DELPHI FINANCIAL GROUP INC/DE
Form 10-Q
November 14, 2001

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

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended September 30, 2001

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

For the transition period from _________ to __________

Commission File Number 001-11462

DELPHI FINANCIAL GROUP, INC.
(Exact name of registrant as specified in its charter)

Delaware	(302) 478-5142	13-34
(State or other jurisdiction of incorporation or organization)	(Registrant's telephone number, including area code)	(I.R.S. Employe Nu

1105 North Market Street, Suite 1230, P.O. Box 8985, Wilmington, Delaware 198
(Address of principal executive offices) (Zip

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to filing requirements for the past 90 days:

Yes X No

As of October 31, 2001, the Registrant had 16,256,354 shares of Class A Common Stock and 4,132,688 shares of Class B Common Stock outstanding.

DELPHI FINANCIAL GROUP, INC.
FORM 10-Q
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AND OTHER INFORMATION

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PART I. FINANCIAL INFORMATION

DELPHI FINANCIAL GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	Three Months Ended September 30,	
	2001	2000
Revenue:		
Premium and fee income	$ 127,068	$ 120,961
Net investment income	38,397	45,687
Net realized investment losses	(6,926)	(2,068)

	158,539	164,580
Benefits and expenses:		
Benefits, claims and interest credited to policyholders	96,972	88,225
Commissions	9,595	9,745
Amortization of cost of business acquired	8,536	8,217
Other operating expenses	23,172	19,712
	138,275	125,899
Operating income	20,264	38,681
Interest expense:		
Corporate debt	2,539	5,357
Dividends on Capital Securities of Delphi Funding L.L.C.....	1,072	2,328
	3,611	7,685
Income before income tax expense and extraordinary gain	16,653	30,996
Income tax expense	5,081	9,694
Income before extraordinary gain	11,572	21,302
Extraordinary gain, net of income taxes	1,233	-
Net income	$ 12,805	$ 21,302
Basic results per share of common stock:		
Income before extraordinary gain	$ 0.56	$ 1.05
Net income	0.62	1.05
Diluted results per share of common stock:		
Income before extraordinary gain	$ 0.55	$ 1.01
Net income	0.61	1.01
Dividend paid per share of common stock	$ 0.07	$ -

See notes to consolidated financial statements.

DELPHI FINANCIAL GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

Sept

Assets:	
Investments:	
Fixed maturity securities, available for sale	$
Short-term investments	
Other investments	
Cash	
Cost of business acquired	
Reinsurance receivables	
Other assets	
Assets held in separate account	
Total assets	$
Liabilities and Shareholders' Equity:	
Future policy benefits	$
Unpaid claims and claim expenses	
Policyholder account balances	
Corporate debt	
Advances from Federal Home Loan Bank	
Other liabilities and policyholder funds	
Liabilities related to separate account	
Total liabilities	
Company-obligated mandatorily redeemable Capital Securities of Delphi Funding L.L.C. holding solely junior subordinated deferrable interest debentures of the Company	
Shareholders' equity:	
Preferred Stock, $.01 par; 10,000,000 shares authorized	
Class A Common Stock, $.01 par; 40,000,000 shares authorized; 17,635,982 and 16,844,982 shares issued and outstanding, respectively	
Class B Common Stock, $.01 par; 20,000,000 shares authorized; 4,132,688 and 4,839,072 shares issued and outstanding, respectively	
Additional paid-in capital	
Net unrealized depreciation on investments	
Retained earnings	
Treasury stock, at cost; 1,495,890 and 1,435,390 shares of Class A Common Stock, respectively	
Total shareholders' equity	
Total liabilities and shareholders' equity	$

See notes to consolidated financial statements.

DELPHI FINANCIAL GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(DOLLARS IN THOUSANDS)
(UNAUDITED)

	Class A Common Stock	Class B Common Stock	Additional Paid-in Capital	Net Unrealized Depreciation on Investments	Ret Ear
Balance, January 1, 2000	$ 163	$ 52	$ 364,390	$(101,465)	$ 27
Net income	-	-	-	-	6
Increase in net unrealized depreciation on investments	-	-	-	(42,298)	
Comprehensive income					
Issuance of stock, exercise of stock options and share conversions	1	-	1,512	-	
Acquisition of treasury stock	-	-	-	-	
Balance, September 30, 2000	$ 164	$ 52	$ 365,902	$(143,763)	$ 34
Balance, January 1, 2001	$ 168	$ 48	$ 366,834	$ (53,622)	$ 27
Net income	-	-	-	-	5
Decrease in net unrealized depreciation on investments	-	-	-	33,001	
Comprehensive income	-	-	-	-	
Issuance of stock, exercise of stock options and share conversions	8	(7)	1,941	-	
Acquisition of treasury stock	-	-	-	-	
Dividends paid on common stock	-	-	-	-	(
Balance, September 30, 2001	$ 176	$ 41	$ 368,775	$ (20,621)	$ 32

See notes to consolidated financial statements.

DELPHI FINANCIAL GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(DOLLARS IN THOUSANDS)
(UNAUDITED)

Operating activities:
Net income ....
Adjustments to reconcile net income to net cash provided (used)
by operating activities:
Change in policy liabilities and policyholder accounts ....
Net change in reinsurance receivables and payables ....
Amortization, principally the cost of business acquired and investments ....
Deferred costs of business acquired ....
Net realized losses on investments ....
Net change in trading account securities ....
Net change in federal income tax liability ....
Extraordinary gain ....
Other ....

Net cash provided (used) by operating activities ....

Investing activities:
Purchases of investments and loans made ....
Sales of investments and receipts from repayment of loans ....
Maturities of investments ....
Net change in short-term investments ....
Sale of real estate ....
Business acquisitions ....
Change in deposit in separate account ....

Net cash provided (used) by investing activities ....

Financing activities:
Deposits to policyholder accounts ....
Withdrawals from policyholder accounts ....
Proceeds from issuance of common stock and exercise of stock options ....
Dividends paid on common stock ....
Acquisition of treasury stock ....
Borrowings under Credit Agreements ....
Principal payments under Credit Agreements ....
Principal payment under SIG Senior Notes ....
Repurchase of Senior Notes ....
Change in liability for Federal Home Loan Bank advances ....
Repurchase of Capital Securities ....
Change in liability for securities loaned or sold under agreements to repurchase ...

Net cash (used) provided by financing activities ....

Increase in cash ....
Cash at beginning of period ....

Cash at end of period ....

See notes to consolidated financial statements

DELPHI FINANCIAL GROUP, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

The financial statements included herein were prepared in conformity with accounting principles generally accepted in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. Such principles were applied on a basis consistent with those reflected in the Company's report on Form 10-K for the year ended December 31, 2000. The information furnished includes all adjustments and accruals of a normal recurring nature, which are, in the opinion of management, necessary for a fair presentation of results for the interim periods. Operating results for the nine months ended September 30, 2001 are not necessarily indicative of the results that may be expected for the year ended December 31, 2001. Certain reclassifications have been made in the 2000 financial statements to conform to the 2001 presentation. For further information refer to the consolidated financial statements and footnotes thereto included in the Company's report on Form 10-K for the year ended December 31, 2000. Capitalized terms used herein without definition have the meanings ascribed to them in the Company's report on Form 10-K for the year ended December 31, 2000.

The Company uses short-term, highly liquid debt instruments purchased with maturities of three months or less as part of its investment management program and, as such, began classifying these investments under the caption "short-term investments" in its Consolidated Balance Sheets and Consolidated Statements of Cash Flows in the third quarter of 2001. Prior to the third quarter of 2001, the Company classified these short-term, highly liquid debt instruments under the caption "cash equivalents" in its Consolidated Balance Sheets and Consolidated Statements of Cash Flows. Financial statements for the periods prior to the third quarter of 2001 have been restated to conform to the third quarter 2001 presentation.

Recently Adopted Accounting Standards. In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 is required to be adopted for fiscal years beginning after December 15, 2001. Under SFAS No. 142, goodwill and intangible assets deemed to have indefinite lives will no longer be amortized over a pre-determined period, but are required to be periodically reviewed for impairment. Other intangible assets with finite lives will continue to be amortized over their useful lives. An impairment loss resulting from the adoption of SFAS No. 142 would be accounted for as a cumulative effect of a change in accounting principle and recognized in the entity's first interim period financial statements regardless of the interim period in which the measurement is completed. Any subsequent impairment losses would be reflected within operating results in the income statement. The Company has not yet determined what the effect of SFAS No. 142 will be on the earnings and financial position of the Company.

NOTE B - INVESTMENTS

At September 30, 2001, the Company had fixed maturity securities available for sale with a carrying value and a fair value of $2,117.1 million and an amortized cost of $2,153.4 million. At December 31, 2000, the Company had fixed maturity securities available for sale with a carrying value and a fair value of $2,010.6 million and an amortized cost of $2,103.2 million.

NOTE C - SEGMENT INFORMATION

	Three Months Ended September 30,		Nin S
	2001	2000	2001
		(dollars in thousands	
Revenues excluding net realized investment losses:			
Group employee benefit products	$ 142,718	$ 140,238	$ 420,2
Asset accumulation products	17,604	21,192	54,1
Other (1)	5,143	5,218	15,4
	$ 165,465	$ 166,648	$ 489,7
Operating income (2):			
Group employee benefit products	$ 25,659	$ 34,435	$ 84,1
Asset accumulation products	2,776	7,129	9,4
Other (1)	(1,245)	(815)	(3,7
	$ 27,190	$ 40,749	$ 89,8

(1) Consists of operations that do not meet the quantitative thresholds for determining reportable segments and includes integrated disability and absence management services and certain corporate activities.

(2) Income excluding net realized investment losses and before interest and income tax expense and extraordinary gain.

NOTE D - REPURCHASE OF SENIOR NOTES AND CAPITAL SECURITIES OF DELPHI FUNDING L.L.C.

In June 2001, the Company repurchased $8.0 million par value of the 8.0% Senior

Notes due in October 2003. The Company also repurchased $64.0 million liquidation amount of the 9.31% Capital Securities, Series A, due in March 2027, during the first nine months of 2001. The Company recognized an extraordinary gain of $7.4 million, net of income tax expense of $4.0 million, in connection with these repurchases.

NOTE E - COMPUTATION OF RESULTS PER SHARE

The following table sets forth the calculation of basic and diluted results per share:

	Three Months Ended September 30,		Nine Mon Septem
	2001	2000	2001
	(dollars in thousands, except per sh		
Numerator:			
Income before extraordinary gain	$ 11,572	$ 21,302	$ 47,672
Extraordinary gain, net of income taxes	1,233	-	7,446
Net income	$ 12,805	$ 21,302	$ 55,118
Denominator:			
Weighted average common shares outstanding	20,564	20,358	20,542
Effect of dilutive securities	585	796	564
Weighted average common shares outstanding, assuming dilution	21,149	21,154	21,106

DELPHI FINANCIAL GROUP, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(UNAUDITED)

NOTE E - COMPUTATION OF RESULTS PER SHARE - (CONTINUED)

	Three Months Ended September 30,		Nine Months E September 3	
	2001	2000	2001	
	(dollars in thousands, except per share			
Basic results per share of common stock:				
Income before extraordinary gain	$ 0.56	$ 1.05	$ 2.32	$
Extraordinary gain, net of income taxes	0.06	-	0.36	

Net income	$ 0.62	$ 1.05	$ 2.68	$
Diluted results per share of common stock:				
Income before extraordinary gain	$ 0.55	$ 1.01	$ 2.26	$
Extraordinary gain, net of income taxes	0.06	-	0.35	
Net income	$ 0.61	$ 1.01	$ 2.61	$

DELPHI FINANCIAL GROUP, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

The following is an analysis of the results of operations and financial condition of Delphi Financial Group, Inc. (the "Company," which term includes the Company and its consolidated subsidiaries unless the context indicates otherwise). This analysis should be read in conjunction with the Consolidated Financial Statements and related notes included in this document, as well as the Company's report on Form 10-K for the year ended December 31, 2000. Capitalized terms used herein without definition have the meanings ascribed to them in the Company's report on Form 10-K for the year ended December 31, 2000.

RESULTS OF OPERATIONS

Nine Months Ended September 30, 2001 Compared to
Nine Months Ended September 30, 2000

Premium and Fee Income. Premium and fee income was $372.9 million for the nine months of 2001 as compared to $345.8 million in the 2000 period, an increase of 8%. Premiums from core group employee benefit products increased 13% to $333.3 million in the first nine months of 2001 from $294.4 million in the comparable period of 2000. This increase reflects normal growth in employment and salary levels for the Company's existing customer base, price increases, production of new business and improved persistency. Core group employee benefit products include group life, disability, excess and large deductible workers' compensation, travel accident and dental insurance and self-insurance workers' compensation bonds. Excess workers' compensation premiums increased 30% to $53.3 million in the first nine months of 2001 from $40.9 million in the comparable period of 2000. This increase reflects improvements in the pricing environment in this market sector and increased demand due to higher primary workers' compensation rates. Disruption in the excess workers' compensation marketplace due to difficulties experienced by some competitors created opportunities for SNCC, which contributed to high levels of new production, particularly during 2000. The Company believes that additional increases in primary workers' compensation rates and rising reinsurance costs as a result of the World Trade Center attacks will further increase the demand for its excess workers' compensation products and result in price increases for these products. The Company has also implemented price increases for certain disability customers. Non-core group employee benefit products include reinsurance pools, loss portfolio transfers ("LPTs"), primary workers' compensation, commercial automobile liability and bail bond insurance, and property and workers' compensation reinsurance. Premiums from non-core group employee benefit products decreased to $26.3 million in the first nine months of 2001 from $37.6 million in the comparable period of 2000 primarily due to a lower level of premium from LPTs, which are episodic in nature. Deposits from the Company's asset accumulation products were $64.8 million for the first nine months of 2001 as compared to $119.6 million for the first nine months of 2000. Deposits for these products, which are long-term in nature, are not recorded as premiums; instead, the deposits are recorded as a liability. The Company made a decision in the first quarter of 2001 to reduce the crediting rates offered on its asset accumulation products due to the decline in market interest rates and the resulting interest rate spreads available to the Company on these products. Accordingly, the Company experienced a lower level of production from its asset accumulation business in the first nine months of 2001 as compared to the same period in 2000.

Net Investment Income. Net investment income for the first nine months of 2001 was $116.9 million as compared to $142.9 million for the 2000 period. The tax equivalent weighted average annualized yield (1) on invested assets was 6.9% on average invested assets(2) of $2,325.7 million for the first nine months of 2001 and 7.7% on average invested assets(2) of $2,561.6 million for the first nine months of 2000. The decrease in investment income reflects the Company's liquidation during the fourth quarter of 2000 of a substantial majority of its holding company investments. The proceeds from these sales were used to repay $150.0 million of outstanding borrowings under the Company's Credit Agreements in the first half of 2001 and to repurchase $64.0 million liquidation amount of the Capital Securities during the first nine months of 2001.

Net realized investment losses. Net realized investment losses were $6.3 million in the first nine months of 2001 as compared to $3.6 million in the first nine months of 2000. The Company's investment strategy results in periodic sales of securities and the recognition of realized investment gains and losses. In the third quarter of 2001, the net loss realized on the Company's investment portfolio includes a $12.5 million provision for the other than temporary decline in the fair value of certain fixed maturity securities.

(1) The tax equivalent weighted average annualized yield on the Company's investment portfolio for each period is computed by dividing net investment income, increased by the tax savings generated from tax exempt interest income and the dividends received deduction, by average invested assets for the period.

(2) Average invested assets are computed by dividing the total of invested assets as reported on the Company's balance sheet at the beginning of each period plus the individual quarter-end balances by the total number of periods and deducting one-half of net investment income, including tax savings.

Benefits and Expenses. Policyholder benefits and expenses for the first nine months of 2001 were $399.9 million as compared to $367.2 million for the 2000 period, an increase of 9%. This increase primarily reflects the increase in premiums from the Company's core group employee benefit products discussed above. Policyholder benefits for the first nine months of 2001 also include losses of $3.8 million, net of reinsurance coverages, as a result of the World Trade Center attacks. The combined ratio (loss ratio plus expense ratio) for the Company's group employee benefits segment was 92.4% in the first nine months of 2001, excluding the World Trade Center losses, and 92.7% for the comparable period of 2000. However, the Company anticipates that this combined ratio will increase in the fourth quarter of 2001 due to a strengthening in its excess workers' compensation reserves. A number of unusual catastrophic losses, unrelated to the World Trade Center attacks, have recently occurred which present the likelihood of higher than previously established reserves for expected claim payments. While presently available information is not sufficient to quantify the level of any reserve strengthening, a review has been undertaken which will be completed by the end of the fourth quarter of 2001. Any resulting reserve strengthening will be reflected in the Company's earnings at that time. In addition, certain non-core group employee benefit products expose the Company to the possibility of episodic losses, which could cause the combined ratio to differ materially from current trends. Benefits and interest credited on asset accumulation products increased by $3.2 million in the first nine months of 2001 principally due to an increase in average funds under management from $659.9 million in the first nine months of 2000 to $743.8 million in the 2001 period. The weighted average annualized crediting rate on asset accumulation products was 5.5% in the first nine months of 2000 and 2001.

Interest Expense and Extraordinary Gain. Interest expense was $13.8 million in the first nine months of 2001 as compared to $23.1 million in the 2000 period, a decrease of $9.3 million. This decrease was primarily a result of the Company's repayment of $150.0 million of outstanding borrowings under the Company's Credit Agreements during the first half of 2001 and the repurchase of $64.0 million liquidation amount of the Capital Securities in the open market which occurred on various dates during the first nine months of 2001. In addition, the Company repurchased $8.0 million par value of the 8.0% Senior Notes in June 2001. The Company recognized an extraordinary gain of $7.4 million, net of income tax expense of $4.0 million, in connection with these repurchases.

Income before extraordinary gain. Management believes the concept of "operating earnings" of companies is helpful in comparing the Company's performance with that of similar companies. However, operating earnings should not be considered a substitute for net income as an indication of the Company's overall performance. Operating earnings for the Company, consisting of income before extraordinary gain adjusted to exclude realized investment losses, were $51.7 million ($2.45 per share, diluted) for the first nine months of 2001 as compared to $67.9 million ($3.23 per share, diluted) for the same period in 2000. The decrease in operating earnings is primarily attributable to the Company's liquidation during the fourth quarter of 2000 of a substantial majority of its holding company investments (see "Net Investment Income"). Operating earnings for the first nine months of 2001 have also been reduced by losses of $2.5 million ($0.12 per share, diluted), net of a tax benefit of $1.3 million, as a result of the World Trade Center attacks.

Three Months Ended September 30, 2001 Compared to
Three Months Ended September 30, 2000

Premium and Fee Income. Premium and fee income for the third quarter of 2001 was $127.1 million as compared to $121.0 million for the 2000 period, an increase of 5%. Premiums from core group employee benefit products increased 13% to $114.2 million in the third quarter of 2001 from $101.2 million in the comparable period of 2000. This increase reflects normal growth in employment and salary levels for the Company's existing customer base, price increases, production of new business and improved persistency. Core group employee benefit products include group life, disability, excess and large deductible workers' compensation, travel accident and dental insurance and self-insurance workers' compensation bonds. Excess workers' compensation premiums increased 28% to $18.9 million from $14.8 million in the comparable period of 2000. This increase reflects improvements in the pricing environment in this market sector and increased demand due to higher primary workers' compensation rates. Disruption in the excess workers' compensation marketplace due to difficulties experienced by some competitors created opportunities for SNCC, which contributed to high levels of new production, particularly during 2000. The Company believes that additional increases in primary workers' compensation rates and rising reinsurance costs as a result of the World Trade Center attacks will further increase the demand for its excess workers' compensation products and result in price increases for these products. The Company has also implemented price increases for certain disability customers. Non-core group employee benefit products include reinsurance pools, loss portfolio transfers ("LPTs"), primary workers' compensation, commercial automobile liability and bail bond insurance, and property and workers' compensation reinsurance. Premiums from non-core group employee benefit products decreased to $8.2 million in the third quarter of 2001 from $15.2 million in the comparable period of 2000 primarily due to a lower level of premium from LPTs, which are episodic in nature. Deposits from the Company's asset accumulation products were $22.7 million for the third quarter of 2001 as compared to $40.9 million for the third quarter of 2000. Deposits for these products, which are long-term in nature, are not recorded as premiums; instead,

the deposits are recorded as a liability. The Company made a decision in the first quarter of 2001 to reduce the crediting rates offered on its asset accumulation products due to the decline in market interest rates and the resulting interest rate spreads available to the Company on these products. Accordingly, the Company experienced a lower level of production from its asset accumulation business in the third quarter of 2001 as compared to the same period in 2000.

Net Investment Income. Net investment income for the third quarter of 2001 was $38.4 million as compared to $45.7 million in the third quarter of 2000. The tax equivalent weighted average annualized yield(1) on invested assets was 6.8% on average invested assets(2) of $2,326.6 million for the third quarter of 2001 and 7.2% on average invested assets(2) of $2,619.2 million for the third quarter of 2000. The decrease in investment income reflects the Company's liquidation during the fourth quarter of 2000 of a substantial majority of its holding company investments. The proceeds from these sales were used to repay $150.0 million of outstanding borrowings under the Company's Credit Agreements and to repurchase $64.0 million liquidation amount of the Capital Securities during the first nine months of 2001.

Net realized investment losses. Net realized investment losses were $6.9 million in the third quarter of 2001 as compared to $2.1 million in the comparable period of 2000. The Company's investment strategy results in periodic sales of securities and the recognition of realized investment gains and losses. In the third quarter of 2001, the net loss realized on the Company's investment portfolio includes a $12.5 million provision for the other than temporary decline in the fair value of certain fixed maturity securities.

Benefits and Expenses. Policyholder benefits and expenses for the third quarter of 2001 were $138.3 million as compared to $125.9 million for the third quarter of 2000, an increase of 10%. This increase primarily reflects the increase in premiums from the Company's core group employee benefit products discussed above. Policyholder benefits for the third quarter of 2001 also include losses of $3.8 million, net of reinsurance coverages, as a result of the World Trade Center attacks. The combined ratio (loss ratio plus expense ratio) for the Company's group employee benefits segment was 92.5% in the third quarter of 2001, excluding the World Trade Center losses, as compared to 90.9% for the 2000 period. However, the Company anticipates that this combined ratio will increase in the fourth quarter of 2001 due to a strengthening in its excess workers' compensation reserves. A number of unusual catastrophic losses, unrelated to the World Trade Center attacks, have recently occurred which present the likelihood of higher than previously established reserves for expected claims payments. While presently available information is not sufficient to quantify the level of any reserve strengthening, a review has been undertaken which will be completed by the end of the fourth quarter of 2001. Any resulting reserve strengthening will be reflected in the Company's earnings at that time. In addition, certain non-core group employee benefit products expose the Company to the possibility of episodic losses, which could cause the combined ratio to differ materially from current trends. Benefits and interest credited on asset accumulation products increased by $0.5 million in the third quarter of 2001 principally due to an increase in average funds under management from $682.9 million in the third quarter of 2000 to $748.2 million in the 2001 period. The weighted average annualized crediting rate on asset accumulation products in the third quarter of 2001 and the comparable period of 2000 was 5.6%.

Interest Expense and Extraordinary Gain. Interest expense was $3.6 million for the third quarter of 2001 as compared to $7.7 million in the third quarter of 2000, a decrease of $4.1 million. This decrease was primarily a result of the Company's repayment of $150.0 million of outstanding borrowings under the Company's Credit Agreements and $54.0 million liquidation amount of the Capital Securities during the first half of 2001. The Company repurchased an additional $10.0 million liquidation amount of the Capital Securities in the open market at the end of the third quarter of 2001. The Company recognized an extraordinary gain of $1.2 million, net of income tax expense of $0.7 million, in connection with this repurchase.

Income before extraordinary gain. Management believes the concept of "operating earnings" of companies is helpful in comparing the Company's performance with that of similar companies. However, operating earnings should not be considered a substitute for net income as an indication of the Company's overall performance. Operating earnings for the Company, consisting of income before extraordinary gain adjusted to exclude realized investment losses, were $16.1 million ($0.76 per share, diluted) for the third quarter of 2001 as compared to $22.6 million ($1.07 per share, diluted) for the same period in 2000. The decrease in operating earnings is primarily attributable to the Company's liquidation during the fourth quarter of 2000 of a substantial majority of its holding company investments (see "Net Investment Income"). Operating earnings for the third quarter of 2001 have also been reduced by losses of $2.5 million ($0.12 per share, diluted), net of a tax benefit of $1.3 million, as a result of the World Trade Center attacks.

(1) The tax equivalent weighted average annualized yield on the Company's investment portfolio for each period is computed by dividing net investment income, increased by the tax savings generated from tax exempt interest income and the dividends received deduction, by average invested assets for the period.

(2) Average invested assets are computed by dividing the total of invested assets as reported on the Company's balance sheet at the beginning of each period plus the individual quarter-end balances by the total number of periods and deducting one-half of net investment income, including tax savings.

LIQUIDITY AND CAPITAL RESOURCES

General. The Company had $74.9 million of financial resources available at the holding company level at September 30, 2001, which was primarily comprised of fixed maturity securities and investments in the common stock of its investment subsidiaries. The assets of the investment subsidiaries are primarily invested in fixed maturity securities. Financial resources available at the holding company level have decreased $192.0 million since December 31, 2000 primarily due to the liquidation of a substantial majority of the investments of its investment subsidiaries. The Company used the proceeds from these sales to repay $150.0 million of outstanding borrowings under the Credit Agreements in the first half of 2001 and to repurchase $64.0 million liquidation amount of the Capital Securities during the first nine months of 2001. In addition, the Company repurchased $8.0 million par value of the 8% Senior Notes in June 2001. The maximum amount of borrowings available under the Credit Agreements, which mature in April 2003, is currently $190.0 million and is scheduled to reduce to $140.0 million in October 2002. The Company has $177.0 million of borrowings available to it as of October 1, 2001. A shelf registration is also in effect under which up to $49.2 million in securities may be issued by the Company.

Other sources of liquidity at the holding company level include dividends paid from subsidiaries, primarily generated from operating cash flows and investments. The Company's insurance subsidiaries are permitted, without prior regulatory or other approval, to make dividend payments of $77.8 million during 2001, of which $26.0 million has been paid during the first nine months of 2001. In general, dividends from the Company's non-insurance subsidiaries are not subject to regulatory or other restrictions.

The Company's current liquidity needs, in addition to funding operating expenses, include principal and interest payments on the Senior Notes, the SIG Senior Notes and the Subordinated Notes and distributions on the Capital Securities. The Senior Notes mature in their entirety in October 2003 and are not subject to any sinking fund requirements nor are they redeemable prior to maturity. The SIG Senior Notes mature in $9.0 million annual installments, with the next installment payable in May 2002 and the Subordinated Notes mature in their entirety in June 2003. The junior subordinated debentures underlying the Capital Securities are not redeemable prior to March 25, 2007.

Operating activities, which include $29.8 million of cash provided by trading account activity, increased cash by $124.1 million in the first nine months of 2001. Operating activities during the first nine months of 2000 increased cash by $70.7 million, excluding $58.1 million of funds related to a rescinded reinsurance transaction that were returned to the ceding company during the first quarter of 2000 and a net cash payment of $19.7 million related to the cession by the Company of group employee benefit product reserves. During the first nine months of 2001, proceeds from investment sales were primarily used to repay $150.0 million of outstanding borrowings under the Company's Credit Agreements in the first half of 2001 and repurchase $64.0 million liquidation amount of the Capital Securities in the first nine months of 2001. Sources of liquidity available to the Company and its subsidiaries are expected to exceed their current and long-term cash requirements.

In September 2001, the Company entered into an agreement with Delphi International Ltd. and Oracle Re to commute various reinsurance agreements that the Company had entered into with Oracle Re in 1998. Upon consummation of the commutation in October 2001, Oracle Re paid approximately $84.0 million to the Company, net of $11.5 million which had been held by the Company, related to group employee benefit reserves ceded to Oracle Re under such agreements. The Company expects that its net investment income and benefit expense (and, therefore, its combined ratio) will increase as a result of the commutation. However, this transaction is not expected to have a material impact on the Company's financial position, liquidity or net income.

MARKET RISK

There have been no material changes in the Company's exposure to market risk or its management of such risk since December 31, 2000.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

In connection with, and because it desires to take advantage of, the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, the Company cautions readers regarding certain forward-looking statements in the above "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this Form 10-Q and in any other statement made by, or on behalf of, the Company, whether in future filings with the Securities and Exchange Commission or otherwise. Forward-looking statements are statements not based on historical information and which relate to future operations, strategies, financial results or other developments. Some forward-looking statements may be identified by the use of terms such as "expects," "believes," "anticipates," "intends," "judgment" or other similar expressions. Forward-looking statements are necessarily based upon estimates and assumptions that are inherently subject to significant business, economic, competitive and other uncertainties and contingencies, many of which are beyond the Company's control and many of which, with respect to

future business decisions, are subject to change. Examples of such uncertainties and contingencies include, among other important factors, those affecting the insurance industry generally, such as the economic and interest rate environment, federal and state legislative and regulatory developments, including but not limited to changes in financial services and tax laws and regulations, and market pricing and competitive trends relating to insurance products and services, and those relating specifically to the Company's business, such as the level of its insurance premiums and fee income, the claims experience and other factors affecting the profitability of its insurance products, the performance of its investment portfolio and changes in the Company's investment strategy, acquisitions of companies or blocks of business, and ratings by major rating organizations of its insurance subsidiaries. These uncertainties and contingencies can affect actual results and could cause actual results to differ materially from those expressed in any forward-looking statements made by, or on behalf of, the Company. The Company disclaims any obligation to update forward-looking information.

PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

10.1 - Commutation, Prepayment and Redemption Agreement, dated September 14, 2001, between Delphi Financial Group, Inc., Safety National Casualty Corporation, Reliance Standard Life Insurance Company, Delphi International Ltd. and Oracle Reinsurance Company Ltd.

11 - Computation of Results per Share of Common Stock (incorporated by reference to Note E to the Consolidated Financial Statements included elsewhere herein)

(b) Reports on Form 8-K

None

SIGNATURES

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.

DELPHI FINANCIAL GROUP, INC. (Registrant)

/s/ ROBERT ROSENKRANZ

Robert Rosenkranz
Chairman of the Board, President and Chief Executive Officer
(Principal Executive Officer)

/s/ THOMAS W. BURGHART

Thomas W. Burghart
Vice President and Treasurer
(Principal Accounting and Financial Officer)

Date: November 14, 2001