

PRIMUS GUARANTY LTD  
Form 10-Q  
August 12, 2011

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

**FORM 10-Q**

**(Mark One)**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
For the quarterly period ended June 30, 2011  
or**

**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: 001-32307**

**Primus Guaranty, Ltd.**  
(Exact name of registrant as specified in its charter)

**Bermuda**  
(State or other jurisdiction of  
incorporation or organization)

**98-0402357**  
(I.R.S. Employer Identification No.)

**Clarendon House  
2 Church Street  
Hamilton HM 11, Bermuda**  
(Address of principal executive offices, including zip code)  
**441-296-0519**  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No   
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

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As of August 5, 2011, the number of shares outstanding of the issuer's common shares, \$0.08 par value, was 37,144,073.

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**Primus Guaranty, Ltd.**  
**Form 10-Q**  
For the quarterly period ended June 30, 2011  
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## Item 1. Financial Statements

**Primus Guaranty, Ltd.**  
**Condensed Consolidated Statements of Financial Condition (Unaudited)**  
*(in thousands except share amounts)*

	<b>June 30, 2011</b>	<b>December 31, 2010</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 115,516	\$ 177,736
Investments (includes \$335,856 and \$288,815 at fair value as of June 30, 2011 and December 31, 2010, respectively)	336,027	288,985
Restricted cash and investments	135,080	138,540
Accrued interest and premiums	5,632	5,860
Unrealized gain on credit swaps, at fair value	2,396	2,006
Debt issuance costs, net	3,865	4,072
Other assets (includes \$9,605 and \$11,559 at fair value as of June 30, 2011 and December 31, 2010, respectively)	12,840	17,660
Total assets	\$ 611,356	\$ 634,859
<b>Liabilities and Equity</b>		
<b>Liabilities</b>		
Accounts payable and accrued expenses	\$ 4,401	\$ 8,701
Unrealized loss on credit swaps, at fair value	255,364	395,164
Payable for credit events	2,531	3,447
Long-term debt	202,688	215,828
Restructuring liabilities	61	3,729
Other liabilities	3,440	6,025
Total liabilities	468,485	632,894
Commitments and contingencies		
<b>Equity (deficit)</b>		
Common shares, \$0.08 par value, 62,500,000 shares authorized, 37,239,493 and 38,078,790 shares issued and outstanding at June 30, 2011 and December 31, 2010, respectively	2,978	3,046
Additional paid-in capital	272,069	275,453
Accumulated other comprehensive income	4,810	3,333
Retained earnings (deficit)	(227,132)	(372,969)
Total shareholders' equity (deficit) of Primus Guaranty, Ltd	52,725	(91,137)
Preferred securities of subsidiary	90,146	93,102
Total equity	142,871	1,965
Total liabilities and equity	\$ 611,356	\$ 634,859

*See accompanying notes.*

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**Primus Guaranty, Ltd.**  
**Condensed Consolidated Statements of Operations (Unaudited)**  
*(in thousands except per share amounts)*

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2011</b>	<b>2010</b>	<b>2011</b>	<b>2010</b>
<b>Revenues</b>				
Net credit swap revenue (loss)	\$ 61,009	\$ (189,708)	\$ 147,107	\$ (102,178)
Interest income	2,569	3,541	5,180	6,240
Gain on retirement of long-term debt		2,676	2,760	7,433
Other income (loss)	321	(51)	618	132
<b>Total revenues</b>	<b>63,899</b>	<b>(183,542)</b>	<b>155,665</b>	<b>(88,373)</b>
<b>Expenses</b>				
Compensation and employee benefits	1,570	4,546	3,692	9,126
Professional and legal fees	674	2,178	1,496	3,663
Interest expense	1,546	1,737	3,113	3,606
Other	1,077	1,777	2,393	3,500
<b>Total expenses</b>	<b>4,867</b>	<b>10,238</b>	<b>10,694</b>	<b>19,895</b>
Income (loss) from continuing operations before provision (benefit) for income taxes	59,032	(193,780)	144,971	(108,268)
Provision (benefit) for income taxes	1	(113)	11	27
Income (loss) from continuing operations, net of tax	59,031	(193,667)	144,960	(108,295)
Income (loss) from discontinued operations, net of tax	2,808	(119,937)	2,538	(28,386)
<b>Net income (loss)</b>	<b>61,839</b>	<b>(313,604)</b>	<b>147,498</b>	<b>(136,681)</b>
Less:				
Distributions on preferred securities of subsidiary	702	724	1,661	1,712
Net loss from discontinued operations attributable to non-parent interests in CLOs		(125,934)		(36,521)
<b>Net income (loss) available to common shares</b>	<b>\$ 61,137</b>	<b>\$ (188,394)</b>	<b>\$ 145,837</b>	<b>\$ (101,872)</b>
Income (loss) per common share:				
<b>Basic:</b>				
Income (loss) from continuing operations	\$ 1.55	\$ (5.00)	\$ 3.78	\$ (2.84)
Income (loss) from discontinued operations	\$ 0.08	\$ 0.16	\$ 0.07	\$ 0.21



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Net income (loss) available to common shares	\$ 1.63	\$ (4.84)	\$ 3.85	\$ (2.63)
<b>Diluted:</b>				
Income (loss) from continuing operations	\$ 1.55	\$ (5.00)	\$ 3.76	\$ (2.84)
Income (loss) from discontinued operations	\$ 0.07	\$ 0.16	\$ 0.07	\$ 0.21
Net income (loss) available to common shares	\$ 1.62	\$ (4.84)	\$ 3.83	\$ (2.63)

**Weighted average common shares outstanding:**

Basic	37,638	38,903	37,881	38,795
Diluted	37,837	38,903	38,124	38,795

*See accompanying notes.*

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**Primus Guaranty, Ltd.**  
**Condensed Consolidated Statements of Cash Flows (Unaudited)**  
*(in thousands)*

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2011</b>	<b>2010</b>
<b>Cash flows from operating activities</b>		
Net income (loss) available to common shares	\$ 145,837	\$ (101,872)
Net loss attributable to non-parent interests in CLOs		(36,521)
Distributions on preferred securities of subsidiary	1,661	1,712
Net income (loss)	147,498	(136,681)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Non-cash items included in net income (loss):		
Net unrealized losses on CLO loans and securities		6,366
Net unrealized losses on CLO notes		92,558
Net realized gains by the CLOs		(42,580)
Net unrealized (gains) losses on credit swaps	(140,190)	67,712
Gain on retirement of long-term debt	(2,760)	(7,433)
Other	3,019	2,336
Increase (decrease) in cash resulting from changes in:		
CLO cash and cash equivalents		(25,219)
CLO other assets		(16,261)
CLO other liabilities		46,444
Proceeds from sale of CLO loans and securities		525,125
Purchases of CLO loans and securities		(514,785)
Restricted cash	(2,010)	(1,992)
Accrued interest and premiums	228	(652)
Other assets	3,654	(446)
Trading account assets		(53,346)
Accounts payable and accrued expenses	(3,405)	(3,260)
Payable for credit events	(916)	(23,964)
Restructuring liabilities	(3,668)	
Other liabilities	(1,510)	24,680
Net cash used in operating activities	(60)	(61,398)
<b>Cash flows from investing activities</b>		
Purchases of available-for-sale investments	(225,063)	(122,569)
Maturities and sales of available-for-sale investments	180,663	77,021
Payments received from CLO investments	1,362	
Purchases of fixed assets	(6)	(23)
Net cash used in investing activities	(43,044)	(45,571)
<b>Cash flows from financing activities</b>		

Repayment of CLO notes by the CLOs		(35,127)
Retirement of long-term debt	(9,069)	(12,500)
Purchase and retirement of common shares	(6,511)	(3,269)
Purchase of preferred securities of subsidiary	(1,875)	
Net preferred distributions of subsidiary	(1,661)	(1,712)
Net cash used in financing activities	(19,116)	(52,608)
Net effect of exchange rate changes on cash		(74)
Net increase (decrease) in cash	(62,220)	(159,651)
Cash and cash equivalents at beginning of period	177,736	299,514
Cash and cash equivalents at end of period	\$ 115,516	\$ 139,863

**Supplemental disclosures of cash flow information:**

Cash paid for interest	\$ 3,161	\$ 3,679
Cash paid for taxes	\$	\$ 41

*See accompanying notes.*

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**Primus Guaranty, Ltd.**  
**Condensed Consolidated Statements of Equity (Unaudited)**  
*(in thousands)*

	<b>Six Months Ended June 30, 2011</b>	<b>Year Ended December 31, 2010</b>
<b>Common shares</b>		
Balance at beginning of period	\$ 3,046	\$ 3,061
Common shares purchased and retired	(98)	(166)
Shares issued under employee compensation plans	30	151
Balance at end of period	2,978	3,046
<b>Additional paid-in capital</b>		
Balance at beginning of period	275,453	280,685
Common shares purchased and retired	(6,443)	(13,135)
Shares vested under employee compensation plans	1,978	7,903
Preferred shares purchased by subsidiary	1,081	
Balance at end of period	272,069	275,453
<b>Accumulated other comprehensive income (loss)</b>		
Balance at beginning of period	3,333	2,148
Foreign currency translation adjustments		30
Change in unrealized holding gains on available-for-sale securities	1,477	1,155
Balance at end of period	4,810	3,333
<b>Retained earnings (deficit)</b>		
Balance at beginning of period	(372,969)	(628,443)
Net income	147,498	197,462
Net loss attributable to non-parent interests in CLOs		61,174
Distributions on preferred securities of subsidiary	(1,661)	(3,162)
Balance at end of period	(227,132)	(372,969)
<b>Appropriated retained earnings from CLO consolidation</b>		
Adoption of ASC Topic 810, <i>Consolidation</i>		265,639
Net loss attributable to non-parent interests in CLOs		(61,174)
Deconsolidation of CLOs		(204,465)
Balance at end of period		

Total shareholders' equity (deficit) of Primus Guaranty, Ltd.	52,725	(91,137)
<b>Preferred securities of subsidiary</b>		
Balance at beginning of period	93,102	93,102
Net purchase of preferred shares	(2,956)	
Balance at end of period	90,146	93,102
Total equity at end of period	\$ 142,871	\$ 1,965

*See accompanying notes.*

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**Primus Guaranty, Ltd.**

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

**1. Organization and Business**

In these notes, the terms Primus Guaranty and the Company refer to Primus Guaranty, Ltd., a Bermuda company, collectively with its subsidiaries; Primus Financial refers to Primus Financial Products, LLC, a Delaware limited liability company, collectively with its subsidiaries, and Primus Asset Management refers to Primus Asset Management, Inc., a Delaware corporation. Primus Financial and Primus Asset Management are subsidiaries of Primus Guaranty, Ltd.

Primus Financial was established to sell credit protection in the form of credit swaps to global financial institutions and major credit swap dealers against primarily investment grade credit obligations of corporate and sovereign issuers. During 2009, the Company announced its intention to amortize Primus Financial's credit swap portfolio. It is expected that Primus Financial's existing credit swap contracts will expire at maturity unless terminated early through credit events or credit risk mitigation transactions. It is not expected that additional credit swaps will be added to Primus Financial's portfolio.

Primus Asset Management acts as manager of the credit swap and investment portfolios of Primus Financial. Primus Asset Management has entered into a Services Agreement with its affiliates, whereby it provides management, consulting, information technology and other services.

On December 1, 2010, the Company divested its collateralized loan obligation (CLO) asset management business, which included the sale of CypressTree Investment Management, LLC (CypressTree).

See note 7 of these notes to condensed consolidated financial statements for further discussion on Discontinued Operations.

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**2. Summary of Significant Accounting Policies**

*Basis of Presentation*

The accompanying unaudited condensed consolidated financial statements of Primus Guaranty have been prepared in accordance with generally accepted accounting principles 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. In the opinion of management, all adjustments (consisting of normal recurring accruals and the use of estimates) considered necessary for a fair presentation pursuant to these requirements have been included. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010. The results of operations for any interim period are not necessarily indicative of the results for a full year.

The condensed consolidated financial statements are presented in U.S. dollar equivalents. During the periods presented, the Company s credit swap activities were conducted by Primus Financial in U.S. dollars and euros. Certain prior year amounts have been reclassified to conform to current year presentation. There was no effect on net income available to common shares as a result of these reclassifications.

*Principles of Consolidation*

The condensed consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest, including CLOs under management during 2010, for which Primus Guaranty was deemed to be the primary beneficiary. All significant intercompany balances have been eliminated.

*Recent Accounting Pronouncements*

In January 2010, the Financial Accounting Standards Board ( FASB ) issued ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820) Improving Disclosures about Fair Value Measurements*. ASU No. 2010-06 provides amended disclosure requirements related to fair value measurements, including transfers in and out of Levels 1 and 2 and activity in Level 3 under the fair value hierarchy. ASU No. 2010-06 is effective for financial statements issued for reporting periods beginning after December 15, 2009 for certain disclosures and for reporting periods beginning after December 15, 2010 for certain additional disclosures regarding activity in Level 3 fair value measurements. Since these amended principles require only additional disclosures concerning fair value measurements, adoption of ASU No. 2010-06 did not affect the Company s financial condition, results of operations or cash flows.

In May 2011, the FASB issued ASU 2011-04, which amends the measurement and disclosure requirements for fair value. The guidance is effective for interim and annual periods beginning after December 15, 2011. The Company is currently assessing the impact of this guidance.

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In June 2011, the FASB issued ASU 2011-05, which will require additional disclosure with respect to other comprehensive income. The guidance is effective for interim and annual periods beginning after December 15, 2011. The Company is currently assessing the impact of this guidance.

**3. Investments**

The following tables summarize the composition of the Company's available-for-sale and held-to-maturity investments at June 30, 2011 and December 31, 2010 (in thousands):

	<b>June 30, 2011</b>			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
<b>Available-for-sale:</b>				
Corporate debt securities	\$ 323,540	\$ 4,639	\$ (61)	\$ 328,118
Asset-backed securities	1,120	251	(18)	1,353
Total available-for-sale	324,660	4,890	(79)	329,471
<b>Held-to-maturity:</b>				
Certificate of deposit	171			171
Total held-to-maturity	171			171
Total investments	\$ 324,831	\$ 4,890	\$ (79)	\$ 329,642
	<b>December 31, 2010</b>			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
<b>Available-for-sale:</b>				
Corporate debt securities	\$ 284,090	\$ 3,378		