

HALLMARK FINANCIAL SERVICES INC  
Form 10-Q  
November 07, 2012

**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 Act of 1934

For the quarterly period ended September 30, 2012

Commission file number 001-11252

**Hallmark Financial Services, Inc.**

(Exact name of registrant as specified in its charter)

Nevada  
(State or other jurisdiction of  
Incorporation or organization)

87-0447375  
(I.R.S.  
Employer  
Identification  
No.)

Edgar Filing: HALLMARK FINANCIAL SERVICES INC - Form 10-Q

777 Main Street, Suite 1000, Fort Worth, Texas 76102

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (817) 348-1600

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: Common Stock, par value \$.18 per share – 19,263,457 shares outstanding as of November 7, 2012.

**PART I**

**FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**INDEX TO FINANCIAL STATEMENTS**

	Page Number
Consolidated Balance Sheets at September 30, 2012 (unaudited) and December 31, 2011	3
Consolidated Statements of Operations (unaudited) for the three months and nine months ended September 30, 2012 and September 30, 2011	4
Consolidated Statements of Comprehensive Income (Loss) (unaudited) for the three months and nine months ended September 30, 2012 and September 30, 2011	5
Consolidated Statements of Stockholders' Equity (unaudited) for the three months and nine months ended September 30, 2012 and September 30, 2011	6
Consolidated Statements of Cash Flows (unaudited) for the nine months ended September 30, 2012 and September 30, 2011	7
Notes to Consolidated Financial Statements (unaudited)	8

**Hallmark Financial Services, Inc. and Subsidiaries****Consolidated Balance Sheets**

(\$ in thousands, except share amounts)

	September 30 2012 (unaudited)	December 31 2011 (as adjusted)
<b>ASSETS</b>		
Investments:		
Debt securities, available-for-sale, at fair value (cost: \$380,495 in 2012 and \$380,578 in 2011)	\$ 384,288	\$ 380,469
Equity securities, available-for-sale, at fair value (cost: \$29,118 in 2012 and \$30,465 in 2011)	41,694	44,159
Total investments	425,982	424,628
Cash and cash equivalents	107,682	74,471
Restricted cash	8,246	9,372
Ceded unearned premiums	21,994	19,470
Premiums receivable	69,182	53,513
Accounts receivable	3,360	3,946
Receivable for securities	1,051	2,617
Reinsurance recoverable	50,109	42,734
Deferred policy acquisition costs	26,408	22,554
Goodwill	44,695	44,695
Intangible assets, net	23,965	26,654
Deferred federal income taxes, net	532	-
Federal income tax recoverable	-	6,738
Prepaid expenses	1,620	1,458
Other assets	11,008	13,209
Total assets	\$ 795,834	\$ 746,059
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Liabilities:		
Revolving credit facility payable	\$ 1,473	\$ 4,050
Subordinated debt securities	56,702	56,702
Reserves for unpaid losses and loss adjustment expenses	315,607	296,945
Unearned premiums	168,197	146,104
Reinsurance balances payable	5,976	3,139
Pension liability	3,245	3,971
Payable for securities	6,749	203
Deferred federal income taxes, net	-	135

Edgar Filing: HALLMARK FINANCIAL SERVICES INC - Form 10-Q

Federal income tax payable	177	-
Accounts payable and other accrued expenses	18,600	17,954
Total liabilities	576,726	529,203
Commitments and Contingencies (Note 17)		
Redeemable non-controlling interest	-	1,284
Stockholders' equity:		
Common stock, \$.18 par value, authorized 33,333,333 shares in 2012 and 2011; issued 20,872,831 in 2012 and 2011	3,757	3,757
Additional paid-in capital	122,412	122,487
Retained earnings	96,181	94,440
Accumulated other comprehensive income	8,316	6,446
Treasury stock (1,609,374 shares in 2012 and 2011), at cost	(11,558 )	(11,558 )
Total stockholders' equity	219,108	215,572
	\$ 795,834	\$ 746,059

The accompanying notes are an integral part

of the consolidated financial statements

**Hallmark Financial Services, Inc. and Subsidiaries****Consolidated Statements of Operations**

(Unaudited)

(\$ in thousands, except per share amounts)

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011 (as adjusted)	2012	2011 (as adjusted)
Gross premiums written	\$99,448	\$ 89,751	\$297,658	\$ 270,834
Ceded premiums written	(14,443 )	(11,869 )	(42,554 )	(37,762 )
Net premiums written	85,005	77,882	255,104	233,072
Change in unearned premiums	(4,524 )	(2,814 )	(19,166 )	(16,313 )
Net premiums earned	80,481	75,068	235,938	216,759
Investment income, net of expenses	3,795	3,980	11,573	11,765
Net realized gains	982	394	1,854	3,177
Finance charges	1,374	1,683	4,538	5,148
Commission and fees	(1,029 )	2,445	(1,033 )	2,617
Other income	17	178	307	203
Total revenues	85,620	83,748	253,177	239,669
Losses and loss adjustment expenses	52,839	56,136	168,859	181,841
Other operating expenses	25,726	24,850	77,077	71,890
Interest expense	1,137	1,159	3,464	3,470
Amortization of intangible assets	897	897	2,690	2,690
Total expenses	80,599	83,042	252,090	259,891
Income (loss) before tax	5,021	706	1,087	(20,222 )
Income tax expense (benefit)	1,350	602	(978 )	(9,048 )
Net income (loss)	3,671	104	2,065	(11,174 )
Less: Net income attributable to non-controlling interest	258	6	324	28
Net income (loss) attributable to Hallmark Financial Services, Inc.	\$3,413	\$ 98	\$1,741	\$ (11,202 )
Net income (loss) per share attributable to Hallmark Financial Services, Inc. common stockholders:				
Basic	\$0.18	\$ 0.01	\$0.09	\$ (0.57 )
Diluted	\$0.18	\$ 0.01	\$0.09	\$ (0.57 )

The accompanying notes are an integral part  
of the consolidated financial statements

**HALLMARK FINANCIAL SERVICES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

(Unaudited)

(\$ in thousands)

	Three Months Ended September		Nine Months Ended September	
	2012	2011 (as adjusted)	2012	2011 (as adjusted)
Net income (loss)	\$ 3,671	\$ 104	\$ 2,065	\$ (11,174 )
Other comprehensive loss:				
Change in net actuarial loss	120	72	362	215
Tax effect on change in net actuarial loss	(42 )	(25 )	(127 )	(75 )
Unrealized holding gains (losses) arising during the period	4,541	(8,134 )	4,560	(8,254 )
Tax effect on unrealized holding gains (losses) arising during the period	(1,589 )	2,847	(1,596 )	2,889
Reclassification adjustment for losses included in net income (loss)	(926 )	(393 )	(2,044 )	(3,177 )
Tax effect on reclassification adjustment for losses included in net income	324	137	715	1,112
Other comprehensive gain (loss), net of tax	2,428	(5,496 )	1,870	(7,290 )
Comprehensive gain (loss)	\$ 6,099	\$ (5,392 )	\$ 3,935	\$ (18,464 )
Less: comprehensive income attributable to non-controlling interest	258	6	324	28
Comprehensive gain (loss) attributable to Hallmark Financial Services, Inc.	\$ 5,841	\$ (5,398 )	\$ 3,611	\$ (18,492 )

The accompanying notes are an integral  
part of the consolidated financial statements





**Hallmark Financial Services, Inc. and Subsidiaries****Consolidated Statements of Stockholders' Equity**

(Unaudited)

(\$ in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011 (as adjusted)	2012	2011 (as adjusted)
<b>Common Stock</b>				
Balance, beginning of period	\$3,757	\$ 3,757	\$3,757	\$ 3,757
Balance, end of period	3,757	3,757	3,757	3,757
<b>Additional Paid-In Capital</b>				
Balance, beginning of period	122,669	122,292	122,487	121,815
Accretion of redeemable noncontrolling interest	(321 )	(31 )	(392 )	(37 )
Equity based compensation	64	94	317	583
Exercise of stock options	-	-	-	(6 )
Balance, end of period	122,412	122,355	122,412	122,355
<b>Retained Earnings</b>				
Balance, beginning of period, as previously reported	92,768	94,567	94,995	105,816
Cumulative effect of adjustments resulting from adoption of change in accounting principle, net of tax	-	(536 )	(555 )	(485 )
Balance, beginning of period, as adjusted	92,768	94,031	94,440	105,331
Net income (loss) attributable to Hallmark Financial Services, Inc.	3,413	98	1,741	(11,202 )
Balance, end of period	96,181	94,129	96,181	94,129
<b>Accumulated Other Comprehensive Income</b>				
Balance, beginning of period	5,888	7,843	6,446	9,637
Additional minimum pension liability, net of tax	78	47	235	140
Net unrealized holding (losses) gains arising during period, net of tax	2,952	(5,287 )	2,964	(5,365 )
Reclassification adjustment for gains included in net income, net of tax	(602 )	(256 )	(1,329 )	(2,065 )
Balance, end of period	8,316	2,347	8,316	2,347
<b>Treasury Stock</b>				

Edgar Filing: HALLMARK FINANCIAL SERVICES INC - Form 10-Q

Balance, beginning of period	(11,558 )	(10,068 )	(11,558 )	(5,262 )
Acquisition of treasury shares	-	(1,490 )	-	(6,401 )
Issuance of treasury stock upon option exercises	-	-	-	105
Balance, end of period	(11,558 )	(11,558 )	(11,558 )	(11,558 )
Total Stockholders' Equity	\$219,108	\$ 211,030	\$219,108	\$ 211,030

The accompanying notes are an integral part  
of the consolidated financial statements

**Hallmark Financial Services, Inc. and Subsidiaries**