executive officers as a group.

Unless otherwise noted below, the address of each person listed on the table is c/o MaxLinear, Inc., 2051 Palomar Airport Road, Suite 100, Carlsbad, California 92011.

We have determined beneficial ownership in accordance with the rules of the SEC. Except as indicated by the footnotes below, we believe, based on the information furnished to us, that the persons and entities named in the table below have sole voting and investment power with respect to all shares of common stock that they beneficially own, subject to applicable community property laws.

Applicable percentage ownership is based on 7,410,714 shares of Class A common stock and 23,855,523 shares of Class B common stock outstanding at September 1, 2010. In computing the number of shares of common stock beneficially owned by a person and the percentage ownership of that person, we deemed outstanding shares of common stock subject to options held by that person that are currently exercisable or exercisable within 60 days of September 1, 2010. We did not deem these shares outstanding, however, for the purpose of computing the percentage ownership of any other person. Beneficial ownership representing less than one percent is denoted with an asterisk (*).

The information provided in the table is based on our records, information filed with the SEC, and information provided to MaxLinear, except where otherwise noted.

	Shares Beneficially Owned				% Total Voting Power	% Total Voting Power
	Class A Common Stock		Class B Common Stock			
Name and Address of Beneficial Owner	**Shares**	**Percentage (%)**	**Shares**	**Percentage (%)**	**M&A and Incentive Plans(1)**	**All Other Matters(2)**
Executive Officers and Directors:						
Kishore Seendripu, Ph.D.(3)			4,366,370	18.26	17.71	13.94
Curtis Ling, Ph.D.(4)			734,841	3.08	2.98	2.35
Joe D. Campa(5)			148,987	*	**	**
Brendan Walsh(6)			419,955	1.75	1.70	1.34
John Graham(7)			108,331	*	**	**
Michael Kastner(8)			121,876	*	**	**

Madhukar Reddy, Ph.D.(9)		306,449	1.27	1.23	1,082,040	5,5[illegible]87,634
Corporate debt, multiple observable inputs	—	1,459,550	—	1,459,550		
Corporate debt, limited observable inputs:						
Other corporate debt, NRSRO ratings available	—	—	10,793	10,793		
Other corporate debt, NRSRO ratings not available	—	—	2,642	2,642		
Residential mortgage-backed securities	—	290,314	—	290,314		
Agency commercial mortgage-backed securities	—	16,893	—	16,893		
Other commercial mortgage-backed securities	—	57,323	—	57,323		
Other asset-backed securities	—	96,119	4,773	100,892		
Equity securities						
Financial	75,141	—	—	75,141		
Utilities/Energy	26,551	—	—	26,551		
Consumer oriented	64,912	—	—	64,912		
Industrial	54,912	—	—	54,912		
Bond funds	53,178	—	—	53,178		
All other	31,937	—	—	31,937		
Short-term investments	94,323	650	—	94,973		
Financial instruments carried at fair value, classified as a part of:						
Investment in unconsolidated subsidiaries	—	—	110,793	110,793		
Other investments	4,830	25,228	—	30,058		
Total assets	$ 405,784	$ 3,248,896	$ 134,595	$ 3,789,275		

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	December 31, 2013			
	Fair Value Measurements Using			Total
(In thousands)	Level 1	Level 2	Level 3	Fair Value
Assets:				
Fixed maturities, available for sale				
U.S. Treasury obligations	$—	$170,714	$—	$170,714
U.S. Government-sponsored enterprise obligations	—	32,768	—	32,768
State and municipal bonds	—	1,147,328	7,338	1,154,666
Corporate debt, multiple observable inputs	—	1,346,977	—	1,346,977
Corporate debt, limited observable inputs:				
Other corporate debt, NRSRO ratings available	—	—	11,449	11,449
Other corporate debt, NRSRO ratings not available	—	—	2,727	2,727
Residential mortgage-backed securities	—	235,614	—	235,614
Agency commercial mortgage-backed securities	—	27,475	—	27,475
Other commercial mortgage-backed securities	—	61,390	—	61,390
Other asset-backed securities	—	67,455	6,814	74,269
Equity securities				
Financial	81,536	—	—	81,536
Utilities/Energy	32,350	—	—	32,350
Consumer oriented	66,461	—	—	66,461
Industrial	57,262	—	—	57,262
All other	15,932	—	—	15,932
Short-term investments	248,605			248,605
Financial instruments carried at fair value, classified as a part of:				
Investment in unconsolidated subsidiaries	—	—	72,062	72,062
Total assets	$502,146	$3,089,721	$100,390	$3,692,257

The fair values for securities included in the Level 2 category, with the few exceptions described below, were developed by one of several third party, nationally recognized pricing services, including services that price only certain types of securities. Each service uses complex methodologies to determine values for securities and subject the values they develop to quality control reviews. Management selected a primary source for each type of security in the portfolio, and reviewed the values provided for reasonableness by comparing data to alternate pricing services and to available market and trade data. Values that appeared inconsistent were further reviewed for appropriateness. If a value did not appear reasonable, the valuation was discussed with the service that provided the value and would have been adjusted, if necessary. No such adjustments were necessary in 2014 or 2013.

Level 2 Valuations

Below is a summary description of the valuation methodologies primarily used by the pricing services for securities in the Level 2 category, by security type:

U.S. Treasury obligations were valued based on quoted prices for identical assets, or, in markets that are not active, quotes for similar assets, taking into consideration adjustments for variations in contractual cash flows and yields to maturity.

U.S. Government-sponsored enterprise obligations were valued using pricing models that consider current and historical market data, normal trading conventions, credit ratings, and the particular structure and characteristics of the security being valued, such as yield to maturity, redemption options, and contractual cash flows. Adjustments to model inputs or model results were included in the valuation process when necessary to reflect recent regulatory, government or corporate actions or significant economic, industry or geographic events affecting the security's fair

value.
State and municipal bonds were valued using a series of matrices that considered credit ratings, the structure of the security, the sector in which the security falls, yields, and contractual cash flows. Valuations were further adjusted, when necessary, to reflect recent significant economic or geographic events or ratings changes affecting the security's fair value.

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Corporate debt with multiple observable inputs consisted primarily of corporate bonds, but also included a small number of bank loans. The methodology used to value Level 2 corporate bonds was the same as the methodology previously described for U.S. Government-sponsored enterprise obligations. Bank loans were valued by an outside vendor based upon a widely distributed, loan-specific listing of average bid and ask prices published daily by an investment industry group. The publisher of the listing derived the averages from data received from multiple market-makers for bank loans.

Residential and commercial mortgage backed securities. Agency pass-through securities were valued using a matrix, considering the issuer type, coupon rate and longest cash flows outstanding. The matrix was developed daily based on available market information. Agency and non-agency collateralized mortgage obligations were both valued using models that consider the structure of the security, current and historical information regarding prepayment speeds, ratings and ratings updates, and current and historical interest rate and interest rate spread data. Valuations of Alt-A mortgages included a review of collateral performance data, which is generally updated monthly.

Other asset-backed securities were valued using models that consider the structure of the security, monthly payment information, current and historical information regarding prepayment speeds, ratings and ratings updates, and current and historical interest rate and interest rate spread data. Spreads and prepayment speeds considered collateral type. Valuations of subprime home equity loans used the same valuation methodology as previously described for Alt-A mortgages.

Short-term investments are securities maturing within one year, carried at cost which approximated the fair value of the security due to the short term to maturity.

Other investments consisted primarily of convertible bond securities. Convertible bonds were valued using a pricing model that incorporated selected dealer quotes as well as real-time market data including equity prices and risk free rates. If dealer quotes were unavailable for the security being valued, quotes for securities with similar terms and credit status were used in the pricing model. Dealer quotes selected for use were those considered most accurate based on parameters such as underwriter status and historical reliability.

Level 3 Valuations

Below is a summary description of the valuation processes and methodologies used as well as quantitative information regarding securities in the Level 3 category.

Level 3 Valuation Processes

- Level 3 securities are priced by the Chief Investment Officer.
- Level 3 valuations are computed quarterly. Prices are evaluated quarterly against prior period prices and the expected change in price.
- Exclusive of Investments in unconsolidated subsidiaries, which are valued at net asset value (NAV), the securities noted in the disclosure are primarily NRSRO rated debt instruments for which comparable market inputs are commonly available for evaluating the securities in question. Valuation of these debt instruments is not overly sensitive to changes in the unobservable inputs used.

Level 3 Valuation Methodologies

State and municipal bonds consisted of auction rate municipal bonds valued internally using either published quotes for similar securities or values produced by discounted cash flow models using yields currently available on fixed rate securities with a similar term and collateral, adjusted to consider the effect of a floating rate and a premium for illiquidity. At September 30, 2014, 100% of the securities were rated; the average rating was A.

Corporate debt with limited observable inputs consisted of corporate bonds valued using dealer quotes for similar securities or discounted cash flow models using yields currently available for similar securities. Similar securities are defined as securities having like terms and payment features that are of comparable credit quality. Assessments of credit quality were based on NRSRO ratings, if available, or were subjectively determined by management if not available. At September 30, 2014, the average rating of rated securities was A-.

Other asset-backed securities consisted of securitizations of receivables valued using dealer quotes for similar securities or discounted cash flow models using yields currently available for similar securities.

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Investment in unconsolidated subsidiaries consisted of limited partnership (LP) and limited liability company (LLC) interests valued using the NAV provided by the LP/LLC, which approximated the fair value of the interest. Such interests include the following:

(In thousands)	Unfunded Commitments September 30, 2014	Fair Value September 30, 2014	December 31, 2013
Investments in LPs/LLCs:			
Secured debt fund (1)	$16,200	$23,896	$13,233
Long equity fund (2)	None	7,034	6,574
Long/Short equity funds (3)	None	25,016	28,385
Non-public equity funds (4)	$71,518	42,818	23,870
Multi-strategy fund of funds (5)	None	8,263	—
Structured credit fund (6)	None	3,766	—
		$110,793	$72,062

(1) The LP is structured to provide income and capital appreciation primarily through investments in senior secured debt. Redemptions are not allowed. Income and capital are to be periodically distributed at the discretion of the LP over an anticipated time frame that spans from 7 to 9 years.

(2) The LP holds long equities of public international companies. Redemptions are allowed at the end of any calendar month with a prior notice requirement of 15 days and are paid within 10 days of the end of the calendar month of the redemption request.

(3) Comprised of interests in multiple unrelated LP funds. The funds hold primarily long and short North American equities, and target absolute returns using strategies designed to take advantage of event-driven market opportunities. The funds generally permit quarterly or semi-annual redemptions of the investors’ existing capital balance with notice requirements of 30 to 90 days. For some funds, redemptions above specified thresholds (lowest threshold is 90%) may be only partially payable until after a fund audit is completed and are then payable within 30 days.

(4) Comprised of interests in three unrelated LP funds, each structured to provide capital appreciation through diversified investments in private equity, which can include investments in buyout, venture capital, mezzanine debt, distressed debt and other private equity-oriented LPs. One LP allows redemption by special consent; the others do not permit redemption. Income and capital are to be periodically distributed at the discretion of the LP over time frames that are anticipated to span from 4 to 12 years.

(5) The LLC is structured to build and manage low volatility, multi-manager portfolios that have little or no correlation to the broader fixed income and equity security markets. Redemptions are not permitted but the LLC Board is permitted discretion to periodically extend offers to repurchase units of the LLC.

(6) The LP seeks to obtain superior risk-adjusted absolute returns by acquiring and actively managing a diversified portfolio of debt securities, including bonds, loans and other asset-backed instruments. Redemptions are allowed at any quarter-end with a prior notice requirement of 90 days.

ProAssurance may not sell, transfer or assign its interest in any of the above LPs/LLCs without special consent from the LPs/LLCs.

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Quantitative Information Regarding Level 3 Valuations
Quantitative Information about Level 3 Fair Value Measurements

(In millions)	Fair Value at September 30, 2014	December 31, 2013	Valuation Technique	Unobservable Input	Range (Weighted Average)
Assets:					
State and municipal bonds	$5.6	$7.3	Market Comparable Securities	Comparability Adjustment	0% - 10% (5%)
			Discounted Cash Flows	Comparability Adjustment	0% - 10% (5%)
Corporate debt with limited observable inputs	$13.4	$14.2	Market Comparable Securities	Comparability Adjustment	0% - 5% (2.5%)
			Discounted Cash Flows	Comparability Adjustment	0% - 5% (2.5%)
Other asset-backed securities	$4.8	$6.8	Market Comparable Securities	Comparability Adjustment	0% - 5% (2.5%)
			Discounted Cash Flows	Comparability Adjustment	0% - 5% (2.5%)

The significant unobservable inputs used in the fair value measurement of the above listed securities were the valuations of comparable securities with similar issuers, credit quality and maturity. Changes in the availability of comparable securities could result in changes in the fair value measurements.
Fair Value Measurements - Level 3 Assets
The following tables (the Level 3 Tables) present summary information regarding changes in the fair value of assets measured at fair value using Level 3 inputs.

	September 30, 2014					
	Level 3 Fair Value Measurements – Assets					
(In thousands)	U.S. Government-sponsored Enterprise Obligations	State and Municipal Bonds	Corporate Debt	Asset-backed Securities	Investment in Unconsolidated Subsidiaries	Total
Balance June 30, 2014	$—	$7,148	$14,544	$5,960	$ 101,342	$128,994
Total gains (losses) realized and unrealized:						
Included in earnings, as a part of:						
Net investment income	—	(4)	16	—	—	12
Equity in earnings of unconsolidated subsidiaries	—	—	—	—	(683)	(683)
Net realized investment gains (losses)	—	—	—	—	—	—
Included in other comprehensive income	—	(76)	35	(6)	—	(47)
Purchases	—	—	(499)	—	12,055	11,556
Sales	—	(1,474)	(661)	—	(1,921)	(4,056)
Transfers in	—	—	—	—	—	—

Transfers out	—	—	—	(1,181)	—	(1,181)
Balance September 30, 2014	$—	$5,594	$13,435	$4,773	$ 110,793	$134,595
Change in unrealized gains (losses) included in earnings for the above period for Level 3 assets held at period-end	$—	$—	$—	$—	$ (683)	$(683)

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	September 30, 2014 Level 3 Fair Value Measurements – Assets					
(In thousands)	U.S. Government-sponsored Enterprise Obligations	State and Municipal Bonds	Corporate Debt	Asset-backed Securities	Investment in Unconsolidated Subsidiaries	Total
Balance December 31, 2013	$—	$7,338	$14,176	$6,814	$ 72,062	$100,390
Total gains (losses) realized and unrealized:						
Included in earnings, as a part of:						
Net investment income	—	(10)	48	—	—	38
Equity in earnings of unconsolidated subsidiaries	—	—	—	—	5,413	5,413
Net realized investment gains (losses)	—	(95)	3	—	—	(92)
Included in other comprehensive income	1	(34)	702	63	—	732
Purchases	1,000	1,861	2,000	3,340	37,430	45,631
Sales	—	(1,731)	(1,469)	(61)	(4,112)	(7,373)
Transfers in	—	2,119	—	305	—	2,424
Transfers out	(1,001)	(3,854)	(2,025)	(5,688)	—	(12,568)
Balance September 30, 2014	$—	$5,594	$13,435	$4,773	$ 110,793	$134,595
Change in unrealized gains (losses) included in earnings for the above period for Level 3 assets held at period-end	$—	$—	$—	$—	$ 5,413	$5,413

	September 30, 2013 Level 3 Fair Value Measurements – Assets					
(In thousands)	U.S. Government-sponsored Enterprise Obligations	State and Municipal Bonds	Corporate Debt	Asset-backed Securities	Investment in Unconsolidated Subsidiaries	Total
Balance June 30, 2013	$—	$5,025	$11,359	$4,679	$ 44,549	$65,612
Total gains (losses) realized and unrealized:						
Included in earnings, as a part of:						
Net investment income	—	—	(1)	—	—	(1)
Equity in earnings of unconsolidated subsidiaries	—	—	—	—	1,301	1,301
Net realized investment gains (losses)	—	—	—	—	—	—
Included in other comprehensive income	—	—	(221)	16	—	(205)
Purchases	—	—	—	—	2,354	2,354

Sales	—	—	(503)	—	(3,548)	(4,051)
Transfers in	—	—	100	—	—	100
Transfers out	—	—	—	—	—	—
Balance September 30, 2013	$—	$5,025	$10,734	$4,695	$ 44,656	$65,110
Change in unrealized gains (losses) included in earnings for the above period for Level 3 assets held at period-end	$—	$—	$—	$—	$ 1,301	$1,301

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	September 30, 2013 Level 3 Fair Value Measurements – Assets					
(In thousands)	U.S. Government-sponsored Enterprise Obligations	State and Municipal Bonds	Corporate Debt	Asset-backed Securities	Investment in Unconsolidated Subsidiaries	Total
Balance December 31, 2012	$—	$7,175	$15,191	$4,035	$ 33,739	$60,140
Total gains (losses) realized and unrealized:						
Included in earnings, as a part of:						
Net investment income	—	—	(103)	(17)	—	(120)
Equity in earnings of unconsolidated subsidiaries	—	—	—	—	3,582	3,582
Net realized investment gains (losses)	—	(44)	(69)	—	—	(113)
Included in other comprehensive income	—	—	(514)	(81)	—	(595)
Purchases	—	—	7,470	1,356	20,975	29,801
Sales	—	(2,106)	(1,368)	(18)	(13,640)	(17,132)
Transfers in	—	—	100	1,701	—	1,801
Transfers out	—	—	(9,973)	(2,281)	—	(12,254)
Balance September 30, 2013	$—	$5,025	$10,734	$4,695	$ 44,656	$65,110
Change in unrealized gains (losses) included in earnings for the above period for Level 3 assets held at period-end	$—	$—	$—	$—	$ 3,582	$3,582

Transfers

There were no transfers between the Level 1 and Level 2 categories during the three and nine months ended September 30, 2014 or 2013.

Transfers shown in the preceding Level 3 Tables were as of the end of the period and were to or from Level 2, unless otherwise noted.

All transfers during the three and nine months ended September 30, 2014 and September 30, 2013 related to securities held for which the level of market activity for identical or nearly identical securities varies from period to period. The securities were valued using multiple observable inputs when those inputs were available; otherwise the securities were valued using limited observable inputs.

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Financial Instruments - Methodologies Other Than Fair Value
The following table provides the estimated fair value of our financial instruments that, in accordance with GAAP for the type of investment, are measured using a methodology other than fair value. All fair values provided fall within the Level 3 fair value category.

(In thousands)	September 30, 2014		December 31, 2013	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
BOLI	$55,918	$55,918	$54,374	$54,374
Other investments	61,952	63,247	52,240	51,833
Other assets	21,298	21,248	17,940	17,940
Financial liabilities:				
Senior notes due 2023	$250,000	$273,750	$250,000	$262,500
Other liabilities	14,022	14,139	13,303	13,303

The fair value of the BOLI was equal to the cash surrender value associated with the policies on the valuation date.
Other investments listed in the table above include interests in certain investment fund LPs/LLCs accounted for using the cost method, investments in Federal Home Loan Bank (FHLB) common stock carried at cost, and an annuity investment carried at amortized cost. The estimated fair value of the LP/LLC interests was based on the NAVs provided by the LP/LLC managers. The estimated fair value of the FHLB common stock was based on the amount ProAssurance would receive if its membership were canceled, as the membership cannot be sold. The fair value of the annuity represents the present value of the expected future cash flows discounted using a rate available in active markets for similarly structured instruments.
Other assets and Other liabilities primarily consisted of related investment assets and liabilities associated with funded deferred compensation agreements. Fair values of the funded deferred compensation assets and liabilities were based on the NAVs of the underlying securities. Other assets also included a secured note receivable and an unsecured receivable under a revolving credit agreement. Fair value of these receivables was based on the present value of expected cash flows from the receivables, discounted at market rates on the valuation date for receivables with similar credit standings and similar payment structures. Other liabilities also included certain contractual liabilities related to prior business combinations. The fair values of the business combination liabilities were based on the present value of the expected future cash outflows, discounted at ProAssurance’s assumed incremental borrowing rate on the valuation date for unsecured liabilities with similar repayment structures.
The fair value of the long-term debt was estimated based on the present value of expected future cash outflows, discounted at rates available on the valuation date for similar debt issued by entities with a similar credit standing to ProAssurance.

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4. Investments

Available-for-sale securities at September 30, 2014 and December 31, 2013 included the following:

	September 30, 2014			
(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities				
U.S. Treasury obligations	$173,632	$4,396	$1,215	$176,813
U.S. Government-sponsored enterprise obligations	42,480	1,709	223	43,966
State and municipal bonds	1,038,278	50,055	699	1,087,634
Corporate debt	1,433,266	48,894	9,175	1,472,985
Residential mortgage-backed securities	282,717	8,817	1,220	290,314
Agency commercial mortgage-backed securities	16,785	172	64	16,893
Other commercial mortgage-backed securities	55,853	1,587	117	57,323
Other asset-backed securities	100,715	346	169	100,892
	$3,143,726	$115,976	$12,882	$3,246,820

	December 31, 2013			
(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities				
U.S. Treasury obligations	$166,115	$6,118	$1,519	$170,714
U.S. Government-sponsored enterprise obligations	30,942	2,251	425	32,768
State and municipal bonds	1,116,060	46,533	7,927	1,154,666
Corporate debt	1,321,838	53,059	13,744	1,361,153
Residential mortgage-backed securities	230,861	7,608	2,855	235,614
Agency commercial mortgage-backed securities	27,268	343	136	27,475
Other commercial mortgage-backed securities	59,066	2,491	167	61,390
Other asset-backed securities	74,106	487	324	74,269
	$3,026,256	$118,890	$27,097	$3,118,049

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The recorded cost basis and estimated fair value of available-for-sale fixed maturities at September 30, 2014, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(In thousands)	Amortized Cost	Due in one year or less	Due after one year through five years	Due after five years through ten years	Due after ten years	Total Fair Value
Fixed maturities, available for sale						
U.S. Treasury obligations	$173,632	$19,612	$104,211	$48,950	$4,040	$176,813
U.S. Government-sponsored enterprise obligations	42,480	8,002	25,465	10,160	339	43,966
State and municipal bonds	1,038,278	49,169	393,569	442,212	202,684	1,087,634
Corporate debt	1,433,266	157,683	694,254	598,183	22,865	1,472,985
Residential mortgage-backed securities	282,717					290,314
Agency commercial mortgage-backed securities	16,785					16,893
Other commercial mortgage-backed securities	55,853					57,323
Other asset-backed securities	100,715					100,892
	$3,143,726					$3,246,820

Excluding obligations of the U.S. Government or U.S. Government-sponsored enterprises, no investment in any entity or its affiliates exceeded 10% of shareholders’ equity at September 30, 2014.
Cash and securities with a carrying value of $48.2 million at September 30, 2014 were on deposit with various state insurance departments to meet regulatory requirements.
As a member of Lloyd's and a capital provider to Syndicate 1729, ProAssurance is required to maintain capital at Lloyd's, referred to as Funds at Lloyd's (FAL). ProAssurance investments at September 30, 2014 included fixed maturities with a fair value of $71.5 million and short term investments with a fair value of approximately $5.7 million on deposit with Lloyd's in order to satisfy these FAL requirements.
Business Owned Life Insurance (BOLI)
ProAssurance holds BOLI policies on management employees that are carried at the current cash surrender value of the policies (original cost $33 million). The primary purpose of the program is to offset future employee benefit expenses through earnings on the cash value of the policies. ProAssurance is the owner and principal beneficiary of these policies.
Other Investments
Other investments at September 30, 2014 and December 31, 2013 was comprised as follows:

(In thousands)	September 30, 2014	December 31, 2013
Investments in LPs/LLCs, at cost	$57,607	$47,258
Convertible securities, at fair value, see Note 1	30,058	—
Other, principally FHLB capital stock, at cost	4,345	4,982
	$92,010	$52,240

FHLB capital stock is not marketable, but may be liquidated by terminating membership in the FHLB. The liquidation process can take up to five years.

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Unconsolidated Subsidiaries
ProAssurance holds investments in unconsolidated subsidiaries, accounted for under the equity method. The investments include the following:

(In thousands)	September 30, 2014 Unfunded Commitments*	Percentage Ownership		Carrying Value September 30, 2014	December 31, 2013
Investment in LPs/LLCs:					
Tax credit partnerships	$15,710	See below		$137,386	$142,174
Secured debt fund	$16,200	<	20%	23,896	13,233
Long equity fund	None	<	20%	7,034	6,574
Long/short equity funds	None	<	25%	25,016	28,385
Non-public equity funds	$88,034	<	20%	46,127	23,870
Multi-strategy fund of funds	None	<	20%	8,263	—
Structured credit fund	None	<	20%	3,766	—
Real estate fund	$6,526	<	20%	3,474	—
				$254,962	$214,236

* Unfunded commitments are included in the carrying value of tax credit partnerships only.
Tax credit partnership interests held by ProAssurance generate investment returns by providing tax benefits to fund investors in the form of project operating losses and tax credits. The related properties are principally low income housing projects. ProAssurance's ownership percentage relative to two of the tax credit partnership interests is almost 100%; these interests had a carrying value of $60.9 million at September 30, 2014. ProAssurance's ownership percentage relative to the remaining tax credit partnership interests is less than 20%; these interests had a carrying value of $76.5 million at September 30, 2014. All are accounted for under the equity method as ProAssurance does not have the ability to exert control over the partnerships.
The Secured debt fund is structured to provide interest distributions and capital appreciation primarily through investments in senior secured debt.
The Long equity fund targets long-term total returns through holdings in public international companies.
The Long/Short equity fund targets absolute returns using a strategy designed to take advantage of event-driven market opportunities.
The Non-public equity funds hold diversified private equities and are structured to provide capital appreciation.
The Multi-strategy fund of funds holds portfolios having little or no correlation to the broader fixed income and equity security markets.
The Structured credit fund seeks to obtain superior risk-adjusted absolute returns by acquiring and actively managing a diversified portfolio of debt securities.
The Real estate fund invests in multi-tenant industrial real estate with the objective of achieving superior absolute returns in all market cycles.

Investments Held in a Loss Position

The following tables provide summarized information with respect to investments held in an unrealized loss position at September 30, 2014 and December 31, 2013, including the length of time the investment had been held in a continuous unrealized loss position.

	September 30, 2014					
	Total		Less than 12 months		12 months or longer	
(In thousands)	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Fixed maturities, available for sale						
U.S. Treasury obligations	$59,770	$1,215	$37,309	$534	$22,461	$681
U.S. Government-sponsored enterprise obligations	7,887	223	2,136	22	5,751	201
State and municipal bonds	71,155	699	32,129	128	39,026	571
Corporate debt	477,806	9,175	372,670	5,909	105,136	3,266
Residential mortgage-backed securities	66,143	1,220	26,012	105	40,131	1,115
Agency commercial mortgage-backed securities	10,432	64	8,536	8	1,896	56
Other commercial mortgage-backed securities	14,592	117	7,528	33	7,064	84
Other asset-backed securities	39,328	169	35,269	77	4,059	92
	$747,113	$12,882	$521,589	$6,816	$225,524	$6,066
Other investments						
Investments in LPs/LLCs carried at cost	$17,106	$582	$15,458	$577	$1,648	$5

	December 31, 2013					
	Total		Less than 12 months		12 months or longer	
(In thousands)	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Fixed maturities, available for sale						
U.S. Treasury obligations	$47,668	$1,519	$44,304	$1,182	$3,364	$337
U.S. Government-sponsored enterprise obligations	6,640	425	5,752	321	888	104
State and municipal bonds	203,970	7,927	184,401	6,640	19,569	1,287
Corporate debt	349,277	13,744	324,510	12,061	24,767	1,683
Residential mortgage-backed securities	93,608	2,855	84,045	2,393	9,563	462
Agency commercial mortgage-backed securities	11,658	136	11,082	116	576	20
Other commercial mortgage-backed securities	11,153	167	10,215	159	938	8
Other asset-backed securities	25,539	324	21,804	77	3,735	247
	$749,513	$27,097	$686,113	$22,949	$63,400	$4,148
Other investments						
Investments in LPs/LLCs carried at cost	$14,752	$1,059	$13,166	$1,018	$1,586	$41

As of September 30, 2014, excluding U.S. government backed securities, there were 617 debt securities (21.1% of all available-for-sale fixed maturity securities held) in an unrealized loss position representing 441 issuers. The greatest and second greatest unrealized loss position among those securities was approximately $0.5 million and $0.3 million,

respectively. The securities were evaluated for impairment as of September 30, 2014.

As of December 31, 2013, excluding U.S. government backed securities, there were 714 debt securities (26.3% of all available-for-sale fixed maturity securities held) in an unrealized loss position representing 516 issuers. Both the greatest and second greatest unrealized loss position among those securities approximated $0.4 million. The securities were evaluated for impairment as of December 31, 2013.

Each quarter, ProAssurance performs a detailed analysis for the purpose of assessing whether any of the securities it holds in an unrealized loss position have suffered an other-than-temporary impairment in value. A detailed discussion of the factors considered in the assessment is included in Note 1 of the Notes to Consolidated Financial Statements included in ProAssurance's December 31, 2013 Form 10-K.

Fixed maturity securities held in an unrealized loss position at September 30, 2014, excluding asset-backed securities, have paid all scheduled contractual payments and are expected to continue doing so. Expected future cash flows of asset-backed securities held in an unrealized loss position were estimated as part of the September 30, 2014 impairment evaluation using the most recently available six-month historical performance data for the collateral (loans) underlying the security or, if historical data was not available, sector based assumptions, and equaled or exceeded the current amortized cost basis of the security.

Net Investment Income

Net investment income by investment category was as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
Fixed maturities	$28,442	$30,672	$85,402	$93,687
Equities	2,661	2,394	7,479	7,000
Short-term investments and Other invested assets	2,793	2,000	4,723	2,514
Business owned life insurance	646	633	1,544	1,508
Investment fees and expenses	(1,712)	(1,810)	(6,360)	(5,427)
Net investment income	$32,830	$33,889	$92,788	$99,282

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Net Realized Investment Gains (Losses)
Realized investment gains and losses are recognized on the specific identification basis. The following table provides detailed information regarding net realized investment gains (losses):

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
Total other-than-temporary impairment losses:				
State and municipal bonds	$—	$—	$(50)	$(71)
Corporate debt	(1,425)	—	(1,425)	—
Portion recognized in (reclassified from) Other Comprehensive Income:				
Corporate debt	268	—	268	—
Net impairments recognized in earnings	$(1,157)	$—	$(1,207)	$(71)
Gross realized gains, available-for-sale securities	736	7,708	3,711	14,631
Gross realized (losses), available-for-sale securities	(52)	(5,305)	(371)	(6,269)
Net realized gains (losses), trading securities	3,227	5,818	21,830	14,650
Net realized gains (losses), Other investments	55	—	321	—
Change in unrealized holding gains (losses), trading securities	(10,402)	3,355	(17,906)	23,784
Change in unrealized holding gains (losses), convertible securities, carried at fair value	(538)	—	1,281	—
Other	—	924	—	925
Net realized investment gains (losses)	$(8,131)	$12,500	$7,659	$47,650

Credit-related impairments related to two corporate debt instruments were recognized in the third quarter of 2014. Additionally, a non-credit impairment related to one of the instruments was recognized as the fair value of the instrument was less than the expected future cash flows from the security. No significant impairment losses were recognized in the 2013 three- and nine-month periods.
The following table presents a roll forward of cumulative credit losses recorded in earnings related to impaired debt securities for which a portion of the other-than-temporary impairment was recorded in Other comprehensive income.

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
Balance beginning of period	$83	$413	$83	$3,301
Additional credit losses recognized during the period, related to securities for which:				
No OTTI has been previously recognized	149	—	149	—
Reductions due to:				
Securities sold during the period (realized)	—	(330)	—	(3,218)
Balance September 30	$232	$83	$232	$83

Other information regarding sales and purchases of available-for-sale securities is as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
(In millions)	2014	2013	2014	2013
Proceeds from sales (exclusive of maturities and paydowns)	$24.8	$319.2	$147.3	$494.8
Purchases	$146.5	$98.8	$511.9	$406.2

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5. Income Taxes
ProAssurance estimates its annual effective tax rate at the end of each quarterly reporting period and uses this estimated rate to record the provision for income taxes in the interim financial statements. The provision for income taxes is different from that which would be obtained by applying the statutory Federal income tax rate to income before taxes primarily because a portion of ProAssurance's investment income is tax-exempt, because ProAssurance utilizes tax credit benefits transferred from tax credit partnership investments, and in 2013, because ProAssurance recognized a non-taxable gain related to an acquisition.
In 2013 the IRS issued a Notice of Proposed Adjustment (NOPA) for the 2009 and 2010 tax years. ProAssurance subsequently protested certain issues in the NOPA, all of which related to the timing of deductions. In April 2014, ProAssurance and the IRS reached a final settlement on all contested issues which resulted in no additional tax liability for ProAssurance. ProAssurance subsequently received IRS refunds totaling $30.6 million, exclusive of interest, which included a refund from the settlement of non-contested issues addressed by the NOPA, and return of a protective payment made in 2013.
The statute of limitations is now closed for all tax years prior to 2011.
The liability for unrecognized tax benefits was $0.6 million at September 30, 2014 and $4.8 million at December 31, 2013. All unrecognized benefits included in the December 31, 2013 balance were attributable to timing issues which fully reversed during the first quarter of 2014; an additional $0.6 million was added to the liability in 2014 as a result of the acquisition of Eastern.
ProAssurance had receivables for federal income taxes of $11.4 million at September 30, 2014 and $27.3 million at December 31, 2013, both carried as a part of Other Assets.
6. Deferred Policy Acquisition Costs
Policy acquisition costs that are primarily and directly related to the successful production of new and renewal insurance contracts, most significantly agent commissions, premium taxes, and underwriting salaries and benefits, are capitalized as policy acquisition costs and amortized to expense, net of ceding commissions earned, as the related premium revenues are earned.
Amortization of deferred policy acquisition costs was $16.7 million and $52.9 million for the three and nine months ended September 30, 2014, respectively, and $13.9 million and $39.0 million for the three and nine months ended September 30, 2013, respectively.
7. Reserve for Losses and Loss Adjustment Expenses
The reserve for losses is established based on estimates of individual claims and actuarially determined estimates of future losses based on ProAssurance's past loss experience, available industry data and projections as to future claims frequency, severity, inflationary trends and settlement patterns. Estimating the reserve, particularly the reserve appropriate for liability exposures, is a complex process. Claims may be resolved over an extended period of time, often five years or more, and may be subject to litigation. Estimating losses requires ProAssurance to make and revise judgments and assessments regarding multiple uncertainties over an extended period of time. As a result, the reserve estimate may vary significantly from the eventual outcome. The assumptions used in establishing ProAssurance's reserve are regularly reviewed and updated by management as new data becomes available. Changes to estimates of previously established reserves are included in earnings in the period in which the estimate is changed.
During the three and nine months ended September 30, 2014, ProAssurance recognized favorable net loss development of $42.9 million and $133.3 million, respectively, related to prior accident years, of which $0.6 million and $2.9 million, respectively, related to the loss reserve assumed in the acquisition of Eastern. The favorable net loss development reflected reductions in the Company's estimates of claims severity, principally related to the 2007 through 2012 accident years.
For the three and nine months ended September 30, 2013, ProAssurance recognized favorable net loss development of $49.4 million and $141.0 million, respectively, to reflect reductions in estimated claims severity. The favorable net loss development reflected reductions in the Company's estimates of claims severity, principally related to the 2005

through 2011 accident years.

8. Commitments and Contingencies

ProAssurance is involved in various legal actions related to insurance policies and claims handling including, but not limited to, claims asserted by policyholders. These types of legal actions arise in the Company's ordinary course of business and, in accordance with GAAP for insurance entities, are considered as a part of the Company's loss reserving process, which is described in detail under the heading "Losses and Loss Adjustment Expenses" in the Accounting Policies section in Note 1 of the Notes to Consolidated Financial Statements in ProAssurance's 2013 Form 10-K.

ProAssurance has funding commitments primarily related to non-public investment entities totaling approximately $164.7 million, expected to be paid as follows: $22.6 million in 2014, $124.7 million in 2015 and 2016 combined, $16.5 million in 2017 and 2018 combined, and $0.9 million thereafter.

As a member of Lloyd's and a capital provider to Syndicate 1729, ProAssurance is required to provide capital, referred to as FAL. At September 30, 2014, ProAssurance is satisfying the FAL requirement with investment securities on deposit with Lloyd's with a carrying value of $77.2 million (see Note 4). ProAssurance anticipates its FAL requirement for the 2015 underwriting year to be approximately £50.9 million, which would require ProAssurance to fund an additional £5.8 million (approximately $9.8 million if funded with U.S. currency) during 2014. At December 31, 2013, the FAL requirement was primarily met through a standby letter of credit (LOC).

ProAssurance has also issued an unconditional revolving credit agreement (the Credit Agreement) of up to £10 million ($16 million at September 30, 2014) to the Premium Trust Fund of Syndicate 1729 for the purpose of providing working capital. Advances under the Credit Agreement bear interest at 8.5% annually, and are repayable upon demand after December 31, 2016. As of September 30, 2014, £5.5 million ($9.2 million) had been advanced under the Credit Agreement.

9. Long-term Debt

ProAssurance’s outstanding long-term debt consisted of the following:

(In thousands)	September 30, 2014	December 31, 2013
Senior notes due 2023, unsecured, interest at 5.3% annually	$250,000	$250,000
Revolving credit agreement, maximum outstanding borrowings of $200 million permitted, expires in 2016	—	—
	$250,000	$250,000

Covenant Compliance

There are no financial covenants associated with the Senior Notes due 2023.

The Revolving credit agreement (the Agreement) contains customary representations, covenants and events constituting default, and remedies for default. The Agreement also defines financial covenants regarding permitted leverage ratios and minimum net worth. ProAssurance is currently in compliance with all covenants of the Agreement.

Additional Information

For additional information regarding ProAssurance's long-term debt, see Note 10 of the Notes to Consolidated Financial Statements included in ProAssurance's December 31, 2013 Form 10-K.

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10. Shareholders' Equity

At September 30, 2014 and December 31, 2013, ProAssurance had 100 million shares of authorized common stock and 50 million shares of authorized preferred stock. The Board has the authority to determine provisions for the issuance of preferred shares, including the number of shares to be issued, the designations, powers, preferences and rights, and the qualifications, limitations or restrictions of such shares. To date, the Board has not approved the issuance of preferred stock.

ProAssurance declared cash dividends of $0.30 per share during each of the first three quarters of 2014, totaling $52.9 million, which included the third quarter dividend of $17.3 million that was paid in October 2014. ProAssurance declared cash dividends of $0.25 per share during each of the first three quarters of 2013, totaling $46.4 million, which included the third quarter dividend of $15.5 million that was paid in October 2013. The liability for unpaid dividends was included in Other liabilities. Though dividends are typically paid in the month following the quarter in which they were declared, no dividends were paid in the first quarter of 2013 because payment of the regular fourth quarter 2012 dividend was accelerated into December 2012.

At September 30, 2014, Board authorizations for the repurchase of common shares or the retirement of outstanding debt of $136.7 million remained available for use. ProAssurance repurchased approximately 3.7 million and 0.2 million shares, having a total cost of $167.2 million and $8.0 million, during the nine months ended September 30, 2014 and 2013, respectively.

Share-based compensation expense was $2.4 million and $8.0 million for the three and nine months ended September 30, 2014, respectively, and $2.2 million and $6.9 million for the three and nine months ended September 30, 2013, respectively. Related tax benefits were $0.8 million and $2.8 million for the three and nine months ended September 30, 2014, respectively, and $0.8 million and $2.4 million for the three and nine months ended September 30, 2013, respectively.

ProAssurance awarded approximately 50,000 restricted share units and 161,000 base performance share units to employees in February 2014. The fair value of each unit awarded was estimated at $46.34, equal to the market value of a ProAssurance common share on the date of grant. All awards are charged to expense as an increase to equity over the service period (generally the vesting period) associated with the award. Restricted share units and performance share units vest in their entirety at the end of a three-year period following the grant date based on a continuous service requirement and, for performance share units, achievement of a performance objective. Partial vesting is permitted for retirees. A ProAssurance common share is issued for each unit once vesting requirements are met, except that units sufficient to satisfy required tax withholdings are paid in cash. The number of common shares issued for performance share units varies from 75% to 125% of base awards depending upon the degree to which stated performance objectives are achieved. ProAssurance issued approximately 29,000 and 111,000 common shares to employees in February 2014 related to restricted share units and performance share units, respectively, granted in 2011. Shares issued for performance share units were awarded at the maximum level (125%).

ProAssurance issued approximately 30,000 common shares to employees in February 2014 as bonus compensation, as approved by the Compensation Committee of the Board. The shares issued were valued at fair value (the market price of a ProAssurance common share on the date of award).

Other Comprehensive Income (Loss) (OCI)

For the three and nine months ended September 30, 2014 and September 30, 2013, OCI was primarily comprised of unrealized gains and losses arising during the period related to available-for-sale securities, less reclassification adjustments as shown in the table below, net of tax. At September 30, 2014 and December 31, 2013, accumulated other comprehensive income was comprised primarily of unrealized gains and losses from available-for-sale securities, including non-credit impairment losses previously recognized in OCI of $0.8 million and 0.5 million, respectively, net of tax. All tax effects were computed using a 35% rate. OCI and accumulated other comprehensive income also included immaterial amounts of foreign currency translation adjustments.

Amounts reclassified from accumulated other comprehensive income to net income and the amounts of deferred tax expense (benefit) included in OCI were as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
Reclassifications from accumulated other comprehensive income to net income, available-for-sale securities:				
Realized investment gains (losses)	$(473)	$2,403	$2,133	$8,638
Non-credit impairment losses reclassified to earnings, due to sale of securities or reclassification as a credit loss	—	—	—	(347)
Total amounts reclassified, before tax effect	(473)	2,403	2,133	8,291
Tax effect (at 35%)	166	(841)	(747)	(2,902)
Net reclassification adjustments	$(307)	$1,562	$1,386	$5,389
Deferred tax expense (benefit) included in OCI	$(5,126)	$(1,746)	$(2,571)	$(26,358)

11. Variable Interest Entities

ProAssurance holds passive interests in a number of entities that are considered to be Variable Interest Entities (VIEs) under GAAP guidance. ProAssurance's VIE interests principally consist of interests in LPs/LLCs formed for the purpose of achieving diversified equity and debt returns. ProAssurance VIE interests carried as a part of Other investments totaled $37.6 million at September 30, 2014 and $27.3 million at December 31, 2013. ProAssurance VIE interests carried as a part of Investment in unconsolidated subsidiaries totaled $58.1 million at September 30, 2014 and $49.5 million at December 31, 2013.

ProAssurance has not consolidated these VIEs because it has either very limited or no power to control the activities that most significantly affect the economic performance of these entities and is not the primary beneficiary of any of the entities. ProAssurance’s involvement with each entity is limited to its direct ownership interest in the entity. ProAssurance has no arrangements with any of the entities to provide other financial support to or on behalf of the entity. At September 30, 2014, ProAssurance’s maximum loss exposure relative to these investments was limited to the carrying value of ProAssurance’s investment in the VIE.

12. Earnings Per Share

Diluted weighted average shares is calculated as basic weighted average shares plus the effect, calculated using the treasury stock method, of assuming that dilutive stock options have been exercised and that performance, restricted and purchase share units have vested. All outstanding stock options, performance, restricted and purchase share units had a dilutive effect for the three and nine months ended September 30, 2014 and 2013.

13. Segment Information

ProAssurance operates in four segments that are organized around the nature of the products and services provided: Specialty P&C, Workers' Compensation, Lloyd's Syndicate, and Corporate. A description of each segment follows.

Specialty P&C is primarily focused on professional liability insurance and medical technology and life sciences products liability insurance. The professional liability business primarily offers professional liability insurance to healthcare providers and institutions and to attorneys and their firms. The medical technology and life sciences business offers products liability insurance for medical technology and life sciences companies that manufacture or distribute products. The Specialty P&C segment cedes certain premium to the Lloyd's Syndicate segment under an agreement with Syndicate 1729. As discussed below, Syndicate 1729 operating results are reported on a quarter delay. The ceded premium associated with the Syndicate 1729 reinsurance agreement has been reported within the Specialty P&C segment on a similar lag, as this results in the ceded premium being reported in the same period in which the Lloyd's Syndicate segment reports the corresponding assumed premium.

Workers' Compensation provides workers' compensation products primarily to employers with 1,000 or fewer employees. The segment also offers alternative market solutions whereby policies written are 100% ceded either to a captive insurer unaffiliated with ProAssurance or to SPCs operated by a wholly owned subsidiary of ProAssurance. The SPCs are fully or partially owned by the employer (or employer group, association or affiliate) insured by the policies ceded. Financial results (underwriting profit or loss, plus investment income) of the SPCs accrue to the owners of that cell. Our workers' compensation segment is comprised entirely of the business acquired through Eastern on January 1, 2014.

Lloyd's Syndicate includes operating results from ProAssurance's 58% participation in Lloyd's of London Syndicate 1729 that began writing business as of January 1, 2014. Syndicate 1729 underwrites risks over a wide range of property and casualty insurance and reinsurance lines. The results of this segment are reported on a quarter delay, except that investment results associated with the FAL investments and certain U.S. paid administrative expenses, primarily start-up costs, are reported concurrently as that information is available on an earlier time frame.

Corporate includes ProAssurance's U.S. investment operations, interest expense and U.S. income taxes, all of which are managed at the corporate level, non-premium revenues generated outside of our insurance entities, and corporate expenses.

The accounting policies of the segments are the same as those described in Note 1 of the Notes to Consolidated Financial Statements in ProAssurance’s December 31, 2013 report on Form 10-K and Note 1 herein. ProAssurance evaluates performance of its Specialty P&C and Workers' Compensation segments based on before tax underwriting profit or loss, and excludes investment performance. Performance of the Lloyd's Syndicate segment is evaluated based on underwriting profit or loss, and investment results of investment assets solely allocated to Syndicate 1729 operations, net of United Kingdom income tax expense. Performance of the Corporate segment is evaluated based on the contribution made to consolidated after tax results. ProAssurance accounts for inter-segment sales and transfers as if the sales or transfers were to third parties at current market prices. Assets are not allocated to segments because investments and assets are not managed at the segment level.

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Financial data by segment for the three and nine months ended September 30, 2014 and 2013 were as follows:

	Three Months Ended September 30, 2014					
(In thousands)	Specialty P&C	Workers' Compensation	Lloyd's Syndicate	Corporate	Eliminations	Consolidated
Net premiums earned	$123,791	$ 49,792	$3,445	$—	$—	$ 177,028
Net investment income	—	—	120	32,710	—	32,830
Equity in earnings (loss) of unconsolidated subsidiaries	—	—	—	298	—	298
Net realized gains (losses)	—	—	—	(8,131)	—	(8,131)
Other income	1,071	179	(79)	824	(187)	1,808
Net losses and loss adjustment expenses	(63,639)	(33,046)	(2,537)	—	—	(99,222)
Underwriting, policy acquisition and operating expenses	(33,814)	(14,785)	(2,584)	(3,189)	187	(54,185)
Segregated portfolio cells dividend expense	—	483	—	—	—	483
Interest expense	—	—	—	(3,606)	—	(3,606)
Income tax expense (benefit)	—	—	—	(12,525)	—	(12,525)
Segment operating results	$27,409	$ 2,623	$(1,635)	$6,381	$—	$ 34,778
Significant non-cash items						
Depreciation and amortization	$2,334	$ 1,602	$157	$8,219	$—	$ 12,312

	Nine Months Ended September 30, 2014					
(In thousands)	Specialty P&C	Workers' Compensation	Lloyd's Syndicate	Corporate	Eliminations	Consolidated
Net premiums earned	$374,704	$ 143,960	$6,397	$—	$—	$ 525,061
Net investment income	—	—	244	92,544	—	92,788
Equity in earnings (loss) of unconsolidated subsidiaries	—	—	—	2,767	—	2,767
Net realized gains (losses)	—	—	—	7,659	—	7,659
Other income	4,167	503	(79)	1,856	(392)	6,055
Net losses and loss adjustment expenses	(191,263)	(91,975)	(4,405)	—	—	(287,643)
Underwriting, policy acquisition and operating expenses	(101,044)	(45,379)	(5,999)	(6,826)	392	(158,856)
Segregated portfolio cells dividend expense	—	(2,355)	—	—	—	(2,355)
Interest expense	—	—	—	(10,697)	—	(10,697)
Income tax expense (benefit)	—	—	—	(43,328)	—	(43,328)
Segment operating results	$86,564	$ 4,754	$(3,842)	$43,975	$—	$ 131,451
Significant non-cash items						
Depreciation and amortization	$6,708	$ 4,384	$329	$24,865	$—	$ 36,286

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	Three Months Ended September 30, 2013					
(In thousands)	Specialty P&C	Workers' Compensation	Lloyd's Syndicate	Corporate	Eliminations	Consolidated
Net premiums earned	$133,598	$ —	$—	$—	$—	$ 133,598
Net investment income	—	—	—	33,889	—	33,889
Equity in earnings (loss) of unconsolidated subsidiaries	—	—	—	(305)	—	(305)
Net realized gains (losses)	—	—	—	12,500	—	12,500
Other income	1,225	—	—	579	—	1,804
Gain on acquisition	—	—	—	494	—	494
Net losses and loss adjustment expenses	(61,637)	—	—	—	—	(61,637)
Underwriting, policy acquisition and operating expenses	(30,708)	—	—	(2,640)	—	(33,348)
Interest expense	—	—	—	(322)	—	(322)
Income tax expense (benefit)	—	—	—	(23,316)	—	(23,316)
Segment operating results	$42,478	$ —	$—	$20,879	$—	$ 63,357
Significant non-cash items						
Depreciation and amortization	$990	$ —	$—	$8,930	$—	$ 9,920

	Nine Months Ended September 30, 2013					
(In thousands)	Specialty P&C	Workers' Compensation	Lloyd's Syndicate	Corporate	Eliminations	Consolidated
Net premiums earned	$398,528	$ —	$—	$—	$—	$ 398,528
Net investment income	—	—	—	99,282	—	99,282
Equity in earnings (loss) of unconsolidated subsidiaries	—	—	—	(3,500)	—	(3,500)
Net realized gains (losses)	—	—	—	47,650	—	47,650
Other income	3,902	—	—	1,410	(7)	5,305
Gain on acquisition	—	—	—	35,986	—	35,986
Net losses and loss adjustment expenses	(189,872)	—	—	—	—	(189,872)
Underwriting, policy acquisition and operating expenses	(95,907)	—	—	(9,692)	7	(105,592)
Interest expense	—	—	—	(1,085)	—	(1,085)
Income tax expense (benefit)	—	—	—	(60,044)	—	(60,044)
Segment operating results	$116,651	$ —	$—	$110,007	$—	$ 226,658
Significant non-cash items						
Depreciation and amortization	$4,845	$ —	$—	$29,519	$—	$ 34,364

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The following table provides detailed information regarding ProAssurance's gross premiums earned by product as well as a reconciliation to net premiums earned. All gross premiums earned are from external customers except as noted. ProAssurance's insured risks are primarily within the United States.

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
Specialty P&C Segment				
Gross premiums earned:				
Healthcare professional liability	$120,623	$128,532	$361,179	$382,678
Legal professional liability	7,145	6,849	21,147	20,328
Medical technology and life sciences products liability	9,258	8,436	27,043	24,442
Other	420	463	1,445	1,336
Ceded premiums earned*	(13,655)	(10,682)	(36,110)	(30,256)
Segment net premiums earned	$123,791	$133,598	$374,704	$398,528
Workers' Compensation Segment				
Gross premiums earned:				
Traditional business	$42,345	$—	$119,702	$—
Alternative market business	14,345	—	40,253	—
Ceded premiums earned	(6,898)	—	(15,995)	—
Segment net premiums earned	$49,792	$—	$143,960	$—
Lloyd's Syndicate Segment				
Gross premiums earned:				
Property and casualty*	$4,085	$—	$7,110	$—
Ceded premiums earned	(640)	—	(713)	—
Segment net premiums earned	$3,445	$—	$6,397	$—
Consolidated net premiums earned	$177,028	$133,598	$525,061	$398,528

* Includes premium ceded from the Specialty P&C Segment to the Lloyd's Syndicate Segment of $1.1 million for the three months and $1.6 million for nine months ended September 30, 2014, respectively.

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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 the Condensed Consolidated Financial Statements and Notes to those statements which accompany this report. A glossary of insurance terms and phrases is available on the investor section of our website. Throughout the discussion, references to "ProAssurance," "PRA," "Company," "we," "us" and "our" refer to ProAssurance Corporation and its consolidated subsidiaries. The discussion contains certain forward-looking information that involves risks and uncertainties. As discussed under the heading "Forward-Looking Statements," our actual financial condition and operating results could differ significantly from these forward-looking statements.

Overview

We report our results in four distinct segments, based on the operational focus of the segment. Our Specialty Property and Casualty (Specialty P&C) segment includes both our professional liability business and our medical technology and life sciences business. Our Workers' Compensation segment includes the business acquired through our January 1, 2014 purchase of Eastern and includes workers' compensation insurance for employers, groups and associations. Our Lloyd's Syndicate segment includes operating results from our participation in Lloyd's Syndicate 1729, which began operations January 1, 2014. Information regarding Lloyd's operations derived from U.K. based entities is reported on a quarter delay, although investment results associated with our Funds at Lloyd's (FAL) investments are reported concurrently as those results are available on an earlier time frame. Our Corporate segment includes our U.S. investment operations which are managed at the corporate level, non-premium revenues generated outside of our insurance entities, corporate expenses, interest and U.S. income taxes. Additional information regarding our segments is included in Note 13 of the Notes to Condensed Consolidated Financial Statements and in Part I of our 2013 Form 10K.

Critical Accounting Estimates

Our Condensed Consolidated Financial Statements are prepared in conformity with U.S. generally accepted accounting principles (GAAP). Preparation of these financial statements requires us to make estimates and assumptions that affect the amounts we report on those statements. We evaluate these estimates and assumptions on an ongoing basis based on current and historical developments, market conditions, industry trends and other information that we believe to be reasonable under the circumstances. There can be no assurance that actual results will conform to our estimates and assumptions; reported results of operations may be materially affected by changes in these estimates and assumptions.

Management considers the following accounting estimates to be critical because they involve significant judgment by management and the effect of those judgments could result in a material effect on our financial statements.

Reserve for Losses and Loss Adjustment Expenses

The largest component of our liabilities is our reserve for losses and loss adjustment expenses ("reserve for losses" or "reserve"), and the largest component of expense for our operations is incurred losses and loss adjustment expenses (also referred to as "losses and loss adjustment expenses," "incurred losses," "losses incurred," and "losses"). Incurred losses reported in any period reflect our estimate of losses incurred related to the premiums earned in that period as well as any changes to our previous estimate of the reserve required for prior periods.

As of September 30, 2014 our reserve is almost entirely comprised of long-tail risk exposures. The estimation of long-tailed insurance losses is inherently difficult and is subject to significant judgment on the part of management. Due to the nature of our claims, our loss costs, even for claims with similar characteristics, can vary significantly depending upon many factors including the specific characteristics of the claim and the manner in which the claim is resolved. Long-tailed insurance is characterized by the extended period of time typically required to assess the viability of a claim, potential damages, if any, and then to reach a resolution of those claims. For ProAssurance the claims resolution process often extends to more than five years. The combination of continually changing conditions and the extended time required for claim resolution results in a loss cost estimation process that requires actuarial skill and the application of significant judgment, and such estimates require periodic revision.

Our reserve is established by management after taking into consideration a variety of factors including premium rates, claims frequency, historical paid and incurred loss development trends, the expected effect of inflation, general

economic trends, the legal and political environment, and the conclusions reached by our internal and consulting actuaries. We update and review the data underlying the estimation of our reserve for losses each reporting period and make adjustments to loss estimation assumptions that we believe best reflect emerging data. Both our internal and consulting actuaries perform an in-depth review of our reserve for losses on at least a semi-annual basis using the loss and exposure data of our insurance subsidiaries, supplemented to the extent necessary by relevant industry loss and exposure data. In periods in which business combinations occur, we must also establish reserves for the loss exposures assumed.

Our reserving process can be broadly grouped into three areas: the establishment of the initial reserve for risks assumed in business combinations (the acquired reserve), the establishment of the reserve for the current accident year (the initial reserve) and the re-estimation of the reserve for prior accident years (development of prior accident years).

Acquired Reserve

The acquisition of Eastern increased our loss reserve by $153.2 million which represented the fair value of Eastern's loss reserve at the time of the acquisition. The fair value of the reserve for losses and loss adjustment expenses and related reinsurance recoverables was based on an actuarial estimate of the expected future net cash flows, a reduction of those cash flows for the time value of money determined utilizing the U.S. Treasury Yield Curve, and a risk adjustment to reflect the net present value of profit that an investor would demand in return for the associated risks. Expected net cash flows were derived from the expected loss payment patterns included in an actuarial analysis of Eastern's reserve performed as of December 31, 2013. Actuarial methods used to evaluate Eastern's reserve included the Bornhuetter-Ferguson Method (Paid and Reported) and the Development Method (Paid and Reported) described in our Critical Accounting Estimates section in Item 7 of our 2013 Form 10K. The fair value of the reserve, reflecting the risk margin discussed above, exceeded the undiscounted loss reserve previously established by Eastern by $9.3 million; this fair value adjustment is being amortized over the average expected life of the reserve of 6 years.

Initial Reserve-Current Accident Year

Considerable judgment is required in establishing our initial reserve for any current accident year period, as there is limited open or closed claims data available for a current accident year period at the time the reserve for that period is estimated. Our process for setting an initial reserve considers the unique characteristics of each line of business, but in general we rely heavily on the loss assumptions that were used to price business during the accident year, as our pricing reflects our analysis of loss costs that we expect to incur relative to the business being priced.

Specialty P&C Segment. Professional and product liability loss costs are impacted by many factors, including but not limited to, the nature of the claim, including whether or not the claim is an individual or a mass tort claim, the personal situation of the claimant or the claimant's family, the outcome of jury trials, the legislative and judicial climate where any potential litigation may occur, general economic conditions and, for claims involving bodily injury, the trend of healthcare costs. Within our Specialty P&C segment, for our healthcare professional liability (HCPL) business (63% of consolidated gross premiums earned for the nine months ended September 30, 2014) we set an initial reserve using the average loss ratio used in our pricing, plus an additional provision in consideration of the historical loss volatility we and others in the industry have experienced. For our HCPL business, our target loss ratio during recent accident years has approximated 75%, and the provision for loss volatility has ranged from 8 to 10 percentage points, producing an overall average initial loss ratio for our HCPL business of approximately 85%. We believe use of a provision for volatility considers inherent risks associated with our rate development process and the historic volatility of professional liability losses (the industry has experienced accident year loss ratios as high as 163% and as low as 53% over the past 30 years) and produces a reasonable best estimate of the reserve required to cover actual ultimate unpaid losses. A similar practice is followed for our legal professional liability business (4% of consolidated gross premiums earned for the nine months ended September 30, 2014). The risks insured in our medical technology and life sciences products liability business (5% of consolidated gross premiums earned for the nine months ended September 30, 2014) are more varied, and policies are individually priced based on the risk characteristics of the policy. Therefore, for this business we establish an initial reserve using our most recently developed actuarial estimates of losses expected to be incurred based on factors which include: results from prior analysis of similar business, industry indications, observed trends and judgment. The products liability line of business exhibits similar volatility to HCPL, and the actuarial estimate includes a provision for volatility.

Severity is defined as the average cost of resolving claims, and the severity trend is the increase or decrease in severity from period to period. The severity trend assumption is a key assumption for both pricing models and the actuarial estimation of our reserve. The severity trend is an explicit component of our pricing models, whereas in our reserving process the severity trend's impact is implicit. Our estimate of this trend and our expectations about changes in this trend impact a variety of factors, from the selection of expected loss ratios to the ultimate point estimates established by management.

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Because of the implicit and wide-ranging nature of severity trend assumptions on the loss reserving process, it is not practical to specifically isolate the impact of changing severity trends. However, because severity is an explicit component of our HCPL pricing process, we can better isolate the impact that changing severity can have on our loss costs and loss ratios as regards our pricing models for this business component. Our current HCPL pricing models assume a severity trend of 2% to 3% in most states and lines of business. If the severity trend were to be higher by 1 percentage point, the impact would be an increase in our expected loss ratio for this business of 3.2 percentage points, based on current claim disposition patterns. An increase in the severity trend of 3 percentage points would result in a 10.1 percentage point increase in our expected loss ratio. Due to the long tailed nature of our claims and the previously discussed historical volatility of loss costs, selection of a severity trend assumption is a subjective process that is inherently likely to prove inaccurate over time. Given the long tail and volatility, we are generally cautious in making changes to the severity assumptions within our pricing models. Also of note is that all open claims and accident years are generally impacted by a change in the severity trend, which compounds the effect of such a change.

For the 2004 to 2009 accident years, both our internal and consulting actuaries observed an unprecedented reduction in the frequency of HCPL claims (or number of claims per exposure unit) that cannot be attributed to any single factor. We believe that much of the reduction in claim frequency is the result of a decline in the filing of non-meritorious lawsuits that have historically been dismissed or otherwise resulted in no payment of indemnity on behalf of our insureds. With fewer non-meritorious claims being filed we expect that the claims that are filed have the potential for greater average losses, or greater severity. As a result, we cannot be certain as to the impact this decline will ultimately have on the average cost of claims, which has complicated the selection of an appropriate severity trend for our pricing models for these lines. It has also made it more challenging to factor severity into the various actuarial methodologies we use to evaluate our reserve. Based on a weighted average of payments, 85% of our HCPL claims are resolved after eight years for a given accident year. Due to this long tail, we continue to be uncertain of the full impact of the observed decline in frequency and whether the expected increase in severity will materialize.

Although we remain uncertain regarding the ultimate severity and frequency trends to project into the future due to the long-tailed nature of our business, we have given consideration to both factors in setting our rates. For our HCPL business this practice has resulted in rate reductions in recent years. For example, on average, excluding our podiatry business acquired in 2009, we have gradually reduced the premium rates we charge on our standard physician renewal business (our largest HCPL line) by approximately 17% from the beginning of 2006 to September 30, 2014. Loss ratios for the current accident years have thus remained fairly constant because expected loss reductions have been reflected in our rates.

Workers' Compensation Segment. Many factors affect the ultimate losses incurred for our workers' compensation coverages (28% of consolidated gross premiums earned for the nine months ended September 30, 2014), including, but not limited to, the type of injury, treatments available for the injury as well as the cost of those treatments, the responsiveness of the worker and the employer to rehabilitation plans, the willingness of claimants to settle claims, the involvement of attorneys, and inflation or deflation of healthcare costs. We do not measure and estimate values for all of these variables individually due to the difficulty of directly measuring the impact of individual factors. Rather, we rely on historical experience to select an expected loss ratio for various premium groupings, based on rate changes, type and geographic location of the insured. We perform an analysis of claims data quarterly and use the information obtained from this analysis to assist us in selecting an expected loss ratio.

Development of Prior Accident Years

We re-evaluate the reserve for prior accident years each period based on our most recently available claims data and currently available industry trend information. Changes to previously established reserve estimates are recognized in the current period if management’s best estimate of ultimate losses differs from the estimate previously established. While management considers a variety of variables in determining its best estimate, in general, as claims age, our methodologies give more weight to actual loss costs which, as a whole, continue to indicate that ultimate loss costs will be lower than our previous estimates. The discussion in our Critical Accounting Estimates section in Item 7 of our 2013 Form 10K includes additional information regarding the methodologies used to evaluate our reserve.

Any change in our estimate of net ultimate losses for prior years is reflected in net income in the period in which such changes are made. Over the past several years such changes have reduced our estimate of net ultimate losses, resulting

in a reduction of reported losses for the period and a corresponding increase in pre-tax income.
We recognized net favorable reserve development of $42.9 million during the three months ended September 30, 2014, of which $42.3 million related to our Specialty P&C segment and $0.6 million related to our Workers' Compensation segment. During the nine months ended September 30, 2014, we recognized net favorable reserve development of $133.3 million, of which $130.4 million related to our Specialty P&C segment and $2.9 million related to our Workers' Compensation segment. The development recognized within the Specialty P&C segment was primarily attributable to the favorable resolution of HCPL

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claims during the period and an evaluation of established case reserves and paid claims data that indicated that the actual severity trend associated with the remaining HCPL claims continues to be less than we had previously estimated. Development recognized within our Workers' Compensation segment includes amortization of the purchase accounting fair value adjustment of $0.4 million and $1.2 million for the three and nine months ended September 30, 2014, respectively; the remaining development of $0.2 million and $1.7 million for the three- and nine-month periods, respectively, was attributable to our segregated portfolio cells (SPCs) which are evaluated at the cell level. Because a relatively small number of claims are open per cell, the closing of claims can affect the actuarial projections for the remaining open claims in the cell to an extent that indicates development should be recognized for the cell.

Due to the size of our consolidated reserve for losses and the large number of claims outstanding at any point in time, even a small percentage adjustment to our total reserve estimate could have a material effect on our results of operations for the period in which the adjustment is made.

Investment Valuations

We record the majority of our investments at fair value as shown in the table below. At September 30, 2014 the distribution of our investments based on GAAP fair value hierarchies (levels) was as follows:

	Distribution by GAAP Fair Value Hierarchy			September 30, 2014
	Level 1	Level 2	Level 3	Total Investments
Investments recorded at:				
Fair value	10%	80%	4%	94%
Other valuations				6%
Total Investments				100%

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 at the measurement date. All of our fixed maturity and equity security investments are carried at fair value. Our short-term securities are carried at amortized cost, which approximates fair value.

Because of the number of securities we own and the complexity and cost of developing accurate fair values, we utilize multiple independent pricing services to assist us in establishing the fair value of individual securities. The pricing services provide fair values based on exchange traded prices, if available. If an exchange traded price is not available, the pricing services, if possible, provide a fair value that is based on multiple broker/dealer quotes or that has been developed using pricing models. Pricing models vary by asset class and utilize currently available market data for securities comparable to ours to estimate the fair value for our security. The pricing services scrutinize market data for consistency with other relevant market information before including the data in the pricing models. The pricing services disclose the types of pricing models used and the inputs used for each asset class. Determining fair values using these pricing models requires the use of judgment to identify appropriate comparable securities and to choose a valuation methodology that is appropriate for the asset class and available data.

The pricing services provide a single value per instrument quoted. We review the values provided for reasonableness each quarter by comparing market yields generated by the supplied value versus market yields observed in the market place. We also compare yields indicated by the provided values to appropriate benchmark yields and review for values that are unchanged or that reflect an unanticipated variation as compared to prior period values. In addition, we compare provided information for consistency with our other pricing services, known market data and information from our own trades, considering both values and valuation trends. We also review weekly trades versus the prices supplied by the services. If a supplied value appears unreasonable, we discuss the valuation in question with the pricing service and make adjustments if deemed necessary. To date, our review has not resulted in any changes to the values supplied by the pricing services.

The pricing services do not provide a fair value unless an exchange traded price or multiple observable inputs are available. As a result, the pricing services may provide a fair value for a security in some periods but not others, depending upon the level of recent market activity for the security or comparable securities.

Level 1 Investments

Fair values for our equity securities and a portion of our convertible securities and short-term securities are determined using exchange traded prices. There is little judgment involved when fair value is determined using an exchange traded price. In accordance with GAAP, for disclosure purposes we classify securities valued using an exchange traded price as Level 1 securities.

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Level 2 Investments

Most fixed income securities do not trade daily, and thus exchange traded prices are generally not available for these securities. However, market information (often referred to as observable inputs or market data, including but not limited to, last reported trade, non-binding broker quotes, bids, benchmark yield curves, issuer spreads, two sided markets, benchmark securities, offers and recent data regarding assumed prepayment speeds, cash flow and loan performance data) is available for most of our fixed income securities. We determine fair value for a large portion of our fixed income securities using available market information. In accordance with GAAP, for disclosure purposes we classify securities valued based on multiple market observable inputs as Level 2 securities.

Level 3 Investments

When a pricing service does not provide a value for one of our fixed maturity securities, management estimates fair value using either a single non-binding broker quote or pricing models that utilize market based assumptions which have limited observable inputs. The process involves significant judgment in selecting the appropriate data and modeling techniques to use in the valuation process. For disclosure purposes we classify fixed maturity securities valued using limited observable inputs as Level 3 securities.

We also classify as Level 3 our investment interests that are carried at equity, valued using a fund-provided net asset value (NAV) for our interest, which approximates fair value. All investments valued in this manner are LP or LLC interests that hold debt and equity securities. At September 30, 2014 interests valued using a fund-provided NAV totaled $110.8 million, or 3% of total investments, and were classified as part of our Investment in Unconsolidated Subsidiaries.

Investments - Other Valuation Methodologies

Certain of our investments, in accordance with GAAP for the type of investment, are measured using methodologies other than fair value. At September 30, 2014 these investments represented approximately 6% of total investments and are detailed in the following table. Additional information about these investments is provided in Notes 3 and 4 of the Notes to Condensed Consolidated Financial Statements.

(In millions)	Carrying Value	GAAP Measurement Method
Other investments:		
Investments in LPs, at cost	$57.6	Cost
Other, principally Federal Home Loan Bank capital stock	4.4	Cost
Total other investments	62.0	
Investment in unconsolidated subsidiaries:		
Investments in tax credit partnerships	137.4	Equity
Equity method LPs/LLCs	6.8	Equity
Total investment in unconsolidated subsidiaries	144.2	
Business owned life insurance	55.9	Cash surrender value
Total investments - Other valuation methodologies	$262.1	

Investment Impairments

We evaluate our investments on at least a quarterly basis for declines in fair value that represent other than temporary impairment (OTTI). We consider an impairment to be an OTTI if we intend to sell the security or if we believe we will be required to sell the security before we fully recover the amortized cost basis of the security. Otherwise, we consider various factors in our evaluation, as discussed below.

For debt securities, we consider whether we expect to fully recover the amortized cost basis of the security, based upon consideration of some or all of the following:

- third party research and credit rating reports;
- the current credit standing of the issuer, including credit rating downgrades;
- the extent to which the decline in fair value is attributable to credit risk specifically associated with the security or its issuer;

- our internal assessments and those of our external portfolio managers regarding specific circumstances surrounding a security, which can cause us to believe the security is more or less likely to recover its value than other securities with a similar structure;
- for asset-backed securities, the origination date of the underlying loans, the remaining average life, the probability that credit performance of the underlying loans will deteriorate in the future, and our assessment of the quality of the collateral underlying the loan;
- failure of the issuer of the security to make scheduled interest or principal payments;
- any changes to the rating of the security by a rating agency;
- recoveries or additional declines in fair value subsequent to the balance sheet date; and
- our intent to sell and whether it is more likely than not we will be required to sell the security before the recovery of its amortized cost basis.

In assessing whether we expect to recover the cost basis of debt securities, particularly asset-backed securities, we must make a number of assumptions regarding the cash flows that we expect to receive from the security in future periods. These judgments are subjective in nature and may subsequently be proved to be inaccurate.

We evaluate our cost method interests in LPs/LLCs for OTTI by considering whether there has been a decline in fair value below the recorded value, which involves assumptions and estimates. We receive a report from each of the LPs/LLCs at least quarterly which provides us a NAV for our interest. The NAV is based on the fair values of securities held by the LP/LLC as determined by the LP/LLC manager. We consider the most recent NAV provided, the performance of the LP/LLC relative to the market, the stated objectives of the LP/LLC, the cash flows expected from the LP/LLC and audited financial statements of the entity, if available, in considering whether an OTTI exists.

Our investments in tax credit partnerships are evaluated for OTTI by considering both qualitative and quantitative factors which include: whether cash flows currently expected from the investment, primarily tax benefits, equal or exceed the carrying value of the investment, whether currently expected cash flows are less than those expected at the time the investment was acquired, and our ability and intent to hold the investment until the recovery of its carrying value.

We also evaluate our holdings of Federal Home Loan Bank (FHLB) securities for impairment. We consider the current capital status of the FHLB, whether the FHLB is in compliance with regulatory minimum capital requirements, and the FHLB’s most recently reported operating results.

Deferred Policy Acquisition Costs

Policy acquisition costs (primarily commissions, premium taxes and underwriting salaries) which are directly related to the successful acquisition of new and renewal premiums are capitalized as deferred policy acquisition costs and charged to expense, net of ceding commissions earned, as the related premium revenue is recognized. We evaluate the recoverability of our deferred policy acquisition costs each reporting period, and any amounts estimated to be unrecoverable are charged to expense in the current period. As of September 30, 2014 we have not determined that any amounts are unrecoverable.

ProAssurance's fair value estimate of the value of business acquired (VOBA), calculated as the present value of future earnings expected from the insurance contracts acquired, approximated the carrying value of Eastern's asset for deferred policy acquisition costs as of the acquisition date. Consequently, Eastern's asset for deferred policy acquisition costs was recognized in the purchase price allocation in lieu of recognizing an intangible asset for VOBA.

Deferred Taxes

Deferred federal income taxes arise from the recognition of temporary differences between the bases of assets and liabilities determined for financial reporting purposes and the bases determined for income tax purposes. Our temporary differences principally relate to our loss reserve, unearned premiums, deferred policy acquisition costs, unrealized investment gains (losses), and basis differences on investment assets. Deferred tax assets and liabilities are measured using the enacted tax rates expected to be in effect when such benefits are realized. We review our deferred tax assets quarterly for impairment. If we determine that it is more likely than not that some or all of a deferred tax asset will not be realized, a valuation allowance is recorded to reduce the carrying value of the asset. In assessing the need for a valuation allowance, management is required to make certain judgments and assumptions about our future

operations based on historical experience and information as of the measurement period regarding reversal of existing temporary differences, carryback capacity, future taxable income (including its capital and operating characteristics) and tax planning strategies. We did not have any significant valuation allowances as of September 30, 2014.

Unrecognized Tax Benefits
We evaluate tax positions taken on tax returns and recognize positions in our financial statements when it is more likely than not that we will sustain the position upon resolution with a taxing authority. If recognized, the benefit is measured as the largest amount of benefit that has a greater than fifty percent probability of being realized. We review uncertain tax positions each period, considering changes in facts and circumstances, such as changes in tax law, interactions with taxing authorities and developments in case law, and make adjustments as we consider necessary. Adjustments to our unrecognized tax benefits may affect our income tax expense, and settlement of uncertain tax positions may require the use of cash. At September 30, 2014, our liability for unrecognized tax benefits approximated $0.6 million.
Goodwill
Management evaluates the carrying value of goodwill annually as of October 1st. If, at any time during the year, events occur or circumstances change that would more likely than not reduce the fair value below the carrying value, we also evaluate goodwill at that time. As of October 1, 2013 we evaluated goodwill as assigned to one reporting unit because, at that time, we operated as a single operating segment and all of our segment components were economically similar. We estimated the fair value of our reporting unit on the evaluation date based on market capitalization and an expected premium that would be paid to acquire control of our Company (a control premium). We then performed a sensitivity analysis using a range of historical stock prices and control premiums. Based on this evaluation, we concluded that the fair value of our reporting unit exceeded the carrying value and no adjustment to impair goodwill was necessary. As of January 1, 2014, due to the acquisition of Eastern and commencement of operations by Syndicate 1729, we are operating in multiple segments and future evaluations of goodwill will reflect multiple reporting units consistent with our segment structure. Note 13 of the Notes to Condensed Consolidated Financial Statements provides additional information regarding our segments.
Goodwill is recognized in conjunction with acquisitions as the excess of the purchase consideration for the acquisition over the fair value of identifiable assets acquired and liabilities assumed. The fair value of identifiable assets and liabilities, and thus goodwill, is subject to redetermination within a measurement period of up to one year following completion of an acquisition.
Intangibles
Intangible assets with definite lives are amortized over the estimated useful life of the asset. Amortizable intangible assets primarily consist of agency and policyholder relationships, renewal rights and trade names. Intangible assets with an indefinite life, primarily state licenses, are not amortized. Increases in both amortizable and non-amortizable intangible assets during 2014 were attributable to intangible assets recognized related to the 2014 acquisition of Eastern. Intangible assets are evaluated for impairment on an annual basis. Additional information regarding intangible assets is included in Note 1 of the Notes to Condensed Consolidated Financial Statements.
Audit Premium
Workers' compensation premiums are determined based upon the payroll of the insured, the applicable premium rates and, where applicable, an experience based modification factor. An audit of the policyholders' records is conducted after policy expiration to make a final determination of applicable premiums. Audit premium due from or due to a policyholder as a result of an audit is reflected in net premiums earned when billed. We track, by policy, the amount of additional premium billed in final audit invoices as a percentage of payroll exposure and use this information to estimate the probable additional amount of earned, but unbilled, (EBUB) premium as of the balance sheet date. We include changes to the EBUB premium estimate in net premiums earned in the period recognized.
Accounting Changes
We are not aware of any accounting changes not yet adopted as of September 30, 2014 that would have a material effect on our results of operations or financial position. Note 1 of the Notes to Condensed Consolidated Financial Statements provides additional detail regarding accounting changes.

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Liquidity and Capital Resources and Financial Condition

Overview

ProAssurance Corporation is a holding company and is a legal entity separate and distinct from its subsidiaries. The holding company has no business operations apart from its investment operations, thus dividends from its operating subsidiaries represent a significant source of funds for its obligations, including debt service and shareholder dividends. At September 30, 2014, we held cash and liquid investments of approximately $263.2 million outside our insurance subsidiaries that were available for use without regulatory approval. Our holding company also has $200 million available under a revolving credit agreement, as discussed in this section under the heading "Debt."

Dividends that may be or have been paid by our insurance subsidiaries during 2014 are as follows:

($ in thousands)	2014
Dividends available to be paid in 2014 without regulatory approval	$260,300
Ordinary dividends paid or declared in 2014:	
Paid during nine months ended 9/30/14	$(62,500)
Declared dividends unpaid at 9/30/14	$(166,200)
Dividends available to be paid during remainder of 2014 without regulatory approval	$31,600
Extraordinary dividends during 2014:	
Paid during during October 2014	$(50,000)
Submitted for approval in 2014 but not yet paid	$(6,300)

Operating Activities and Related Cash Flows

The principal components of our operating cash flows are the excess of premiums collected and net investment income over losses paid and operating costs, including income taxes. Timing delays exist between the collection of premiums and the payment of losses associated with the premiums. Premiums are generally collected within the twelve-month period after the policy is written, while our claim payments are generally paid over a more extended period of time. Likewise, timing delays exist between the payment of claims and the collection of any associated reinsurance recoveries.

Our operating activities provided cash of approximately $101.1 million and $24.0 million for the nine months ended September 30, 2014 and 2013, respectively. The table below summarizes changes in our operating cash flows as compared to the prior year.

(In Millions)	Operating Cash Flow 2014 vs 2013	2013 vs 2012
Cash provided (used) by operating activities for the nine months ended September 30, 2013 and 2012, respectively	$24	$61
Increase (decrease) in operating cash flows:		
Increase (decrease) in premium receipts (1)	(15)	(28)
(Increase) decrease in payments to reinsurers (2)	(10)	(6)
(Increase) decrease in losses paid, net of reinsurance recoveries (3)	9	14
Increase (decrease) in deposit contracts (4)	—	(5)
Increase (decrease) in cash received from investments (5)	(12)	(1)
(Increase) decrease in cash paid for other expenses and operating liabilities (6)	4	(1)
(Increase) decrease in cash paid for interest (7)	(6)	1
(Increase) decrease in Federal and state income tax payments (8)	85	(1)
Net cash flows provided (used) by acquisitions completed during 2014 and 2013, respectively, and, in 2014, net cash flows from our participation in Syndicate 1729 (9)	21	(11)
Other amounts not individually significant, net	1	1
Cash provided (used) by operating activities for the nine months ended September 30, 2014 and September 30, 2013, respectively	$101	$24

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(1) The reduction in premium receipts for both 2014 and 2013 reflected lower premium volume during the preceding twelve month periods, exclusive of the effect of acquisitions.

(2) The increase in payments to reinsurers for both 2014 and 2013 was primarily attributable to expansion of our shared risk arrangements and, for 2014, to payments made pursuant to our quota share reinsurance agreement with Syndicate 1729. Our 58% share of Syndicate 1729 net cash flows, reported in item 9 below, reflects receipt of these payments. See the discussion in the Premiums section for our Specialty P&C segment under the heading "Ceded Premiums Written" for additional information.

(3) The timing of our net loss payments varies from period to period because the process for resolving claims is complex and occurs at an uneven pace depending upon the circumstances of the individual claim. The reduction in loss payments for both 2014 and 2013 primarily related to the number of large settlements paid and the timing of reinsurance collections on those settlements as compared to claim settlement activity in the prior year.

(4) We are party to certain contracts that involve claims handling but do not transfer insurance risk. These contracts do not constitute a significant business activity for us, but did reduce cash flows in 2013 as compared to 2012.

(5) The decline in cash received from investments for 2014 primarily reflects lower receipts from our fixed income securities.

(6) Settlements of certain operating liabilities were lower in 2014 than in 2013 primarily due to timing differences. Also, approximately $2.2 million of the 2014 decrease in other expenses was attributable to transaction costs paid in 2013 for a business combination completed in 2013. Transaction costs paid in 2014 for a business combination completed in 2014 are included in item 9 below.

(7) The increase in cash paid for interest during 2014 is primarily due to a higher interest rate on a greater amount of outstanding long-term debt as compared to 2013.

(8) The decrease in net tax payments during 2014 as compared to those made in 2013 primarily reflected the following:

- Tax refunds totaling $30.6 million, exclusive of interest, received in 2014 related to an Internal Revenue Service (IRS) examination, as discussed in further detail in this section under the heading "Taxes." The refunds included the return of a $20.6 million protective tax payment made in 2013.
- Final tax payments made during 2014 for the prior fiscal year were $29.1 million lower than those made in 2013.
- Estimated tax payments for the current fiscal year were $7.1 million lower during 2014 than those made in 2013.

The net increase in tax payments during 2013 as compared to those made in 2012 primarily reflected the following:

- A $20.6 million protective tax payment made in 2013 as noted above. No such payment was made in 2012.
- Final tax payments made during 2014 for the prior fiscal year were $8.3 million lower than those made in 2012.
- Estimated tax payments for the current fiscal year were $7.9 million lower during 2013 than those made in 2012.

(9) Operations acquired in 2014 as a part of the Eastern transaction produced positive operating cash flows of approximately $22.0 million in 2014. Our Lloyd's Syndicate operations used operating cash flows of approximately $1.3 million, primarily due to the payment of start-up expenses.

Operations acquired in 2013 used cash of approximately $11.0 million, primarily due to the payment of transaction costs, the payment of several large prior accident year claims, and normal expenses for which the timing of the payment differed from the recognition of the expense.

Reinsurance

Within our Specialty P&C segment, we use insurance and reinsurance (collectively, "reinsurance") to provide capacity to write larger limits of liability, to provide reimbursement for losses incurred under the higher limit coverages we offer, to provide protection against losses in excess of policy limits, and, in the case of risk sharing arrangements, to provide custom insurance solutions for large customer groups. Within our Workers' Compensation segment, we use reinsurance to reduce our net liability on individual risks, to mitigate the effect of significant loss occurrences (including catastrophic events), to stabilize underwriting results, and to increase underwriting capacity by decreasing leverage. The purchase of reinsurance does not relieve us from the ultimate risk on our policies, but it does provide reimbursement for certain losses we pay.

Within our Specialty P&C segment, we generally reinsure professional liability risks under annual treaties (our excess of loss reinsurance arrangements) pursuant to which the reinsurers agree to assume all or a portion of all risks that we

insure above our individual risk retention of $1 million per claim, up to the maximum individual limit offered. Historically, our professional liability per claim retention level has been 100% of the first $1 million of coverage and up to 15% of claims exceeding those levels depending on the coverage year and the state in which business was written. Large professional liability

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risks that are above the limits of our basic reinsurance treaties are reinsured on a facultative basis, whereby the reinsurer agrees to insure a particular risk up to a designated limit. We also have in place a number of risk sharing arrangements that apply to the first $1 million of losses for certain large healthcare systems and other insurance entities. Medical technology and life sciences products coverages are separately reinsured; subsequent to 2010, retention has been 100% on the first $1 million of coverage and between 20% and 33% of coverage exceeding those levels.

There are also in place various older reinsurance contracts acquired as a part of business combinations. The structure of these acquired arrangements typically reflects a lower retention level than our excess of loss reinsurance arrangements.

Within our Workers' Compensation segment, our traditional business is reinsured under an excess of loss arrangement under which the Company retains the first $500,000 on each loss occurrence. Loss occurrences in excess of $500,000 are covered up to a maximum of $149.5 million per occurrence.

Over 90% of the alternative market business within our Workers' Compensation segment is fully reinsured under 100% quota share agreements to the SPC's of our wholly owned subsidiary, Eastern Re Ltd., SPC (Eastern Re), domiciled in the Cayman Islands, net of a ceding commission. Each SPC has preferred shareholders and the underwriting profit or loss of each cell accrues fully to these preferred shareholders. We participate as a preferred shareholder in certain SPC's. Our ownership interest in the segregated portfolio cells for which we participate is generally 50%, but we have ownership interests as low as 25% and as high as 82.5%. Each SPC has in place its own reinsurance arrangements:

- Each cell has an aggregate excess reinsurance agreement with another of our insurance subsidiaries. This agreement provides for cession of 100% of losses of the cell which exceed a specified attachment point (typically 89% of premiums assumed), up to a maximum of $100,000.
- For losses that exceed the attachment point, each segregated portfolio cell further purchases two types of external reinsurance coverage:
- Per occurrence reinsurance agreements cover each SPC for a catastrophic claim resulting from one event with respect to its SPC business. The specific retentions for per occurrence coverage for an SPC range from $300,000 to $350,000, with limits of approximately $149.5 million. For example, in the case of an SPC with a $300,000 retention that has a $3.0 million claim relating to the injury and/or death of a covered employee, the SPC would cover the first $300,000 of the claim with the third party reinsurer paying the remaining $2.7 million in claims.
- Aggregate reinsurance agreements cover each SPC for losses and LAE beyond the $100,000 aggregate coverage provided by us. The need for this coverage would arise in the event of a series of losses as opposed to a single, catastrophic event. Aggregate reinsurance coverage purchased through external reinsurers has ultimate loss limits of $1.0 million or $2.0 million, depending on the underlying risks. This external reinsurance combined with the aggregate coverage provided by us provides aggregate loss limits for each segregated portfolio cell ranging from $1.1 million to $2.1 million.

Each SPC maintains a loss fund for the cell initially equal to the difference between premium assumed by the cell and the ceding commission. The external participants of each cell provide a letter of credit to us that is equal to the difference between the loss fund (amount of funds available to pay losses after deduction of ceding commission) and the aggregate attachment point of the reinsurance.

Within our Lloyd's Syndicate segment, Syndicate 1729 purchases reinsurance to limit its liability on individual risks and to protect against catastrophic loss. The level of reinsurance that the Syndicate purchases is dependent on a number of factors, including its underwriting risk appetite for catastrophe risk, the specific risks inherent in each line or class of business risk written and the pricing, coverage and terms and conditions available from the reinsurance market. Both quota share reinsurance and excess-of-loss reinsurance is utilized to manage the net loss exposure. The Syndicate may still be exposed to loss that exceeds the level of reinsurance purchased, as well as to reinstatement premiums triggered by additional loss events.

For all of our segments, we make a determination of the amount of insurance risk we choose to retain based upon numerous factors, including our risk tolerance and the capital we have to support it, the price and availability of reinsurance, the volume of business, our level of experience with a particular set of claims and our analysis of the

potential underwriting results. We purchase reinsurance from a number of companies to mitigate concentrations of credit risk. We utilize a reinsurance broker to assist us in the placement of our reinsurance program and in the analysis of the credit quality of our reinsurers. The determination of which reinsurers we choose to do business with is based upon an evaluation of their then-current financial strength, rating and stability. However, the financial strength of our reinsurers, and their corresponding ability to pay us, may change in the future due to forces or events we cannot control or anticipate.

Taxes

In 2013 we received a Notice of Proposed Adjustment (NOPA) from the IRS related to the examination of our 2009 and 2010 tax years. We subsequently protested certain issues in the NOPA, all of which related to the timing of deductions, and also

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made a related $20.6 million protective payment. In April 2014, we reached a final settlement with the IRS on all contested issues, which did not increase our tax liability. We received refunds from the IRS related to the NOPA in July 2014 of $30.6 million in total, exclusive of interest, which included a refund from the settlement of non-contested issues addressed by the NOPA and the return of the protective payment.

Litigation

We are involved in various legal actions related to insurance policies and claims handling including, but not limited to, claims asserted against us by policyholders. These types of legal actions arise in the ordinary course of business and, in accordance with GAAP for insurance entities, are generally considered as a part of our loss reserving process, which is described in detail in our Critical Accounting Estimates section under the heading "Reserve for Losses and Loss Adjustment Expenses." We also have other direct actions against the Company unrelated to our claims activity which we evaluate and account for as a part of our other liabilities. For these corporate legal actions, we evaluate each case separately and establish what we believe is an appropriate reserve based on GAAP guidance related to contingent liabilities. As of September 30, 2014 there were no material reserves established for corporate legal actions.

Investing Activities and Related Cash Flows

Investment Exposures - The following table provides summarized information regarding our investments as of September 30, 2014:

($ in thousands)	Carrying Value	Included in Carrying Value:		Average Rating	(1)	% Total Investments
		Unrealized Gains	Unrealized Losses			
Fixed Maturities						
Government						
U.S. Treasury	$176,813	$ 4,396	$ 1,215	AA+	(2)	4%
U.S. Government-sponsored enterprise	43,966	1,709	223	AA+	(2)	1%
Total government	220,779	6,105	1,438	AA+	(2)	5%
State and Municipal Bonds						
Pre-refunded	152,738	5,990	47	AA		4%
General obligation	281,360	13,882	83	AA		7%
Special revenue	653,536	30,183	569	AA		16%
Total state and municipal bonds	1,087,634	50,055	699	AA		27%
Corporate Debt						
Financial institutions	430,075	12,988	1,161	A		11%
Consumer oriented	303,638	10,869	2,353	BBB+		7%
Utilities/Energy	296,918	11,767	2,636	BBB+		7%
Industrial	418,523	12,944	3,004	BBB+		10%
Other	23,831	326	21	AA		1%
Total corporate debt	1,472,985	48,894	9,175	A-		36%
Securities backed by:						
Agency mortgages	279,755	8,778	1,069	AA+	(2)	7%
Non-agency mortgages	10,559	39	151	AA+		<1%
Agency commercial mortgages	16,893	172	64	AA+	(2)	<1%
Other commercial mortgages	57,323	1,587	117	AAA		1%
Automobile loans	49,845	73	66	AAA		1%
Other asset loans	51,047	273	103	AA+		1%
Total asset-backed securities	465,422	10,922	1,570	AAA		11%
Total fixed maturities	3,246,820	115,976	12,882	A+		80%
Equities						
Financial	75,141	—	—			2%
Utilities/Energy	26,551	—	—			1%
Industrial	54,912	—	—			1%
Consumer oriented	64,912	—	—			2%
Bond funds	53,178	—	—			1%
All Other	31,937	—	—			1%
Total equities	306,631	—	—			8%
Short-Term	94,973	—	—			2%
Business-owned life insurance	55,918	—	—			1%
Investment in Unconsolidated Subsidiaries						
Investment in tax credit partnerships	137,386	—	—			3%
Equity method LPs/LLCs	117,576	—	—			3%
Total investment in unconsolidated subsidiaries	254,962	—	—			6%
Other Investments						
Investments in LPs, carried at cost	57,607	—	—			1%
Convertible securities, at fair value	30,058	—	—			1%

FHLB capital stock and other	4,345	—	—	<1%	
Total other investments	92,010	—	—	2	%
Total Investments	$4,051,314	$ 115,976	$ 12,882	100	%

(1) A weighted average rating is calculated using available ratings from Standard & Poor’s, Moody’s and Fitch. The table presents the Standard & Poor’s rating that is equivalent to the computed average.

(2) The rating presented is the Standard & Poor’s rating rather than the average. The Moody’s rating is Aaa and the Fitch rating is AAA.

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A detailed listing of our investment holdings as of September 30, 2014 is presented in an Investor Supplement we make available in the Investor Relations section of our website, www.proassurance.com, or directly at www.proassurance.com/investorrelations/supplemental.aspx.

We manage our investments to ensure that we will have sufficient liquidity to meet our obligations, taking into consideration the timing of cash flows from our investments, including interest payments, dividends and principal payments, as well as the expected cash flows to be generated by our operations. In addition to the interest and dividends we will receive, we anticipate that between $80 million and $140 million of our investments will mature (or be paid down) each quarter of the next year and become available, if needed, to meet our cash flow requirements. The primary outflow of cash at our insurance subsidiaries is related to paid losses and operating costs, including income taxes. The payment of individual claims cannot be predicted with certainty; therefore, we rely upon the history of paid claims in estimating the timing of future claims payments. To the extent that we may have an unanticipated shortfall in cash we may either liquidate securities or borrow funds under existing borrowing arrangements through our credit facility and the FHLB system. Currently, $200 million is available for use through our credit facility, as discussed in this section under the heading "Debt." Given the duration of our investments, we do not foresee a shortfall that would require us to meet operating cash needs through additional borrowings. Additional information regarding the credit facility is detailed in Note 9 of the Notes to Condensed Consolidated Financial Statements.

Our investment portfolio continues to be primarily composed of high quality fixed income securities with approximately 93% of our fixed maturities being investment grade securities as determined by national rating agencies. The weighted average effective duration of our fixed maturity securities at September 30, 2014 was 3.6 years; the weighted average effective duration of our fixed maturity securities combined with our short-term securities was 3.5 years.

Our acquisition of Eastern added the following to our investment holdings as of January 1, 2014, the date of acquisition:

(In thousands)	
Fixed maturities	$107,131
Equities	65,945
Short-Term	23,931
Equity Method LPs/LLCs	11,994
Convertible Securities	30,139
Total	$239,140

As discussed under the heading "Business Combinations and Ventures" and in Note 4 of the Notes to Condensed Consolidated Financial Statements, our fixed maturity and short term investments include securities deposited with Lloyd's in order to meet our FAL requirement. At September 30, 2014 securities on deposit with Lloyd's included fixed maturities having a fair value of $71.5 million and short term investments with a fair value of $5.7 million.

The carrying value of our tax credit partnerships was approximately $137.4 million at September 30, 2014 and $142.2 million at December 31, 2013. Carrying value reflects our total commitments (both funded and unfunded) to the partnerships, less amortization, since our initial investment. We fund these investments based on funding schedules maintained by the partnerships. During the nine months ended September 30, 2014 and 2013 we funded approximately $8.4 million and $58.8 million, respectively. As of September 30, 2014, approximately $15.7 million of our total commitments to the tax credit partnerships had not yet been funded.

At September 30, 2014 and December 31, 2013 the total carrying value of our investment fund LPs/LLCs was approximately $175.2 million and $119.3 million, respectively, all of which has been funded. During the nine months ended September 30, 2014 and 2013, we funded investment LPs/LLCs, net of capital returned, in the amount of $35.2 million and $8.4 million, respectively. As of September 30, 2014, we had active commitments to investment fund LPs/LLCs of approximately $149.0 million that had not yet been funded. The unfunded commitments will be paid over a period of approximately 5 years as requested by the fund managers.

Business Combinations and Ventures

We acquired 100% of the outstanding common shares of Eastern on January 1, 2014 for cash totaling $205 million. Funds for the transaction were deposited with an intermediate third-party several days prior to the close date.

Additional information related to our acquisition of Eastern is detailed in Note 2 of the Notes to Condensed Consolidated Financial Statements.

Late in 2013, we became a Lloyd's member and a primary (58%) capital provider to Syndicate 1729, which began active operations effective January 1, 2014. We are required to provide capital, referred to as FAL, to support Syndicate 1729. As of December 31, 2013, we met the FAL requirements through a fully secured standby letter of credit (LOC) (£41.9 million or approximately $69.3 million at December 31, 2013) and a deposit of approximately $8.7 million (included in Other assets at December 31, 2013). During the first quarter of 2014 we elected to begin satisfying the FAL requirement by placing securities

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on deposit with Lloyd's (see "Investment Exposures"). We subsequently canceled the LOC and our deposit was returned. Funds which had secured the LOC (classified as restricted cash at December 31, 2013) were also returned to us during the first quarter of 2014. We anticipate our FAL requirement for the 2015 underwriting year will be approximately £50.9 million, which would require us to fund an additional £5.8 million (approximately $9.8 million if funded with U.S. currency) during 2014. As discussed in Note 8 of the Notes to Condensed Consolidated Financial Statements, we have agreed to provide Syndicate 1729 with operating funds of up to £10 million (approximately $16 million at September 30, 2014) under an unconditional revolving credit agreement (the Credit Agreement). As of September 30, 2014, we had advanced £5.5 million ($9.2 million) to Syndicate 1729 under the Credit Agreement.

Financing Activities and Related Cash Flows

Treasury Shares

We repurchased approximately 3.7 million common shares, having a total cost of approximately $167.2 million, during the nine months ended September 30, 2014 (including approximately 1.0 million shares at a total cost of $45.0 million during the three months ended September 30, 2014). During the nine months ended September 30, 2013 we repurchased approximately 0.2 million shares, having a total cost of approximately $8.0 million, all in the third quarter period. In May 2014 our Board increased its authorization for the repurchase of common shares or the retirement of outstanding debt by $100 million. Subsequent to September 30, 2014, through our 10b5-1 plan, we reacquired an additional 551,000 common shares at a cost of approximately $24.8 million. As of October 31, 2014 our remaining Board authorization was approximately $111.9 million.

Shareholder Dividends

Our Board of Directors declared cash dividends of $0.30 per share during each of the first three quarters of 2014 and $0.25 per share during each of the first three quarters of 2013. During the nine months ended September 30, 2014 we paid the dividends declared in first and second quarters of 2014, as well as the dividends declared in the fourth quarter of 2013. During the nine months ended September 30, 2013 we paid only the 2013 first and second quarter dividends as payment of the dividends declared in fourth quarter 2012 was accelerated to December 2012. Any decision to pay future cash dividends is subject to the Board’s final determination after a comprehensive review of financial performance, future expectations and other factors deemed relevant by the Board.

Debt

At September 30, 2014 our long-term debt consisted of $250 million of outstanding unsecured senior notes. The notes bear interest at 5.3% annually and are due in 2023 although they may be redeemed in whole or part prior to maturity. There are no financial covenants associated with these notes.

We have a revolving credit agreement (the Agreement) which allows us to borrow up to $200 million for general corporate purposes, including, but not limited to, short-term working capital, share repurchases as authorized by the Board, and support for other activities we enter into in the normal course of business. The Agreement expires in April 2016. No borrowings have been outstanding under the Agreement during 2014. We are in compliance with the financial covenants of the Agreement.

Additional information regarding our long-term debt is provided in Note 9 of the Notes to Condensed Consolidated Financial Statements.

We are a member of a number of FHLBs. Through membership, we have access to secured cash advances which can be used for liquidity purposes or other operational needs. To date, we have not established a FHLB line of credit or materially utilized our membership.

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Results of Operations – Three and Nine Months Ended September 30, 2014 Compared to Three and Nine Months Ended September 30, 2013

Selected consolidated financial data for each period is summarized in the table below.

	Three Months Ended September 30			Nine Months Ended September 30		
($ in thousands, except per share data)	2014	2013	Change	2014	2013	Change
Revenues:						
Net premiums written	$200,909	$157,641	$43,268	$568,575	$417,813	$150,762
Net premiums earned	$177,028	$133,598	$43,430	$525,061	$398,528	$126,533
Net investment result	33,128	33,584	(456)	95,555	95,782	(227)
Net realized investment gains (losses)	(8,131)	12,500	(20,631)	7,659	47,650	(39,991)
Other income	1,808	1,804	4	6,055	5,305	750
Total revenues	203,833	181,486	22,347	634,330	547,265	87,065
Expenses:						
Losses and loss adjustment expenses	106,486	65,619	40,867	306,591	203,885	102,706
Reinsurance recoveries	(7,264)	(3,982)	(3,282)	(18,948)	(14,013)	(4,935)
Net losses and loss adjustment expenses	99,222	61,637	37,585	287,643	189,872	97,771
Underwriting, policy acquisition and operating expenses	54,185	33,348	20,837	158,856	105,592	53,264
Segregated portfolio cells dividend expense	(483)	—	(483)	2,355	—	2,355
Interest expense	3,606	322	3,284	10,697	1,085	9,612
Total expenses	156,530	95,307	61,223	459,551	296,549	163,002
Gain on acquisition	—	494	(494)	—	35,986	(35,986)
Income before income taxes	47,303	86,673	(39,370)	174,779	286,702	(111,923)
Income taxes	12,525	23,316	(10,791)	43,328	60,044	(16,716)
Net income	$34,778	$63,357	$(28,579)	$131,451	$226,658	$(95,207)
Operating income	$40,131	$54,800	$(14,669)	$126,020	$159,746	$(33,726)
Earnings per share:						
Basic	$0.59	$1.02	$(0.43)	$2.20	$3.67	$(1.47)
Diluted	$0.59	$1.02	$(0.43)	$2.19	$3.65	$(1.46)
Operating earnings per share:						
Basic	$0.68	$0.89	$(0.21)	$2.11	$2.59	$(0.48)
Diluted	$0.68	$0.88	$(0.20)	$2.10	$2.57	$(0.47)
Net loss ratio	56.0%	46.1%	9.9	54.8%	47.6%	7.2
Underwriting expense ratio	30.6%	25.0%	5.6	30.3%	26.5%	3.8
Combined ratio	86.6%	71.1%	15.5	85.1%	74.1%	11.0
Operating ratio	68.1%	45.7%	22.4	67.4%	49.2%	18.2
Effective tax rate	26.5%	26.9%	(0.4)	24.8%	20.9%	3.9
Return on equity*	5.9%	10.7%	(4.8)	7.4%	10.9%	(3.5)

* Annualized. Gain on acquisition is excluded from this calculation.

In all tables that follow, the abbreviation "nm" indicates that the information or the percentage change is not meaningful.

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Revenues

Our consolidated net premiums earned were as follows:

($ in thousands)	Three Months Ended September 30 2014	2013	Change		Nine Months Ended September 30 2014	2013	Change	
Net Premiums Earned								
Specialty P&C	$ 123,791	$ 133,598	$ (9,807)	(7.3 %)	$ 374,704	$ 398,528	$ (23,824)	(6.0 %)
Workers' Compensation	49,792	—	49,792	nm	143,960	—	143,960	nm
Lloyd's Syndicate	3,445	—	3,445	nm	6,397	—	6,397	nm
Consolidated total	$ 177,028	$ 133,598	$ 43,430	32.5 %	$ 525,061	$ 398,528	$ 126,533	31.8 %

Consolidated net premiums earned increased in 2014 as compared to 2013 primarily due to the contribution of our recently acquired Workers' Compensation segment. The decline in net premiums earned for our Specialty P&C segment was primarily attributable to the pro-rata effect of lower physician premiums written during the preceding twelve months and also reflected an increase in ceded premiums earned. Given the start-up nature of Syndicate 1729 it added only $3.4 million and $6.4 million in net premiums earned for the 2014 three- and nine-month periods, respectively (as compared to net written premium of $3.9 million and $24.2 million for the three- and nine-month periods, respectively).

Our net investment result (which includes both net investment income and earnings from unconsolidated subsidiaries) decreased $0.5 million or 1.4% for the 2014 three-month period and decreased $0.2 million or 0.2% for the 2014 nine-month period. Net investment income decreased during the 2014 three- and nine-month periods primarily due to reduced earnings on our fixed income portfolio, which was partially offset by increased earnings from our other invested assets. Earnings from unconsolidated subsidiaries increased $0.6 million in the 2014 three-month period and increased $6.3 million in the 2014 nine-month period, primarily reflecting increased earnings from investment LPs. Amortization from tax credit partnerships was higher for the 2014 three-month period, but lower for the 2014 nine-month period.

Net realized investment gains (losses) decreased $20.6 million and $40.0 million for the 2014 three- and nine-month periods, respectively, as compared to 2013. The changes primarily relate to trading securities which are carried at fair value. Net impairments were approximately $1.2 million in both the 2014 three- and nine-month periods and nominal in both the 2013 three- and nine-month periods.

Expenses

The following table shows our net loss ratio by segment:

($ in millions)	Three Months Ended September 30 2014	2013	Change	Nine Months Ended September 30 2014	2013	Change
Current accident year net loss ratio						
Consolidated ratio	80.3 %	83.1 %	(2.8)	80.2 %	83.0 %	(2.8)
Specialty P&C	85.6 %	83.1 %	2.5	85.8 %	83.0 %	2.8
Workers' Compensation	67.6 %	— %	nm	65.9 %	— %	nm
Lloyd's Syndicate	73.6 %	— %	nm	68.9 %	— %	nm
Calendar year net loss ratio						
Consolidated ratio	56.0 %	46.1 %	9.9	54.8 %	47.6 %	7.2
Specialty P&C	51.4 %	46.1 %	5.3	51.0 %	47.6 %	3.4
Workers' Compensation	66.4 %	— %	nm	63.9 %	— %	nm
Lloyd's Syndicate	73.6 %	— %	nm	68.9 %	— %	nm
Favorable net loss development, prior accident years						
Consolidated	$ 42.9	$ 49.4	$ (6.5)	$ 133.3	$ 141.0	$ (7.7)
Specialty P&C	$ 42.3	$ 49.4	$ (7.1)	$ 130.4	$ 141.0	$ (10.6)

Workers' Compensation	$0.6	$—	nm	$2.9	$—	nm
Lloyd's Syndicate	$—	$—	nm	$—	$—	nm

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The decrease in our consolidated current accident year net loss ratio for the 2014 three- and nine-month periods was primarily attributable to the addition of our workers' compensation business. The start-up of Syndicate 1729 during 2014 had only a nominal effect on the consolidated ratio. Combined, these new operations decreased our 2014 consolidated current accident year net loss ratio by 5.3 percentage points for the three-month period and 5.6 percentage points for the nine-month period. The current accident year net loss ratio of our Specialty P&C segment (our historical business) reflected an increase primarily attributable to a higher accrual for internal claims adjustment expenses on a lower volume of premiums earned and additional administrative claims costs now recognized on a more timely, quarterly basis.

Our consolidated calendar year net loss ratio is lower than our consolidated current accident year net loss ratio due to the recognition of net favorable loss development in our Specialty P&C and Workers' Compensation segments as shown in the table above.

Our underwriting expense ratio reflected the following:

	Three Months Ended September 30					Nine Months Ended September 30				
	2014		2013		Change	2014		2013		Change
Underwriting Expense Ratio, as reported										
Consolidated	30.6	%	25.0	%	5.6	30.3	%	26.5	%	3.8
Underwriting Expense Ratio, excluding the effect of discrete events, and Syndicate 1729										
Consolidated	27.7	%	24.4	%	3.3	27.8	%	25.3	%	2.5
Specialty P&C	25.9	%	22.8	%	3.1	25.6	%	23.5	%	2.1
Workers' Compensation	29.4	%	—	%	nm	29.6	%	—	%	nm

Our consolidated expense ratio increased in 2014 due to a number of factors, including the acquisition of Eastern and additional expenses associated with our participation in Syndicate 1729. The ratios for both 2014 and 2013 were also impacted by expenses attributable to discrete events, such as the effect of purchase accounting on deferred policy acquisition cost amortization, transaction and other costs associated with business combinations or expansions, and costs associated with technology initiatives. Exclusive of expenses attributable to discrete events, we estimate that the addition of our workers' compensation business, which carries a higher expense ratio, increased our 2014 consolidated expense ratio by approximately 0.3 and 0.4 percentage points for the 2014 three- and nine-month periods, respectively. We estimate that the Lloyd's Syndicate segment, which had a high expense ratio due to its start-up phase, increased our consolidated expense ratio by approximately 0.9 and 0.8 percentage points for the 2014 three- and nine-month periods, respectively.

Exclusive of the effect of discrete events, the increase in our Specialty P&C segment ratio principally reflects the effects of higher compensation costs and a lower premium base. Approximately 2.6 and 2.7 percentage points of the Workers' Compensation segment expense ratio for the 2014 three- and nine-month periods, respectively, was attributable to the amortization of intangible assets recognized in the acquisition of Eastern.

Taxes

Our effective tax rate was 26.5% for the 2014 three-month period, a 0.4 percentage point decrease as compared to the 2013 three-month period, and was 24.8% for the 2014 nine-month period, a 3.9 percentage point increase as compared to the 2013 nine-month period. The increase for the nine-month period principally reflects a reduction to our effective tax rate in 2013 due to a gain on acquisition that was not taxable.

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Operating Ratio and Return on Equity

Our operating ratio (calculated as our combined ratio, less our investment income ratio) increased by 22.4 percentage points in the 2014 three-month period and increased by 18.2 percentage points in the 2014 nine-month period, reflecting higher net loss and expense ratios, and a decline in our investment ratio of 6.9 percentage points and 7.2 percentage points for the three- and nine-month periods, respectively, primarily due to the acquisition of Eastern. Compared to our professional liability business, workers' compensation generally requires lower reserves which necessitates lower investment assets to support those reserves in proportion to earned premium.

Return on equity (ROE) was 5.9% and 7.4% for the 2014 three- and nine-month periods, respectively, and was 10.7% and 10.9% for the same respective periods of 2013. Our calculation of return on equity for the 2013 three- and nine-month periods excluded the effect of the $0.5 million and $36.0 million gain on acquisition, respectively.

Book Value per Share

Our book value per share at September 30, 2014 as compared to December 31, 2013 is shown in the following table. The past growth rates of our book value per share do not necessarily predict similar future results.

	Book Value Per Share
Book Value Per Share at December 31, 2013	$39.13
Increase (decrease) to book value per share during the nine months ended September 30, 2014 attributable to:	
Net income	2.20
Increase in accumulated other comprehensive income	0.12
Dividends declared	(0.90)
Other, primarily the repurchase of shares	(0.31)
Book Value Per Share at September 30, 2014	$40.24

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Non-GAAP Financial Measures

Operating income is a non-GAAP financial measure that is widely used to evaluate performance within the insurance sector. In calculating operating income, we have excluded the after-tax effects of net realized investment gains or losses, guaranty fund assessments or recoupments, gain on acquisition and the effect of confidential settlements that do not reflect normal operating results. We believe operating income presents a useful view of the performance of our insurance operations, but should be considered in conjunction with net income computed in accordance with GAAP.

The following table is a reconciliation of Net income to Operating income:

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands, except per share data)	2014	2013	2014	2013
Net income	$34,778	$63,357	$131,451	$226,658
Items excluded in the calculation of operating income:				
Net realized investment (gains) losses	8,131	(12,500)	(7,659)	(47,650)
Guaranty fund assessments (recoupments)	104	95	147	71
Gain on acquisition	—	(494)	—	(35,986)
Effect of confidential settlements, net	—	—	(843)	—
Pre-tax effect of exclusions	8,235	(12,899)	(8,355)	(83,565)
Tax effect, at 35%, exclusive of non-taxable gain on acquisition	(2,882)	4,342	2,924	16,653
Operating income	$40,131	$54,800	$126,020	$159,746
Per diluted common share:				
Net income	$0.59	$1.02	$2.19	$3.65
Effect of exclusions	0.09	(0.14)	(0.09)	(1.08)
Operating income per diluted common share	$0.68	$0.88	$2.10	$2.57

Note: The 35% rate above is the annual expected incremental tax rate associated with the taxable or tax deductible items listed. We record the provision for income taxes in our interim financial statements based upon our estimated annual effective tax rate.

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Segment Operating Results - Specialty Property & Casualty

Our Specialty P&C segment focuses on professional liability insurance and medical technology and life sciences products liability insurance as discussed in Note 13 of the Notes to Condensed Consolidated Financial Statements. Specialty P&C segment operating results reflect pre-tax underwriting profit or loss from these insurance lines, exclusive of investment results, which are included in our Corporate segment. Segment operating results for the three and nine months ended September 30, 2014 were $27.4 million and $86.6 million, respectively, as compared to $42.5 million and $116.7 million for the same respective periods of 2013, and included the following:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Net premiums written	$142,733	$157,641	$(14,908)	(9.5%)	$379,428	$417,813	$(38,385)	(9.2%)
Net premiums earned	$123,791	$133,598	$(9,807)	(7.3%)	$374,704	$398,528	$(23,824)	(6.0%)
Net losses and loss adjustment expenses	$63,639	$61,637	$2,002	3.2%	$191,263	$189,872	$1,391	0.7%
Underwriting, policy acquisition and operating expenses	$33,814	$30,708	$3,106	10.1%	$101,044	$95,907	$5,137	5.4%
Net loss ratio	51.4%	46.1%	5.3		51.0%	47.6%	3.4	
Underwriting expense ratio	27.3%	23.0%	4.3		27.0%	24.1%	2.9	

Premiums Written

Changes in our premium volume within our Specialty P&C segment are driven by four primary factors: (1) the amount of new business, (2) our retention of existing business, (3) the premium charged for business that is renewed, which is affected by rates charged and by the amount and type of coverage an insured chooses to purchase, and (4) the timing of premium written through multi-period policies. In addition, premium volume may periodically be affected by shifts in the timing of renewals between periods. The healthcare professional liability market, which accounts for a majority of the revenues in this segment, remains challenging as physicians continue joining hospitals or larger group practices and are thus no longer purchasing insurance in the standard market. In addition, some competitors have chosen to compete primarily on price; both factors impact our ability to write new business and retain existing business.

Gross, ceded and net premiums written were as follows:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Gross premiums written	$163,134	$165,794	$(2,660)	(1.6%)	$429,730	$451,819	$(22,089)	(4.9%)
Ceded premiums written	(20,401)	(8,153)	(12,248)	<(100%)	(50,302)	(34,006)	(16,296)	(47.9%)
Net premiums written	$142,733	$157,641	$(14,908)	(9.5%)	$379,428	$417,813	$(38,385)	(9.2%)

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Gross Premiums Written

Gross premiums written by component were as follows:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Professional liability								
Physicians (1):								
Twelve month term	$115,698	$118,347	$(2,649)	(2.2%)	$289,533	$310,880	$(21,347)	(6.9%)
Twenty-four month term	5,311	7,720	(2,409)	(31.2%)	17,648	22,865	(5,217)	(22.8%)
Total Physicians	121,009	126,067	(5,058)	(4.0%)	307,181	333,745	(26,564)	(8.0%)
Other healthcare providers (2)	10,203	10,381	(178)	(1.7%)	26,458	25,852	606	2.3%
Healthcare facilities (3)	9,291	6,195	3,096	50.0%	28,932	27,106	1,826	6.7%
Legal professionals (4)	7,097	6,984	113	1.6%	23,095	22,174	921	4.2%
Tail coverages (5)	4,630	5,884	(1,254)	(21.3%)	15,132	16,467	(1,335)	(8.1%)
Total professional liability	152,230	155,511	(3,281)	(2.1%)	400,798	425,344	(24,546)	(5.8%)
Medical technology and life sciences products liability (6)	10,473	9,759	714	7.3%	27,561	25,040	2,521	10.1%
Other	431	524	(93)	(17.7%)	1,371	1,435	(64)	(4.5%)
Total	$163,134	$165,794	$(2,660)	(1.6%)	$429,730	$451,819	$(22,089)	(4.9%)

(1) Physician policies were our greatest source of premium revenues in both 2014 and 2013. We offer twenty-four month term policies to our physician insureds in one selected jurisdiction. The decline in twenty-four month premium, as compared to 2013, primarily reflects the normal cycle of renewals (policies subject to renewal in 2014 were previously written in 2012 rather than in 2013). There was no significant volume change associated with twenty-four month policies during the three- and nine-month periods of 2014.

(2) Our other healthcare providers are primarily dentists, chiropractors and allied health professionals.

(3) Our healthcare facilities premium (which includes hospitals, surgery centers and other facilities) increased in 2014, principally due to a shift in the timing of renewals between periods.

(4) Our legal professionals policies are offered throughout the United States, principally through agent and brokerage arrangements.

(5) We offer extended reporting endorsement or "tail" coverage to insureds who discontinue their claims-made coverage with us, and we also periodically offer "tail" coverage through custom policies. The amount of tail coverage premium written can vary widely from period to period.

(6) Our medical technology and life sciences products liability (products liability) business is marketed throughout the United States; coverage is offered on a primary basis, within specified limits, to manufacturers and distributors of medical technology and life sciences products. In addition to the previously listed factors that affect our premium volume, our products liability premium volume is impacted by the sales volume of insureds.

New business written by component was as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
(In millions)	2014	2013	2014	2013
Physicians	$5.3	$5.6	$13.2	$13.1
Other healthcare providers	$0.9	$0.8	$2.3	$1.9
Healthcare facilities	$2.1	$1.0	$3.9	$3.3
Legal professionals *	$1.2	$0.5	$3.4	$1.5
Medical technology and life sciences products liability *	$1.4	nm	$4.0	nm

* Excludes new business attributable to our Medmarc acquisition for the 2013 three- and nine-month periods, as the entire Medmarc book of business was new to us in 2013.

We calculate our retention rate as annualized renewed premium divided by all annualized premium subject to renewal. Retention rates are affected by a number of factors. We may lose insureds to competitors or to alternative insurance mechanisms such as risk retention groups or self-insurance entities (often when physicians join hospitals or large group practices) or due to pricing or other issues. We may choose not to renew an insured as a result of our underwriting evaluation. Insureds may also terminate coverage because they have left the practice of medicine for various reasons, principally for retirement but also for personal reasons or due to disability or death.
Retention by component is shown in the following table.

	Three Months Ended September 30		Nine Months Ended September 30	
	2014	2013	2014	2013
Physicians, standard lines only	90 %	89 %	89 %	89 %
Other healthcare providers	85 %	85 %	81 %	82 %
Healthcare facilities	84 %	82 %	82 %	83 %
Legal professionals *	80 %	90 %	82 %	87 %
Medical technology and life sciences products liability *	83 %	nm	87 %	nm

* Premiums contributed by our Medmarc acquisition are excluded from the calculation of retention for the 2013 three- and nine-month periods, as the entire Medmarc book of business was new to us in 2013.
The pricing of our business includes the effects of filed rates, surcharges and discounts. We continue to base our pricing on expected losses, as indicated by our historical loss data and available industry loss data. We are committed to a rate structure that will allow us to fulfill our obligations to our insureds, while generating competitive returns for our shareholders. The pricing of our standard physician business averaged 2% higher during the 2014 three-month period and 1% higher during the 2014 nine-month period. Rate increases resulted in an increase in average pricing of 4% and 7% for our legal professionals business for the 2014 three- and nine-month periods, respectively, which, when combined with our choosing to be more selective in the coverages we insure, contributed to lower retention for the same respective periods.

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Ceded Premiums Written

Ceded premiums represent the amounts owed to our reinsurers for their assumption of a portion of our losses. Through our current excess of loss reinsurance arrangements we retain the first $1 million in risk insured by us and cede any coverages in excess of this amount, and for our products liability coverages, we also retain 20% of the next $9 million of risk for coverages in excess of $1 million. We pay our reinsurers a ceding premium in exchange for their accepting the risk, the ultimate amount of which is determined by the loss experience of the business ceded, subject to certain minimum and maximum amounts.

Ceded premiums written for the three and nine months ended September 30, 2014 and 2013 were comprised as follows:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Excess of loss reinsurance arrangements	$8,382	$7,657	$725	9.5 %	$24,406	$22,867	$1,539	6.7 %
Premium ceded to Syndicate 1729 (1)	4,974	—	4,974	nm	9,847	—	9,847	nm
Other shared risk arrangements (2)	7,837	2,132	5,705	>100%	19,319	15,987	3,332	20.8 %
Other ceded premiums written	2,365	2,039	326	16.0 %	6,870	7,157	(287)	(4.0 %)
Reduction in premiums owed under reinsurance agreements, prior accident years, net (3)	(3,157)	(3,675)	518	14.1 %	(10,140)	(12,005)	1,865	15.5 %
Total ceded premiums written	$20,401	$8,153	$12,248	>100%	$50,302	$34,006	$16,296	47.9 %

(1) Effective January 1, 2014, one of our subsidiaries began ceding premium to Syndicate 1729 under a quota share agreement, net of a related ceding commission. As previously discussed, we are a 58% participant in Syndicate 1729 and record our pro rata share of its operating results in our Lloyd's Syndicate segment on a quarter delay. We also record the Specialty P&C segment results for this agreement on a quarter delay as the amounts are not material and this permits the cession to be reported by both the Lloyd's Syndicate segment and the Specialty P&C segment in the same reporting period. Premium ceded to Syndicate 1729 reported for the three- and nine-month periods of 2014 in the table above reflects cessions that occurred during the three- and six-months ended June 30, 2014, respectively. The related ceding commission income recorded as an offset to deferred policy acquisition costs for the three- and nine-month periods of 2014 was $1.3 million and $2.7 million, respectively. The third quarter cession of $11.1 million and the related ceding commission income of $3.0 million will be recorded in the fourth quarter of 2014. Eliminations of the inter-segment portion (58% of the Specialty P&C cession) of the transactions are also recorded on a quarter delay.

(2) We have entered into various shared risk arrangements, including quota share, fronting, and captive arrangements, with certain large healthcare systems and other insurance entities. These arrangements include our Ascension Health Certitude and CAPAssurance Programs. The increase in ceded premiums written under our shared risk arrangements for the 2014 three- and nine-month periods principally reflected premiums ceded under arrangements begun after the third quarter of 2013. The increase for the 2014 nine-month period was partially offset by decreases attributable to a shift in renewal period for one arrangement from the second quarter to the fourth quarter and a large policy under one of the arrangements that did not renew in 2014.

(3) Given the length of time that it takes to resolve our claims, many years may elapse before all losses recoverable under a reinsurance arrangement are known. As a part of the process of estimating our loss reserve we also make estimates regarding the amounts recoverable under our reinsurance arrangements. As previously discussed, the premiums ultimately ceded under our excess of loss reinsurance arrangements are subject to the losses ceded under the arrangements. In both 2014 and 2013, on a net basis, we reduced our estimate of expected losses and associated recoveries for prior year ceded losses, as well as our estimate of ceded premiums owed to reinsurers. Changes to estimates of premiums ceded related to prior accident years are fully earned in the period the change in estimates occur.

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Ceded Premiums Ratio

As shown in the table below, our ceded premiums ratio was affected in both 2014 and 2013 by revisions to our estimate of premiums owed to reinsurers related to coverages provided in prior accident years.

	Three Months Ended September 30			Nine Months Ended September 30		
	2014	2013	Change	2014	2013	Change
Ceded premiums ratio, as reported	12.5 %	4.9 %	7.6	11.7 %	7.5 %	4.2
Less the effect of reduction in premiums owed under reinsurance agreements, prior accident years (as previously discussed)	(1.9 %)	(2.2 %)	0.3	(2.4 %)	(2.7 %)	0.3
Ratio, current accident year	14.4 %	7.1 %	7.3	14.1 %	10.2 %	3.9

The remaining increase in the current accident year ceded premiums ratio for the three- and nine-month periods was primarily attributable to the increase in ceded premiums written under the quota share arrangement with Syndicate 1729 and our shared risk arrangements, as previously discussed. Additionally, premium volume from retained coverages was lower in 2014 than in 2013, which reduced gross premiums written but had no effect on ceded premiums written, and thus increased the ratio.

Net Premiums Earned

Net premiums earned were as follows:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Gross premiums earned	$137,446	$144,280	$(6,834)	(4.7 %)	$410,814	$428,784	$(17,970)	(4.2 %)
Ceded premiums earned	(13,655)	(10,682)	(2,973)	(27.8 %)	(36,110)	(30,256)	(5,854)	(19.3 %)
Net premiums earned	$123,791	$133,598	$(9,807)	(7.3 %)	$374,704	$398,528	$(23,824)	(6.0 %)

Net premiums earned consist of gross premiums earned less the portion of earned premiums that we cede to our reinsurers for their assumption of a portion of our losses. Because premiums are generally earned pro rata over the entire policy period, fluctuations in premiums earned tend to lag those of premiums written. Generally, our policies carry a term of one year, but as discussed above, we write certain policies with a twenty-four month term, and certain of our medical technology and life sciences products liability policies carry a multi-year term. Tail coverage premiums are generally 100% earned in the period written because the policies insure only incidents that occurred in prior periods and are not cancellable. Additionally, ceded premium changes due to changes to estimates of premiums owed under reinsurance agreements are fully earned in the period of change.

The decrease in gross premiums earned in 2014 primarily reflected the pro-rata effect of lower physician premiums written during the preceding twelve months, partially offset by an increase in premiums earned due to growth associated with our shared risk arrangements. The increase in premiums ceded during 2014 primarily reflects growth associated with certain shared risk arrangements that were either new in 2014 or not in effect for all of 2013 and premiums ceded under the quota share arrangement with Syndicate 1729. Also, for the 2014 three- and nine-month periods, prior accident year ceded premiums reductions were $0.5 million and $1.9 million lower, respectively, than for the 2013 three- and nine-month periods (see discussion under the heading "Ceded Premiums Written").

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Losses and Loss Adjustment Expenses

The determination of calendar year losses involves the actuarial evaluation of incurred losses for the current accident year and the actuarial re-evaluation of incurred losses for prior accident years, including an evaluation of the reserve amounts required for losses in excess of policy limits.

Accident year refers to the accounting period in which the insured event becomes a liability of the insurer. For claims-made policies, which represent over 90% of the premiums written in our Specialty P&C segment, the insured event generally becomes a liability when the event is first reported to the insurer. For occurrence policies the insured event becomes a liability when the event takes place. We believe that measuring losses on an accident year basis is the best measure of the underlying profitability of the premiums earned in that period, since it associates policy premiums earned with the estimate of the losses incurred related to those policy premiums.

The following table summarizes calendar year net loss ratios by separating losses between the current accident year and all prior accident years. Additionally, the table shows our current accident year net loss ratio was significantly affected by revisions to our estimate of premiums owed to reinsurers related to coverages provided in prior accident years. Our current accident year net loss ratios for the three and nine months ended September 30, 2014 and 2013 compare as follows:

	Net Loss Ratios (1)									
	Three Months Ended September 30					Nine Months Ended September 30				
	2014		2013		Change	2014		2013		Change
Calendar year net loss ratio	51.4	%	46.1	%	5.3	51.0	%	47.6	%	3.4
Less impact of prior accident years on the net loss ratio	(34.2	%)	(37.0	%)	2.8	(34.8	%)	(35.4	%)	0.6
Current accident year net loss ratio, as reported	85.6	%	83.1	%	2.5	85.8	%	83.0	%	2.8
Less estimated ratio increase (decrease) attributable to:										
Ceded premium reductions, prior accident years (2)	(2.2	%)	(2.3	%)	0.1	(2.4	%)	(2.6	%)	0.2
Current accident year net loss ratio, excluding the effect of prior year ceded premium (3)	87.8	%	85.4	%	2.4	88.2	%	85.6	%	2.6

(1) Net losses as specified divided by net premiums earned.

(2) Reductions to premiums owed under reinsurance agreements for prior accident years increased net premiums earned (the denominator of the current accident year ratio) in both 2014 and 2013. See the discussion in the Premiums section for our Specialty P&C segment under the heading "Ceded Premiums Written" for additional information.

(3) The remaining increase in the current accident year net loss ratio reflects the effect of a higher accrual for internal claims adjustment expenses on a lower volume of premiums earned and additional costs for administrative claims now recognized on a more timely, quarterly basis rather than as part of the fourth quarter reserve review adjustment.

We recognized favorable loss development related to our previously established reserve, on a gross basis, of $47.8 million and $146.9 million during the three and nine months ended September 30, 2014, respectively. On a net basis, we recognized favorable development of $42.3 million and $130.4 million during three and nine months ended September 30, 2014, respectively. The net basis reflects the favorable development recognized with respect to our ceded coverage layers. We re-evaluate our previously established reserve each quarter based on our most recently available claims data and currently available industry trend information. Development recognized during the three and nine months ended September 30, 2014 principally related to accident years 2007 through 2012.

We recognized favorable loss development related to our previously established reserve, on a gross basis, of $54.6 million and $158.1 million during the three and nine months ended September 30, 2013, respectively. On a net basis, we recognized favorable development of $49.4 million and $141.0 million during the three and nine months ended September 30, 2013, respectively. Development recognized during the 2013 three- and nine-month periods principally

related to accident years 2005 through 2011.

A detailed discussion of factors influencing our recognition of loss development recognized is included in our Critical Accounting Estimates section under the heading "Reserve for Losses and Loss Adjustment Expenses" and in our 2013 Form 10K under the same heading. Assumptions used in establishing our reserve are regularly reviewed and updated by management as new data becomes available. Any adjustments necessary are reflected in the then current operations. Due to the size of our reserve, even a small percentage adjustment to the assumptions can have a material effect on our results of operations for the period in which the change is made, as was the case in both 2014 and 2013.

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Underwriting, Policy Acquisition and Operating Expenses

The table below provides a comparison of underwriting, policy acquisition and operating expenses for the three and nine months ended September 30, 2014 and 2013:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Underwriting, policy acquisition and operating expenses	$33,814	$30,708	$3,106	10.1 %	$101,044	$95,907	$5,137	5.4 %

The following table highlights the more significant items affecting the comparability of expenses between 2014 and 2013:

(In millions)	Expense Increase (Decrease) 2014 vs 2013 Three Months Ended September 30	Nine Months Ended September 30
Excluding the effect from purchase accounting (see below), the decrease in DPAC amortization primarily reflects the decline in premium volume and an increased amount of ceding commission income during 2014, partially offset by an increased amount of underwriting compensation costs capitalized beginning in the third quarter of 2013. The increase in ceding commission income, which is accounted for as an offset to DPAC amortization, reflected the 2014 increase in ceded premiums earned.	$(0.9)	$(0.2)
Costs associated with ongoing technology enhancement initiatives	0.1	0.9
Higher compensation costs. The three-month increase was primarily attributable to allocation adjustments made in the 2013 three-month period. The nine-month increase was primarily attributable to higher stock compensation costs in 2014 relative to a performance based plan.	1.3	1.2
Other variances not individually significant	1.2	0.3
Expenses associated with discrete events:		
Amortization of deferred policy acquisition costs associated with entities acquired in 2013 increased in 2014. Application of GAAP purchase accounting rules lowered amortization recorded in 2013.	0.7	3.6
Transaction-related costs associated with entities acquired in 2013, principally professional fees and one time compensation costs	—	(1.4)
Technology enhancement initiatives	0.7	0.7
Net change in expenses	$3.1	$5.1

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Underwriting Expense Ratio (the Expense Ratio)

As shown in the following table, our expense ratio was affected in both 2014 and 2013 by ceded premium reductions related to prior accident years as discussed under the heading "Ceded Premiums Written," and by expenses associated with discrete events, as identified in the previous table.

	Underwriting Expense Ratio							
	Three Months Ended September 30				Nine Months Ended September 30			
	2014		2013		Change	2014		2013		Change
Underwriting expense ratio, as reported	27.3	%	23.0	%	4.3	27.0	%	24.1	%	2.9
Less estimated ratio increase (decrease) attributable to:										
Net ceded premium reductions, prior accident years	(0.7	%)	(0.6	%)	(0.1)	(0.7	%)	(0.7	%)	—
Expenses associated with discrete events (see table above)	1.4	%	0.2	%	1.2	1.4	%	0.6	%	0.8
Underwriting expense ratio, less listed effects	26.6	%	23.4	%	3.2	26.3	%	24.2	%	2.1

The remaining difference in our 2014 and 2013 expense ratios is attributable to the following:

	Increase (decrease), 2014 versus 2013	
(In percentage points)	Comparative three-month periods	Comparative nine-month periods
Estimated ratio increase (decrease) attributable to:		
Increase in compensation costs included in DPAC amortization, as previously discussed	0.5	0.9
Costs associated with ongoing technology enhancement initiatives	0.1	0.3
Higher compensation costs	1.0	0.3
Lower net premiums earned, partially offset by the effect of higher ceding commission income	0.7	0.6
Other variances not individually significant	0.9	—
Net increase/(decrease) in ratio	3.2	2.1

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Segment Operating Results - Workers' Compensation

Our Workers' Compensation segment provides traditional workers' compensation insurance products to employers with 1,000 employees or fewer and alternative market solutions, as discussed in Note 13 to the Notes to Condensed Consolidated Financial Statements. Our Workers' Compensation operations are the primary business operations acquired through our purchase of Eastern in 2014. Segment operating results reflect pre-tax underwriting profit or loss, exclusive of investment results which are included in our Corporate segment. Segment operating results for the three and nine months ended September 30, 2014 were $2.6 million and $4.8 million, respectively, and included the following:

($ in thousands)	September 30, 2014 Three Months Ended		Nine Months Ended	
Net premiums written	$54,287		$164,984	
Net premiums earned	$49,792		$143,960	
Net losses and loss adjustment expenses	$33,046		$91,975	
Underwriting, policy acquisition and operating expenses	$14,785		$45,379	
Segregated portfolio cell dividend expense	$(483	)	$2,355	
Net loss ratio	66.4	%	63.9	%
Underwriting expense ratio	29.7	%	31.5	%

Premiums Written

Our workers’ compensation premium volume is driven by four primary factors: 1) the amount of new business written, 2) retention of our existing book of business, 3) premium rates charged on our renewal book of business, and 4) audit premium.

Gross, ceded and net premiums written for the three and nine months ended September 30, 2014 were as follows:

(In thousands)	September 30, 2014 Three Months Ended		Nine Months Ended	
Gross premiums written	$60,307		$181,130	
Ceded premiums written	(6,020	)	(16,146	)
Net premiums written	$54,287		$164,984	

Gross Premiums Written

Gross premiums written in our traditional and alternative market business for the three and nine months ended September 30, 2014 were as follows:

(In thousands)	September 30, 2014 Three Months Ended	Nine Months Ended
Traditional business	$46,666	$136,752
Alternative market business	13,641	44,378
Gross premiums written	$60,307	$181,130

Our traditional workers’ compensation insurance products include guaranteed cost, dividend, deductible, and retrospectively-rated policies. Our alternative market business is ceded 100% to the segregated portfolio cells at our wholly owned Cayman Islands reinsurance subsidiary, Eastern Re, and an unaffiliated captive insurer. Additional information regarding the operations of the segregated portfolio cells is included in the Underwriting, policy acquisition and operating expense section below.

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Gross premiums written for the three and nine months ended September 30, 2014 reflected the following:
Our retention rate was approximately 85% and 83% for the 2014 three- and nine-month periods, respectively, reflecting the impact of price competition in the marketplace. We calculate our workers' compensation retention rate as annualized renewed premium divided by all annualized premium subject to renewal.
The pricing of our renewed business averaged 2% higher than that of our expiring premium during both the 2014 three month period and the 2014 nine-month period. The pricing of our business includes an assessment of the underlying policy exposure and the effects of current market conditions. We continue to base our pricing on expected losses, as indicated by our historical loss data.
In addition to the effects of retention and renewal pricing factors discussed above, premium volume reflected new business of approximately $12.6 million and $36.4 million and audit premium of $2.2 million and $3.0 million for the three and nine months ended September 30, 2014, respectively.
Ceded Premiums Written
Ceded premiums written reflect our external reinsurance programs and alternative market business ceded to an unaffiliated captive insurance company.
Ceded premiums written for three and nine months ended September 30, 2014 were as follows:

	September 30, 2014	
(In thousands)	Three Months Ended	Nine Months Ended
Premiums ceded to external reinsurers	$4,502	$12,396
Return premium estimate under external reinsurance	750	(213)
Premiums ceded to unaffiliated captive insurers	768	3,963
Total ceded premiums written	$6,020	$16,146

We retain the first $0.5 million in risk insured by us and cede losses in excess of this amount on each loss occurrence under our primary external reinsurance contract. The external reinsurance contract contains a return premium provision under which we estimate return premium based on the underlying loss experience of policies covered under the contract. Changes in the return premium estimate reflect the loss experience under the reinsurance contract for the three and nine months ended September 30, 2014. We cede 100% of premiums written under two alternative market programs to an unaffiliated captive insurer.
Ceded Premiums Ratio

	September 30, 2014	
	Three Months Ended	Nine Months Ended
Ceded premiums ratio, as reported	10.0%	8.9%
Less the effect of:		
Return premium estimated under external reinsurance	1.2%	(0.1%)
Premiums ceded to unaffiliated captive insurer (100%)	1.3%	2.2%
Ceded premiums ratio, less the effects of above	7.5%	6.8%

Ceded premiums under our primary external reinsurance contract represented 7.5% and 6.8% of gross premiums written for the three and nine months ended September 30, 2014, respectively. We cede premiums related to our traditional business on an earned premium basis, whereas alternative market premiums are ceded on a written premium basis.

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Net Premiums Earned

Net premiums earned for the three and nine months ended September 30, 2014 were as follows:

	September 30, 2014	
(In thousands)	Three Months Ended	Nine Months Ended
Gross premiums earned	$56,690	$159,955
Ceded premiums earned	(6,898)	(15,995)
Net premiums earned	$49,792	$143,960

Net premiums earned consist of gross premiums earned less the portion of earned premiums that we cede to our reinsurers for their assumption of a portion of our losses. Our workers' compensation policies are twelve-month policies and premiums are earned on a pro-rata basis over the policy period. Net premiums earned also include premium adjustments related to the audit of our insureds' payrolls. Payroll audits are conducted subsequent to the end of the policy period and any related adjustments are recorded in the current period. In addition, we record an estimate for EBUB and evaluate the estimate on a quarterly basis. We increased the EBUB estimate by $0.8 million and $0.4 million during the three and nine months ended September 30, 2014, respectively, and the impact of that change is included in Audit premium.

Losses and Loss Adjustment Expenses

The following table summarizes calendar year net loss ratios by separating losses between the current accident year and all prior accident years. The components of the calendar year loss ratio were as follows:

	Net Loss Ratios September 30, 2014	
	Three Months Ended	Nine Months Ended
Calendar year net loss ratio	66.4%	63.9%
Less impact of prior accident years on the net loss ratio	(1.2%)	(2.0%)
Current accident year net loss ratio, as reported	67.6%	65.9%
Less impact of audit premium on loss ratio	(3.1%)	(1.4%)
Current accident year net loss ratio, excluding the effect of audit premium	70.7%	67.3%

The increase in the current accident year loss ratio for the three and nine months ended September 30, 2014 primarily reflects severity-related claims activity in the alternative market business.

We recorded favorable prior accident year development of $0.6 million and $2.9 million for three and nine months ended September 30, 2014, respectively, related to our SPCs due to better than anticipated loss experience during 2014, and we also recognized amortization associated with the purchase accounting fair value adjustment. There were no prior accident year reserve adjustments related to our traditional business. We recognized audit premium from customers during 2014, which reduced the current accident year net loss ratio. Audit premium from customers results in a decrease in the net loss ratio, whereas audit premium returned to customers results in an increase in the net loss ratio.

Underwriting, Policy Acquisition and Operating Expenses

Underwriting, policy acquisition and operating expenses for the three and nine months ended September 30, 2014 were $14.8 million and $45.4 million, respectively. These expenses include commissions, premium taxes, and underwriter salaries, which are capitalized and deferred over the related workers' compensation policy period, net of ceding commissions earned. The capitalization of these costs can vary as they are subject to the success rate of our contract acquisition efforts.

The following table highlights certain discrete events affecting expenses in the 2014 three- and nine-month periods:

	Expense Increase (Decrease) September 30, 2014	
(In thousands)	Three Months Ended	Nine Months Ended
One-time professional fees	$—	$661
Transaction-related expenses	$146	$2,055

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Underwriting Expense Ratio (the Expense Ratio)

Our expense ratio for the three and nine months ended September 30, 2014, including the impact of audit premium and certain discrete items, was as follows:

	Underwriting Expense Ratio September 30, 2014			
	Three Months Ended		Nine Months Ended	
Underwriting expense ratio, as reported	29.7	%	31.5	%
Less estimated ratio increase (decrease) attributable to:				
Transaction-related expenses	0.3	%	1.4	%
One-time professional fees	—	%	0.5	%
Amortization of intangible assets	2.6	%	2.7	%
Impact of return premium estimate	0.4	%	(0.1	%)
Impact of audit premium	(1.4	%)	(0.7	%)
Underwriting expense ratio, less listed effects	27.8	%	27.7	%

Segregated Portfolio Cell (SPC) Dividend Expense

Our Workers' Compensation segment provides turn-key workers' compensation alternative market solutions that include program design, fronting, claims administration, risk management, SPC rental, asset management and SPC management services. The asset management and SPC management services are outsourced to a third party. Alternative market customers include individual companies, groups and/or associations (known as SPC dividend participants). SPC dividend expense for each period represents the difference between total revenue and the sum of net losses and loss adjustment expenses and underwriting, policy acquisition and operating expenses attributable to the alternative market business ceded to the SPC's of Eastern Re, net of any participation we have taken in the SPC's. The SPC's are segregated pools of assets and liabilities that provide an insurance facility for a defined set of risks. Assets of each SPC are solely for the benefit of that individual cell and each SPC is solely responsible for the liabilities of that individual cell. Assets of one SPC are statutorily protected from the creditors of the others. We participate to a varying degree in the results of selected SPC's. Our ownership interest in the SPC's in which we participate is generally 50%, but we have ownership interests as low as 25% and as high as 82.5%. Under the SPC structure, the net operating results of each cell, net of our participation, are due to the SPC participants of that cell.

SPC dividend expense for the three and nine months ended September 30, 2014 was as follows:

	September 30, 2014			
(In thousands)	Three Months Ended		Nine Months Ended	
Segregated portfolio cell dividend expense before Eastern participation	$(598	)	$3,297	
Eastern participation	$115		$(942	)
Segregated portfolio cell dividend expense	$(483	)	$2,355	

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Segment Operating Results - Lloyd's Syndicate

Through a wholly owned and consolidated subsidiary (the Corporate Member), we are a corporate member of Lloyd's of London. Our Corporate Member is the majority (58%) capital provider to Syndicate 1729, which began writing and reinsuring property and casualty business as of January 1, 2014. The remaining capital for Syndicate 1729 is provided by unrelated third parties, including private names and other corporate members. We have provided $77.2 million of capital in the form of FAL for the first year of Syndicate 1729 operations, as discussed under the heading "Investment Exposures" in Liquidity and Capital Resources and Financial Condition and have a total capital commitment to Syndicate 1729 through 2019 of up to $200 million. Syndicate 1729 covers a range of property and casualty insurance and reinsurance lines, and has a maximum underwriting capacity of £75 million for the 2014 underwriting year, of which £43.2 million ($70.0 million based on September 30, 2014 exchange rates) is our allocated underwriting capacity as a corporate member.

Syndicate 1729 functions as the medium through which we and the other capital providers participate in the property and casualty business underwritten by the Syndicate. Syndicate 1729 is led by Duncan Dale, an underwriter with more than 30 years of experience at Lloyd’s and in the London insurance and reinsurance market. A service company, 70% owned by Mr. Dale and 30% owned by ProAssurance, provides underwriting and other services to Syndicate 1729 on a fee basis. We account for our interest in the service company using the equity method as we do not control the service company. We have provided a £10 million credit facility to the Trustees of Syndicate 1729 to provide initial operating funds, £5.5 million ($9.2 million) of which had been advanced at September 30, 2014. See discussion under the heading "Business Combinations and Ventures" in Liquidity and Capital Resources and Financial Condition for additional detail.

Our Lloyd's Syndicate segment (comprised of our 58% participation in Syndicate 1729 operating results and 100% of the operating results of our wholly owned subsidiaries that support Syndicate 1729) reported net operating losses for the three and nine months ended September 30, 2014 of $1.6 million and $3.8 million, respectively. We report results from our Syndicate 1729 involvement on a quarter delay, except that investment results associated with our FAL investments and certain U.S. paid administrative expenses, primarily start-up costs, are reported concurrently as that information is available on an earlier time frame.

Segment results reported for the three and nine months ended September 30, 2014 included the following:

	September 30, 2014			
($ in thousands)	Three Months Ended		Nine Months Ended	
Net premiums written	$3,889		$24,163	
Net premiums earned	$3,445		$6,397	
Net investment income	$120		$244	
Net losses and loss adjustment expenses	$2,537		$4,405	
Underwriting, policy acquisition and operating expenses	$2,584		$5,999	
Net loss ratio	73.6	%	68.9	%
Underwriting expense ratio	75.0	%	93.8	%

Net premiums written were $3.9 million and $24.2 million for the three and nine months ended September 30, 2014, respectively, and included casualty, property, and property reinsurance coverages. As discussed in our Specialty P&C segment operating results, effective January 1, 2014, Syndicate 1729 entered into a quota share reinsurance agreement with one of our Specialty P&C wholly owned insurance subsidiaries and pays a ceding commission related to the amount assumed. Our Specialty P&C segment reports this ceding arrangement on a quarter delay as the amounts are not material and this permits the cession to be reported by both the Lloyd's Syndicate segment and the Specialty P&C segment in the same reporting period. Net premiums written in the above table included $2.9 million and $5.7 million for the three and nine months ended September 30, 2014, respectively, attributable to our 58% participation in this arrangement.

Net premiums earned consist of gross premiums earned less the portion of earned premiums that we cede to our reinsurers for their assumption of a portion of our losses. Because premiums are generally earned pro rata over the entire policy period, fluctuations in premiums earned tend to lag those of premiums written. Policies written to date primarily carry a term of one year.

The net loss ratio was 73.6% and 68.9% for the three and nine months ended September 30, 2014, respectively. Losses for the three- and nine-month periods were recorded using the loss assumptions incorporated into the business plan submitted to Lloyd's for Syndicate 1729; these assumptions are consistent with loss results reflected in Lloyd's historical data for similar risks. We expect loss ratios to fluctuate from quarter to quarter as Syndicate 1729 writes more business and the book begins to mature.

Underwriting expenses were $2.6 million and $6.0 million for the three and nine months ended September 30, 2014, respectively, and primarily consisted of underwriting and administrative salaries and benefits, professional fees and amortization of policy acquisition costs (approximately $0.9 million and $1.7 million, respectively). No underwriting salaries or benefits were deferred during the period due to the Syndicate being in a start-up phase. The high expense ratio for the segment reflects these and other start-up costs expensed during the three- and nine-month periods, and a low level of earned premium due to Syndicate 1729 being in its initial stage of operations.

Net investment income for the 2014 three- and nine-month periods related entirely to the income earned on the FAL investments. Our FAL investments are primarily in the form of short-term investments and investment-grade corporate debt securities.

Operating results of this segment are primarily taxed in the U.K. No tax benefit has been recognized related to the operations of this segments as the loss is not currently deductible for tax purposes in either the U.K. or the U.S. and does not meet GAAP criteria for recognition of a deferred tax asset.

Segment Operating Results - Corporate

Segment operating results for our Corporate segment for the three and nine months ended September 30, 2014 were $6.4 million and $44.0 million, respectively, and were $20.9 million and $110.0 million for same respective periods of 2013. Results included the following:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Net investment income	$32,710	$33,889	$(1,179)	(3.5%)	$92,544	$99,282	$(6,738)	(6.8%)
Equity in earnings (loss) of unconsolidated subsidiaries	$298	$(305)	$603	>100%	$2,767	$(3,500)	$6,267	>100%
Total net realized investment gains (losses)	$(8,131)	$12,500	$(20,631)	<(100%)	$7,659	$47,650	$(39,991)	(83.9%)
Operating expense	$3,189	$2,640	$549	20.8%	$6,826	$9,692	$(2,866)	(29.6%)
Interest expense	$3,606	$322	$3,284	>100%	$10,697	$1,085	$9,612	>100%
Income taxes	$12,525	$23,316	$(10,791)	(46.3%)	$43,328	$60,044	$(16,716)	(27.8%)
Gain on acquisition	$—	$494	$(494)	nm	$—	$35,986	$(35,986)	nm

Net Investment Income, Equity in Earnings (Loss) of Unconsolidated Subsidiaries, Net Realized Investment Gains (Losses)

Net Investment Income

Net investment income is primarily derived from the income earned by our fixed maturity securities and also includes dividend income from equity securities, income from our short-term and cash equivalent investments, earnings from other investments and increases in the cash surrender value of business owned life insurance (BOLI) contracts. Investment fees and expenses are deducted from investment income.

Net investment income by investment category was as follows:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Fixed maturities	$28,302	$30,672	$(2,370)	(7.7%)	$85,132	$93,687	$(8,555)	(9.1%)
Equities	2,661	2,394	267	11.2%	7,479	7,000	479	6.8%
Short-term investments and Other invested assets	2,793	2,000	793	39.7%	4,723	2,514	2,209	87.9%
Business owned life insurance	646	633	13	2.1%	1,544	1,508	36	2.4%
Investment fees and expenses	(1,692)	(1,810)	118	6.5%	(6,334)	(5,427)	(907)	(16.7%)
Net investment income	$32,710	$33,889	$(1,179)	(3.5%)	$92,544	$99,282	$(6,738)	(6.8%)

Fixed Maturities

The decrease in our income from fixed maturity securities for both the three- and the nine-month periods of 2014 was primarily due to lower average investment balances. Although we added fixed securities valued at $107 million to our portfolio in 2014 as a result of the Eastern acquisition, we reduced the size of our fixed portfolio over the last year in order to purchase Eastern, repay debt, repurchase stock, pay dividends and invest in other asset classes. On an overall basis our average investment in fixed securities was approximately 7% lower for both the three- and nine-month periods of 2014, respectively, as compared to the same periods in 2013.

Average yields for our fixed maturity portfolio were as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2014	2013	2014	2013
Average income yield	3.7%	3.7%	3.7%	3.7%
Average tax equivalent income yield	4.2%	4.3%	4.3%	4.3%

Yields on fixed maturity securities remained relatively flat as compared to the same period in the prior year. Yields for the 2014 three- and nine-month periods reflected a decline of less than 10 basis points related to fixed maturity securities acquired

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in the Eastern transaction. In accordance with purchase accounting guidance, all Eastern securities were valued at fair value on the date acquired, which resulted in these securities having a lower yield on average than our other securities. Income from Treasury Inflation-Protected Securities showed little change for the 2014 three-month period but increased approximately $0.7 million for the 2014 nine-month period.

Equities

Income from our equity portfolio increased approximately 11% and 7% for the 2014 three- and nine-month periods, respectively, as compared to the same periods in 2013. Average investment balances increased for the 2014 three- and nine-month periods primarily due to the acquisition of Eastern. The equities acquired in the Eastern transaction were predominately bond funds which produce lower average yields than our traditional equities.

Short-term Investments and Other Invested Assets

Income from our other invested assets increased for the 2014 three- and nine-month periods, principally due to increased distributions received from our interests in LPs that we account for using the cost method.

Investment Fees and Expenses

Investment fees and expenses were relatively flat for the 2014 three-month period but increased for the 2014 nine-month period due to the addition of Eastern and some associated transition expenses in the first two quarters of 2014.

Equity in Earnings (Loss) of Unconsolidated Subsidiaries

Equity in earnings (loss) of unconsolidated subsidiaries is derived from our investment interests accounted for under the equity method. Results were as follows:

	Three Months Ended September 30				Nine Months Ended September 30			
($ in thousands)	2014	2013	Change		2014	2013	Change	
Investment LPs/LLCs	$2,760	$1,597	$1,163	72.8 %	$9,255	$3,877	$5,378	>100%
Tax credit partnerships	(2,462)	(1,902)	(560)	(29.4 %)	(6,488)	(7,377)	889	12.1 %
Equity in earnings (loss) of unconsolidated subsidiaries	$298	$(305)	$603	>100%	$2,767	$(3,500)	$6,267	>100%

We hold interests in certain LPs/LLCs that generate earnings from trading portfolios, secured debt, debt securities, multi-strategy funds and private equity investments. The additional income in 2014 reflects the contribution of an LP changed from the cost to the equity method in the fourth quarter of 2013 and higher earnings from our other LPs.

Our tax credit investments are designed to generate returns by providing tax benefits in the form of tax credits and tax-deductible project operating losses. We account for our tax credit investments on the equity method and record amortization of our investment each period based on our allocable portion of the projected operating losses of the underlying properties. Amortization is adjusted periodically as actual operating results of the underlying properties become available. The comparative amortization increase for the three-month period is primarily attributable to the re-estimation of inception-to-date amortization of certain partnership interests during the 2013 three-month period. The comparative nine-month decrease reflects lower amortization which occurs as the underlying projects mature.

The tax benefits received from our tax credit partnerships, which are not reflected in our investment results above, reduced our tax expenses in 2014 and 2013 as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
Tax credits recognized during the period	$4,649	$4,473	$13,432	$13,418
Tax benefit of amortization	$862	$666	$2,271	$2,582

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Non-GAAP Financial Measure – Tax Equivalent Investment Result

We believe that to fully understand our investment returns it is important to consider the current tax benefits associated with certain investments as the tax benefit received represents a portion of the return provided by our tax-exempt bonds, BOLI, common and preferred stocks, and tax credit partnership investments (our tax-preferred investments). We impute a pro-forma tax-equivalent result by estimating the amount of fully-taxable income needed to achieve the same after-tax result as is currently provided by our tax-preferred investments. We believe this better reflects the economics behind our decision to invest in certain asset classes that are either taxed at lower rates and/or result in reductions to our current federal income tax expense. Our pro forma tax-equivalent investment result is shown in the table that follows as is a reconciliation of our tax equivalent result to our GAAP net investment result.

	Three Months Ended September 30		Nine Months Ended September 30	
(In thousands)	2014	2013	2014	2013
GAAP net investment result:				
Net investment income	$32,710	$33,889	$92,544	$99,282
Equity in earnings (loss) of unconsolidated subsidiaries	298	(305)	2,767	(3,500)
GAAP net investment result	$33,008	$33,584	$95,311	$95,782
Pro forma tax-equivalent investment results	$45,077	$46,015	$130,860	$132,694
Reconciliation of pro forma and GAAP tax-equivalent investment results:				
Pro forma tax-equivalent investment results	$45,077	$46,015	$130,860	$132,694
Taxable equivalent adjustments, calculated using the 35% federal statutory tax rate:				
State and municipal bonds	(4,070)	(4,639)	(12,699)	(14,270)
BOLI	(348)	(341)	(831)	(812)
Dividends received	(479)	(570)	(1,286)	(1,187)
Tax credit partnerships	(7,152)	(6,881)	(20,665)	(20,643)
Other investments	(20)	—	(68)	—
GAAP net investment result	$33,008	$33,584	$95,311	$95,782

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Net Realized Investment Gains (Losses)

The following table provides detailed information regarding our net realized investment gains (losses).

(In thousands)	Three Months Ended September 30 2014	Three Months Ended September 30 2013	Nine Months Ended September 30 2014	Nine Months Ended September 30 2013
Other-than-temporary impairment losses, total:				
State and municipal bonds	$—	$—	$(50)	$(71)
Corporate debt	(1,425)	—	(1,425)	—
Portion recognized in (reclassified from) Other Comprehensive Income:				
Corporate debt	268	—	268	—
Net impairments, attributable to fixed maturity impairments recognized in earnings	$(1,157)	$—	$(1,207)	$(71)
Gross realized gains, available-for-sale securities	736	7,708	3,711	14,631
Gross realized (losses), available-for-sale securities	(52)	(5,305)	(371)	(6,269)
Net realized gains (losses), trading securities	3,227	5,818	21,830	14,650
Net realized gains (losses), other investments	55	—	321	—
Change in unrealized holding gains (losses), trading securities	(10,402)	3,355	(17,906)	23,784
Change in unrealized holding gains (losses), convertible securities, carried at fair value as a part of Other investments	(538)	—	1,281	—
Other	—	924	—	925
Net realized investment gains (losses)	$(8,131)	$12,500	$7,659	$47,650

During the third quarter of 2014, we recognized credit-related impairments of $1.4 million related to two corporate debt instruments. Additionally, we recognized a non-credit impairment related to one of the instruments of $0.3 million as the fair value of the instrument was less than the expected future cash flows from the security. All impairments of debt securities recognized during 2013 were credit-related.

In both 2014 and 2013, sales of securities in our trading portfolio generated realized gains which reduced trading security unrealized holding gains (losses). For the 2014 three-month period, unrealized holding gains (losses) were further reduced by declines in market valuations. On the whole, market valuations improved during the nine-month periods of both 2014 and 2013. In 2013, the improvement more than offset the effect of sales during the period, but only partially offset the effect of sales during the 2014 nine-month period.

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Operating Expenses

Operating expenses were $3.2 million and $6.8 million for the three and nine months ended September 30, 2014, respectively, and $2.6 million and $9.7 million for the three and nine months ended September 30, 2013, respectively. Corporate expenses in 2014 reflected cost increases as compared to 2013 of approximately $1.2 million for the three-month period and cost reductions of approximately $1.8 million for the nine-month period that were attributable to discrete events of one period or the other, including in 2013 costs associated with business combinations or expansions, and in 2014, recoveries associated with the settlement of litigation and a reserve established related to discontinued operations of an acquired entity. Otherwise, we reduced corporate expenses by approximately $0.7 million during the 2014 three-month period and $1.1 million during the 2014 nine-month period.

Interest Expense

Interest expense increased during the three and nine months ended September 30, 2014 as compared to the same periods in 2013 primarily due to the issuance of unsecured senior notes in the fourth quarter of 2013 which carry a higher interest rate and are greater in amount than our average borrowing outstanding in 2013. Our weighted average outstanding debt approximated $250 million for both the three and nine months ended September 30, 2014 as compared to $125 million for the same periods in 2013.

Interest expense for the three and nine months ended September 30, 2014 and 2013 is provided in the following table:

	Three Months Ended September 30			Nine Months Ended September 30		
(In thousands)	2014	2013	Change	2014	2013	Change
Senior notes due 2023	$3,467	$—	$3,467	$10,186	$—	$10,186
Revolving credit agreement (including fees and amortization)	129	322	(193)	376	1,077	(701)
Other	10	—	10	135	8	127
	$3,606	$322	$3,284	$10,697	$1,085	$9,612

Taxes

We calculate our effective tax rate on a consolidated basis, dividing consolidated tax expense by consolidated pre-tax income. Factors affecting our effective tax rate include the following:

	Three Months Ended September 30		Nine Months Ended September 30	
	2014	2013	2014	2013
Statutory rate	35.0 %	35.0 %	35.0 %	35.0 %
Tax-exempt income	(4.5 %)	(4.1 %)	(4.9 %)	(5.3 %)
Tax credits	(7.2 %)	(5.2 %)	(6.9 %)	(6.9 %)
Non-taxable gain on acquisition	—%	(0.5 %)	— %	(2.9 %)
Non-U.S. loss	0.4 %	— %	0.4 %	— %
Other	2.8 %	1.7 %	1.2 %	1.0 %
Effective tax rate	26.5 %	26.9 %	24.8 %	20.9 %

We estimate our annual effective tax rate at the end of each quarterly reporting period, which is used to record the provision for income taxes in our interim financial statements. Our effective tax rates for both 2014 and 2013 were different from the statutory Federal income tax rate primarily due to the following:

- a portion of our investment income was tax-exempt
- we utilized tax credits transferred to us from our tax credit partnership investments
- we did not recognize a tax benefit related to the operating loss associated with our participation in Lloyd's Syndicate 1729, a U.K. tax entity
- the gain on acquisition recognized in 2013 was not taxable

Tax benefits recognized, related to the tax credits, approximated $4.6 million and $13.4 million for the three and nine months ended September 30, 2014 as compared to $4.5 million and $13.4 million for the 2013 three- and nine-month periods.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

We believe that we are principally exposed to three types of market risk related to our investment operations. These risks are interest rate risk, credit risk and equity price risk. We have limited exposure to foreign currency risk as we issue few insurance contracts denominated in currencies other than the U. S. dollar and we have few monetary assets or obligations denominated in foreign currencies.

Interest Rate Risk

Our fixed maturities portfolio is exposed to interest rate risk. Fluctuations in interest rates have a direct impact on the market valuation of these securities. As interest rates rise, market values of fixed income portfolios fall and vice versa. Certain of the securities are held in an unrealized loss position; we do not intend to sell and believe we will not be required to sell any of the debt securities held in an unrealized loss position before its anticipated recovery.

The following table summarizes estimated changes in the fair value of our available-for-sale fixed maturity securities for specific hypothetical changes in interest rates by asset class at September 30, 2014 and December 31, 2013. There are principally two factors that determine interest rates on a given security: market interest rates and credit spreads. As different asset classes can be affected in different ways by movements in those two factors, we have broken out our portfolio by asset class in the following table.

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	Interest Rate Shift in Basis Points				
	September 30, 2014				
	(200)	(100)	Current	100	200
Fair Value (in millions):					
U.S. Treasury obligations	$185	$183	$177	$177	$173
U.S. Government-sponsored enterprise obligations	46	45	44	43	41
State and municipal bonds	1,137	1,121	1,088	1,048	1,007
Corporate debt	1,568	1,527	1,473	1,417	1,365
Asset-backed securities	477	474	465	450	436
All fixed maturity securities	$3,413	$3,350	$3,247	$3,135	$3,022
Duration:					
U.S. Treasury obligations	3.65	3.61	3.57	3.53	3.50
U.S. Government-sponsored enterprise obligations	2.47	2.45	2.86	3.00	2.98
State and municipal bonds	3.31	3.44	3.61	3.79	3.92
Corporate debt	3.69	3.74	3.83	3.78	3.72
Asset-backed securities	1.57	2.10	2.87	3.44	3.73
All fixed maturity securities	3.25	3.38	3.59	3.71	3.77
	December 31, 2013				
Fair Value (in millions):					
U.S. Treasury obligations	$176	$174	$171	$168	$165
U.S. Government-sponsored enterprise obligations	34	34	33	32	30
State and municipal bonds	1,220	1,195	1,155	1,107	1,061
Corporate debt	1,453	1,413	1,361	1,308	1,257
Asset-backed securities	410	406	398	385	371
All fixed maturity securities	$3,293	$3,222	$3,118	$3,000	$2,884
Duration:					
U.S. Treasury obligations	3.85	3.81	3.77	3.72	3.68
U.S. Government-sponsored enterprise obligations	2.82	3.07	3.15	3.12	3.07
State and municipal bonds	3.61	3.84	4.07	4.20	4.25
Corporate debt	4.10	4.13	4.09	4.03	3.96
Asset-backed securities	2.08	2.55	3.12	3.57	3.80
All fixed maturity securities	3.60	3.80	3.90	4.00	4.00

Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including the maintenance of the existing level and composition of fixed income security assets, and should not be relied on as indicative of future results.

Certain shortcomings are inherent in the method of analysis presented in the computation of the fair value of fixed rate instruments. Actual values may differ from the projections presented should market conditions vary from assumptions used in the calculation of the fair value of individual securities, including non-parallel shifts in the term structure of interest rates and changing individual issuer credit spreads.

Our cash and short-term investment portfolio at September 30, 2014 was carried on a cost basis which approximates its fair value. Our portfolio lacks significant interest rate sensitivity due to its short duration.

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Credit Risk

We have exposure to credit risk primarily as a holder of fixed income securities. We control this exposure by emphasizing investment grade credit quality in the fixed income securities we purchase.

As of September 30, 2014, 93% of our fixed maturity securities were rated investment grade as determined by Nationally Recognized Statistical Rating Organizations (NRSROs), such as Fitch, Moody’s and Standard & Poor’s. We believe that this concentration in investment grade securities reduces our exposure to credit risk on our fixed income investments to an acceptable level. However, investment grade securities, in spite of their rating, can rapidly deteriorate and result in significant losses. Ratings published by the NRSROs are one of the tools used to evaluate the credit worthiness of our securities. The ratings reflect the subjective opinion of the rating agencies as to the credit worthiness of the securities, and therefore, we may be subject to additional credit exposure should the rating prove to be unreliable.

We also have exposure to credit risk related to our receivables from reinsurers. Our receivables from reinsurers (with regard to both paid and unpaid losses) approximated $262 million at September 30, 2014 and $251 million at December 31, 2013, with the 2014 increase primarily attributable to our acquisition of Eastern. We monitor the credit risk associated with our reinsurers using publicly available financial and rating agency data.

Equity Price Risk

At September 30, 2014 the fair value of our equity investments, excluding our equity investments in bond investment funds as discussed below, was $253 million. These equity securities are subject to equity price risk, which is defined as the potential for loss in fair value due to a decline in equity prices. The weighted average beta of this group of securities was 0.94. Beta measures the price sensitivity of an equity security or group of equity securities to a change in the broader equity market, in this case the S&P 500 Index. If the value of the S&P 500 Index increased by 10%, the fair value of these securities would be expected to increase by 9.4% to $277 million. Conversely, a 10% decrease in the S&P 500 Index would imply a decrease of 9.4% in the fair value of these securities to $230 million. The selected hypothetical changes of plus or minus 10% do not reflect what could be considered the best or worst case scenarios and are used for illustrative purposes only.

Our equity investments include equity investments in certain bond investment funds which are not significantly subject to equity price risk, and thus we have excluded these investments from the above analysis. Furthermore, these bond fund investments are primarily held by the segregated portfolio cells of our Eastern Re insurance subsidiary and changes in the fair value of these investments, when realized, accrue to the preferred stockholders of the related portfolio cell.

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ITEM 4. CONTROLS AND PROCEDURES.

The Chief Executive Officer and Chief Financial Officer of the Company participated in management’s evaluation of our disclosure controls and procedures (as defined in SEC Rule 13a-15(e)) as of September 30, 2014. ProAssurance’s disclosure controls and procedures are designed to reasonably assure that information required to be disclosed by us in reports we file or submit under the Exchange Act is accumulated and communicated to our management as appropriate to allow timely decisions regarding disclosure and is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective.

Changes in Internal Control over Financial Reporting

There have been no significant changes in our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, those controls during the quarter. On January 1, 2014 we completed the acquisition of Eastern Insurance Holdings, Inc. (Eastern). Our management has concluded that it will exclude Eastern's systems and processes from the scope of ProAssurance's assessment of internal control over financial reporting as of December 31, 2014 in reliance on the guidance set forth in Question 3 of a "Frequently Asked Questions" interpretive release issued by the staff of the Securities and Exchange Commission's Office of the Chief Accountant and the Division of Corporation Finance in September 2004 (and revised on October 6, 2004). We are excluding Eastern from that scope because we will not have completed our assessment of Eastern's systems and processes by that date.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

See Note 8 of the Notes to Condensed Consolidated Financial Statements.

ITEM 1A. RISK FACTORS.

There are no changes to the "Risk Factors" in Part 1, Item 1A of the 2013 Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

(a) Not applicable.

(b) Not applicable.

(c) Information required by Item 703 of Regulation S-K.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (*) (in thousands)
July 1 - 31, 2014	423,910	$44.67	423,910	$162,677
August 1 - 31, 2014	226,329	$45.10	226,329	$152,464
September 1 - 30, 2014	349,030	$45.26	349,030	$136,660
Total	999,269	$44.97	999,269	

* Under its current plan begun in November 2010, the ProAssurance Board of Directors has authorized $400 million for the repurchase of common shares or the retirement of outstanding debt. This is ProAssurance’s only plan for the repurchase of common shares, and the plan has no expiration date.

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ITEM 6. EXHIBITS

Exhibit Number	Description
31.1	Certification of Principal Executive Officer of ProAssurance as required under SEC rule 13a-14(a).
31.2	Certification of Principal Financial and Accounting Officer of ProAssurance as required under SEC rule 13a-14(a).
32.1	Certification of Principal Executive Officer of ProAssurance as required under SEC Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code, as amended (18 U.S.C. 1350).
32.2	Certification of Principal Financial and Accounting Officer of ProAssurance as required under SEC Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code, as amended (18 U.S.C. 1350).
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PROASSURANCE CORPORATION
November 5, 2014

/s/ Edward L. Rand, Jr.
Edward L. Rand, Jr.
Chief Financial Officer
(Duly authorized officer and principal financial officer)

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