

KINGSWAY FINANCIAL SERVICES INC

Form 10-Q

August 13, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

June 30, 2012

or

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

For the quarterly period ended June 30, 2012

Commission File Number: 001-15204

Kingsway Financial Services Inc.

(Exact name of registrant as specified in its charter)

Ontario, Canada

(State or other jurisdiction of
incorporation or organization)

Not Applicable (I.R.S. Employer
Identification No.)

45 St. Clair Avenue West, Suite 400 Toronto, Ontario M4V 1K9

(Address of principal executive offices and zip code)

1-416-848-1171

(Registrant's telephone number, including area code)

Indicate by checkmark 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 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 ☐
(Do not check if a smaller reporting company) Smaller Reporting Company ☒

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

The number of shares outstanding of the registrant's common stock as of August 13, 2012 was 13,148,971.

KINGSWAY FINANCIAL SERVICES INC.

Table Of Contents

PART I - FINANCIAL INFORMATION	<u>3</u>
ITEM 1. FINANCIAL STATEMENTS	<u>3</u>
Consolidated Balance Sheets as of June 30, 2012 (unaudited) and December 31, 2011	<u>3</u>
Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2012 and 2011 (unaudited)	<u>4</u>
Consolidated Statements of Comprehensive Loss for the Three and Six Months Ended June 30, 2012 and 2011 (unaudited)	<u>5</u>
Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2012 and 2011 (unaudited)	<u>6</u>
Notes to Consolidated Financial Statements (unaudited)	<u>7</u>
ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	<u>31</u>
ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	<u>41</u>
ITEM 4. CONTROLS AND PROCEDURES	<u>41</u>
PART II - OTHER INFORMATION	<u>42</u>
ITEM 1. LEGAL PROCEEDINGS	<u>42</u>
ITEM 1A. RISK FACTORS	<u>42</u>
ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	<u>42</u>
ITEM 3. DEFAULTS UPON SENIOR SECURITIES	<u>43</u>
ITEM 4. MINE SAFETY DISCLOSURES	<u>44</u>
ITEM 5. OTHER INFORMATION	<u>42</u>
ITEM 6. EXHIBITS	<u>43</u>
SIGNATURES	<u>44</u>

KINGSWAY FINANCIAL SERVICES INC.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets

(in thousands, except per share data)

	June 30, 2012 (unaudited)	December 31, 2011
ASSETS		
Investments:		
Fixed maturities, at fair value (amortized cost of \$101,091 and \$91,344, respectively)	\$ 102,963	\$93,651
Equity investments, at fair value (cost of \$2,689 and \$2,689, respectively)	3,225	2,960
Other investments, at cost which approximates fair value	—	488
Short-term investments, at cost which approximates fair value	335	20,334
Total investments	106,523	117,433
Investment in investees	47,904	48,689
Cash and cash equivalents	63,101	85,486
Accrued investment income	2,652	1,999
Premiums receivable, net of allowance for doubtful accounts of \$3,779 and \$3,653, respectively	27,608	28,732
Service fee receivable	18,752	12,947
Other receivables, net of allowance for doubtful accounts of \$806 and \$806, respectively	5,789	6,322
Reinsurance recoverable	5,685	697
Prepaid reinsurance premiums	3,188	2,024
Deferred policy acquisition costs, net	7,634	8,116
Income taxes recoverable	7,132	8,134
Property and equipment, net of accumulated depreciation of \$28,799 and \$27,736	12,479	13,040
Goodwill	510	510
Intangible assets	39,121	39,121
Other assets	1,831	831
TOTAL ASSETS	\$349,909	\$374,081
LIABILITIES AND EQUITY		
LIABILITIES		
Unpaid loss and loss adjustment expenses	\$99,650	\$120,258
Unearned premiums	41,906	39,423
Reinsurance payable	4,376	1,913
LROC preferred units	11,778	8,845
Senior unsecured debentures	27,947	28,337
Subordinated debt	20,603	16,432
Deferred income tax liability	2,653	2,653
Notes payable	2,418	2,418
Deferred revenue	13,545	11,128
Accrued expenses and other liabilities	28,437	26,269
TOTAL LIABILITIES	253,313	257,676

EQUITY

Common stock, no par value; unlimited number authorized; 13,148,971 and 13,086,471 issued and outstanding at June 30, 2012 and December 31, 2011, respectively	\$296,621	\$296,489	
Additional paid-in capital	15,504	15,403	
Accumulated deficit	(218,230)	(201,208))
Accumulated other comprehensive income	13,047	12,749	
Shareholders' equity attributable to common shareholders	106,942	123,433	
Noncontrolling interests in consolidated subsidiaries	(10,346)	(7,028))
TOTAL EQUITY	96,596	116,405	
TOTAL LIABILITIES AND EQUITY	\$349,909	\$374,081	

See accompanying notes to unaudited consolidated financial statements.

KINGSWAY FINANCIAL SERVICES INC.

Consolidated Statements of Operations
(in thousands, except per share data)
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Revenue:				
Net premiums earned	\$30,985	\$42,575	\$60,252	\$88,211
Service fee and commission income	8,138	7,806	17,667	16,778
Net investment income	802	1,152	1,632	2,229
Net realized (losses) gains	(23	)(3	)250	(2
Other-than-temporary impairment loss	(488	)—	(488)—
(Loss) gain on change in fair value of debt	(2,418	)11,237	(6,749	)8,632
Other income	2,744	1,311	3,827	3,222
Total revenues	39,740	64,078	76,391	119,070
Expenses:				
Loss and loss adjustment expenses	23,616	37,014	\$45,391	\$78,591
Commissions and premiums taxes	4,747	6,908	9,166	14,286
General and administrative expenses	17,154	22,810	35,955	44,381
Interest expense	1,916	1,833	3,765	3,736
Amortization of other intangible assets	—	18	—	36
Total expenses	47,433	68,583	94,277	141,030
Loss before gain on buy-back of debt, equity				
in net income (loss) of investees and income	(7,693	)(4,505	)(17,886	)(21,960
tax expense (benefit)				
Gain on buy-back of debt	—			