

HALLMARK FINANCIAL SERVICES INC  
Form DEF 14A  
April 25, 2012

**SCHEDULE 14A INFORMATION**

Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

<input type="checkbox"/>	<input type="checkbox"/>	Preliminary Proxy Statement
<input type="checkbox"/>	<input type="checkbox"/>	Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Definitive Proxy Statement
<input type="checkbox"/>	<input type="checkbox"/>	Definitive Additional Materials
<input type="checkbox"/>	<input type="checkbox"/>	Soliciting Material under Rule 14a-12

**HALLMARK FINANCIAL SERVICES, INC.**

(Name of the Registrant as Specified In Its Charter)

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

Payment of Filing Fee (Check the appropriate box):

No fee required.

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

1. Title of each class of securities to which transaction applies:

2. Aggregate number of securities to which transaction applies:

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

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1. Amount Previously Paid:

2. Form, Schedule or Registration Statement No.:

3. Filing Party:

4. Date Filed:

**HALLMARK FINANCIAL SERVICES, INC.**

**777 Main Street, Suite 1000**

**Fort Worth, Texas 76102**

**NOTICE OF ANNUAL MEETING OF SHAREHOLDERS**

**TO BE HELD MAY 31, 2012**

To Our Shareholders:

NOTICE IS HEREBY GIVEN that the 2012 Annual Meeting of Shareholders of Hallmark Financial Services, Inc. (the "Company") will be held in the 11<sup>th</sup> Floor Conference Room at 777 Main Street, Fort Worth, Texas, at 10:00 a.m., Central Daylight Time, on Thursday, May 31, 2012, for the following purposes:

1. To elect four directors to serve until the next annual meeting of shareholders or until their successors are duly elected and qualified;
2. To conduct an advisory vote approving the Company's compensation of its named executive officers; and
3. To transact such other business that may properly come before the meeting or any adjournment thereof.

Shareholders of record at the close of business on April 5, 2012, are entitled to notice of and to vote at the Annual Meeting or any adjournment thereof.

All shareholders of the Company are cordially invited to attend the Annual Meeting.

BY ORDER OF THE BOARD OF DIRECTORS

/s/ CECIL R. WISE

Cecil R. Wise, Secretary

Dated: May 4, 2012

**WHETHER OR NOT YOU PLAN TO ATTEND THE MEETING, PLEASE SIGN AND DATE THE ENCLOSED PROXY AND RETURN IT PROMPTLY IN THE ENCLOSED STAMPED ENVELOPE. IF YOU ATTEND THE MEETING, YOU MAY REVOKE YOUR PROXY AND VOTE IN PERSON.**

**HALLMARK FINANCIAL SERVICES, INC.**

**777 Main Street, Suite 1000**

**Fort Worth, Texas 76102**

**PROXY STATEMENT**

**FOR**

**ANNUAL MEETING OF SHAREHOLDERS**

**TO BE HELD MAY 31, 2012**

**SOLICITATION AND REVOCABILITY OF PROXIES**

This Proxy Statement is furnished in connection with the solicitation of proxies by the Board of Directors (the "Board") of Hallmark Financial Services, Inc., a Nevada corporation (the "Company"), to be voted at the 2012 Annual Meeting of Shareholders (the "Annual Meeting") to be held on Thursday, May 31, 2012, at the time and place and for the purposes set forth in the accompanying Notice of Annual Meeting of Shareholders (the "Notice"), and at any adjournment thereof. When proxies in the accompanying form are properly executed and received, the shares represented thereby will be voted at the Annual Meeting in accordance with the directions noted thereon. If no direction is indicated on the proxy, the shares represented thereby will be voted for the election of each of the nominees for director and in the discretion of the proxy holder on any other matter that may properly come before the meeting.

Submitting a proxy will not affect a shareholder's right to vote in person at the Annual Meeting. Any shareholder who gives a proxy may revoke it at any time before it is exercised by delivering written notice of revocation to the Company, by substituting a new proxy executed on a later date, or by making a written request in person at the Annual Meeting that the proxy be returned. However, mere attendance at the Annual Meeting will not revoke the proxy.

All expenses of preparing, assembling and mailing this Proxy Statement and the enclosed materials and all costs of soliciting proxies will be paid by the Company. In addition to solicitation by mail, proxies may be solicited by officers and regular employees of the Company by telephone or in person. Such officers and employees who solicit proxies will receive no compensation for their services other than their regular salaries. Arrangements will also be made with brokerage houses and other custodians, nominees and fiduciaries to forward solicitation materials to the beneficial owners of shares they hold, and the Company may reimburse them for reasonable out-of-pocket expenses they incur in forwarding these materials.

The principal executive offices of the Company are located at 777 Main Street, Suite 1000, Fort Worth, Texas 76102. The Company's mailing address is the same as that of its principal executive offices.

This Proxy Statement and the accompanying form of proxy are first being mailed or given to shareholders on or about May 4, 2012. A copy of the Company's Annual Report to Shareholders for the fiscal year ended December 31, 2011, is enclosed herewith. Such Annual Report does not constitute a part of the materials used for the solicitation of proxies.

## **PURPOSES OF THE MEETING**

At the Annual Meeting, the shareholders of the Company will consider the following matters:

1. Election of four directors to serve until the next annual meeting of shareholders or until their successors are duly elected and qualified;
2. An advisory vote on a resolution approving the Company's compensation of its executive officers (the "Say-On-Pay Resolution"); and
3. Such other business as may properly come before the meeting or any adjournment thereof.

## **QUORUM AND VOTING**

The record date for the determination of shareholders entitled to notice of and to vote at the Annual Meeting was the close of business on April 5, 2012 (the "Record Date"). On the Record Date, there were 19,263,457 shares of common stock of the Company, par value \$0.18 per share (the "Common Stock"), issued and outstanding, each of which is entitled to one vote on all matters to be acted upon at the Annual Meeting. There are no cumulative voting rights. The presence, in person or by proxy, of holders of one-third of the outstanding shares of Common Stock entitled to vote at the meeting is necessary to constitute a quorum to transact business. Assuming the presence of a quorum, directors will be elected by a plurality of the votes cast. The affirmative vote of the holders of a majority of the shares of Common Stock actually voted will be required for approval of the Say-On-Pay Resolution and all other matters to come before the Annual Meeting.

Abstentions and broker non-votes will be counted solely for purposes of determining whether a quorum is present at the Annual Meeting. Pursuant to the Bylaws of the Company, abstentions and broker non-votes will not be counted in determining the number of shares voted on any matter. Therefore, abstentions and broker non-votes will have no effect on the election of directors or the approval of any other matter submitted to a vote of the shareholders at the Annual Meeting.

## **ELECTION OF DIRECTORS**

**(Item 1)**



At the Annual Meeting, four directors will be elected for a term expiring at the 2013 annual meeting of the Company's shareholders or when their successors are elected and qualify. Directors will be elected by a plurality of the votes cast at the Annual Meeting. Cumulative voting is not permitted in the election of directors.

The Board has proposed the following slate of nominees for election as directors at the Annual Meeting. None of the nominees was selected on the basis of any special arrangement or understanding with any other person. None of the nominees bears any family relationship to any other nominee or to any executive officer of the Company. The Board has determined that all of its nominees other than Mark E. Schwarz meet the current independence requirements of The Nasdaq Stock Market ("Nasdaq").

In the absence of instructions to the contrary, shares represented by proxy will be voted for the election of each nominee named below. Each nominee has accepted nomination and agreed to serve if elected. If any nominee becomes unable to serve before election, shares represented by proxy may be voted for the election of a substitute nominee designated by the Board.

**The Board recommends a vote FOR election of each nominee below.**

**Director**

<b>Name</b>	<b>Age</b>	<b>Since</b>	<b>Current Position(s) with the Company</b>
Mark E. Schwarz	51	2001	Director and Executive Chairman
Scott T. Berlin	42	2001	Director
James H. Graves	63	1995	Director
Jim W. Henderson	65	2009	Director

**Mark E. Schwarz** was elected Executive Chairman of the Company in August, 2006. He served as Chief Executive Officer of the Company from January, 2003 until August, 2006, and as President from November, 2003 through March, 2006. Since 1993, Mr. Schwarz has, through Newcastle Capital Management, L.P. and Newcastle Capital Group, L.L.C., controlled the general partner of Newcastle Partners, L.P., a private investment firm. Mr. Schwarz presently serves as Chairman of the boards of directors of Pizza Inn, Inc., an operator and franchisor of pizza restaurants; Bell Industries, Inc., a company primarily engaged in providing computer systems integration services; and Wilhelmina International, Inc., a model management and talent representation company. Mr. Schwarz is also presently a director of SL Industries, Inc., a developer of power systems used in a variety of aerospace, computer, datacom, industrial, medical, telecom, transportation and utility equipment applications. Within the past five years, Mr. Schwarz has also served as a director of MedQuist, Inc., a provider of clinical documentation workflow solutions in support of electronic health records; Nashua Corporation, a manufacturer of specialty papers, labels and printing supplies; Vesta Insurance Group, Inc., a property and casualty insurance holding company; and WebFinancial Corporation, a banking and specialty finance company. The Board believes that Mr. Schwarz should serve as a director of the Company due to his extensive business and investment expertise, broad director experience and significant direct and indirect shareholdings in the Company. (See, *Principal Shareholders and Stock Ownership of Management.*)

**Scott T. Berlin** is a Managing Director and principal of Brown, Gibbons, Lang & Company, an investment banking firm serving middle market companies. His professional activities are focused on the corporate finance and mergers/acquisitions practice. Prior to joining Brown, Gibbons, Lang & Company in 1997, Mr. Berlin was a lending officer in the Middle Market Group at The Northern Company. The Board believes that Mr. Berlin should serve as a director of the Company due to his general background in investment banking and his particular experience in advising public and private companies and their boards in merger, acquisition and financing transactions.

**James H. Graves** has served as Managing Director and Partner of Erwin, Graves & Associates, LP, a management consulting firm, since 2002. He also served as an Executive Vice President of Financial Strategy for

DeviceFidelity Inc., a financial services technology company, from 2008 through 2011. Mr. Graves was a director, Vice Chairman and Chief Operating Officer of Detwiler, Mitchell & Co., a securities research firm, from 2002 until 2006. Prior to 2002, he served as a senior executive in Dean Witter Reynolds Investment Banking Division and as the Chief Operating Officer of J.C. Bradford & Company. Mr. Graves also presently serves as a director of DeviceFidelity, Inc.; Cash America International, Inc., a company operating pawn shops and jewelry stores; and BankCap Partners, LP, a private equity fund which he co-founded in 2006. The Board believes Mr. Graves should serve as a director due to his executive leadership and management experience in several businesses, including large corporations and businesses within the financial services industry, his over 30 years of experience analyzing financial statements and his experience as a director of both private and public companies, including his service as chairman of the audit committee of another public company.

**Jim W. Henderson** became Chairman and Chief Executive Officer of AssuredPartners, Inc., a middle market insurance brokerage firm, in March, 2011. Mr. Henderson was previously employed by Brown & Brown, Inc., a diversified insurance agency and wholesale broker, as Vice Chairman and Chief Operating Officer since 2008, as President and Chief Operating Officer from 2002 to 2008, as Executive Vice President from 1995 to 2002, as Senior Vice President from 1993 to 1995, as Senior Vice President of a predecessor corporation from 1989 to 1993, and as Chief Financial Officer of such predecessor from 1985 to 1989. He also served as a director of Brown & Brown from 1993 to 2011. Previously, Mr. Henderson had served as Senior Vice President, Chief Financial Officer and Treasurer of Ormond Reinsurance Group from 1975 to 1985. Mr. Henderson is currently a director of Overland Solutions, Inc., an insurance services outsourcing firm. The Board believes that Mr. Henderson should serve as a director of the Company due to his extensive knowledge of and significant executive experience in the property and casualty insurance industry, as well as his prior experience as a director of a public company.

## **ADVISORY VOTE ON SAY-ON-PAY RESOLUTION**

### **(Item 2)**

Section 14A of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and Rule 14a-21 promulgated by the Securities and Exchange Commission (“SEC”) thereunder, require the Company to (i) at least once every three years, present to the shareholders a non-binding, advisory vote on a resolution approving the compensation of certain executive officers, and (ii) at least once every six years, present to the shareholders a non-binding, advisory vote on the frequency of future such resolutions to approve executive compensation. In accordance with the majority vote at the Company’s 2011 Annual Meeting of Shareholders, the Board has determined to provide the shareholders an opportunity to approve executive compensation every year. Accordingly, at the 2012 Annual Meeting the Board will submit to the shareholders for a non-binding, advisory vote the following Say-On-Pay Resolution:

“RESOLVED, that the shareholders hereby approve the compensation paid to the Company’s executive officers as disclosed pursuant to Item 402 of Regulation S-K under the heading ‘EXECUTIVE COMPENSATION’ in the Company’s 2012 Proxy Statement, including the compensation tables and narrative discussion.”

The advisory vote on the Say-On-Pay Resolution is intended to address the overall compensation of the Company’s executive officers rather than any specific element or amount of compensation. This advisory vote on the Say-On-Pay Resolution is not binding on the Board or the Company. However, the Compensation Committee will take into account the results of the advisory vote on the Say-On-Pay Resolution when considering future executive compensation arrangements.

**The Board recommends a vote FOR approval of the Say-On-Pay Resolution.**

A vote on the frequency of future such resolutions to approve executive compensation will be submitted to the shareholders not later than the 2017 Annual Meeting of Shareholders.

**OTHER BUSINESS**

**(Item 3)**

The Board knows of no other business to be brought before the Annual Meeting. If, however, any other business should properly come before the Annual Meeting, the persons named in the accompanying proxy will vote the proxy as they in their discretion may deem appropriate, unless they are directed by the proxy to do otherwise.

## **BOARD OF DIRECTORS**

### **Leadership Structure and Risk Oversight**

Mark E. Schwarz serves as the Executive Chairman of the Company. In such capacity, he functions as both the chairman of the Board and an executive officer with responsibilities for corporate strategy, capital allocation and management of the Company's investment portfolio. Mark J. Morrison serves as the President and Chief Executive Officer of the Company but is not a director. The Board believes that this leadership structure is appropriate because it permits Mr. Schwarz to provide Board leadership independent of operational management, while still providing the Company the benefit of his business and investment expertise. As a result, the Board believes that all directors are able to objectively evaluate the management and operations of the Company. The Board also believes that, as a result of his significant beneficial ownership of Common Stock, Mr. Schwarz's role as Executive Chairman enhances the focus of the Board on building shareholder value. (See, *Principal Shareholders and Stock Ownership of Management*.)

The Board is responsible for providing general oversight over all of the Company's strategies, operations and affairs, including its management of risk. The Board and its standing committees regularly discuss material risk exposures, the potential impact of such exposures on the Company and the efforts of management to mitigate the identified risks. The Company has adopted enterprise risk management policies based on the Integrated Framework of the Committee of Sponsoring Organizations. Executive management periodically report on the Company's risk management policies and practices to the Board and relevant standing committees. The Audit Committee reviews the Company's major financial risk exposures and a number of operational, compliance and strategic risks, including steps to monitor and manage those risks. The Nomination and Governance Committee also monitors the Company's corporate governance and certain compliance risks, while the Compensation Committee is primarily responsible for oversight of risks associated with employee relations and compensation strategy. The Board believes that its leadership structure supports the ability of the Board to effectively oversee the risk management policies and procedures of the Company.

### **Board Composition**

The Board is presently composed of Mark E. Schwarz, Scott T. Berlin, James H. Graves and Jim W. Henderson. George R. Manser also served as a director of the Company until his retirement from the Board on June 2, 2011. None of these directors was selected on the basis of any special arrangement or understanding with any other person. None of these directors bears any family relationship to any other director or to any executive officer of the Company. The Board has determined that all of these directors other than Mr. Schwarz meet the current Nasdaq independence requirements. Information concerning the business experience of each of the director nominees is provided under *Election of Directors*.

**Board Committees**

Standing committees of the Board of the Company include the Audit Committee, the Nomination and Governance Committee, and the Compensation Committee. Messrs. Berlin, Graves and Henderson presently serve on the standing committees set forth below. Mr. Schwarz does not presently serve on any of these standing committees.

	Nomination and		
	Audit	Governance	Compensation
	Committee	Committee	Committee
Scott T. Berlin	X	X	X
James H. Graves	X	X	X
Jim W. Henderson	X		X

Audit Committee. James H. Graves currently serves as chairman of the Audit Committee. The Board has determined that all members of the Audit Committee satisfy the current independence and experience requirements of Nasdaq and the SEC. The Board has also determined that Mr. Graves satisfies the requirements for an “audit committee financial expert” under applicable rules of the SEC and has designated Mr. Graves as its “audit committee financial expert.”

The Audit Committee oversees the conduct of the financial reporting processes of the Company, including (i) reviewing with management and the outside auditors the audited financial statements included in the Company’s Annual Report, (ii) reviewing with management and the outside auditors the interim financial results included in the Company’s quarterly reports filed with the SEC, (iii) discussing with management and the outside auditors the quality and adequacy of internal controls, and (iv) reviewing the independence of the outside auditors. (See, *Audit Committee Report*.) A copy of the Amended and Restated Audit Committee Charter is available for review on the Company’s website at [www.hallmarkgrp.com](http://www.hallmarkgrp.com). The Audit Committee held eight meetings during 2011.

Nomination and Governance Committee. Scott T. Berlin currently serves as chairman of the Nomination and Governance Committee. The Nomination and Governance Committee is responsible for advising the Board about the appropriate composition of the Board and its committees, identifying and evaluating candidates for Board service, recommending director nominees for election at annual meetings of shareholders or for appointment to fill vacancies, and recommending the directors to serve on each committee of the Board. The Nomination and Governance Committee is also responsible for periodically reviewing and making recommendations to the Board regarding corporate governance policies and responses to shareholder proposals. A copy of the Nomination and Governance Committee Charter is available for review on the Company’s website at [www.hallmarkgrp.com](http://www.hallmarkgrp.com). The Nomination and Governance Committee met once during fiscal 2011.

The Nomination and Governance Committee strives to identify and attract director nominees of personal integrity whose diversity of business background and experience will represent the interests of all shareholders. The Nomination and Governance Committee has not established any policy regarding specific minimum qualifications that must be met by a director nominee. However, factors considered in evaluating potential candidates include educational achievement, managerial experience, business acumen, financial sophistication, insurance industry expertise and strategic planning and policy-making skills. Depending upon the current needs of the Board, some factors may be weighed more or less heavily than others in the deliberations. The Nomination and Governance Committee evaluates the suitability of a potential director nominee on the basis of written information concerning the candidate, discussions with persons familiar with the background and character of the candidate and personal interviews with the candidate.

The Nomination and Governance Committee will consider candidates for nomination to the Board from any reasonable source, including shareholder recommendations. The Nomination and Governance Committee does not evaluate candidates differently based on the source of the proposal. The Nomination and Governance Committee has not, and has no present intention to, use consultants or search firms to assist in the process of identifying and evaluating director candidates.



Shareholders may recommend director candidates for consideration by the Nomination and Governance Committee by writing to its chairman in care of the Company's headquarters in Fort Worth, Texas, giving the candidate's name, contact information, biographical data and qualifications. A written statement from the candidate consenting to be named as a candidate and, if nominated and elected, to serve as a director should accompany any such recommendation. The Nomination and Governance Committee has not implemented any formal procedures for consideration of director nominees submitted by shareholders of the Company. The Nomination and Governance Committee has not received any recommendations of nominees for election to the Board at the 2012 Annual Meeting from any person or group beneficially owning more than five percent of the Common Stock.

Compensation Committee. Jim W. Henderson currently serves as chairman of the Compensation Committee. The Compensation Committee reviews, evaluates and recommends to the Board compensation policies of the Company with respect to directors, executive officers and senior management. The Compensation Committee also administers the Company's 2005 Long Term Incentive Plan (the "2005 LTIP"). The Compensation Committee does not have a charter. The Compensation Committee met four times during 2011.

The Compensation Committee has the authority to approve the compensation of the directors, executive officers and senior management of the Company. The Compensation Committee also has the authority to grant stock options and other equity awards under the 2005 LTIP. The Compensation Committee does not delegate any of its authority to any other person. The Executive Chairman and Chief Executive Officer of the Company provide recommendations to the Compensation Committee concerning most of these compensation decisions. Neither the Company nor the Compensation Committee currently engages any consultant to assist in the review of director or executive officer compensation.

#### **Attendance at Meetings**

The Board held five meetings during 2011. Various matters were also approved by the unanimous written consent of the directors during the last fiscal year. Each director attended at least 75% of the aggregate of (i) the total number of meetings of the Board, and (ii) the total number of meetings held by all committees of the Board on which such director served. The Company has no formal policy with respect to the attendance of Board members at the Annual Meeting, but encourages all incumbent directors and all director nominees to attend each annual meeting of shareholders. Three incumbent directors attended the Company's last annual meeting of shareholders held on June 2, 2011.

#### **Compensation of Directors in 2011 Fiscal Year**

The Company's standard compensation arrangement for each non-employee director is currently a \$30,000 annual retainer plus a fee of \$1,500 for each Board meeting attended in person or telephonically and a fee of \$750 for each committee meeting attended in person or telephonically. The chairman of the Audit Committee also receives an additional \$7,500 annual retainer. No other cash compensation was paid to any non-employee director during 2011. The Compensation Committee also periodically grants stock options to the directors of the Company. However, no stock options were granted to any of the non-employee directors of the Company during 2011.

The following table sets forth information concerning the compensation of the non-employee directors of the Company for the fiscal year ended December 31, 2011.

Name	Fees Earned or		Option Awards (\$)		All Other	Total (\$)
	Paid in Cash (\$)				Compensation (\$)	
Scott T. Berlin	133,500	1	—	2	—	133,500 <sup>1</sup>
James H. Graves	56,250		—	2	—	56,250
Jim W. Henderson	48,750		—	2	—	48,750

<sup>1</sup> Includes \$84,000 in special remuneration for ten years of meritorious service on the Board approved in 2011 but paid in 2012.

<sup>2</sup> As of December 31, 2011, options to purchase 30,000, 30,000 and 15,000 shares of Common Stock were outstanding to Messrs. Berlin, Graves and Henderson, respectively.

## Shareholder Communications

The Board believes that, in light of the accessibility of its directors to informal communications, a formal process for shareholders to communicate with directors is unnecessary. Any shareholder communication sent to the Board, either generally or in care of the Executive Chairman, will be forwarded to members of the Board without screening. Any shareholder communication to the Board should be addressed in care of the Executive Chairman and transmitted to the Company's headquarters in Fort Worth, Texas. In order to assure proper handling, the transmittal envelope should include a notation indicating "Board Communication" or "Director Communication." All such correspondence should identify the author as a shareholder and clearly state whether the intended recipients are all members of the Board or only specified directors. The Executive Chairman will circulate all such correspondence to the appropriate directors.

## EXECUTIVE OFFICERS

The following persons are currently the only executive officers of the Company:

Name	Age	Position(s) with the Company
Mark E. Schwarz	51	Executive Chairman and Director
Mark J. Morrison	52	President and Chief Executive Officer
Kevin T. Kasitz	49	Executive Vice President for Commercial Lines and Chief Operating Officer
Jeffrey R. Passmore	44	Senior Vice President and Chief Accounting Officer

Each executive officer serves at the will of the Board. No executive officer was selected on the basis of any special arrangement or understanding with any other person. No executive officer bears any family relationship to any other executive officer or to any director or nominee for director of the Company. No director, nominee for director or executive officer of the Company has been involved in any legal proceedings that would be material to an evaluation of the management of the Company. Information concerning the business experience of Mark E. Schwarz is provided under *Election of Directors*.

**Mark J. Morrison** was named President of the Company in April, 2006 and became Chief Executive Officer in August, 2006. He joined the Company in March, 2004, as Executive Vice President and Chief Financial Officer and was appointed to the additional position of Chief Operating Officer in April, 2005. Mr. Morrison has been employed in the property and casualty insurance industry since 1993. Prior to joining the Company, he had since 2001 served as

President of Associates Insurance Group, a subsidiary of The Travelers Companies, Inc. From 1996 through 2000, he served as Senior Vice President and Chief Financial Officer of Associates Insurance Group, the insurance division of Associates First Capital Corporation. From 1995 to 1996, Mr. Morrison served as Vice President and Controller of American Eagle Insurance Group, and from 1993 to 1995 was Director of Corporate Accounting for Republic Insurance Group. From 1991 to 1993, he served as Director of Strategic Planning and Analysis at Anthem, Inc. Mr. Morrison began his career as a public accountant with Ernst & Young, LLP from 1982 to 1991, where he completed his tenure as a Senior Manager.

**Kevin T. Kasitz** was named an Executive Vice President of the Company effective April, 2006, and became Chief Operating Officer in December, 2006. He has also served as the President of the Standard Commercial business unit, a functional division of the Company handling standard lines commercial insurance, since April, 2003. Prior to joining the Company, Mr. Kasitz had since 1991 been employed by Benfield Blanch Inc., a reinsurance intermediary, where he served as a Senior Vice President in the Program Services division (2000 to 2003) and Alternative Distribution division (1999 to 2000), a Vice President in the Alternative Distribution division (1994 to 1999) and a Manager in the Wholesale Insurance Services division (1991 to 1994). From 1989 to 1991, he was a personal lines underwriter for Continental Insurance Company and from 1986 to 1989 was an internal auditor for National County Mutual Insurance Company, a regional non-standard automobile insurer.

**Jeffrey R. Passmore** has served as Senior Vice President and Chief Accounting Officer of the Company since June, 2003, and previously served as Vice President of Business Development for the Company. Prior to joining the Company in November, 2002, Mr. Passmore had since 2000 served as Vice President and Controller of Benfield Blanch, Inc. and its predecessor E.W. Blanch Holdings, Inc., a reinsurance intermediary. From 1998 to 1999, he served E.W. Blanch Holdings, Inc. as Assistant Vice President of Financial Reporting. From 1994 to 1998, he was a senior financial analyst with TIG Holdings, Inc., a property/casualty insurance holding company. Mr. Passmore began his career as an accountant for Gulf Insurance Group from 1990 to 1993. Mr. Passmore is a certified public accountant licensed in Texas.

## **EXECUTIVE COMPENSATION**

### **Compensation Discussion and Analysis**

Role of the Compensation Committee. The Company's Compensation Committee reviews, evaluates and recommends to the Board compensation policies with respect to directors, executive officers and senior management of the Company. The Compensation Committee has the authority to approve the compensation of the directors, executive officers and senior management of the Company. The Compensation Committee also has the authority to grant stock options and other equity awards under the 2005 LTIP. The Compensation Committee does not delegate any of its authority to any other person. The Executive Chairman and Chief Executive Officer of the Company provide recommendations to the Compensation Committee concerning most of these compensation decisions. Neither the Company nor the Compensation Committee currently engages any consultant to assist in the review of director or executive officer compensation.

Compensation Objectives and Components. The compensation policies of the Company are intended to reinforce the Company's annual and long-term performance objectives, reward and encourage quality performance, and assist the Company in attracting, retaining and motivating executive officers and other senior management with exceptional leadership abilities. Consistent with these objectives, the Compensation Committee has established a compensation program consisting primarily of base salary, annual bonus and stock options. These components of compensation are

intended to reward performance, responsibility, initiative and teamwork in developing and implementing the Company's strategic goals.

The Compensation Committee believes that competitive base salaries are a prerequisite to attracting and retaining a qualified and motivated leadership team. Annual bonuses are primarily intended to encourage performance which contributes to achieving annual and other near-term corporate objectives. Stock options are primarily intended to align the financial interests of management and directors with those of other shareholders and thereby provide incentives for achieving long-term growth in the value of the Company. The Compensation Committee strives for an appropriate balance among the elements of compensation but has not established any formula or policy for the allocation of total compensation among the base salary, annual bonus and stock option components. Although the Company endeavors to provide a total compensation package for its executive officers and senior management which is competitive in its segment of the insurance industry, the Compensation Committee has not engaged in any benchmarking of total compensation or any component of compensation.

Determination of Compensation. Base salaries of the Company's executive officers and senior management are determined based on factors including scope of responsibilities, level of experience, contributions to the achievement of business objectives, leadership skills and overall management effectiveness. Base salaries are generally intended to be competitive with those offered in the markets in which the Company competes for executive talent. However, the overall assessment is primarily subjective, reflecting the level of responsibility and personal performance of the individual executive.

The Compensation Committee evaluates the propriety of discretionary annual bonuses primarily on the basis of the Company's financial performance and the job performance of each executive officer, including characteristics of cooperation, positive attitude and teamwork in achieving corporate goals. The primary measure of the Company's financial performance used in determining any discretionary annual bonuses is business unit and/or consolidated pre-tax income as compared to the annual budget. The Compensation Committee retains and exercises discretion with respect to whether any annual bonus is paid to a particular executive officer and, if so, the ultimate amount of such annual bonus. In light of the Company's financial performance, the Compensation Committee did not award discretionary annual bonuses to any of the executive officers of the Company for fiscal 2011.

The Compensation Committee believes that periodically granting stock options to the executive officers and other senior management promotes the Company's long-term performance by aligning the officers' economic interests with shareholder value. Stock options are typically granted on the same date as the Company's annual meeting of shareholders and are exercisable at the closing market price of the Common Stock on the date of grant. The amount of stock option grants are based on various subjective factors primarily relating to the responsibilities of the officer and his past and expected future contributions to the growth and profitability of the Company. During fiscal 2011, the Compensation Committee did not award stock options to any of the executive officers of the Company other than Mark E. Schwarz. On December 30, 2011, Mr. Schwarz was granted non-qualified stock options in recognition of ten years of meritorious service on the Board, which options will fully vest on July 1, 2012 and will expire on the tenth anniversary of the date of grant.

Consideration of Shareholder Advisory Vote. At the Company's 2011 annual meeting of shareholders, an advisory resolution approving the compensation of the Company's executive officers was favored by approximately 73% of the shares voted. The Compensation Committee has considered these results in determining to continue its current compensation policies. The Compensation Committee believes that its subsequent compensation decisions have been consistent with both its existing compensation policies and the 2011 shareholder advisory vote.

Tax and Accounting Implications. Section 162(m) of the Internal Revenue Code generally imposes a \$1.0 million per person annual limit on the amount the Company may deduct as compensation expense for its executive officers. The Compensation Committee has not established any policy precluding the payment of compensation in excess of the amount deductible under IRC Section 162(m). However, the compensation of all executive officers was fully deductible during fiscal 2011, and the Company does not presently anticipate that the compensation of any executive officer will exceed this limit on deductibility for fiscal 2012.



The Company accounts for all equity compensation, including awards under the 2005 LTIP, in accordance with Accounting Standards Codification 718 promulgated by the Financial Accounting Standards Board. Pursuant to these provisions, the grant date fair value of equity compensation is recognized pro rata over the vesting periods of the awards.

### **Employment Agreements**

The Company does not have employment agreements with any of its executive officers.

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**Summary Compensation Table**

The following table sets forth information for the fiscal years ended December 31, 2011, 2010 and 2009 concerning the compensation of the Chief Executive Officer, Chief Accounting Officer and every other person who served as an executive officer of the Company at any time during fiscal 2011 (the “Named Executive Officers”).

<b>Name and Current Principal Position</b>	<b>Year</b>	<b>Salary (\$)</b>	<b>Bonus (\$)<sup>1</sup></b>	<b>Option Awards (\$)<sup>2</sup></b>	<b>All Other Compensation (\$)<sup>3</sup></b>	<b>Total (\$)</b>
Mark E. Schwarz Executive Chairman Director	2011	195,000	—	21,064	8,995	225,059
	2010	195,000	—	—	10,914	205,914
	2009	195,000	—	—	10,717	205,717
Mark J. Morrison President Chief Executive Officer	2011	392,500	—	—	9,218	401,718
	2010	385,000	—	—	11,458	396,458
	2009	365,000	140,000	4 228,000	11,174	744,174
Kevin T. Kasitz Executive Vice President Chief Operating Officer	2011	260,000	—	—	12,604	272,604
	2010	255,000	—	—	14,841	269,841
	2009	245,000	80,000	4 167,200	14,568	506,768
Jeffrey R. Passmore Senior Vice President Chief Accounting Officer	2011	182,250	—	—	12,515	194,765
	2010	178,500	—	—	14,343	192,843
	2009	170,000	52,000	106,400	13,610	342,010
Brookland F. Davis <sup>5</sup>	2011	181,541	—	—	8,390	189,931
	2010	260,000	—	—	17,442	277,442
	2009	235,000	115,000	4 167,200	17,091	534,291

<sup>1</sup> Bonuses earned for a fiscal year were awarded in the following fiscal year.

Reflects the fair value of each stock option estimated on the date of grant using the Black-Scholes option pricing model. Assumptions used in calculating this amount are included in Note 13 to the Company’s audited financial statements included in its Annual Report on Form 10-K for the year ended December 31, 2011. Information concerning material terms of stock option grants is provided under *Executive Compensation – Outstanding Equity Awards at 2011 Fiscal Year-End*.

<sup>3</sup> Represents the employee portion of medical coverage paid by the Company and the Company’s matching contributions to employee 401(k) accounts. In 2011, the Company matched \$0.17 for each dollar of employee contribution to the 401(k) plan up to 6% of annual salary, which becomes fully vested after three years of eligible

employment. In 2010 and 2009, the Company matched \$0.33 for each dollar of employee contribution to the 401(k) plan up to 6% of annual salary, which becomes fully vested after three years of eligible employment.

Of the total bonus amount, 75% was paid when awarded and the remaining 25% is payable in two equal annual installments of cash, without interest, on the first and second anniversaries of the initial payment. Receipt of the deferred payments is conditioned upon continued employment with the Company.

Mr. Davis served as Executive Vice President for Personal Lines until leaving the Company effective August 10, 2011.

#### **Grants of Plan-Based Awards in 2011 Fiscal Year**

The following table sets forth information concerning grants of plan-based awards to the Named Executive Officers during the fiscal year ended December 31, 2011, consisting solely of stock options granted under the 2005 LTIP.

Name	Grant Date	Option Awards: Number of Securities Underlying Options (#) <sup>1</sup>	Exercise Price	Grant Date Fair Value of Option Awards (\$)²
			Of Option Awards (\$/Sh)	
Mark E. Schwarz	12/30/2011	14,157	6.99	21,064
Mark J. Morrison	—	—	—	—
Kevin T. Kasitz	—	—	—	—
Jeffrey R. Passmore	—	—	—	—
Brookland F. Davis	—	—	—	—

Options are to purchase shares of the Company's Common Stock. Options were granted to Mr. Schwarz in his capacity as a director, become fully vested on July 1, 2012, and expire ten years from the date of grant, subject to earlier termination due to death, disability or termination of employment.

Reflects the fair value of stock options estimated on the date of grant using the Black-Scholes option pricing model.  
<sup>2</sup>Assumptions used in calculating this amount are included in Note 13 to the Company's audited financial statements included in its Annual Report on Form 10-K for the year ended December 31, 2011.

### Outstanding Equity Awards at 2011 Fiscal Year-End

The following table sets forth information concerning all equity awards to the Named Executive Officers which were outstanding as of December 31, 2011, consisting solely of unexercised stock options granted under the 2005 LTIP.

Name	Number of Securities		Option Exercise Price (\$)	Option Expiration Date
	Underlying Unexercised Options Exercisable (#)	Unexercisable (#) <sup>1</sup>		
Mark E. Schwarz	10,000	—	12.52	05/24/2017
	5,000	—	11.46	05/22/2018
	57,143	142,857	6.61	04/01/2019
	—	14,157	6.99	12/30/2021

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Mark J. Morrison	16,667	—	7.14	05/27/2015
	20,833	—	11.34	05/25/2016
	100,000	—	12.52	05/24/2017
	30,000	20,000	11.46	05/22/2018
	21,429	53,571	6.61	04/01/2019
Kevin T. Kasitz	16,667	—	7.14	05/27/2015
	16,667	—	11.34	05/25/2016
	75,000	—	12.52	05/24/2017
	22,500	15,000	11.46	05/22/2018
	15,714	39,286	6.61	04/01/2019
Jeffrey R. Passmore	8,333	—	7.14	05/27/2015
	8,333	—	11.34	05/25/2016
	50,000	—	12.52	05/24/2017
	15,000	10,000	11.46	05/22/2018
	10,000	25,000	6.61	04/01/2019
Brookland F. Davis	—	—	—	—

<sup>1</sup> Unexercisable options expiring May 22, 2018, vest on May 22, 2012. Options expiring April 1, 2019, vest in seven equal annual installments commencing April 1, 2010. Options expiring December 30, 2021, vest on July 1, 2012.

**Option Exercises in 2011 Fiscal Year**

None of the Named Executive Officers exercised any stock options, stock appreciation rights or similar instruments during the fiscal year ended December 31, 2011. No restricted stock, restricted stock units or similar instruments held by the Named Executive Officers vested during the fiscal year ended December 31, 2011.

**Deferred Compensation**

The Company does not maintain any elective deferred compensation plans. However, the discretionary annual bonus earned by certain of the Named Executive Officers for fiscal 2009 was paid 75% in cash when awarded and the remaining 25% in two equal annual installments of cash, without interest, on the first and second anniversaries of the initial payment. Receipt of the deferred amount is conditioned upon each executive officer's continued employment with the Company. The following table sets forth information concerning these mandatory cash deferrals of discretionary annual bonuses as of December 31, 2011.

Name	<b>Amount Deferred</b>	<b>Distributions</b>	<b>Balance at</b>
	<b>In Last</b>	<b>In Last</b>	<b>Last Fiscal</b>
	<b>Fiscal Year (\$)</b>	<b>Fiscal Year (\$)</b>	<b>Year End (\$)</b>
Mark E. Schwarz	—	—	—
Mark J. Morrison	—	28,125	17,500
Kevin T. Kasitz	—	16,250	10,000
Jeffrey R. Passmore	—	—	—
Brookland F. Davis	—	23,125	—

**Equity Compensation Plan Information**

The following table sets forth information regarding shares of the Common Stock authorized for issuance under the Company's equity compensation plans as of December 31, 2011.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans [excluding securities reflected in column (a)] (c)
Equity compensation plans approved by security holders	1,419,989	\$ 9.66	564,178
Equity compensation plans not approved by security holders	—	—	—
Total	1,419,989	\$ 9.66	564,178

## COMPENSATION COMMITTEE REPORT

The Compensation Committee of the Board has reviewed and discussed with management of the Company the Compensation Discussion and Analysis contained in this Proxy Statement. Based on such review and discussion, the Compensation Committee recommended to the Board that the Compensation Discussion and Analysis be included in this Proxy Statement.

Respectfully submitted by the Compensation Committee:

Jim W. Henderson (chairman)

Scott T. Berlin

James H. Graves

## COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

Messrs. Henderson, Berlin and Graves comprised the Compensation Committee during fiscal 2011. Messrs. Henderson, Berlin and Graves have never been officers or employees of the Company. During fiscal 2011, no executive officer of the Company served on the board of directors or compensation committee of any other entity any of whose executive officers served on the Board or Compensation Committee of the Company.

## CERTAIN RELATIONSHIPS AND TRANSACTIONS

The Executive Chairman of the Company, Mark E. Schwarz, is the managing member of Newcastle Capital Group, L.L.C. ("NCG"), which entity is the sole general partner of Newcastle Capital Management, L.P. ("NCM"), which entity is the sole general partner of Newcastle Partners, L.P. ("Newcastle Fund"). In addition, Mr. Schwarz and NCG are the sole shareholders of DSC Services, Inc., which in turn is the sole shareholder of Detroit Stoker Company ("Detroit Stoker"). As a result of these relationships, Mr. Schwarz has sole investment and voting control over the shares of Common Stock beneficially owned by NCM, the Newcastle Fund and Detroit Stoker, which collectively are the largest holders of the Common Stock. (See, *Principal Shareholders and Stock Ownership of Management*.)

Also as a result of these relationships, the Company, Mr. Schwarz, NCG, NCM and the Newcastle Fund may be deemed a "group" for purposes of Section 13(d)(3) of the Securities Exchange Act of 1934 with respect to their



respective investments in Pizza Inn, Inc., an operator and franchisor of pizza restaurants in which Mr. Schwarz serves as Chairman of the board of directors. During 2011, 2010 and 2009, the Company purchased an aggregate of 1,030,629 shares of the common stock of Pizza Inn in the open market at an average price of \$1.56 per share. As of December 31, 2011, the Company held approximately 12.8% of the total outstanding shares of the common stock of Pizza Inn. The Company has no other financial transactions, arrangements or relationships with Pizza Inn.

## **CODE OF ETHICS**

The Board has adopted a Code of Ethics applicable to all of the Company's employees, officers and directors. The Code of Ethics covers compliance with law; fair and honest dealings with the Company, its competitors and others; full, fair and accurate disclosure to the public; and procedures for compliance with the Code of Ethics. This Code of Ethics is posted on the Company's website at [www.hallmarkgrp.com](http://www.hallmarkgrp.com).

## **SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

The Company's executive officers, directors and beneficial owners of more than 10% of the Company's Common Stock are required to file reports of ownership and changes in ownership of the Common Stock with the SEC. Based solely upon information provided to the Company by individual directors, executive officers and beneficial owners, the Company believes that all such reports were timely filed during and with respect to the fiscal year ended December 31, 2011.

**PRINCIPAL SHAREHOLDERS AND STOCK OWNERSHIP OF MANAGEMENT**

The following table and the notes thereto set forth certain information regarding the beneficial ownership of the Common Stock as of the Record Date by (i) the Company's current executive officers, (ii) each current director and nominee for director of the Company, (iii) all current executive officers and current directors of the Company as a group; and (iv) each other person known to the Company to own beneficially more than five percent of the presently outstanding Common Stock. Except as otherwise indicated, (a) the persons identified in the table have sole voting and dispositive power with respect to the shares shown as beneficially owned by them, (b) the mailing address for all persons is the same as that of the Company, and (c) the current directors and executive officers have not pledged any of such shares as security.

<b><u>Shareholder</u></b>	<b>No. of Shares</b>	<b>Percent of Class</b>
	<b>Beneficially Owned</b>	<b>Beneficially Owned</b>
Mark E. Schwarz <sup>1</sup>	4,952,857	25.6
Mark J. Morrison <sup>2</sup>	294,643	1.5
Kevin T. Kasitz <sup>3</sup>	195,831	1.0
Jeffrey R. Passmore <sup>4</sup>	106,666	*
Scott T. Berlin <sup>5</sup>	40,000	*
James H. Graves <sup>5</sup>	44,659	*
Jim W. Henderson <sup>6</sup>	38,000	*
All current executive officers and directors, as a group (7 persons) <sup>7</sup>	5,672,656	28.5
Newcastle Partners, L.P. <sup>8</sup>	3,730,430	19.4
Bares Capital Management, Inc. <sup>9</sup>	1,906,687	9.9
Dimensional Fund Advisors LP <sup>10</sup>	1,331,464	6.9
The Killen Group, Inc. <sup>11</sup>	1,285,509	6.7
Overbrook Limited Partnership <sup>12</sup>	1,295,778	6.7

\*

Represents less than 1%.

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<sup>1</sup> Includes 130,806 shares directly owned by Mr. Schwarz, 134,375 shares owned by NCM, 3,730,430 shares owned by the Newcastle Fund and 856,533 shares owned by Detroit Stoker, all of which are pledged to secure margin accounts. (See *Certain Relationships and Transactions* and Note 8, below.) Also includes 100,713 shares which may be acquired by Mr. Schwarz pursuant to stock options exercisable on or within 60 days after the Record Date,

<sup>2</sup> Includes 219,643 shares which may be acquired pursuant to stock options exercisable on or within 60 days after the Record Date.

<sup>3</sup> Includes 169,405 shares which may be acquired pursuant to stock options exercisable on or within 60 days after the Record Date.

<sup>4</sup> Includes 106,666 shares which may be acquired pursuant to stock options exercisable on or within 60 days after the Record Date.

<sup>5</sup> Includes 30,000 shares which may be acquired pursuant to stock options exercisable on or within 60 days after the Record Date.

<sup>6</sup> Includes 15,000 shares which may be acquired pursuant to stock options exercisable on or within 60 days after the Record Date.

<sup>7</sup> Includes 671,428 shares which may be acquired pursuant to stock options exercisable on or within 60 days after the Record Date.

<sup>8</sup> Shares are pledged to secure margin accounts. Does not include shares beneficially owned by Mark E. Schwarz, Detroit Stoker or Newcastle Focus Fund II, L.P. (See *Certain Relationships and Transactions*.)

<sup>9</sup> Per Schedule 13G/A filed February 14, 2012, Bares Capital Management, Inc. shares voting and dispositive power. The address of Bares Capital Management, Inc. is 12600 Hill Country Boulevard, Suite R-230, Austin, Texas 78738.

<sup>10</sup> Per Schedule 13G/A filed February 14, 2012, includes 39,785 shares over which Dimensional Fund Advisors LP has no voting power. The address of Dimensional Fund Advisors LP is Palisades West, Building One, 6300 Bee Cave Road, Austin, Texas 78746.

<sup>11</sup> Per Schedule 13G filed February 13, 2012, includes 90,330 shares over which The Killen Group, Inc. has no voting power. The address of The Killen Group, Inc. is 1189 Lancaster Avenue, Berwyn, Pennsylvania 19312.

<sup>12</sup> Per Schedule 13G filed January 23, 2012, the shares beneficially owned by Overbrook Limited Partnership may also be deemed to be beneficially owned by its general partner, Caxton Corporation, and its sole shareholder, Bruce S. Kovner. Such persons have shared voting and dispositive power. The address of Overbrook Limited Partnership and Caxton Corporation is Princeton Plaza, Building 2, 731 Alexander Road, Princeton, New Jersey 08540. The address of Mr. Kovner is 500 Park Avenue, New York, New York 10022.

## **AUDIT COMMITTEE REPORT**

The Audit Committee is composed of three independent directors and operates under a written charter adopted by the Board in accordance with applicable rules of the SEC and Nasdaq. A copy of the Amended and Restated Audit Committee Charter is posted on the Company's website at [www.hallmarkgrp.com](http://www.hallmarkgrp.com).

The primary purpose of the Audit Committee is to assist the Board in fulfilling its responsibility to oversee management's conduct of the Company's financial reporting process. In discharging its oversight role, the Audit Committee is empowered to investigate any matter brought to its attention with full access to all books, records, facilities and personnel of the Company and is authorized to retain outside counsel, auditors or other experts for this purpose. Subject to any action that may be taken by the full Board, the Audit Committee also has the authority and responsibility to select, evaluate and, where appropriate, replace the Company's independent registered public accountants.

The Company's management is responsible for preparing the Company's financial statements and the independent registered public accountants are responsible for auditing those financial statements. The role of the Audit Committee is to monitor and oversee these processes.

In this context, the Audit Committee has reviewed and discussed the consolidated financial statements with both management and the independent registered public accountants. The Audit Committee also discussed with the independent registered public accountants the matters required to be discussed by Statement on Auditing Standards No. 61 (Communication with Audit Committees). The Audit Committee received from the independent registered public accountants the written disclosures required by applicable requirements of the Public Company Accounting Oversight Board regarding the independent registered public accountants' communications with the Audit Committee concerning independence, and the Audit Committee discussed with the independent registered public accountants their independence.

Based on the Audit Committee's review and discussions with management and the independent registered public accountants, the Audit Committee recommended to the Board that the audited financial statements be included in the Company's Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2011.

Respectfully submitted by the Audit Committee:

James H. Graves (chairman)

Scott T. Berlin

Jim W. Henderson

**INDEPENDENT REGISTERED PUBLIC ACCOUNTANTS**

The Audit Committee has selected Ernst & Young LLP (“E&Y”) as the independent registered public accounting firm to audit the consolidated financial statements of the Company for the 2012 fiscal year. E&Y also reported on the Company’s consolidated financial statements for the fiscal years ended December 31, 2010 and 2011. Representatives of E&Y are expected to be present at the Annual Meeting, will have the opportunity to make a statement if they so desire and are expected to be available to respond to appropriate questions from shareholders.

The following table presents fees for professional services rendered by E&Y for the audit of the Company’s consolidated financial statements for the fiscal years ended December 31, 2011 and 2010, as well as fees billed for other services rendered by E&Y during each period.

	Fiscal 2011	Fiscal 2010
Audit Fees <sup>1</sup>	\$ 890,119	\$ 746,593
Audit-Related Fees <sup>2</sup>	\$ 24,872	\$ 14,679
Tax Fees	\$ 14,750	—
All Other Fees	—	—

<sup>1</sup> Reflects fees for services attributable to the indicated fiscal year, a portion of which fees were paid in the subsequent fiscal year.

<sup>2</sup> Audit-related fees in fiscal 2011 pertained primarily to evaluating a change in the date for testing for goodwill impairment. Audit-related fees in fiscal 2010 pertained primarily to the transition of auditors and the response to an SEC comment letter.

<sup>3</sup> Tax fees in fiscal 2011 pertained to service in connection with the review of the Company’s tax return for fiscal 2010.

The Audit Committee has pre-approved the retention of E&Y to perform audit and non-audit services in an amount up to \$5,000, provided that (i) the chairman of the Audit Committee is notified of each such retention within 48 hours, and (ii) the annual aggregate of such pre-approved services does not exceed \$15,000. The current policy of the Audit Committee is to review and approve all other proposed audit and non-audit services prior to the engagement of independent registered public accountants to perform such services. Review and approval of such services generally occur at the Audit Committee’s regularly scheduled quarterly meetings. In situations where it is impractical to wait until the next regularly scheduled quarterly meeting, the Audit Committee has delegated to its chairman the authority to approve audit and non-audit services. Any audit or non-audit services approved pursuant to such delegation of

authority must be reported to the full Audit Committee at its next regularly scheduled meeting. During fiscal 2011 and 2010, all pre-approved audit and non-audit services performed by E&Y were in accordance with the policies and procedures established by the Audit Committee and all other audit and non-audit services performed by the Company's independent registered public accountants were approved in advance by the Audit Committee.

## SHAREHOLDER PROPOSALS FOR 2013 ANNUAL MEETING

Any shareholder desiring to submit a proposal for inclusion in the proxy material relating to the 2013 annual meeting of shareholders must do so in writing. The proposal must be received at the Company's principal executive offices by January 5, 2013. In addition, with respect to any matter proposed by a shareholder at the 2013 annual meeting but not included in the Company's proxy materials, the proxy holders designated by the Company may exercise discretionary voting authority if appropriate notice of the shareholder proposal is not received by the Company at its principal executive office by March 20, 2013.

By Order of the Board of Directors,

/s/ CECIL R. WISE

Cecil R. Wise, Secretary

May 4, 2012

Fort Worth, Texas



**THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS**

**PROXY**

**FOR THE ANNUAL MEETING OF SHAREHOLDERS OF**

**HALLMARK FINANCIAL SERVICES, INC.**

**TO BE HELD MAY 31, 2012**

The undersigned hereby appoints Mark E. Schwarz, Mark J. Morrison and Kevin T. Kasitz, and each of them individually, as the lawful agents and Proxies of the undersigned, with full power of substitution, and hereby authorizes each of them to represent and vote, as designated below, all shares of Common Stock of Hallmark Financial Services, Inc. held of record by the undersigned as of April 5, 2012, at the Annual Meeting of Shareholders to be held on May 31, 2012, or at any adjournment thereof. The undersigned hereby revokes all previous proxies relating to the shares covered hereby and confirms all that said Proxies may do by virtue hereof.

1. **ELECTION OF DIRECTORS:**

**FOR** all nominees listed below

£ **WITHHOLD AUTHORITY** to vote for all nominees listed below  
(except as marked to the contrary)

**Instructions:** To *withhold* authority to vote for any nominee, mark the space beside the nominee's name with an "X".

Mark E. Schwarz \_\_\_\_\_ Scott T. Berlin \_\_\_\_\_ James H. Graves \_\_\_\_\_ Jim W. Henderson \_\_\_\_\_

**2. ADVISORY RESOLUTION TO APPROVE EXECUTIVE COMPENSATION:**

£FOR£AGAINST£ABSTAIN

3. **OTHER BUSINESS:** In their discretion, the Proxies are authorized to vote on any other matter which may properly come before the Annual Meeting or any adjournment thereof.

When properly executed, this proxy will be voted in the manner directed herein by the undersigned shareholder. IF NO DIRECTION IS SPECIFIED, THIS PROXY WILL BE VOTED **FOR** THE ELECTION OF ALL DIRECTORS PROPOSED IN ITEM 1 AND **FOR** THE ADVISORY RESOLUTION TO APPROVE EXECUTIVE COMPENSATION.

*Please sign below exactly as your shares are held of record. When shares are held by joint tenants, both should sign. When signing as attorney, executor, administrator, trustee or guardian, please give full title as such. If a corporation, please sign in full corporate name by President or other authorized officer. If a partnership, please sign in partnership name by authorized person.*

Date: \_\_\_\_\_, 2012

Signature

Signature, if held jointly:

**PLEASE MARK, SIGN, DATE AND RETURN THIS PROXY PROMPTLY, USING THE ENCLOSED ENVELOPE. PLEASE CHECK THIS BOX IF YOU INTEND TO BE PRESENT AT THE ANNUAL MEETING OF SHAREHOLDERS. "**