

INVESTORS TITLE CO  
Form 10-Q  
November 02, 2006

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

**FORM 10-Q**

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

For the Quarterly Period Ended September 30, 2006

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: 0-11774

**INVESTORS TITLE COMPANY**  
(Exact name of registrant as specified in its charter)

North Carolina  
(State of Incorporation)

56-1110199  
(I.R.S. Employer Identification No.)

121 North Columbia Street, Chapel Hill, North Carolina 27514  
(Address of Principal Executive Offices) (Zip Code)

(919) 968-2200  
(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 of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):  
Large accelerated filer Accelerated filer Non-accelerated filer x

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

As of October 23, 2006, there were 2,506,892 common shares of the registrant outstanding.



**INVESTORS TITLE COMPANY  
AND SUBSIDIARIES**

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**Item 1. Financial Statements**

**Investors Title Company and Subsidiaries**  
**Consolidated Balance Sheets**  
*As of September 30, 2006 and December 31, 2005*  
*(Unaudited)*

|  | September 30, 2006    | December 31, 2005     |
|--|-----------------------|-----------------------|
| <b>Assets</b>  |                       |                       |
| Cash and cash equivalents  | \$ 3,957,098          | \$ 14,608,481         |
| Investments in securities:   |                       |                       |
| Fixed maturities:  |                       |                       |
| Held-to-maturity, at amortized cost (fair value:<br>2006: \$1,246,739; 2005: \$1,719,190)  | 1,200,276             | 1,648,708             |
| Available-for-sale, at fair value  | 96,677,536            | 75,472,342            |
| Equity securities, available-for-sale, at fair value   | 12,363,984            | 9,437,678             |
| Short-term investments   | 3,000,463             | 7,257,734             |
| Other investments  | 1,629,631             | 1,336,111             |
| Total investments  | 114,871,890           | 95,152,573            |
| Premiums and fees receivable, less allowance for<br>doubtful accounts of<br>\$2,536,000 and \$2,444,000 for 2006 and 2005,<br>respectively |                       |                       |
|  | 7,326,398             | 7,818,558             |
| Accrued interest and dividends   | 1,081,266             | 1,010,198             |
| Prepaid expenses and other assets  | 6,796,132             | 1,592,326             |
| Property acquired in settlement of claims  | 417,800               | 359,980               |
| Property, net  | 6,119,700             | 5,466,765             |
| Deferred income taxes, net   | 2,011,981             | 2,462,647             |
| <b>Total Assets</b>  | <b>\$ 142,582,265</b> | <b>\$ 128,471,528</b> |
| <b>Liabilities and Stockholders' Equity</b>  |                       |                       |
| <b>Liabilities:</b>  |                       |                       |
| Reserves for claims (Note 2)   | \$ 36,477,000         | \$ 34,857,000         |
| Accounts payable and accrued liabilities   | 12,758,421            | 7,928,384             |
| Commissions and reinsurance payables   | 353,362               | 442,098               |
| Current income taxes payable   | 126,255               | 946,790               |
| Total liabilities  | 49,715,038            | 44,174,272            |
| <b>Commitments and Contingencies (Note 7)</b>  |                       |                       |
| <b>Stockholders' Equity:</b>   |                       |                       |
| Class A Junior Participating preferred stock (shares<br>authorized 100,000; no shares issued)  | -                     | -                     |
| Common stock-no par value (shares authorized<br>10,000,000;  |                       |                       |

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2,506,784 and 2,549,434 shares issued and outstanding 2006 and 2005, respectively, excluding 291,676 and 297,783 shares 2006 and 2005, respectively, of common stock held by the Company's subsidiary)

|  |                       |           |                    |
|--|-----------------------|-----------|--------------------|
|  | <b>1</b>              |           | <b>1</b>           |
| Retained earnings  | <b>90,002,406</b>     |           | 81,477,022         |
| Accumulated other comprehensive income (net unrealized gain on investments) (Note 3) | <b>2,864,820</b>      |           | 2,820,233          |
| Total stockholders' equity   | <b>92,867,227</b>     |           | 84,297,256         |
| <b>Total Liabilities and Stockholders' Equity</b>                                    | <b>\$ 142,582,265</b> | <b>\$</b> | <b>128,471,528</b> |

*See notes to Consolidated Financial Statements.*

**Investors Title Company and Subsidiaries**  
**Consolidated Statements of Income**  
*For the Three and Nine Months Ended September 30, 2006 and 2005*  
*(Unaudited)*

|   | Three Months Ended<br>September 30 |               | Nine Months Ended<br>September 30 |               |
|---|------------------------------------|---------------|-----------------------------------|---------------|
|   | 2006                               | 2005          | 2006                              | 2005          |
| <b>Revenues:</b>  |                                    |               |                                   |               |
| Underwriting income:  |                                    |               |                                   |               |
| Premiums written  | \$ 18,347,342                      | \$ 21,035,519 | \$ 54,315,786                     | \$ 58,333,687 |
| Less - premiums for reinsurance ceded                         | 104,666                            | 49,419        | 317,893                           | 234,234       |
| Net premiums written  | 18,242,676                         | 20,986,100    | 53,997,893                        | 58,099,453    |
| Investment income - interest and dividends                    | 1,036,155                          | 812,659       | 3,064,905                         | 2,373,983     |
| Net realized gain (loss) on sales of investments              | (55,930)                           | 69,597        | 488,527                           | 89,504        |
| Exchange services revenue (Note 5)                            | 1,604,992                          | 1,222,602     | 4,541,081                         | 3,272,034     |
| Other   | 894,441                            | 942,365       | 2,935,397                         | 2,381,990     |
| Total   | 21,722,334                         | 24,033,323    | 65,027,803                        | 66,216,964    |
| <b>Operating Expenses:</b>                                    |                                    |               |                                   |               |
| Commissions to agents   | 6,796,146                          | 8,209,799     | 20,368,864                        | 23,050,329    |
| Provision for claims (Note 2)                                 | 1,992,901                          | 2,283,372     | 5,878,592                         | 6,354,485     |
| Salaries, employee benefits and payroll taxes (Notes 4 and 6) | 4,901,427                          | 4,540,061     | 14,824,296                        | 14,320,940    |
| Office occupancy and operations                               | 1,247,299                          | 1,133,563     | 3,978,654                         | 3,722,639     |
| Business development  | 568,982                            | 591,506       | 1,622,145                         | 1,483,367     |
| Taxes, other than payroll and income                          | 196,707                            | 67,234        | 493,599                           | 387,218       |
| Premium and retaliatory taxes                                 | 396,851                            | 411,084       | 1,067,461                         | 1,204,399     |
| Professional fees   | 554,487                            | 370,297       | 1,879,643                         | 1,461,478     |
| Other   | 92,435                             | 186,878       | 531,002                           | 298,088       |
| Total   | 16,747,235                         | 17,793,794    | 50,644,256                        | 52,282,943    |
| <b>Income Before Income Taxes</b>                             |                                    |               |                                   |               |
|   | 4,975,099                          | 6,239,529     | 14,383,547                        | 13,934,021    |
| <b>Provision For Income Taxes</b>                             | 1,303,030                          | 1,910,000     | 3,521,000                         | 4,162,000     |
| <b>Net Income</b>   | \$ 3,672,069                       | \$ 4,329,529  | \$ 10,862,547                     | \$ 9,772,021  |
| <b>Basic Earnings Per Common Share (Note 4)</b>               |                                    |               |                                   |               |
|   | \$ 1.46                            | \$ 1.69       | \$ 4.29                           | \$ 3.81       |

|   |                  |           |                  |           |
|---|------------------|-----------|------------------|-----------|
| <b>Weighted Average Shares<br/>Outstanding - Basic (Note 4)</b> | <b>2,517,691</b> | 2,559,154 | <b>2,534,883</b> | 2,562,247 |
|---|------------------|-----------|------------------|-----------|

|   |                |         |                |         |
|---|----------------|---------|----------------|---------|
| <b>Diluted Earnings Per<br/>Common Share (Note 4)</b> | \$ <b>1.44</b> | \$ 1.67 | \$ <b>4.23</b> | \$ 3.74 |
|---|----------------|---------|----------------|---------|

|   |                  |           |                  |           |
|---|------------------|-----------|------------------|-----------|
| <b>Weighted Average Shares<br/>Outstanding - Diluted (Note<br/>4)</b> | <b>2,550,607</b> | 2,600,289 | <b>2,569,585</b> | 2,611,073 |
|---|------------------|-----------|------------------|-----------|

*See notes to Consolidated  
Financial Statements.*

**Investors Title Company and Subsidiaries**  
**Consolidated Statements of Stockholders' Equity**  
*For the Nine Months Ended September 30, 2006 and 2005*  
*(Unaudited)*

|   | <b>Common Stock<br/>Shares</b> | <b>Common Stock<br/>Amount</b> | <b>Retained<br/>Earnings</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income (Net<br/>Unrealized<br/>Gain (Loss)<br/>on Investments)</b> | <b>Total<br/>Stockholders'<br/>Equity</b> |
|---|--------------------------------|--------------------------------|------------------------------|---|---|
| Balance, December 31,<br>2004                                 | 2,481,024                      | \$ 1                           | \$ 69,272,092                | \$ 3,235,178  | \$ 72,507,271                             |
| Net income  |                                |                                | 9,772,021                    |   | 9,772,021                                 |
| Dividends (\$.12 per<br>share)                                |                                |                                | (307,911)                    |   | (307,911)                                 |
| Shares of common<br>stock repurchased                         | (87,043)                       |                                | (2,815,515)                  |   | (2,815,515)                               |
| Issuance of common stock in<br>payment of<br>bonuses and fees | 1,010                          |                                | 38,068                       |   | 38,068                                    |
| Stock options exercised                                       | 162,720                        |                                | 2,410,249                    |   | 2,410,249                                 |
| Net unrealized loss on<br>investments                         |                                |                                |                              | (351,274)   | (351,274)                                 |
| <b>Balance, September 30,<br/>2005</b>                        | <b>2,557,711</b>               | <b>\$ 1</b>                    | <b>\$ 78,369,004</b>         | <b>\$ 2,883,904</b>   | <b>\$ 81,252,909</b>                      |
| Balance, December 31,<br>2005                                 | 2,549,434                      | \$ 1                           | \$ 81,477,022                | \$ 2,820,233  | \$ 84,297,256                             |
| Net income  |                                |                                | 10,862,547                   |   | 10,862,547                                |
| Dividends (\$.18 per<br>share)                                |                                |                                | (456,005)                    |   | (456,005)                                 |
| Shares of common<br>stock repurchased                         | (500)                          |                                | (22,445)                     |   | (22,445)                                  |
| Shares of common stock<br>repurchased and retired             | (49,107)                       |                                | (2,130,841)                  |   | (2,130,841)                               |
| Issuance of common stock in<br>payment of<br>bonuses and fees | 392                            |                                | 16,813                       |   | 16,813                                    |
| Stock options exercised                                       | 6,565                          |                                | 167,184                      |   | 167,184                                   |
| Share based<br>compensation expense                           |                                |                                | 63,753                       |   | 63,753                                    |
| Change in investment accounting<br>method                     |                                |                                | 24,378                       |   | 24,378                                    |
| Net unrealized gain on<br>investments                         |                                |                                |                              | 44,587  | 44,587                                    |



|  |                  |           |          |           |                   |           |                  |           |                   |
|--|------------------|-----------|----------|-----------|-------------------|-----------|------------------|-----------|-------------------|
| <b>Balance, September<br/>30, 2006</b> | <b>2,506,784</b> | <b>\$</b> | <b>1</b> | <b>\$</b> | <b>90,002,406</b> | <b>\$</b> | <b>2,864,820</b> | <b>\$</b> | <b>92,867,227</b> |
|--|------------------|-----------|----------|-----------|-------------------|-----------|------------------|-----------|-------------------|

*See notes to  
Consolidated Financial  
Statements.*

**Investors Title Company and Subsidiaries**  
**Consolidated Statements of Cash Flows**  
*For the Nine Months Ended September 30, 2006 and 2005*  
*(Unaudited)*

|   | 2006          | 2005         |
|---|---------------|--------------|
| <b>Operating Activities:</b>  |               |              |
| Net income  | \$ 10,862,547 | \$ 9,772,021 |
| Adjustments to reconcile net income to net cash provided by operating activities: |               |              |
| Depreciation  | 803,632       | 715,064      |
| Amortization, net   | 140,236       | 57,234       |
| Issuance of common stock in payment of bonuses and fees                           | 16,813        | 38,068       |
| Share based compensation expense related to stock options                         | 63,753        | -            |
| Provision for losses on premiums receivable                                       | 92,000        | 360,000      |
| Net gain on disposals of property   | (13,042)      | (24,684)     |
| Net realized gain on sales of investments   | (488,527)     | (89,504)     |
| Provision for claims  | 5,878,592     | 6,354,485    |
| Provision for deferred income taxes   | 428,000       | 188,000      |
| Changes in assets and liabilities:  |               |              |
| (Increase) decrease in receivables and other assets                               | 67,466        | (3,262,585)  |
| Increase in accounts payable and accrued liabilities                              | 593,284       | 1,186,424    |
| Decrease in commissions and reinsurance payables                                  | (88,736)      | (4,268)      |
| Decrease in current income taxes payable  | (820,535)     | (172,758)    |
| Payments of claims, net of recoveries   | (4,258,592)   | (3,888,485)  |
| Net cash provided by operating activities   | 13,276,891    | 11,229,012   |
| <b>Investing Activities:</b>  |               |              |
| Purchases of available-for-sale securities  | (41,809,590)  | (25,569,390) |
| Purchases of short-term securities  | (71,631)      | (16,099,896) |
| Purchases of and net earnings (losses) from other investments                     | (648,000)     | (432,014)    |
| Proceeds from sales and maturities of available-for-sale securities               | 18,086,066    | 34,283,148   |
| Proceeds from maturities of held-to-maturity securities                           | 456,000       | 507,000      |
| Proceeds from sales and maturities of short-term securities                       | 4,328,902     | 408,948      |
| Proceeds from sales and distributions of other investments                        | 444,480       | 315,684      |
| Other investment transactions   | (65,622)      | -            |
| Purchases of property   | (1,474,540)   | (546,429)    |
| Proceeds from disposals of property   | 7,330         | 31,632       |
| Other property transactions   | 23,685        | -            |
| Net change in pending trades  | (763,247)     | (1,975,561)  |
| Net cash used in investing activities   | (21,486,167)  | (9,076,878)  |
| <b>Financing Activities:</b>  |               |              |

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|                                       |             |             |
|---------------------------------------|-------------|-------------|
| Repurchases of common stock, net      | (2,153,286) | (2,815,515) |
| Exercise of options                   | 167,184     | 2,410,249   |
| Dividends paid                        | (456,005)   | (307,911)   |
| Net cash used in financing activities | (2,442,107) | (713,177)   |

|   |                     |                     |
|---|---------------------|---------------------|
| <b>Net Increase (Decrease) in Cash and Cash Equivalents</b> | <b>(10,651,383)</b> | 1,438,957           |
| <b>Cash and Cash Equivalents, Beginning of Period</b>       | <b>14,608,481</b>   | 4,726,443           |
| <b>Cash and Cash Equivalents, End of Period</b>             | <b>\$ 3,957,098</b> | <b>\$ 6,165,400</b> |

**Supplemental Disclosures:**

**Cash Paid During the Period for:**

|                              |              |              |
|------------------------------|--------------|--------------|
| Income Taxes, net of refunds | \$ 3,909,000 | \$ 4,154,000 |
|------------------------------|--------------|--------------|

*See notes to Consolidated Financial Statements.*

**INVESTORS TITLE COMPANY  
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

September 30, 2006

(Unaudited)

**Note 1 - Basis of Presentation and Significant Accounting Policies**

Reference should be made to the "Notes to Consolidated Financial Statements" of Investors Title Company's ("the Company") Annual Report to Shareholders for the year ended December 31, 2005 for a complete description of the Company's significant accounting policies.

*Principles of Consolidation* - The accompanying unaudited consolidated financial statements include the accounts and operations of Investors Title Company and its subsidiaries (Investors Title Insurance Company, Northeast Investors Title Insurance Company, Investors Title Exchange Corporation, Investors Title Accommodation Corporation, Investors Title Management Services, Inc., Investors Title Commercial Agency, LLC, Investors Capital Management Company and Investors Trust Company), and have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in annual financial statements have been condensed or omitted. All intercompany balances and transactions have been eliminated in consolidation.

In the opinion of management, all adjustments considered necessary for a fair presentation of the financial position, results of operations and cash flows in the accompanying unaudited consolidated financial statements have been included. All such adjustments are of a normal recurring nature. Operating results for the quarter and the nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ended December 31, 2006.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2005.

*Use of Estimates and Assumptions* - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates and assumptions used.

*Reclassification* - Certain 2005 amounts have been reclassified to conform to 2006 classifications. These reclassifications had no effect on net income or stockholders' equity as previously reported.

*Stock-Based Compensation* - In December 2004, the Financial Accounting Standards Board ("FASB") revised Statement of Financial Accounting Standards No. 123 ("SFAS 123R"), "Share-Based Payment," which establishes accounting for share-based awards exchanged for employee services and requires companies to expense the estimated fair value of these awards over the requisite employee service period. On April 14, 2005, the Securities and Exchange Commission adopted a new rule amending the effective dates for SFAS 123R. In accordance with the new rule, the Company adopted the accounting provisions of SFAS 123R beginning in the first quarter of 2006.

Under SFAS 123R, share-based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period. The Company has no awards with market or performance conditions. The Company adopted the provisions of SFAS 123R on January 1, 2006, the first day of the Company's fiscal year 2006, using a modified prospective application, which provides for certain changes to the method for valuing share-based compensation. Under the modified prospective application, prior periods are not revised for comparative purposes. The valuation provisions of SFAS 123R apply to new awards and to awards that are outstanding on the effective date and subsequently modified or cancelled. Estimated compensation expense for awards outstanding at the effective date will be recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123").

As share-based compensation expense recognized in the consolidated statements of income for the three and nine months ended September 30, 2006 is based on awards ultimately expected to vest, it should be reduced for estimated forfeitures. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In the Company's pro forma information required under SFAS 123 for the periods prior to fiscal 2006, the Company accounted for forfeitures as they occurred.

Prior to adopting the provisions of SFAS 123R, the Company recorded estimated compensation expense for employee stock options based upon their intrinsic value on the date of grant pursuant to Accounting Principles Board Opinion No. 25, ("APB 25"), "Accounting for Stock Issued to Employees" and provided the required pro forma disclosures of SFAS 123. Because the Company established the exercise price based on the fair market value of the Company's stock at the date of grant, the stock options had no intrinsic value upon grant, and therefore no estimated expense was recorded prior to adopting SFAS 123R. Each accounting period, the Company reported the potential dilutive impact of stock options in its diluted earnings per common share using the treasury-stock method. Out-of-the-money stock options (i.e., the average stock price during the period was below the exercise price of the stock option) were not included in diluted earnings per common share as their effect was anti-dilutive.

Pro forma net earnings for 2005, including effects of expensing stock options is as follows:

|  | <b>Three Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2005</b> |
|--|--|---|
| Net income as reported   | \$ 4,329,529   | \$ 9,772,021  |
| Add back issuance of common stock in payment of bonuses and fees, net of tax   | 20,772   | 25,124  |
| Deduct total stock-based employee compensation expense determined under fair value based method for all awards, net of tax | (57,897)   | (135,094)   |
| Pro forma net income   | \$ 4,292,404   | \$ 9,662,051  |
| Net income per share:  |  |   |
| Basic - as reported  | \$ 1.69  | \$ 3.81   |
| Basic - pro forma  | \$ 1.68  | \$ 3.77   |
| Diluted - as reported  | \$ 1.67  | \$ 3.74   |
| Diluted - pro forma  | \$ 1.65  | \$ 3.70   |

As a result of adopting SFAS 123R, the Company's income before income taxes for the three and nine months ended September 30, 2006, was lower by \$27,456 and \$63,753, respectively, than if it had continued to account for share-based compensation under APB 25. The net income for the three and nine months ended September 30, 2006, was lower by \$22,709 and \$55,841, respectively, than if it had continued to account for share-based compensation under APB 25. Basic and diluted earnings per share for the three months ended September 30, 2006 would have increased \$0 .01 per share basic and \$0 .01 per share diluted, while the earnings per share for the nine months ended September 30, 2006 would have increased \$0 .02 per share basic and \$0.02 per share diluted.

SFAS 123R also requires a change to the statement of cash flow classification of certain tax benefits from share-based compensation deductions beginning on January 1, 2006. As there was no tax benefit recorded for the nine months ended September 30, 2005, no adjustment was necessary.

*Recently Issued Accounting Standards* - In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective as of the beginning of the Company's 2007 fiscal year, with the cumulative effect, if any, of the change in accounting principle recorded as an adjustment to beginning retained earnings. The Company is currently evaluating the impact of adopting FIN 48 on its consolidated financial position and results of operations.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"). SFAS No. 157 establishes a common definition for fair value to be applied to US GAAP guidance requiring use of fair value, establishes a framework for measuring fair value, and expands disclosure about such fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing the impact of SFAS No. 157 on its consolidated financial position and results of operations.

In September 2006, the FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" ("SFAS No. 158"). SFAS No. 158 requires that employers recognize on a prospective basis the funded status of their defined benefit pension and other postretirement plans on their consolidated balance sheet and recognize as a component of other comprehensive income, net of tax, the gains or losses and prior service costs or credits that arise during the period but are not recognized as components of net periodic benefit cost. SFAS No. 158 also requires additional disclosures in the notes to financial statements. SFAS No. 158 is effective as of the end of fiscal years ending after December 15, 2006. The Company is currently assessing the impact of adopting SFAS No. 158, but it does not expect that it will have a material effect on its consolidated financial position or results of operations.

In September 2006, the SEC staff issued Staff Accounting Bulletin 108 "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 requires that public companies utilize a "dual-approach" to assessing the quantitative effects of financial misstatements. This dual approach includes both an income statement focused assessment and a balance sheet focused assessment. The guidance in SAB 108 must be applied to annual financial statements for fiscal years ending after November 15, 2006. The Company is currently assessing the impact of adopting SAB 108, but it does not expect that it will have a material effect on its consolidated financial position or results of operations.

Note 2 - Reserves for Claims

Transactions in the reserves for claims for the nine months ended September 30, 2006 and the year ended December 31, 2005 were as follows:

|                                       | <b>Nine Months Ended</b>  | <b>Year Ended</b>        |
|---------------------------------------|---------------------------|--------------------------|
|                                       | <b>September 30, 2006</b> | <b>December 31, 2005</b> |
| Balance, beginning of year            | \$ 34,857,000             | \$ 31,842,000            |
| Provision, charged to operations      | 5,878,592                 | 8,164,783                |
| Payments of claims, net of recoveries | (4,258,592)               | (5,149,783)              |
| Ending balance                        | \$ 36,477,000             | \$ 34,857,000            |

The total reserve for all reported and unreported losses the Company incurred through September 30, 2006 is represented by the reserves for claims. The Company's reserves for unpaid losses and loss adjustment expenses are established using estimated amounts required to settle claims for which notice has been received (reported) and the amount estimated to be required to satisfy incurred claims of policyholders which may be reported in the future. Despite the variability of such estimates, management believes that the reserves are adequate to cover claim losses which might result from pending and future claims for policies issued through September 30, 2006. The Company continually reviews and adjusts its reserve estimates to reflect its loss experience and any new information that becomes available. Adjustments resulting from such reviews may be significant.

Claims and losses paid are charged to the reserves for claims. Although claims losses are typically paid in cash, occasionally claims are settled by purchasing the interest of the insured or the claimant in the real property. When this event occurs, the Company carries assets at the lower of cost or estimated realizable value, net of any indebtedness on the property.

Note 3 - Comprehensive Income

Total comprehensive income for the three months ended September 30, 2006 and 2005 was \$4,926,511 and \$4,027,018, respectively. Comprehensive income for the nine months ended September 30, 2006 and 2005 was \$10,907,134 and \$9,420,747, respectively. Other comprehensive income is comprised solely of unrealized gains or losses on the Company's available-for-sale securities.

Note 4 - Earnings Per Common Share and Stock Options

Basic earnings per common share is computed by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings per common share is computed by dividing net income by the combination of dilutive common share equivalents, comprised of shares issuable under the Company's share-based compensation plans and the weighted-average number of common shares outstanding during the reporting period. Dilutive common share equivalents include the dilutive effect of in-the-money shares, which is calculated based on the average share price for each period using the treasury stock method. Under the treasury stock method, the exercise price of a share, the amount of compensation cost, if any, for future service that the Company has not yet recognized, and the amount of estimated tax benefits that would be recorded in additional paid-in capital, if any, when the share is exercised are assumed to be used to repurchase shares in the current period. The incremental dilutive common share equivalents, calculated using the treasury stock method were 32,916 and 41,135 for the three months ended September 30, 2006 and 2005, respectively and 34,702 and 48,826 for the nine months ended September 30, 2006 and 2005, respectively.



The Company has adopted Employee Stock Option Purchase Plans (the "Plans") under which options or Stock Appreciation Rights ("SARS") to purchase shares (not to exceed 500,000 shares) of the Company's stock may be granted to key employees of the Company at a price not less than the market value on the date of grant. SARS and options, which are predominantly incentive stock options, are exercisable and vest immediately or within one year or at 10% to 20% per year beginning on the date of grant and generally expire in five to ten years.

A summary of stock option transactions for all stock option plans follows:

|                                      | <b>Number<br/>Of Shares</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Average<br/>Remaining<br/>Contractual<br/>Term (years)</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> |
|--------------------------------------|-----------------------------|--|---|--|
| Outstanding as of December 31, 2005  | 82,001                      | \$ 20.50   |   |  |
| Options granted                      | 3,000                       | \$ 43.78   |   |  |
| Options exercised                    | (6,565)                     | \$ 16.89   |   |  |
| Options cancelled/forfeited/expired  | (1,610)                     | \$ 22.12   |   |  |
| Outstanding as of September 30, 2006 | 76,826                      | \$ 21.68   | 4.54  | \$ 1,868,079                             |
| Exercisable as of September 30, 2006 | 44,706                      | \$ 22.50   | 4.34  | \$ 1,050,744                             |
| Unvested as of September 30, 2006    | 32,120                      | \$ 20.55   | 4.82  | \$ 817,334                               |

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the quoted price of the Company's common stock at September 30, 2006. There were no options excluded from the calculation as all options were in the money. The intrinsic value of options exercised during the nine months ended September 30, 2006 was approximately \$173,000.

During the second quarter of 2006, the Company issued 3,000 Stock Settled Stock Appreciation Rights to the directors of the Company. SARS give the holder the right to receive stock in the appreciation in the value of shares of stock from the grant date for a specified period of time, and as a result, are accounted for as equity instruments. As such, these were valued using the Black-Scholes option valuation model. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the weighted-average assumptions noted in the following table. Expected volatilities are based on both the implied and historical volatility of the Company's stock. The Company uses historical data to estimate option exercise and employee termination within the valuation model. The expected term of options represents the period of time that options granted are expected to be outstanding. The interest rate for periods during the expected life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. The weighted average-fair value for the SARS issued was \$13.96 and was estimated using the following weighted-average assumptions:

|                        |        |
|------------------------|--------|
|                        | 2006   |
| Expected Life in Years | 5.0    |
| Volatility             | 27.16% |
| Interest Rate          | 4.97%  |
| Yield Rate             | 0.55%  |

There was approximately \$64,000 of compensation expense relating to shares vesting on or before September 30, 2006 included in salaries, employee benefits and payroll taxes of the consolidated statement of income for the nine months ended September 30, 2006. As of September 30, 2006, there was approximately \$286,000 of total unrecognized compensation cost related to unvested share-based compensation arrangements granted under the Company's stock awards plans. That cost is expected to be recognized over a weighted-average period of 4.82 years.

#### Note 5 - Segment Information

Consistent with SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", the Company has aggregated its operating segments into two reportable segments: 1) title insurance services; and 2) tax-deferred exchange services.

| <b>Three Months Ended<br/>September 30, 2006</b> | <b>Title<br/>Insurance</b> | <b>Exchange<br/>Services</b> | <b>All<br/>Other</b> | <b>Intersegment<br/>Eliminations</b> | <b>Total</b>   |
|--|----------------------------|------------------------------|----------------------|--------------------------------------|----------------|
| Operating revenues                               | \$ 18,603,562              | \$ 1,604,992                 | \$ 743,424           | \$ (209,869)                         | \$ 20,742,109  |
| Investment income                                | 904,388                    | 4,030                        | 145,237              | (17,500)                             | 1,036,155      |
| Net realized (loss) on sales<br>of investments   | (55,930)                   | -                            | -                    | -                                    | (55,930)       |
| Total revenues                                   | \$ 19,452,020              | \$ 1,609,022                 | \$ 888,661           | \$ (227,369)                         | \$ 21,722,334  |
| Operating expenses                               | 15,900,745                 | 395,864                      | 660,495              | (209,869)                            | 16,747,235     |
| Income before<br>income taxes                    | \$ 3,551,275               | \$ 1,213,158                 | \$ 228,166           | \$ (17,500)                          | \$ 4,975,099   |
| Assets, net                                      | \$ 116,325,540             | \$ 1,688,913                 | \$ 24,567,812        | -                                    | \$ 142,582,265 |

| <b>Three Months Ended<br/>September 30, 2005</b> | <b>Title<br/>Insurance</b> | <b>Exchange<br/>Services</b> | <b>All<br/>Other</b> | <b>Intersegment<br/>Eliminations</b> | <b>Total</b>   |
|--|----------------------------|------------------------------|----------------------|--------------------------------------|----------------|
| Operating revenues                               | \$ 21,527,738              | \$ 1,222,602                 | \$ 585,434           | \$ (184,707)                         | \$ 23,151,067  |
| Investment income                                | 748,873                    | 9,499                        | 67,213               | (12,926)                             | 812,659        |
| Net realized gain on sales of investments        | 51,132                     | -                            | 18,465               | -                                    | 69,597         |
| Total revenues                                   | \$ 22,327,743              | \$ 1,232,101                 | \$ 671,112           | \$ (197,633)                         | \$ 24,033,323  |
| Operating expenses                               | 17,280,896                 | 277,343                      | 421,576              | (186,021)                            | 17,793,794     |
| Income before income taxes                       | \$ 5,046,847               | \$ 954,758                   | \$ 249,536           | \$ (11,612)                          | \$ 6,239,529   |
| Assets, net                                      | \$ 102,495,320             | \$ 1,458,268                 | \$ 19,478,639        | \$ -                                 | \$ 123,432,227 |

| <b>Nine Months Ended<br/>September 30, 2006</b> | <b>Title<br/>Insurance</b> | <b>Exchange<br/>Services</b> | <b>All<br/>Other</b> | <b>Intersegment<br/>Eliminations</b> | <b>Total</b>   |
|---|----------------------------|------------------------------|----------------------|--------------------------------------|----------------|
| Operating revenues                              | \$ 55,254,217              | \$ 4,541,081                 | \$ 2,312,548         | \$ (633,475)                         | \$ 61,474,371  |
| Investment income                               | 2,707,816                  | 15,443                       | 394,546              | (52,900)                             | 3,064,905      |
| Net realized gain on sales of investments       | 488,527                    | -                            | -                    | -                                    | 488,527        |
| Total revenues                                  | \$ 58,450,560              | \$ 4,556,524                 | \$ 2,707,094         | \$ (686,375)                         | \$ 65,027,803  |
| Operating expenses                              | 48,008,265                 | 944,692                      | 2,324,774            | (633,475)                            | 50,644,256     |
| Income before income taxes                      | \$ 10,442,295              | \$ 3,611,832                 | \$ 382,320           | \$ (52,900)                          | \$ 14,383,547  |
| Assets, net                                     | \$ 116,325,540             | \$ 1,688,913                 | \$ 24,567,812        | \$ -                                 | \$ 142,582,265 |

| <b>Nine Months Ended<br/>September 30, 2005</b> | <b>Title<br/>Insurance</b> | <b>Exchange<br/>Services</b> | <b>All<br/>Other</b> | <b>Intersegment<br/>Eliminations</b> | <b>Total</b>   |
|---|----------------------------|------------------------------|----------------------|--------------------------------------|----------------|
| Operating revenues                              | \$ 59,354,631              | \$ 3,272,034                 | \$ 1,648,948         | \$ (522,136)                         | \$ 63,753,477  |
| Investment income                               | 2,197,854                  | 12,142                       | 200,079              | (36,092)                             | 2,373,983      |
| Net realized gain on sales of investments       | 71,039                     | -                            | 18,465               | -                                    | 89,504         |
| Total revenues                                  | \$ 61,623,524              | \$ 3,284,176                 | \$ 1,867,492         | \$ (558,228)                         | \$ 66,216,964  |
| Operating expenses                              | 50,508,764                 | 646,686                      | 1,650,943            | (523,450)                            | 52,282,943     |
| Income before income taxes                      | \$ 11,114,760              | \$ 2,637,490                 | \$ 216,549           | \$ (34,778)                          | \$ 13,934,021  |
| Assets, net                                     | \$ 102,495,320             | \$ 1,458,268                 | \$ 19,478,639        | \$ -                                 | \$ 123,432,227 |

Operating revenues represent net premiums written and other revenues.

Note 6 - Retirement and Other Postretirement Benefit Plans

On November 17, 2003, Investors Title Insurance Company entered into employment agreements with key executives that provide for the continuation of certain employee benefits upon retirement. The executive employee benefits include health insurance, dental insurance, vision insurance and life insurance. The plan is unfunded. The following sets forth the net periodic benefits cost for the executive benefits for the three and nine months ended September 30, 2006 and 2005:

|   | <b>Three Months Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|---|---|-------------|--|-------------|
|   | <b>2006</b>                                 | <b>2005</b> | <b>2006</b>                                | <b>2005</b> |
| Service cost                                    | \$ 3,557                                    | \$ 3,592    | \$ 10,671                                  | \$ 10,775   |
| Interest cost                                   | 3,515                                       | 3,418       | 10,545                                     | 10,256      |
| Amortization of unrecognized prior service cost | 5,097                                       | 5,097       | 15,291                                     | 15,291      |
| Amortization of unrecognized gains              | (416)                                       | (148)       | (1,248)                                    | (444)       |
| Net Periodic Benefits Costs                     | \$ 11,753                                   | \$ 11,959   | \$ 35,259                                  | \$ 35,878   |

Note 7 - Commitments and Contingencies

The Company and its subsidiaries are involved in various legal proceedings that are incidental to their business. In the Company's opinion, based on the present status of these proceedings, any potential liability of the Company or its subsidiaries with respect to these legal proceedings will not, in the aggregate, be material to the Company's consolidated financial condition or operations.

Note 8 - Subsequent Events

Subsequent to September 30, 2006, the Company retired 291,676 shares of its common stock that it received as a dividend from one of its subsidiaries. As this was an intercompany transaction, it will have no effect to the consolidated financial statements except that issued shares will be reduced by 291,676.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The Company's 2005 Form 10-K and 2005 Annual Report to Shareholders should be read in conjunction with the following discussion since they contain important information for evaluating the Company's operating results and financial condition.

Overview

*Title Insurance:* Investors Title Company (the "Company") engages primarily in two segments of business. Its primary business activity is the issuance of title insurance through two subsidiaries, Investors Title Insurance Company ("ITIC") and Northeast Investors Title Insurance Company ("NE-ITIC") which accounted for 89.9% of the Company's operating revenues in 2006. Through ITIC and NE-ITIC, the Company underwrites land title insurance for real estate owners and mortgagees as a primary insurer. Title insurance protects against loss or damage resulting from title defects that affect real property. The commitment and policies issued are predominately the standard American Land Title Association approved forms.

There are two basic types of title insurance policies - one for the mortgage lender and one for the real estate owner. A lender often requires property owners to purchase title insurance to protect its position as a holder of a mortgage loan, but the lender's title insurance policy does not protect the property owner. The property owner has to purchase a separate owner's title insurance policy to protect their investment. When real property is conveyed from one party to another, occasionally there is an undisclosed defect in the title or a mistake or omission in a prior deed, will or mortgage that may give a third party a legal claim against such property. If a claim is made against real property, title insurance provides a corporate guarantee against insured defects, pays all legal expenses to eliminate any title defects, pays any claims arising from errors in title examination and recording, and pays any losses arising from hidden defects in title and defects that are not of record. Title insurance provides an assurance that the insurance holder's ownership and use of such property will be defended promptly against claims, at no cost, whether or not the claim is valid.

ITIC delivers title insurance coverage through a home office, branch offices and issuing agents. In North Carolina, ITIC issues policies primarily through a home office and 27 branch offices. The Company also has branch offices in South Carolina and Nebraska. Title policies are issued primarily through issuing agents in other states. Issuing agents are typically real estate attorneys or subsidiaries of community and regional mortgage lending institutions, depending on local customs and regulations and the Company's marketing strategy in a particular territory. The ability to attract and retain issuing agents is a key determinant of the Company's growth in premiums written.

The Company's overall level of premiums written in the land title insurance industry is affected by a number of factors, including the level of interest rates, the availability of mortgage funds, the level of real estate transactions and mortgage refinance activity, the cost of real estate, employment levels, family income levels and general economic conditions. Generally, real estate activity declines as a result of higher interest rates or an economic downturn, thus leading to a corresponding decline in title insurance premiums written and profitability of the Company. The cyclical nature of the land title insurance industry has historically caused fluctuations in revenues and profitability and it is expected to continue to do so in the future. Revenues for this segment result from refinance activity, purchases of new and existing residential and commercial real estate and certain other types of mortgage lending such as home equity lines of credit.

Volume is a key factor in the Company's profitability due to the existence of fixed costs such as personnel and occupancy expenses associated with the support of the issuance of title insurance policies and general corporate operations. These expenses will be incurred by the Company regardless of the level of premiums written. The resulting operating leverage has historically tended to amplify the impact of changes in volume on the Company's profitability.

Since the title insurance business generally is closely related to the overall level of real estate activity, and title insurance volumes generally fluctuate based on the effect changes in interest rates have on the level of real estate activity, any substantial increases in interest rates will likely have a negative impact on mortgage originations. Operating results for the third quarter and the nine months ended September 30, 2006, therefore, should not be viewed as indicative of the Company's future operating results.

The Company continues to monitor and strives to manage operating expenses such as office occupancy and operations and salaries, employee benefits and payroll taxes to offset the cyclical nature of the real estate market and with knowledge of the potential for further declines in title insurance revenues if interest rates continue to rise or the economy slows.

*Exchange Services:* The Company's second business segment provides customer services in connection with tax-deferred real property exchanges through its subsidiaries, Investors Title Exchange Corporation ("ITEC") and Investors Title Accommodation Corporation ("ITAC"). ITEC serves as a qualified intermediary in Section 1031 like-kind exchanges of real or personal property. In its role as qualified intermediary, ITEC coordinates the exchange aspects of the real estate transaction with the closing agents. ITEC's duties include drafting standard exchange documents, holding the exchange funds between the sale of the old property and the purchase of the new property, and accepting the formal identification of the replacement property within the required identification period. ITAC serves as exchange accommodation titleholder in reverse exchanges. As exchange accommodation titleholder, ITAC offers a vehicle for accommodating a reverse exchange when the taxpayer must acquire replacement property before selling the relinquished property.

Factors that influence the title insurance industry will also generally affect the exchange services industry. In addition, the services provided by the Company's exchange services are pursuant to provisions in the Internal Revenue Code. From time to time, these exchange provisions are subject to review and proposed changes.

On February 3, 2006, the IRS proposed new regulations which, if adopted, may negatively affect the ability of qualified intermediaries to retain interest earned on exchange funds held during exchange transactions. If passed as proposed, these regulations would materially adversely impact the exchange services segment and the Company's net income, since a major portion of the exchange segment's revenues are based on interest income earned on deposits held by the Company. A public hearing on the proposed regulations was held on June 6, 2006, but no official response has been issued by the IRS on whether or not they plan to finalize the regulations as proposed.

*Other Services:* Other services include those offered by Investors Trust Company ("INTC"), Investors Capital Management Company ("ICMC") and Investors Title Management Services, Inc. ("ITMS"), wholly owned subsidiaries of the Company. In conjunction with INTC, ICMC provides investment management and trust services to individuals, companies, banks and trusts. ITMS offers a variety of consulting services, including training and guidance, to provide partners with the technical expertise to start and successfully operate a title insurance agency.

Critical Accounting Estimates and Policies

The preparation of the Company's financial statements requires management to make estimates and judgments that affect the reported amounts of certain assets, liabilities, revenue, expenses and related disclosures surrounding contingencies and commitments. Actual results could differ from these estimates. During the three and nine months ended September 30, 2006, the Company made no material changes in its critical accounting policies as previously disclosed within Management's Discussion and Analysis in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 as filed with the Securities and Exchange Commission.

Results of Operations

For the third quarter ended September 30, 2006, net premiums written decreased 13.1% to \$18,242,676, investment income increased 27.5% to \$1,036,155, revenues decreased 9.6% to \$21,722,334 and net income decreased 15.2% to \$3,672,069, all compared with the third quarter of 2005. Net income per basic and diluted common share decreased 13.6% and 13.8%, respectively, to \$1.46 and \$1.44 as compared with the prior year quarter. For the third quarter of 2006, the title insurance segment's operating revenues decreased 13.4% compared with the third quarter of 2005, while the exchange services segment's operating revenues increased 31.3% for the third quarter of 2006, compared with the same quarter in 2005.

For the nine-month period ended September 30, 2006, net premiums written decreased 7.1% to \$53,997,893, investment income increased 29.1% to \$3,064,905, revenues decreased 1.8% to \$65,027,803 and net income increased 11.2% to \$10,862,547, all compared with the same period in 2005. Net income per basic and diluted common share increased 12.6% and 13.1%, respectively, to \$4.29 and \$4.23 compared with the first nine months of 2005. For the nine months ended September 30, 2006, the title insurance segment's operating revenues decreased 6.7% compared with the same period in 2005, while the exchange services segment's operating revenues increased 38.8% for the nine months ended September 30, 2006 compared with the same nine-month period in 2005.

*Operating revenues:* Operating revenues include premiums written and reinsurance assumed, net of reinsurance ceded (net premiums written), exchange segment income, plus other income as well as gains and losses on the disposal of fixed assets. Investment income and realized gains and losses are not included in operating revenues and are discussed separately following operating revenues.

Following is a schedule of premiums written for the three and nine months ended September 30, 2006 and 2005 in all states in which the Company's two insurance subsidiaries, ITIC and NE-ITIC, currently underwrite insurance:

| State                  | Three Months Ended<br>September 30, 2006 |                      | Nine Months Ended<br>September 30, 2006 |                      |
|------------------------|--|----------------------|---|----------------------|
|                        | 2006                                     | 2005                 | 2006                                    | 2005                 |
| Alabama                | \$ 185,318                               | \$ 304,229           | \$ 759,499                              | \$ 1,034,232         |
| Florida                | 359,531                                  | 410,075              | 965,822                                 | 1,182,015            |
| Illinois               | 291,810                                  | 244,111              | 819,718                                 | 735,441              |
| Kentucky               | 618,829                                  | 616,986              | 1,775,866                               | 1,601,826            |
| Maryland               | 344,598                                  | 471,464              | 1,126,272                               | 1,331,992            |
| Michigan               | 825,711                                  | 1,229,606            | 2,584,541                               | 3,614,984            |
| Minnesota              | 200,469                                  | 227,850              | 842,538                                 | 756,642              |
| Mississippi            | 225,319                                  | 249,728              | 526,996                                 | 811,321              |
| Nebraska               | 172,005                                  | 212,204              | 503,451                                 | 597,899              |
| New York               | 602,667                                  | 998,587              | 1,815,458                               | 2,358,964            |
| North Carolina         | 9,185,274                                | 10,111,914           | 27,400,208                              | 27,477,382           |
| Pennsylvania           | 373,498                                  | 460,000              | 1,100,005                               | 1,287,648            |
| South Carolina         | 2,045,816                                | 1,748,951            | 4,984,670                               | 5,136,939            |
| Tennessee              | 686,497                                  | 775,812              | 1,967,589                               | 2,066,396            |
| Virginia               | 1,515,282                                | 2,078,630            | 5,087,324                               | 6,032,643            |
| West Virginia          | 577,884                                  | 728,273              | 1,673,725                               | 1,740,338            |
| Other States           | 135,101                                  | 167,099              | 373,945                                 | 552,979              |
| <b>Direct Premiums</b> | <b>18,345,609</b>                        | <b>21,035,519</b>    | <b>54,307,627</b>                       | <b>58,319,641</b>    |
| Reinsurance Assumed    | 1,733                                    | -                    | 8,159                                   | 14,046               |
| Reinsurance Ceded      | (104,666)                                | (49,419)             | (317,893)                               | (234,234)            |
| <b>Net Premiums</b>    | <b>\$ 18,242,676</b>                     | <b>\$ 20,986,100</b> | <b>\$ 53,997,893</b>                    | <b>\$ 58,099,453</b> |

Net premiums written were negatively impacted during the latest reporting period primarily as a result of a softening real estate market and overall higher interest rate environment. According to data published by Freddie Mac, the monthly average 30-year fixed mortgage interest rates increased to an average of 6.47% for the nine months ended September 30, 2006, compared with 5.75% for the nine months ended September 30, 2005. Mortgage originations and real estate activity continued to slow from 2005 record levels as a result of higher interest rates, inventory imbalances and other market factors. The total number of policies and commitments issued declined in the nine months ended September 30, 2006 to 192,382, a decrease of 8.1% compared with 209,317 policies and commitments issued in the same period of 2005.



Following is a breakdown of branch and agency premiums for the three and the nine months ended September 30, 2006 and 2005:

|        | Three Months Ended September 30, |     |               |     | Nine Months Ended September 30, |     |               |     |
|--------|----------------------------------|-----|---------------|-----|---------------------------------|-----|---------------|-----|
|        | 2006                             | %   | 2005          | %   | 2006                            | %   | 2005          | %   |
| Branch | \$ 8,602,081                     | 47  | \$ 9,636,878  | 46  | \$ 25,333,046                   | 47  | \$ 26,017,989 | 45  |
| Agency | 9,640,595                        | 53  | 11,349,222    | 54  | 28,664,847                      | 53  | 32,081,464    | 55  |
| Total  | \$ 18,242,676                    | 100 | \$ 20,986,100 | 100 | \$ 53,997,893                   | 100 | \$ 58,099,453 | 100 |

Net premiums written from branch operations decreased 10.7% for the third quarter ended September 30, 2006, compared with the same period in the prior year. Net premiums written from branch operations decreased 2.6% for the nine months ended September 30, 2006, compared with the same period in 2005. Of the Company's 29 branch locations that underwrite title insurance policies, 27 are located in North Carolina and, as a result, branch net premiums written primarily represent North Carolina business.

Agency net premiums decreased 15.1% for the quarter ended September 30, 2006, compared with the same period in the prior year. Agency net premiums decreased 10.6% for the nine months ended September 30, 2006, compared with the same period in the prior year.

Operating revenues from the Company's two subsidiaries that provide tax-deferred exchange services (ITEC and ITAC) increased 31.3% for the current quarter compared with the third quarter of 2005. For the nine month period ended September 30, 2006, operating revenues from ITEC and ITAC increased 38.8% compared with the same period in 2005. The increase in year to date 2006 was due to higher levels of interest income earned on exchange fund deposits held by the Company and, to a lesser extent, an increase in the average balances of deposits held. Slowing real estate sales, however, led to a decline in transaction volume and average balances in the latest period. Also, see overview for discussion of proposed IRS rules.

Other revenues include agency management fees and investment management fee income, as well as search fee and other ancillary fee income and income related to the Company's other equity method investments. Other revenues increased 23.2% for the nine months ended September 30, 2006 compared with the same period in the prior year, primarily due to increases in investment management fee income generated by the Company's Trust division and increases in ancillary income.

*Non-operating revenues:* Investment income and realized gains and losses are included in non-operating revenues.

For the nine months ended September 30, 2006, total revenues were favorably impacted by a 29.1% increase in investment income, resulting primarily from higher investment balances and higher rates of interest earned on short-term investments.

Net realized gains on the sale of investment securities totaled \$488,527 for the nine months ended September 30, 2006, compared with net realized gains of \$89,504 for the corresponding period in 2005. The increase was the result of capital gains realized on several equity securities sold during the first quarter 2006 primarily due to repositioning of the Company's investment portfolio and in response to market changes.

*Operating Expenses:* The Company's operating expenses consist primarily of commissions to agents, salaries, employee benefits and payroll taxes, provision for claims and office occupancy and operations. Total operating expenses decreased 5.9% and 3.1% for the three and nine months ended September 2006, respectively, compared with the same periods in 2005. These decreases were due primarily to decreases in commissions to agents and the provision for possible claims, partially offset by increases in salaries, employee benefits and payroll taxes and professional fees. A summary by segment of the Company's operating expenses is as follows for the quarter and the nine months ended September 30:

|                   | Three Months Ended September 30, |     |               |     | Nine Months Ended September 30, |     |               |     |
|-------------------|----------------------------------|-----|---------------|-----|---------------------------------|-----|---------------|-----|
|                   | 2006                             | %   | 2005          | %   | 2006                            | %   | 2005          | %   |
| Title insurance   | \$ 15,725,740                    | 94  | \$ 17,108,943 | 96  | \$ 47,492,639                   | 94  | \$ 50,017,671 | 96  |
| Exchange services | 378,574                          | 2   | 264,527       | 2   | 888,578                         | 2   | 617,612       | 1   |
| All other         | 642,921                          | 4   | 420,324       | 2   | 2,263,039                       | 4   | 1,647,660     | 3   |
| Total             | \$ 16,747,235                    | 100 | \$ 17,793,794 | 100 | \$ 50,644,256                   | 100 | \$ 52,282,943 | 100 |

Agent commissions represent the portion of premiums retained by agents pursuant to the terms of their respective agency contracts. Although commissions paid to agents declined, the commissions as a percentage of agency premiums remained relatively stable in the third quarter of 2006 when compared with the third quarter of last year and in the nine months ended September 30, 2006 compared with the same period in the previous year.

The provision for claims as a percentage of net premiums written was 10.9% for the third quarter of 2006 and 2005. For the nine months ended September 30, 2006 and 2005, the provision for claims as a percentage of net premiums written was also 10.9%. Loss provision rates are subject to variability and are reviewed and adjusted as experience develops. Declining economic conditions and/or substantial declines in transaction volumes have historically been factors in increased claim expenses due to increased mechanics liens, defalcations and other matters which may be discovered during property foreclosures. Title claims are typically reported and paid within the first several years of policy issuance. The provision reflects actual payments of claims, net of recovery amounts, plus adjustments to the specific and incurred but not reported claims reserves, the latter of which are actuarially reviewed based on historical claims experience. At September 30, 2006, the total reserves for claims were \$36,477,000. Of that total, \$4,334,305 was reserved for specific claims, and \$32,142,695 was reserved for claims for which the Company had no notice.

On a consolidated basis, salaries, employee benefits and payroll taxes as a percentage of revenues were 22.6% and 18.9% for the third quarter of 2006 and 2005, respectively. For the first nine months, salaries, employee benefits and payroll taxes as a percentage of revenues were 22.8% and 21.6% for 2006 and 2005, respectively. Personnel costs increased compared with the nine months ending September 30, 2005 due to increases in certain employee benefits and stock based compensation related to the adoption of SFAS 123R.

The title insurance segment's total salaries, employee benefits and payroll taxes accounted for 86.4% and 91.1% of the consolidated total for the third quarter of 2006 and 2005, respectively and 86.2% and 90.1% for the nine months ended September 30, 2006 and 2005, respectively.

Overall office occupancy and operations as a percentage of total revenues was 5.7% and 4.7% for the third quarter of 2006 and 2005, respectively, and 6.1% and 5.6% for the nine months ended September 30, 2006 and 2005, respectively. The increases in office occupancy and operations expense were due to increases in various items, including depreciation expense, maintenance services and computer hardware expenses.

Professional fees increased for the three and nine months ended September 30, 2006 compared with the same periods in 2005 primarily due to additional contract labor and consulting fees incurred, mostly related to various information system projects which have occurred during 2006.

Other expenses primarily include miscellaneous operating expenses of the Trust division and other miscellaneous expenses of the title segment.

*Income Taxes:* The provision for income taxes was approximately 26.2% and 30.6% of income before income taxes for the three months ended September 30, 2006 and 2005, respectively. For the nine months ended September 30, 2006 and 2005, the provision for income taxes was approximately 24.5% and 29.9%, respectively, of income before income taxes. The declines in the effective tax rates for the quarter and the nine months ended September 30, 2006 resulted primarily from higher interest rates and higher balances invested in tax-exempt securities.

#### Liquidity and Capital Resources

*Cash flows:* Total cash and cash equivalents decreased \$10,651,383 for the nine months ended September 30, 2006 to \$3,957,098 as a result of investing available cash and cash equivalents in securities and other investments. Net cash provided by operating activities was \$13,276,891 and \$11,229,012 for the first nine months of 2006 and 2005, respectively. Cash flow from operations has been the primary source of financing for expanding operations, additions to property and equipment, dividends to shareholders and other requirements. This net increase is primarily the result of a decrease in receivables and other assets and the increase in net income, partially offset by the decrease in current income taxes payable, a smaller increase in accounts payable and accrued liabilities, and the decrease in the provision for claims as a result of the decrease in premiums written.

The principal non-operating uses of cash and cash equivalents for the three and nine month periods ended September 30, 2006 and 2005 were additions to the investment portfolio and repurchases of common stock. The Company used cash for the purchases of investments in the amounts of approximately \$42 million in the first nine months of both 2006 and 2005.

As of September 30, 2006, prepaid expenses and other assets on the consolidated balance sheet includes \$5,000,000 of pending receivables related to investment sales, while accounts payable and accrued liabilities includes \$4,236,753 of pending payables related to investment purchases.

*Payment of dividends:* The Company's significant sources of funds are dividends and distributions from its insurance subsidiaries, which are subject to regulation in the states in which they do business. These regulations, among other things, require prior regulatory approval of the payment of dividends and other intercompany transfers. The Company believes that amounts available for transfer from the insurance subsidiaries are adequate to meet the Company's operating needs.

Subsequent to September 30, 2006, the Company retired 291,676 shares of its common stock that it received as a dividend from one of its subsidiaries. As this was an intercompany transaction, it will have no effect to the consolidated financial statements except that issued shares will be reduced by 291,676.

*Liquidity:* Due to the Company's historical ability to generate positive cash flows from its operations, management believes that funds generated from operations will enable the Company to adequately meet its anticipated cash needs and is unaware of any trend or occurrence that is likely to result in material adverse liquidity changes. The Company's cash requirements include operating expenses, taxes, capital expenditures and dividends on its common stock declared by the Board. In addition to operational liquidity, the Company maintains a high degree of liquidity within its investment portfolio in the form of short-term investments and other readily marketable securities. As of September 30, 2006, the Company held cash and cash equivalents of \$3,957,098, short-term investments of \$3,000,463 and various other readily marketable securities.

*Capital Expenditures:* During 2006, the Company has plans for various capital improvement projects, including several software development projects. The Company anticipates additional capital expenditures of approximately \$135,000 during the remainder of 2006 in connection with these capital improvement projects.

*Off-Balance Sheet Arrangements and Contractual Obligations:* It is not the general practice of the Company to enter into off-balance sheet arrangements nor is it the policy of the Company to issue guarantees to third parties. Off-balance sheet arrangements are generally limited to the future payments under noncancelable operating leases, payments due under various agreements with third-party service providers, and unaccrued obligations pursuant to certain executive employment agreements.

The total reserve for all reported and unreported losses the Company incurred through September 30, 2006 is represented by the reserves for claims. Information regarding the claims reserves can be found in Note 2 to the consolidated financial statements of this Form 10-Q. Further information on contractual obligations related to the reserves for claims can be found in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 as filed with the Securities and Exchange Commission.

*Equity Investments:* The Company's equity investments are in public companies whose security prices are subject to volatility. Should the fair value of these investments fall below the Company's cost bases and the financial condition or prospects of these companies deteriorate, the Company may determine in a future period that this decline in fair value is other than temporary, requiring that an impairment loss be recognized.

### New Accounting Standards

Refer to Note 1 to the consolidated financial statements for a discussion of Statement of Financial Accounting Standards No. 123R, "Share-Based Payment," which was adopted in the first quarter of 2006.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective as of the beginning of the Company's 2007 fiscal year, with the cumulative effect, if any, of the change in accounting principle recorded as an adjustment to beginning retained earnings. The Company is currently evaluating the impact of adopting FIN 48 on its consolidated financial position and results of operations.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"). SFAS No. 157 establishes a common definition for fair value to be applied to US GAAP guidance requiring use of fair value, establishes a framework for measuring fair value, and expands disclosure about such fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing the impact of SFAS No. 157 on its consolidated financial position and results of operations.

In September 2006, the FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" ("SFAS No. 158"). SFAS No. 158 requires that employers recognize on a prospective basis the funded status of their defined benefit pension and other postretirement plans on their consolidated balance sheet and recognize as a component of other comprehensive income, net of tax, the gains or losses and prior service costs or credits that arise during the period but are not recognized as components of net periodic benefit cost. SFAS No. 158 also requires additional disclosures in the notes to financial statements. SFAS No. 158 is effective as of the end of fiscal years ending after December 15, 2006. The Company is currently assessing the impact of adopting SFAS No. 158, but it does not expect that it will have a material effect on its consolidated financial position or results of operations.

In September 2006, the SEC staff issued Staff Accounting Bulletin 108 "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 requires that public companies utilize a "dual-approach" to assessing the quantitative effects of financial misstatements. This dual approach includes both an income statement focused assessment and a balance sheet focused assessment. The guidance in SAB 108 must be applied to annual financial statements for fiscal years ending after November 15, 2006. The Company is currently assessing the impact of adopting SAB 108, but it does not expect that it will have a material effect on its consolidated financial position or results of operations.

### Safe Harbor Statement

This Quarterly Report on Form 10-Q, as well as information included in future filings by the Company with the Securities and Exchange Commission and information contained in written material, press releases and oral statements issued by or on behalf of the Company, contains, or may contain, forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that reflect management's current outlook for future periods. These statements may be identified by the use of words such as "plan," "expect," "aim," "believe," "project," "anticipate," "intend," "estimate," "should," "could" and other expressions that indicate future events and trends. All statements that address expectations or projections about the future, including statements about the Company's strategy for growth, product and service development, market share position, claims, expenditures, financial results and cash requirements, are forward-looking statements. Forward-looking statements are based on certain assumptions and expectations of future events that are subject to risks and uncertainties.



Actual future results and trends may differ materially from historical results or those projected in any such forward-looking statements depending on a variety of factors, including, but not limited to, the following: (1) the Company's results of operations and financial condition are susceptible to housing markets and changes in mortgage interest rates and general economic conditions; (2) insurance regulations limit the ability of the Company's insurance subsidiaries to pay dividends to it without prior regulatory approval; (3) losses from claims may be greater than anticipated such that reserves for possible claims are inadequate; (4) adverse changes in government and IRS regulations could prohibit or limit the Company's operations or make it more burdensome to conduct operations; (5) the performance of the Company's investments depends on conditions that are outside its control; (6) the Company may encounter difficulties managing growth, which could adversely affect its results; (7) competition in the Company's business affects its revenues; and (8) the Company's success depends on its ability to attract and retain key personnel and agents. These and other risks and uncertainties may be described from time to time in the Company's other reports and filings with the Securities and Exchange Commission. For more details on factors that could affect expectations, see the Company's Annual Reports on Form 10-K for the year ended December 31, 2005.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

No material changes in the Company's market risk or market strategy occurred during the current period. A detailed discussion of market risk is provided in the Company's 2005 Annual Report on Form 10-K for the year ended December 31, 2005.

**Item 4. Controls and Procedures**

The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 (the "Act") was recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission's rules and forms. An evaluation was performed by the Company's management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-15(b) under the Act as of September 30, 2006. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2006. In reaching this conclusion, the Company's Chief Executive Officer and Chief Financial Officer determined that the Company's disclosure controls and procedures were effective in ensuring that such information was accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure.

During the quarter ended September 30, 2006, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

(a) None

(b) None

(c) The following table provides information about purchases by the Company (and all affiliated purchasers) during the quarter ended September 30, 2006 of equity securities that are registered by the Company pursuant to Section 12 of the Exchange Act:

| <b><u>Issuer Purchases of Equity Securities</u></b> |   |                                     |  |  |
|---|---|-------------------------------------|--|--|
| <b>Period</b>                                       | <b>Total Number of Shares Purchased</b> | <b>Average Price Paid per Share</b> | <b>Total Number of Shares Purchased as Part of Publicly Announced Plan</b> | <b>Maximum Number of Shares that May Yet Be Purchased Under the Plan</b> |
| <b><u>Beginning of period</u></b>                   |   |                                     |  | 376,833  |
| <b><u>07/01/06 - 07/31/06</u></b>                   | 950                                     | \$ 44.03                            | 950  | 375,883  |
| <b><u>08/01/06 - 08/31/06</u></b>                   | 20,118                                  | \$ 43.20                            | 20,118   | 355,765  |
| <b><u>09/01/06 - 09/30/06</u></b>                   | 6,650                                   | \$ 44.20                            | 6,650  | 349,115  |
| <b>Total:</b>                                       | <b>27,718</b>                           | <b>\$ 43.47</b>                     | <b>27,718</b>  | <b>349,115</b>   |

- (1) For the quarter ended September 30, 2006, ITC purchased an aggregate of 27,718 shares of the Company's common stock pursuant to the purchase plan (the "Plan") that was publicly announced on June 5, 2000.
- (2) In 2000, 2004 and 2005, the Board of Directors of ITIC and ITC approved the purchase by ITIC or ITC of up to an aggregate of 500,000 and 125,000 shares, respectively, of the Company's common stock pursuant to the Plan. Unless terminated earlier by resolution of the Board of Directors, the Plan will expire when ITC has purchased all shares authorized for purchase thereunder.
- (3) ITC intends to make further purchases under this Plan.



**Item 6. Exhibits**

(a) Exhibits

- 31(i) Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31(ii) Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURE

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

INVESTORS TITLE COMPANY

Dated: November 2, 2006

By: /s/ James A. Fine, Jr.

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James A. Fine, Jr.  
President, Principal Financial Officer and  
Principal Accounting Officer

