KINGSWAY FINANCIAL SERVICES INC
Form 10-Q
August 08, 2013
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)

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

June 30, 2013
or

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

For the quarterly period ended June 30, 2013

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 x No o

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 x No o

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 o	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller Reporting Company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x
The number of shares outstanding of the registrant's common stock as of August 8, 2013 was 13,148,971.

KINGSWAY FINANCIAL SERVICES INC.

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KINGSWAY FINANCIAL SERVICES INC.

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
Consolidated Balance Sheets
(in thousands, except per share data)

	June 30, 2013 (unaudited)	December 31, 2012
ASSETS		
Investments:		
Fixed maturities, at fair value (amortized cost of $71,254 and $77,858, respectively)	$72,256	$79,534
Equity investments, at fair value (cost of $27,775 and $2,305, respectively)	31,110	3,548
Limited liability investments	2,268	2,333
Other investments, at cost which approximates fair value	3,031	2,000
Short-term investments, at cost which approximates fair value	586	585
Total investments	109,251	88,000
Cash and cash equivalents	71,351	80,813
Investment in investee	—	41,733
Accrued investment income	635	2,263
Premiums receivable, net of allowance for doubtful accounts of $3,977 and $4,040, respectively	34,864	35,598
Service fee receivable	19,313	15,173
Other receivables, net of allowance for doubtful accounts of $1,002 and $1,002, respectively	4,852	4,750
Reinsurance recoverable	15,133	8,557
Prepaid reinsurance premiums	11,835	7,316
Deferred acquisition costs, net	11,797	14,102
Property and equipment, net of accumulated depreciation of $23,707 and $22,887, respectively	2,159	2,709
Goodwill	9,484	8,421
Intangible assets, net of amortization of $20,329 and $19,263, respectively	50,569	50,583
Other assets	4,542	4,045
Asset held for sale	7,291	8,737
TOTAL ASSETS	$353,076	$372,800
LIABILITIES AND EQUITY		
LIABILITIES		
Unpaid loss and loss adjustment expenses:		
Property and casualty	$96,703	$103,116
Vehicle service agreements	3,140	3,448
Total unpaid loss and loss adjustment expenses	99,843	106,564
Unearned premiums	47,308	45,047
Reinsurance payable	7,620	4,956
LROC preferred units	14,204	13,655
Senior unsecured debentures	26,356	23,730
Subordinated debt	26,674	23,774
Deferred income tax liability	3,602	3,054

Deferred service fees	49,198	48,987
Income taxes payable	2,821	2,879
Accrued expenses and other liabilities	34,533	34,740
TOTAL LIABILITIES	$312,159	$307,386
EQUITY		
Common stock, no par value; unlimited number authorized; 13,148,971 issued and outstanding at June 30, 2013 and December 31, 2012	$296,621	$296,621
Additional paid-in capital	15,824	15,757
Accumulated deficit	(289,784)	(262,069)
Accumulated other comprehensive income	16,862	14,762
Shareholders' equity attributable to common shareholders	39,523	65,071
Noncontrolling interests in consolidated subsidiaries	1,394	343
TOTAL EQUITY	40,917	65,414
TOTAL LIABILITIES AND EQUITY	$353,076	$372,800

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,	
	2013	2012	2013	2012
Revenue:				
Net premiums earned	$28,297	$30,985	$56,365	$60,252
Service fee and commission income	12,052	8,138	25,176	17,667
Net investment income	816	797	1,396	1,623
Net realized gains (losses)	32	(23)	(1,377)	250
Other-than-temporary impairment loss	(1,800)	(488)	(1,800)	(488)
Gain (loss) on change in fair value of debt	2,338	(2,418)	(6,613)	(6,749)
Other income	2,174	2,744	4,392	3,827
Total revenues	43,909	39,735	77,539	76,382
Expenses:				
Loss and loss adjustment expenses	24,615	23,616	46,446	45,391
Commissions and premium taxes	5,171	4,747	11,883	9,166
General and administrative expenses	20,289	17,154	40,048	35,955
Restructuring expense	147	—	927	—
Interest expense	1,927	1,916	3,760	3,765
Amortization of intangible assets	508	—	1,066	—
Impairment of asset held for sale	1,446	—	1,446	—
Total expenses	54,103	47,433	105,576	94,277
Loss before loss on buy-back of debt, equity in net income (loss) of investee and income tax (benefit) expense	(10,194)	(7,698)	(28,037)	(17,895)
Loss on buy-back of debt	—	—	(24)	—
Equity in net income (loss) of investee	—	97	255	(2,169)
Loss before income tax (benefit) expense	(10,194)	(7,601)	(27,806)	(20,064)
Income tax (benefit) expense	(525)	116	(801)	175
Net loss	(9,669)	(7,717)	(27,005)	(20,239)
Less: net income (loss) attributable to noncontrolling interests in consolidated subsidiaries	617	(1,700)	712	(3,214)
Net loss attributable to common shareholders	$(10,286)	$(6,017)	$(27,717)	$(17,025)
Loss per share – net loss:				
Basic:	$(0.74)	$(0.59)	$(2.05)	$(1.54)
Diluted:	(0.74)	(0.59)	(2.05)	(1.54)
Weighted average shares outstanding (in ‘000s):				
Basic:	13,149	13,149	13,149	13,117
Diluted:	13,149	13,149	13,149	13,117

See accompanying notes to unaudited consolidated financial statements.

KINGSWAY FINANCIAL SERVICES INC.

Consolidated Statements of Comprehensive Loss
(in thousands)
(unaudited)

	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
Net loss	$(9,669)	$(7,717)	$(27,005)	$(20,239)
Other comprehensive income (loss), net of taxes[1]:				
Unrealized gains (losses) on fixed maturities and equity investments:				
Unrealized gains arising during the period	1,639	417	1,136	197
Reclassification adjustment for losses (gains) included in net loss	34	(509)	282	(367)
Foreign currency translation adjustments	(2)	(1,497)	(1)	27
Equity in other comprehensive income of investee	747	28	642	339
Other comprehensive income (loss)	2,418	(1,561)	2,059	196
Comprehensive loss	(7,251)	(9,278)	(24,946)	(20,043)
Less: comprehensive income (loss) attributable to noncontrolling interests in consolidated subsidiaries	605	(1,722)	671	(3,318)
Comprehensive loss attributable to common shareholders	$(7,856)	$(7,556)	$(25,617)	$(16,725)

(1) Net of income tax (benefit) expense of $0 and $0 for the three and six months ended June 30, 2013 and June 30, 2012, respectively.

See accompanying notes to unaudited consolidated financial statements

KINGSWAY FINANCIAL SERVICES INC.

Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Six months ended June 30, 2013	2012
Cash provided by (used in):		
Operating activities:		
Net loss	$(27,005)	$(20,239)
Adjustments to reconcile net loss to net cash used in operating activities:		
Equity in net (income) loss of investee	(255)	2,169
Equity in net (income) loss of limited liability investments	(155)	9
Depreciation and amortization	1,885	1,063
Stock based compensation expense, net of forfeitures	67	101
Net realized losses (gains)	1,377	(250)
Loss on change in fair value of debt	6,613	6,749
Deferred income taxes	(136)	—
Other than temporary impairment loss	1,800	488
Amortization of fixed maturities premiums and discounts	1,906	1,574
Impairment of asset held for sale	1,446	—
Realized loss on buy-back of debt	24	—
Changes in operating assets and liabilities:		
Premiums and service fee receivable	(3,406)	(4,681)
Reinsurance recoverable	(6,576)	(4,988)
Deferred acquisition costs	2,305	482
Income taxes recoverable	—	1,002
Unpaid loss and loss adjustment expenses	(6,721)	(20,608)
Unearned premiums	2,261	2,483
Reinsurance payable	2,664	2,463
Deferred service fees	211	2,080
Other, net	(3,897)	(834)
Net cash used in operating activities	(25,592)	(30,937)
Investing activities:		
Proceeds from sales and maturities of fixed maturities	10,878	51,145
Proceeds from sales of equity investments	377	—
Proceeds from sales of investment in investee	13,638	—
Purchase of fixed maturities	(4,892)	(42,223)
Purchase of equity investments	(23)	—
Net acquisition of limited liability investments	(588)	—
Purchase of other investments	(1,031)	—
Net purchases of short-term investments	(325)	—
Acquisition of business, net of cash acquired	(1,052)	—
Net purchases of property and equipment and intangible assets	(269)	(502)
Net cash provided by investing activities	16,713	8,420
Financing activities:		
Common stock issued	—	132
Redemption of senior unsecured debentures	(583)	—
Net cash (used in) provided by financing activities	(583)	132
Net decrease in cash and cash equivalents	(9,462)	(22,385)

Cash and cash equivalents at beginning of period	80,813	85,486
Cash and cash equivalents at end of period	$71,351	$63,101

See accompanying notes to unaudited consolidated financial statements.

KINGSWAY FINANCIAL SERVICES INC.
Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

NOTE 1 BUSINESS
Kingsway Financial Services Inc. (the "Company" or "Kingsway") was incorporated under the Business Corporations Act (Ontario) on September 19, 1989. Kingsway is a holding company and is primarily engaged, through its subsidiaries, in the property and casualty insurance business.

NOTE 2 BASIS OF PRESENTATION
The accompanying unaudited consolidated interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements of the Company. In the opinion of management, all adjustments necessary for a fair presentation have been included and are of a normal recurring nature. Interim results are not necessarily indicative of the results that may be expected for the year.
The accompanying unaudited consolidated interim financial statements and footnotes should be read in conjunction with the audited consolidated financial statements and footnotes included within our Annual Report on Form 10-K ("2012 Annual Report") for the year ended December 31, 2012.
The unaudited consolidated interim financial statements include the accounts of the Company and its subsidiaries. All material intercompany transactions and balances have been eliminated in consolidation.
The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect application of policies and the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from these estimates. Estimates and their underlying assumptions are reviewed on an ongoing basis. Changes in estimates are recorded in the accounting period in which they are determined. The critical accounting estimates and assumptions in the accompanying unaudited consolidated interim financial statements include the provision for unpaid loss and loss adjustment expenses, valuation of fixed maturities and equity investments, valuation of deferred income taxes, valuation of intangible assets, goodwill recoverability, deferred acquisition costs, and fair value assumptions for debt obligations.
The fair values of the Company's investments in fixed maturities and equity investments, LROC preferred units, senior unsecured debentures and subordinated debt are estimated using a fair value hierarchy to categorize the inputs it uses in valuation techniques. Fair values for other investments approximate their unpaid principal balances. The carrying amounts reported in the consolidated balance sheets approximate fair values for cash, short-term investments and certain other assets and other liabilities because of their short-term nature.
The Company's financial results contained herein are reported in U.S. dollars unless otherwise indicated.
NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
There have been no material changes to our significant accounting policies as reported in our 2012 Annual Report.
NOTE 4 RECENTLY ISSUED ACCOUNTING STANDARDS
Adoption of New Accounting Standards:

In July 2012, the FASB issued ASU 2012-02, Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment ("ASU 2012-02"). ASU 2012-02 provides entities with an option to first assess qualitative factors to determine whether events or circumstances indicate that it is more likely than not that the indefinite-lived intangible asset is impaired. If an entity concludes that it is more than 50% likely that an indefinite-lived intangible asset is not impaired, no further analysis is required. However, if an entity concludes otherwise, it would be required to determine the fair value of the indefinite-lived intangible asset to measure the amount of actual impairment, if any, as currently required under US GAAP. Effective January 1, 2013, the Company adopted ASU 2012-02 and the adoption did not have an impact on the consolidated financial statements. There have been no triggering events that would suggest possible impairment or that it is more-likely-than-not that the fair values of indefinite-lived intangible assets are less than their carrying amounts. The Company will utilize the new guidance during its annual impairment testing in December 2013.

In February 2013, the FASB issued ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income ("ASU 2013-02"), which is intended to improve the reporting of reclassifications out of accumulated other comprehensive income. The ASU requires an entity to report, either on the face of the income statement or in the notes to the financial statements, the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in the income statement if the amount being reclassified is required to be reclassified in its entirety to net income. For other amounts that are not required to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other required disclosures that provide additional detail about those amounts. Effective January 1, 2013, the Company adopted ASU 2013-02. Except for the new disclosure requirements, the adoption of the standard did not have an impact on the consolidated financial statements. The required disclosures are included in Note 16, "Accumulated Other Comprehensive Income."

In July 2013, the FASB issued ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists ("ASU 2013-11"). ASU 2013-11 is effective for the first interim or annual period beginning on or after December 15, 2013 with early adoption permitted. ASU 2013-11 amends ASC Topic 740, Income Taxes, to provide guidance and reduce diversity in practice on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. Except for the changes, if any, in the Company's presentation, the initial application of the standard will not impact the Company.

NOTE 5 ACQUISITIONS

(a) IWS Acquisition Corporation:

Effective November 16, 2012, the Company's subsidiary, IWS Acquisition Corporation ("IWS"), acquired certain tangible and intangible assets and liabilities of Intercontinental Warranty Services, Inc. for total consideration consisting of approximately $4.9 million in cash, future contingent payments and common equity in a newly formed entity.

IWS is based in Florida and is a provider of after-market vehicle protection services distributed by credit unions throughout the United States and Puerto Rico to their members. The acquisition allows the Company to benefit from the institutional knowledge of the credit unions' vehicle loan programs and expand into the vehicle protection service business.

This acquisition was accounted for as a business combination using the purchase method of accounting. The purchase price was allocated to the assets purchased and liabilities assumed based upon their estimated fair values at the date of acquisition. During the fourth quarter of 2012, the Company began its fair value analysis on the assets acquired and liabilities assumed. In accordance with U.S. GAAP, fair value accounting effects may be adjusted up to one year from the acquisition date upon finalization of the valuation process. The Company recorded adjustments related to the acquisition during the first six months of 2013, which resulted in an increase to goodwill of $1.1 million from the amount recorded at December 31, 2012.

After allocation of additional purchase price, goodwill of $9.0 million was recognized in addition to $12.4 million of separately identifiable intangible assets. Of this amount, $8.7 million of separately identifiable intangible assets related to this acquisition resulted from the valuations of acquired database, customer-related relationships, trade name and non-compete agreement. An additional $3.7 million of separately identifiable intangible assets resulted from the valuation of vehicle service agreements in-force ("VSA in-force"). Refer to Note 10, "Intangible Assets," for further disclosure on intangible assets related to this acquisition. The fair value analysis performed included $3.9 million related to present value of future contingent payments. The maximum the Company can pay in future contingent payments is $11.1 million, on an undiscounted basis. The contingent payments are payable annually beginning in 2013 through 2018 and are subject to the achievement of certain targets and may be adjusted in future periods based on actual performance achieved. As of June 30, 2013, the recorded value of the contingent earn-out agreement is $4.3 million, which is included in accrued expenses and other liabilities on the consolidated balance sheets.

(b) Trinity Warranty Solutions LLC:
Effective May 22, 2013, the Company's subsidiary, Trinity Warranty Solutions LLC ("TWS"), acquired certain intangible assets of Trinity Warranty Corp. for total consideration consisting of approximately $1.1 million in cash and future contingent payments. The consolidated statements of operations include the earnings of TWS from the date of acquisition. As further discussed in Note 17, "Segmented Information," TWS is included in the Insurance Services segment. TWS is based in Illinois and is a provider of warranty products and maintenance support to consumers and businesses in the heating, ventilation, air conditioning and refrigeration industry.

This acquisition will be accounted for as a business combination using the purchase method of accounting. The purchase price is expected to be allocated during the third quarter of 2013 to the assets purchased based upon their estimated fair values at the date of acquisition. Refer to Note 10, "Intangible Assets," for further disclosure on intangible assets related to this acquisition.

KINGSWAY FINANCIAL SERVICES INC.
Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

NOTE 6 INVESTMENTS

The amortized cost, gross unrealized gains and losses, and estimated fair value of the Company's investments in fixed maturities and equity investments at June 30, 2013 and December 31, 2012 are summarized in the tables shown below:

(in thousands)	June 30, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities:				
U.S. government, government agencies and authorities	$26,015	$749	$13	$26,751
Canadian government	4,283	—	101	4,182
States municipalities and political subdivisions	7,142	134	1	7,275
Mortgage-backed	282	16	—	298
Asset-backed securities and collateralized mortgage obligations	156	2	—	158
Corporate	33,376	228	12	33,592
Total fixed maturities	71,254	1,129	127	72,256
Equity investments:				
Common stock	11,575	3,356	21	14,910
Preferred stock	16,200	—	—	16,200
Total equity investments	27,775	3,356	21	31,110
Total fixed maturities and equity investments	$99,029	$4,485	$148	$103,366

(in thousands)	December 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities:				
U.S. government, government agencies and authorities	$23,954	$962	$1	$24,915
Canadian government	3,822	—	40	3,782
States municipalities and political subdivisions	7,158	187	—	7,345
Mortgage-backed	4,850	193	—	5,043
Asset-backed securities and collateralized mortgage obligations	1,084	8	—	1,092
Corporate	36,990	391	24	37,357
Total fixed maturities	77,858	1,741	65	79,534
Equity investments:				
Common stock	2,305	1,256	13	3,548
Total fixed maturities and equity investments	$80,163	$2,997	$78	$83,082

KINGSWAY FINANCIAL SERVICES INC.
Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

Amortized cost, gross unrealized gains and estimated fair value for common stock in the preceding table at June 30, 2013 include $9.3 million, $2.0 million and $11.3 million, respectively, for the Company's investment in the common stock of the Company's former investee, Atlas Financial Holdings, Inc. ("Atlas"). As discussed further in Note 7, Investment in Investee, the Company's investment in the common stock of Atlas was accounted for under the equity method of accounting and reported as investment in investee in the consolidated balance sheets at December 31, 2012.

Amortized cost and estimated fair value for preferred stock in the preceding table at June 30, 2013 include $16.2 million and $16.2 million, respectively, for the Company's investment in the preferred stock of Atlas. The Company's investment in the preferred stock of Atlas was reported as investment in investee in the consolidated balance sheets at December 31, 2012.

The table below summarizes the Company's fixed maturities at June 30, 2013 by contractual maturity periods. Actual results may differ as issuers may have the right to call or prepay obligations, with or without penalties, prior to the contractual maturity of these obligations.

(in thousands)	June 30, 2013	
	Amortized Cost	Estimated Fair Value
Due in one year or less	$25,289	$25,380
Due after one year through five years	44,587	45,392
Due after five years through ten years	1,130	1,221
Due after ten years	248	263
Total	$71,254	$72,256

The following tables highlight the aggregate unrealized loss position, by security type, of fixed maturities and equity investments in unrealized loss positions as of June 30, 2013 and December 31, 2012. The tables segregate the holdings based on the period of time the investments have been continuously held in unrealized loss positions.

(in thousands)					June 30, 2013	
	Less than 12 Months		Greater than 12 Months		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Fixed maturities:						
U.S. government, government agencies and authorities	$4,848	$13	$—	$—	$4,848	$13
Canadian government	4,182	101	—	—	4,182	101
States municipalities and political subdivisions	1,002	1	—	—	1,002	1
Mortgage-backed	127	—	—	—	127	—
Corporate	1,031	10	1,008	2	2,039	12
Total fixed maturities	11,190	125	1,008	2	12,198	127
Equity investments:						
Common stock	154	21	—	—	154	21
Total	$11,344	$146	$1,008	$2	$12,352	$148

KINGSWAY FINANCIAL SERVICES INC.
Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

(in thousands)					December 31, 2012	
	Less than 12 Months		Greater than 12 Months		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Fixed maturities:						
U.S. government, government agencies and authorities	$4,612	$1	$—	$—	$4,612	$1
Canadian government	3,782	40	—	—	3,782	40
Mortgage-backed	—	—	267	—	267	—
Corporate	4,169	14	—	10	4,169	24
Total fixed maturities	12,563	55	267	10	12,830	65
Equity investments:						
Common stock	8	1	38	12	46	13
Total	$12,571	$56	$305	$22	$12,876	$78

Fixed maturities and equity investments contain approximately 17 and 19 individual investments that were in unrealized loss positions as of June 30, 2013 and December 31, 2012, respectively.

The establishment of an other-than-temporary impairment on an investment requires a number of judgments and estimates. The Company performs a quarterly analysis of the individual investments to determine if declines in market value are other-than-temporary. The analysis includes some or all of the following procedures as deemed appropriate by the Company:

- identifying all unrealized loss positions that have existed for at least six months;
- identifying other circumstances which management believes may impact the recoverability of the unrealized loss positions;
- obtaining a valuation analysis from third-party investment managers regarding the intrinsic value of these investments based on their knowledge and experience together with market-based valuation techniques;
- reviewing the trading range of certain investments over the preceding calendar period;
- assessing if declines in market value are other-than-temporary for debt instruments based on the investment grade credit ratings from third-party rating agencies;
- assessing if declines in market value are other-than-temporary for any debt instrument with a non-investment grade credit rating based on the continuity of its debt service record;
- determining the necessary provision for declines in market value that are considered other-than-temporary based on the analyses performed; and
- assessing the Company's ability and intent to hold these investments at least until the investment impairment is recovered.

The risks and uncertainties inherent in the assessment methodology used to determine declines in market value that are other-than-temporary include, but may not be limited to, the following:

- the opinions of professional investment managers could be incorrect;
- the past trading patterns of individual investments may not reflect future valuation trends;
- the credit ratings assigned by independent credit rating agencies may be incorrect due to unforeseen or unknown facts related to a company's financial situation; and
- the debt service pattern of non-investment grade instruments may not reflect future debt service capabilities and may not reflect a company's unknown underlying financial problems.

As a result of the analysis performed by the Company to determine declines in market value that are other-than-temporary, a write-down for other-than-temporary impairment related to other investments of zero and $0.5 million was recorded for the three months ended June 30, 2013 and June 30, 2012, respectively (zero and $0.5 million for the six months ended June 30, 2013 and June 30, 2012, respectively).

On July 8, 2013, the Company announced that it had entered into a non-binding letter of intent with Atlas to sell its holdings of Atlas preferred stock for 90.0% of liquidation value, or $16.2 million. On August 1, 2013, the Company announced that the transaction had closed. As a result, the Company recorded a write-down for other-than-temporary impairment related to its investment in Atlas preferred stock of $1.8 million for the three months ended June 30, 2013.

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There were no write-downs related to fixed maturities for other-than-temporary impairments for the three and six months ended June 30, 2013 and June 30, 2012. There were no other-than-temporary losses recognized in other comprehensive income (loss) for the three and six months ended June 30, 2013 and June 30, 2012.

The Company has reviewed currently available information regarding investments with estimated fair values that are less than their carrying amounts and believes that these unrealized losses are not other-than-temporary and are primarily due to temporary market and sector-related factors rather than to issuer-specific factors. The Company does not intend to sell those investments, and it is not likely that it will be required to sell those investments before recovery of its amortized cost.

The Company does not have any exposure to subprime mortgage-backed investments.

Limited liability investments include investments in limited liability companies and a limited partnership that primarily invest in income-producing real estate. The Company's interests in these investments are not deemed minor and, therefore, are accounted for under the equity method of accounting. As of June 30, 2013 and December 31, 2012, the carrying value of limited liability investments totaled $2.3 million and $2.3 million, respectively. At June 30, 2013, the Company has unfunded commitments totaling $4.0 million to fund limited liability investments. Income from limited liability investments is recognized based on the Company's share of the earnings of the limited liability entities and is included in net investment income.

Other investments include collateral and mortgage loans and are reported at their unpaid principal balance. As of June 30, 2013 and December 31, 2012, the carrying value of other investments totaled $3.0 million and $2.0 million, respectively.

Gross realized gains and losses on fixed maturities, equity investments and limited liability investments for the three and six months ended June 30, 2013 and June 30, 2012 were as follows:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Gross realized gains	$64	$51	$373	$324
Gross realized losses	(32)	(74)	(32)	(74)
Total	$32	$(23)	$341	$250

Gross realized losses for the six months ended June 30, 2013 reported in the preceding table excludes the realized loss on sale of Atlas common stock recorded during the first quarter of 2013. Refer to Note 7, Investment in Investee, for further discussion.

Net investment income for the three and six months ended June 30, 2013 and June 30, 2012, respectively, is comprised as follows:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Investment income				
Interest from fixed maturities	$368	$600	$650	$1,118
Dividends	237	262	490	504
Income (loss) from limited liability investments	105	(5)	155	(9)
Other	167	63	259	229
Gross investment income	877	920	1,554	1,842
Investment expenses	(61)	(123)	(158)	(219)
Net investment income	$816	$797	$1,396	$1,623

At June 30, 2013, fixed maturities and short-term investments with an estimated fair value of $14.4 million were on deposit with state and provincial regulatory authorities. Also, from time to time, the Company pledges investments to third-parties to collateralize liabilities incurred under its policies of insurance. At June 30, 2013, the amount of such pledged securities was $24.5 million.

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NOTE 7 INVESTMENT IN INVESTEE

Investment in investee includes the Company's investment in the preferred and restricted voting common stock of Atlas. On February 12, 2013, the Company executed an underwriting agreement to sell 2,625,000 shares of Atlas common stock. The shares were being offered as part of Atlas' United States initial public offering at a price per share of $5.85. During the first quarter of 2013, the Company received net proceeds of $13.6 million and recognized a loss of $1.7 million, which is included in net realized losses on the consolidated statements of operations, resulting from commissions and other expenses incurred as part of the sale. As a result of this sale, the Company's approximate voting percentage in Atlas was reduced to 16.5%. As a result of this change in ownership and other qualitative factors, the Company determined that its investment in the common stock of Atlas no longer qualified for the equity method of accounting. Accordingly, the Company's investments in Atlas common stock and preferred stock are included in equity investments and reported at their fair values of $11.3 million and $16.2 million, respectively, in the consolidated balance sheets at June 30, 2013. The Company's share of its investee's equity adjustments for other comprehensive income of $0.7 million was offset against the carrying value of the Company's investment in Atlas common stock during the second quarter of 2013. Prior to discontinuing the use of the equity method of accounting for Atlas, the Company used a reporting lag of three months to report its proportionate share of Atlas' results.

The carrying value, estimated fair value and approximate voting and equity percentages for the Company's investment in the common stock of Atlas, which was accounted for under the equity method of accounting and reported as investment in investee in the Company's consolidated balance sheets at December 31, 2012, were as follows:

(in thousands, except for percentages)

	December 31, 2012			
	Voting percentage	Equity percentage	Estimated Fair Value	Carrying value
Atlas	30.0 %	63.3 %	$38,758	$41,733

The fair value of the Company's investment in Atlas at December 31, 2012 in the table above is calculated based on the published closing price of Atlas at September 30, 2012 to be consistent with the three-month lag in reporting its carrying value under the equity method.

Equity in net income (loss) of investee was income of zero and $0.1 million for the three months ended June 30, 2013 and June 30, 2012, respectively (income of $0.3 million and loss of $2.2 million, respectively, year to date). The Company also recognized an increase to shareholders' equity attributable to common shareholders of $0.7 million and $0.6 million for the three and six months ended June 30, 2013, respectively, for the Company's pro rata share of its investee's accumulated other comprehensive income.

NOTE 8 DEFERRED ACQUISITION COSTS

Policy acquisition costs consist primarily of commissions, premium taxes, and underwriting and agency expenses incurred related to successful efforts to acquire new or renewal insurance contracts, net of ceding commission income, and vehicle service agreements. Acquisition costs deferred on both property and casualty insurance products and vehicle service agreements are amortized over the period in which the related revenues are earned.

The components of deferred acquisition costs and the related amortization expense for the three and six months ended June 30, 2013 and 2012, respectively, is comprised as follows:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Beginning balance, net	$12,685	$8,403	$14,102	$8,116
Additions	6,595	2,649	15,767	8,858
Amortization	(7,483)	(3,418)	(18,072)	(9,340)
Balance at June 30, net	$11,797	$7,634	$11,797	$7,634

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NOTE 9 GOODWILL
Goodwill was $9.5 million and $8.4 million at June 30, 2013 and December 31, 2012, respectively. As further discussed in Note 5, "Acquisitions," during the first six months of 2013, the Company continued its evaluation of certain tangible and intangible assets and liabilities of Intercontinental Warranty Services, Inc. that were acquired on November 16, 2012, which resulted in an increase to goodwill of $1.1 million from the amount recorded at December 31, 2012.
NOTE 10 INTANGIBLE ASSETS
Intangible assets are comprised as follows:
(in thousands)

	June 30, 2013	December 31, 2012
Intangible assets subject to amortization		
Database	$4,611	$4,907
VSA in-force	2,116	2,770
Customer-related relationships	4,004	3,056
Non-compete agreement	54	66
Intangible assets not subject to amortization		
Insurance licenses	7,803	7,803
Renewal rights	31,318	31,318
Trade name	663	663
Intangible assets	$50,569	$50,583

As further discussed in Note 5, "Acquisitions," during the second quarter of 2013, the Company acquired certain intangible assets of Trinity Warranty Corp. for total consideration consisting of approximately $1.1 million in cash and future contingent payments. The purchase price is expected to be allocated to the intangible assets purchased based upon their estimated fair values at the date of acquisition during the third quarter of 2013. Accordingly, the customer-related relationships intangible asset in the preceding table includes $1.1 million related to the estimated TWS intangible asset acquired.
The Company's intangible assets with indefinite useful lives are not amortized. The Company's intangible assets with definite useful lives are amortized over their estimated useful lives. Accumulated amortization for these intangibles as of June 30, 2013 and December 31, 2012 was $20.4 million and $19.3 million, respectively. Amortization of intangible assets was $0.5 million and zero for the three months ended June 30, 2013 and June 30, 2012, respectively ($1.1 million and zero for the six months ended June 30, 2013 and June 30, 2012, respectively).
NOTE 11 ASSET HELD FOR SALE
As of June 30, 2013, property consisting of building and land located in Miami, Florida with a carrying value of $7.3 million was classified as held for sale. During the three months ended June 30, 2013, the Company recorded a write-down of $1.4 million related to the asset held for sale. At June 30, 2013, the carrying value of the property is equal to its fair value net of estimated selling costs.

NOTE 12 UNPAID LOSS AND LOSS ADJUSTMENT EXPENSES
The establishment of the provision for unpaid loss and loss adjustment expenses is based on known facts and interpretation of circumstances and is therefore a complex and dynamic process influenced by a large variety of factors. These factors include the Company's experience with similar cases and historical trends involving loss payment patterns, pending levels of unpaid loss and loss adjustment expenses, product mix or concentration, loss severity and loss frequency patterns.
Other factors include the continually evolving and changing regulatory and legal environment; actuarial studies; professional experience and expertise of the Company's claims departments' personnel and independent adjusters retained to handle individual claims; the quality of the data used for projection purposes; existing claims management practices including claims-handling and settlement practices; the effect of inflationary trends on future loss settlement costs; court decisions; economic conditions; and public attitudes.

Consequently, the process of determining the provision necessarily involves risks that the actual results will deviate, perhaps materially, from the best estimates made.

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The Company's evaluation of the adequacy of unpaid loss and loss adjustment expenses includes a re-estimation of the liability for unpaid loss and loss adjustment expenses relating to each preceding financial year compared to the liability that was previously established.

(a) Property and Casualty

The results of this comparison and the changes in the provision for property and casualty unpaid loss and loss adjustment expenses, net of amounts recoverable from reinsurers, as of June 30, 2013 and June 30, 2012 were as follows:

(in thousands)	June 30, 2013		June 30, 2012	
Balance at beginning of period, gross	$103,116		$120,258	
Less reinsurance recoverable related to property and casualty unpaid loss and loss adjustment expenses	5,478		298	
Balance at beginning of period, net	97,638		119,960	
Incurred related to:				
Current year	43,992		45,064	
Prior years	(834	)	327	
Paid related to:				
Current year	(20,116	)	(19,870	)
Prior years	(31,897	)	(47,582	)
Balance at end of period, net	88,783		97,899	
Plus reinsurance recoverable related to property and casualty unpaid loss and loss adjustment expenses	7,920		1,751	
Balance at end of period, gross	$96,703		$99,650	

(b) Vehicle Service Agreements

The results of the comparison and the changes in the provision for vehicle service agreement unpaid loss and loss adjustment expenses as of June 30, 2013 are presented below. The changes in and the provision for vehicle service agreement unpaid loss and loss adjustment expenses were zero as of June 30, 2012.

(in thousands)	June 30, 2013	
Balance at beginning of period	$3,448	
Incurred related to:		
Current year	3,288	
Prior years	—	
Paid related to:		
Current year	(3,515	)
Prior years	(81	)
Balance at end of period	$3,140	

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NOTE 13 DEBT
Debt consists of the following instruments:

(in thousands)	June 30, 2013		December 31, 2012	
	Principal	Fair Value	Principal	Fair Value
7.5% Senior notes due 2014	$26,356	$26,356	$26,966	$23,730
LROC preferred units due 2015	15,020	14,204	15,879	13,655
Subordinated debt	90,500	26,674	90,500	23,774
Total	$131,876	$67,234	$133,345	$61,159

Subordinated indebtedness mentioned above consists of the following trust preferred debt instruments:

Issuer	Principal	Issue date	Interest	Redemption date
Kingsway CT Statutory Trust I	15,000	12/4/2002	annual interest rate equal to LIBOR, plus 4.00% payable quarterly	12/4/2032
Kingsway CT Statutory Trust II	17,500	5/15/2003	annual interest rate equal to LIBOR, plus 4.10% payable quarterly	5/15/2033
Kingsway CT Statutory Trust III	20,000	10/29/2003	annual interest rate equal to LIBOR, plus 3.95% payable quarterly	10/29/2033
Kingsway DE Statutory Trust III	15,000	5/23/2003	annual interest rate equal to LIBOR, plus 4.20% payable quarterly	5/23/2033
Kingsway DE Statutory Trust IV	10,000	9/30/2003	annual interest rate equal to LIBOR, plus 3.85% payable quarterly	9/30/2033
Kingsway DE Statutory Trust VI	13,000	1/8/2004	annual interest rate equal to LIBOR, plus 4.00% payable quarterly	1/8/2034

During the first quarter of 2011, the Company gave notice to its Trust Preferred trustees of its intention to exercise its voluntary right to defer interest payments for up to 20 quarters, pursuant to the contractual terms of its outstanding Trust Preferred indentures, which permit interest deferral. This action does not constitute a default under the Company's Trust Preferred indentures or any of its other debt indentures. At June 30, 2013, deferred interest payable of $10.5 million is included in accrued expenses and other liabilities in the consolidated balance sheets. The cash interest due in 2016 is subject to changes in the London interbank offered interest rate for three-month U.S. dollar deposits ("LIBOR") over the deferral period.

No debt repurchases were made during the second quarter of 2013. During the first quarter of 2013, the Company purchased for $0.6 million, including accrued interest, $0.6 million of par value of its senior unsecured debentures with a carrying value of $0.6 million, including accrued interest, recording a loss of $0.0 million. The Company subsequently canceled the acquired debentures. During the three and six months ended June 30, 2012, respectively, the Company did not buy-back any of its outstanding debt.

NOTE 14 INCOME TAXES

Income tax benefit for the three and six months ended June 30, 2013 varies from the amount that would result by applying the applicable United States income tax rate of 34% to loss before income tax benefit primarily due to a valuation allowance being applied to the Company's operating losses, a tax expense being recorded attributable to the Company's indefinite life intangible assets and a tax benefit being recorded for a Canadian income tax refund. Income tax expense for the three and six months ended June 30, 2012 varies from the amount that would result by applying the applicable United States income tax rate of 34% to loss before income tax expense primarily due to a valuation allowance being applied to the Company's operating losses.

The Company maintains a valuation allowance for its gross deferred tax assets at June 30, 2013 and December 31, 2012. The Company's operations have generated substantial operating losses during the last several years. These losses can be available to reduce income taxes that might otherwise be incurred on future taxable income. The Company's operations, however, remain challenged and, as a result, it is uncertain whether the Company will generate the taxable income necessary to utilize these losses or other reversing temporary differences. This uncertainty has caused management to place a full valuation allowance on its June 30, 2013 and December 31, 2012 net deferred tax asset. The Company carries a deferred tax liability of $3.6 million and $3.1 million at June 30, 2013 and December 31, 2012, respectively, all of which relates to indefinite life intangible assets.

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As of June 30, 2013 and December 31, 2012, the Company carried a liability for unrecognized tax benefits of $3.0 million and $3.0 million, respectively. The Company generally recognizes interest and penalties related to unrecognized tax benefits in income tax (benefit) expense.

NOTE 15 NET LOSS PER SHARE

Net loss per share is based on the weighted-average number of shares outstanding. Diluted weighted-average shares is calculated by adjusting basic weighted-average shares outstanding by all potentially dilutive stock options. Since the Company is reporting a net loss for the three and six months ended June 30, 2013 and June 30, 2012, all stock options outstanding were excluded from the calculation of both basic and diluted loss per share since their inclusion would have been anti-dilutive.

On July 3, 2012, the Company announced that the Board of Directors of the Company authorized the implementation of a share consolidation at a ratio of one post-consolidation share for every four pre-consolidation shares. The share consolidation, which was approved by the stockholders at the Company's Annual and Special Meeting held on May 31, 2012, was effective as of July 3, 2012 (the "Effective Date"). As a result of the consolidation, every four of the Company's common shares that were issued and outstanding on the Effective Date were automatically combined into one issued and outstanding common share, without any change in the par value of such shares. Any fractional shares resulting from the consolidation were rounded up to the nearest whole. The consolidation had the effect of reducing the number of common shares of the Company issued and outstanding from 52,595,828 shares pre-consolidation to 13,148,971 shares post-consolidation. The issued and outstanding shares reported in the consolidated balance sheets and the number of weighted-average shares outstanding included in the loss per share computations, as reported in the consolidated statements of operations, have been restated for all periods presented to reflect the impact of the share consolidation.

NOTE 16 ACCUMULATED OTHER COMPREHENSIVE INCOME

The table below details the components of accumulated other comprehensive income, net of tax, for the three and six months ended June 30, 2013 and June 30, 2012 as relates to shareholders' equity attributable to common shareholders on the consolidated balance sheets. On the other hand, the unaudited consolidated statements of comprehensive loss present the components of other comprehensive income (loss), net of tax, only for the three and six months ended June 30, 2013 and June 30, 2012 and inclusive of the components attributable to noncontrolling interests in consolidated subsidiaries.

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Beginning balance	$14,433	$14,588	$14,762	$12,749
Unrealized gains on fixed maturities and equity investments arising during the period	1,650	425	1,152	304
Reclassification adjustment for losses (gains) included in net loss	34	(509)	282	(367)
Foreign currency translation adjustments	(2)	(1,485)	24	22
Equity in other comprehensive income of investee	747	28	642	339
Balance at June 30	$16,862	$13,047	$16,862	$13,047

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Components of accumulated other comprehensive income were reclassified to the following lines of the consolidated statements of operations for the three and six months ended June 30, 2013 and June 30, 2012:

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Reclassification of accumulated other comprehensive income from unrealized gains on fixed maturities and equity investments to:				
Net realized (losses) gains	$(34)	$509	$(282)	$367
Other-than-temporary impairment loss	—	—	—	—
(Loss) gains before income tax (benefit) expense	(34)	509	(282)	367
Income tax (benefit) expense	—	—	—	—
Net (loss) gain	$(34)	$509	$(282)	$367

NOTE 17 SEGMENTED INFORMATION

The Company is primarily engaged, through its subsidiaries, in the property and casualty insurance business. The Company conducts its business through the following two reportable segments: Insurance Underwriting and Insurance Services.

On September 17, 2012, the Company announced that it was restructuring its Insurance Underwriting and Insurance Services segments under two separate management teams. As a result of the Company's intent to streamline its non-standard property and casualty insurance business operations under one management team, KAI Advantage Auto, Inc. ("Advantage Auto"), formerly included in Insurance Services, is now part of Insurance Underwriting. All segmented information has been restated for all periods presented to include Advantage Auto in Insurance Underwriting.

Insurance Underwriting Segment

Insurance Underwriting includes the following subsidiaries of the Company: Mendota Insurance Company, Mendakota Insurance Company, Universal Casualty Company, Maison Insurance Company ("Maison"), Kingsway Amigo Insurance Company ("Amigo"), Advantage Auto, Kingsway Reinsurance Corporation and Kingsway Reinsurance (Bermuda) Ltd. (collectively, "Insurance Underwriting"). In November 2012, the Company formed Maison, a Louisiana-domiciled property and casualty insurance company, which provides homeowners policies for wind and hail-related property losses of residential dwellings and certain contents. Insurance Underwriting principally offers personal automobile insurance to drivers who do not meet the criteria for coverage by standard automobile insurers and actively conducts business in 17 states.

During the fourth quarter of 2012, the Company began taking steps to place all of Amigo into voluntary run-off. On November 19, 2012, the Florida Office of Insurance Regulation (“OIR”) approved Amigo's plan to withdraw from the business of offering commercial lines insurance in Florida. On January 30, 2013, the OIR approved Amigo's plan to withdraw from the business of offering personal lines insurance in Florida. In April 2013, Kingsway filed a comprehensive run-off plan with the OIR, which outlines plans for Amigo's run-off. The comprehensive run-off plan is subject to OIR approval.

Insurance Services Segment

Insurance Services includes the following subsidiaries of the Company: Assigned Risk Solutions Ltd. ("ARS"), IWS and TWS (collectively, "Insurance Services"). During the first quarter of 2013, Northeast Alliance Insurance Agency, LLC, formerly included in Insurance Services, was merged into ARS.

ARS is a licensed property and casualty agent, full service managing general agent and third-party administrator focused primarily on the assigned risk market. ARS is licensed to administer business in 22 states but generates its revenues primarily by operating in the states of New York and New Jersey.

IWS is a licensed motor vehicle service agreement company and is a provider of after-market vehicle protection services distributed by credit unions in 26 states and Puerto Rico to their members.

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TWS is a provider of warranty products and maintenance support to consumers and businesses in the heating, ventilation, air conditioning ("HVAC") and refrigeration industry. TWS distributes its warranty products through original equipment manufacturers, HVAC distributors and commercial and residential contractors. It distributes its maintenance support direct through corporate owners of retail spaces throughout the United States.

Results for the Company's reportable segments are based on the Company's internal financial reporting systems and are consistent with those followed in the preparation of the unaudited consolidated interim financial statements. The following tables provide financial data used by management. Segment assets are not allocated for management use and, therefore, are not included in the segment disclosures below.

Segment revenues for the three and six months ended June 30, 2013 and 2012 were:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Revenues:				
Insurance Underwriting:				
Net premiums earned	$28,297	$30,985	$56,365	$60,252
Other income	2,199	1,866	4,656	3,753
Total Insurance Underwriting	30,496	32,851	61,021	64,005
Insurance Services:				
Service fee and commission income	12,052	8,138	25,176	17,667
Total Insurance Services	12,052	8,138	25,176	17,667
Total segment revenues	42,548	40,989	86,197	81,672
Net investment income	816	797	1,396	1,623
Net realized gains (losses)	32	(23)	(1,377)	250
Other-than-temporary impairment loss	(1,800)	(488)	(1,800)	(488)
Gain (loss) on change in fair value of debt	2,338	(2,418)	(6,613)	(6,749)
Other income not allocated to segments	(25)	878	(264)	74
Total revenues	$43,909	$39,735	$77,539	$76,382

The operating (loss) income of each segment in the following table is before income taxes and includes revenues and direct segment costs. For the three months ended June 30, 2013 and 2012, Insurance Services operating income includes amortization expense of $0.3 million and zero, respectively, related to its VSA in-force intangible asset. For the six months ended June 30, 2013 and 2012, Insurance Services operating income includes amortization expense of $0.7 million and zero, respectively, related to its VSA in-force intangible asset.

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Segment (loss) income for the three and six months ended June 30, 2013 and 2012 were:

(in thousands)	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
Segment operating (loss) income				
Insurance Underwriting	$(5,355)	$(3,838)	$(9,725)	$(6,963)
Insurance Services	(60)	991	1,289	2,724
Total segment operating loss	(5,415)	(2,847)	(8,436)	(4,239)
Net investment income	816	797	1,396	1,623
Net realized gains (losses)	32	(23)	(1,377)	250
Other-than-temporary impairment loss	(1,800)	(488)	(1,800)	(488)
Gain (loss) on change in fair value of debt	2,338	(2,418)	(6,613)	(6,749)
Other income and expenses not allocated to segments, net	(2,611)	(803)	(5,589)	(4,527)
Interest expense	(1,927)	(1,916)	(3,760)	(3,765)
Amortization of intangible assets not allocated to segments	(181)	—	(412)	—
Impairment of asset held for sale	(1,446)	—	(1,446)	—
Loss on buy-back of debt	—	—	(24)	—
Equity in net income (loss) of investee	—	97	255	(2,169)
Loss before income tax (benefit) expense	$(10,194)	$(7,601)	$(27,806)	$(20,064)
Income tax (benefit) expense	(525)	116	(801)	175
Net loss	$(9,669)	$(7,717)	$(27,005)	$(20,239)

Net premiums earned by line of business for the three and six months ended June 30, 2013 and 2012 were:

(in thousands)	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
Insurance Underwriting:				
Private passenger auto liability	$19,176	$20,415	$37,837	$39,820
Auto physical damage	8,330	7,515	16,173	14,819
Total non-standard automobile	27,506	27,930	$54,010	$54,639
Commercial auto liability	97	3,057	746	5,613
Homeowners	694	—	1,609	—
Other	—	(2)	—	—
Total net premiums earned	$28,297	$30,985	$56,365	$60,252

NOTE 18 RESTRUCTURING

On September 17, 2012, the Company announced that it was restructuring its Insurance Underwriting and Insurance Services segments under two separate management teams. As part of the restructuring, the Company intends to streamline its non-standard property and casualty insurance business operations. Specific to Insurance Underwriting, during the fourth quarter of 2012, the Company began taking steps to place all of Amigo into voluntary run-off. On November 19, 2012, the OIR approved Amigo's plan to withdraw from the business of offering commercial lines insurance in Florida. On January 30, 2013, the OIR approved Amigo's plan to withdraw from the business of offering personal lines insurance in Florida. In April 2013, Kingsway filed a comprehensive run-off plan with the OIR, which outlines plans for Amigo's run-off. The comprehensive run-off plan is subject to OIR approval.

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As part of the restructuring, the Company will reduce staffing levels to be consistent with placing Amigo into run-off. The Company continues to estimate that Insurance Underwriting will incur approximately $2.0 million in cash severance expenses due to reductions-in-force as part of the restructuring, and the Company now expects that these expenses will be incurred during the period beginning with the announcement through the end of 2013. From the time the restructuring was announced on September 17, 2012 through June 30, 2013, the Company has incurred severance expense of $1.6 million.
Changes in the restructuring liability, which is included in accrued expenses and other liabilities in the consolidated balance sheets, and the related restructuring expense for the three and six months ended June 30, 2013 is as follows:

(in thousands)	Three months ended June 30, 2013		
	Severance	Lease abandonment	Total
Restructuring liability, beginning of period	$486	$1,139	$1,625
Restructuring expense	127	20	147
Cash payments	(569)	(88)	(657)
Restructuring liability, end of period	$44	$1,071	$1,115

(in thousands)	Six months ended June 30, 2013		
	Severance	Lease abandonment	Total
Restructuring liability, beginning of period	$214	$1,207	$1,421
Restructuring expense	886	41	927
Cash payments	(1,056)	(177)	(1,233)
Restructuring liability, end of period	$44	$1,071	$1,115

NOTE 19 FAIR VALUE OF FINANCIAL INSTRUMENTS
Fair value amounts represent estimates of the consideration that would currently be agreed upon between knowledgeable, willing parties who are under no compulsion to act. Fair value is best evidenced by quoted bid or ask price, as appropriate, in an active market. Where bid or ask prices are not available, such as in an illiquid or inactive market, the closing price of the most recent transaction of that instrument subject to appropriate adjustments as required is used. Where quoted market prices are not available, the quoted prices of similar financial instruments or valuation models with observable market based inputs are used to estimate the fair value. These valuation models may use multiple observable market inputs, including observable interest rates, foreign exchange rates, index levels, credit spreads, equity prices, counterparty credit quality, corresponding market volatility levels and option volatilities. Minimal management judgment is required for fair values calculated using quoted market prices or observable market inputs for models. Greater subjectivity is required when making valuation adjustments for financial instruments in inactive markets or when using models where observable parameters do not exist. Also, the calculation of estimated fair value is based on market conditions at a specific point in time and may not be reflective of future fair values. For the Company's financial instruments carried at cost or amortized cost, the book value is not adjusted to reflect increases or decreases in fair value due to market fluctuations, including those due to interest rate changes, as it is the Company's intention to hold them until there is a recovery of fair value, which may be to maturity.
The Company classifies its investments in fixed maturities and equity investments as available-for-sale and reports these investments at fair value. The Company's LROC preferred units, senior unsecured debentures and subordinated debt are measured and reported at fair value.
Fair values of common stock equity investments are considered to approximate quoted market values based on the latest bid prices in active markets. Fair values of fixed maturities and preferred stock equity investments for which no active market exists are derived from quoted market prices of similar instruments or other third-party evidence.
The fair value of the LROC preferred units is based on quoted market prices, and the fair value of the subordinated debt is estimated using an internal model based on significant market observable inputs. The fair values of senior

unsecured debentures, for which no active market exists, are derived from quoted market prices of similar instruments or other third-party evidence.

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The Company employs a fair value hierarchy to categorize the inputs it uses in valuation techniques to measure the fair value. The extent of use of quoted market prices (Level 1), valuation models using observable market information (Level 2) and internal models without observable market information (Level 3) in the valuation of the Company's financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2013 and December 31, 2012 was as follows:

(in thousands)		June 30, 2013		
		Fair Value Measurements at the End of the Reporting Period Using		
	Total	Quoted Prices in Active Markets for Identical Assets(Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring fair value measurements				
Assets:				
Fixed maturities:				
U.S. government, government agencies and authorities	$26,751	$—	$26,751	$—
Canadian government	4,182	—	4,182	—
States municipalities and political subdivisions	7,275	—	7,275	—
Mortgage-backed	298	—	298	—
Asset-backed securities and collateralized mortgage obligations	158	—	158	—
Corporate	33,592	—	33,592	—
Total fixed maturities	72,256	—	72,256	—
Equity investments:				
Common stock	14,910	14,910	—	—
Preferred stock	16,200	—	16,200	—
Total equity investments	31,110	14,910	16,200	—
Other investments	3,031	—	3,031	—
Short-term investments	586	—	586	—
Total assets	$106,983	$14,910	$92,073	$—
Liabilities:				
LROC preferred units	14,204	14,204	—	—
Senior unsecured debentures	26,356	—	26,356	—
Subordinated debt	26,674	—	26,674	—
Total liabilities	$67,234	$14,204	$53,030	$—

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(in thousands)	December 31, 2012			
		Fair Value Measurements at the End of the Reporting Period Using		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring fair value measurements				
Assets:				
Fixed maturities:				
U.S. government, government agencies and authorities	$24,915	$—	$24,915	$—
Canadian government	3,782	—	3,782	—
States municipalities and political subdivisions	7,345	—	7,345	—
Mortgage-backed	5,043	—	5,043	—
Asset-backed securities and collateralized mortgage obligations	1,092	—	1,092	—
Corporate	37,357	—	37,357	—
Total fixed maturities	79,534	—	79,534	—
Equity investments:				
Common stock	3,548	3,548	—	—
Other investments	2,000	—	2,000	—
Short-term investments	585	—	585	—
Total assets	$85,667	$3,548	$82,119	$—
Liabilities:				
LROC preferred units	13,655	13,655	—	—
Senior unsecured debentures	23,730	—	23,730	—
Subordinated debt	23,774	—	23,774	—
Total liabilities	$61,159	$13,655	$47,504	$—

NOTE 20 RELATED PARTY TRANSACTIONS

Related party transactions, including services provided to or received by the Company's subsidiaries, are carried out in the normal course of operations and are measured in part by the amount of consideration paid or received as established and agreed by the parties. Management believes that consideration paid for such services in each case approximates fair value. Except where disclosed elsewhere in these unaudited consolidated interim financial statements, the following is a summary of related party transactions.
In August 2011, the Company and its subsidiary, 1347 Advisors, entered into a management services agreement with United Insurance Holdings Corp. ("United"), a third-party. This agreement provided that 1347 Advisors supply the services of an interim Chief Financial Officer to United, as well as certain strategy consulting, corporate development, corporate finance and actuarial services. Pursuant to the management services agreement, Hassan Baqar was appointed interim Chief Financial Officer at United. Mr. Baqar is currently a Managing Director of 1347 Advisors as well as a Vice President of KAI. Mr. Larry G. Swets, Jr., Chief Executive Officer and President of the Company, also

served on the Board of Directors of United. In February 2012, Amigo received a letter from the OIR which stated that Amigo, the Company and its subsidiaries, and United are affiliated entities due to their common managerial control. As a result of the foregoing, among other things, the Company may not transfer any assets to United or any of its affiliates without the prior written approval of the OIR. Subsequently, the Company and United mutually

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agreed to terminate their management services agreement effective April 2, 2012. Furthermore, Mr. Swets resigned as a member of United's Board of Directors effective April 5, 2012.

NOTE 21 COMMITMENTS AND CONTINGENCIES

(a) Legal proceedings:

In connection with its operations in the ordinary course of business, the Company and its subsidiaries are named as defendants in various actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the loss, or range of loss, if any, that may be incurred in connection with any of the various proceedings at this time, it is possible that individual actions may result in a loss having a material adverse effect on the Company's financial condition or results of operations.

(b) Guarantee:

The Company provided a letter of guarantee to a third-party for customs bonds reinsured by Lincoln General Insurance Company ("Lincoln General"). This guarantee may require the Company to compensate the third-party if Lincoln General is unable to fulfill its obligations relating to the customs bonds. On May 25, 2012, U.S. Customs made a demand on the third-party for $12.0 million plus interest. At this time, no demand has been made of the Company. The Company continues to believe that it has substantial defenses and that the potential loss in not probable; therefore, no liability has been recorded in the financial statements at June 30, 2013.

(c) Commitment:

During the second quarter of 2012, the Company entered into a subscription agreement to commit up to $6.0 million of capital to allow for participation in a limited liability investment which invests principally in income-producing real estate. At June 30, 2013, the unfunded commitment was $4.0 million.

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NOTE 22 SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

In 2004, KAI issued $125.0 million 7.5% senior notes due in 2014 through a private offering. These notes are redeemable at KAI's option on or after February 1, 2009 and are fully and unconditionally guaranteed by the Company (a "Guarantor"). The following tables show condensed consolidating financial information for the Company as of June 30, 2013 and December 31, 2012 and for the periods ended June 30, 2013 and 2012, with a separate column for the Guarantor, the issuer and the other businesses of the Company combined ("Non-Guarantor subsidiaries").

Condensed Consolidating Statement of Operations
For the six months ended June 30, 2013

	KFSI (a "Guarantor")	KAI (an "Issuer")	Other subsidiaries (the "Non-Guarantor subsidiaries")	Consolidation adjustments	Total
Revenue:					
Net premiums earned	$—	$—	$ 56,365	$—	$56,365
Service fee and commission income	—	—	25,176	—	25,176
Net investment income, net realized losses, other-than-temporary impairment loss and other income	(273)	(2,742)	5,626	—	2,611
Gain (loss) on change in fair value of debt	—	(6,063)	(550)	—	(6,613)
Total revenues	(273)	(8,805)	86,617	—	77,539
Expenses:					
Loss and loss adjustment expenses	—	—	46,446	—	46,446
Commissions and premium taxes	—	—	11,883	—	11,883
Other expenses	1,499	3,280	38,708	—	43,487
Interest expense	—	5,686	(1,926)	—	3,760
Total expenses	1,499	8,966	95,111	—	105,576
Loss before loss on buy-back of debt, equity in net income (loss) of investee and income tax (benefit) expense	(1,772)	(17,771)	(8,494)	—	(28,037)
Loss on buy-back of debt	—	(24)	—	—	(24)
Equity in net income (loss) of investee	—	255	—	—	255
Loss before income tax (benefit) expense	(1,772)	(17,540)	(8,494)	—	(27,806)
Income tax (benefit) expense	(710)	—	(91)	—	(801)
Equity in undistributed net (loss) income of subsidiaries	(25,941)	(8,685)	—	34,626	—
Net (loss) income	$(27,003)	$(26,225)	$ (8,403)	$34,626	$(27,005)

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Condensed Consolidating Statement of Operations
For the six months ended June 30, 2012

	KFSI (a "Guarantor")	KAI (an "Issuer")	Other subsidiaries (the "Non-Guarantor subsidiaries")	Consolidation adjustments	Total
Revenue:					
Net premiums earned	$—	$—	$ 60,252	$—	$60,252
Service fee and commission income	—	—	17,667	—	17,667
Net investment income, net realized losses, other-than-temporary impairment loss and other income	169	1,714	3,329	—	5,212
Gain (loss) on change in fair value of debt	—	(3,504)	(3,245)	—	(6,749)
Total revenues	169	(1,790)	78,003	—	76,382
Expenses:					
Loss and loss adjustment expenses	—	—	45,391	—	45,391
Commissions and premium taxes	—	—	9,166	—	9,166
Other expenses	2,258	1,842	31,855	—	35,955
Interest expense	—	7,113	(3,348)	—	3,765
Total expenses	2,258	8,955	83,064	—	94,277
Loss before loss on buy-back of debt, equity in net income (loss) of investee and income tax (benefit) expense	(2,089)	(10,745)	(5,061)	—	(17,895)
Equity in net income (loss) of investee	—	(2,165)	(4)	—	(2,169)
Loss before income tax (benefit) expense	(2,089)	(12,910)	(5,065)	—	(20,064)
Income tax (benefit) expense	—	—	175	—	175
Equity in undistributed net (loss) income of subsidiaries	(15,850)	(5,746)	—	21,596	—
Net (loss) income	$(17,939)	$(18,656)	$ (5,240)	$21,596	$(20,239)

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KINGSWAY FINANCIAL SERVICES INC.
Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

	Condensed Consolidating Balance Sheets As of June 30, 2013				
	KFSI (a "Guarantor")	KAI (an "Issuer")	Other subsidiaries (the "Non-Guarantor subsidiaries")	Consolidation adjustments	Total
Assets:					
Investments in subsidiaries	$35,207	$192,544	$—	$(227,751)	$—
Total investments	—	16,547	139,809	(47,105)	109,251
Investment in investee	—	—	—	—	—
Cash and cash equivalents	1,917	6,871	62,563	—	71,351
Goodwill	—	—	9,484	—	9,484
Intangible assets	—	7,803	42,766	—	50,569
Other assets	4,088	238,199	472,730	(609,887)	105,130
Asset held for sale	—	—	7,291		7,291
Total assets	41,212	461,964	734,643	(884,743)	353,076
Liabilities and Equity:					
Liabilities:					
Unpaid loss and loss adjustment expenses:	—	—	99,843	—	99,843
Unearned premiums	—	—	47,308	—	47,308
LROC preferred units	—	—	14,204	—	14,204
Senior unsecured debentures	—	26,356	—	—	26,356
Subordinated debt	—	26,674	—	—	26,674
Notes payable	—	70,222	(70,222)	—	—
Other liabilities	295	18,588	98,538	(19,647)	97,774
Total liabilities	295	141,840	189,671	(19,647)	312,159
Equity:					
Common stock	296,621	829,681	560,562	(1,390,243)	296,621
Additional paid-in capital	15,824	—	—	—	15,824
Accumulated deficit	(289,784)	(482,744)	(24,054)	506,798	(289,784)
Accumulated other comprehensive income (loss)	16,862	(26,813)	8,464	18,349	16,862
Shareholders' equity attributable to common shareholders	39,523	320,124	544,972	(865,096)	39,523
Noncontrolling interests in consolidated subsidiaries	1,394	—	—	—	1,394
Total equity	40,917	320,124	544,972	(865,096)	40,917
Total liabilities and equity	$41,212	$461,964	$734,643	$(884,743)	$353,076

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Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

	Condensed Consolidating Balance Sheets As of December 31, 2012				
	KFSI (a "Guarantor")	KAI (an "Issuer")	Other subsidiaries (the "Non-Guarantor subsidiaries")	Consolidation adjustments	Total
Assets:					
Investments in subsidiaries	$58,709	$185,079	$—	$(243,788)	$—
Total investments	—	—	142,499	(54,499)	88,000
Investment in investee	—	36,723	—	5,010	41,733
Cash and cash equivalents	1,932	6,371	72,510	—	80,813
Goodwill	—	—	8,421	—	8,421
Intangible assets	—	7,803	42,780	—	50,583
Other assets	5,004	229,206	452,199	(591,896)	94,513
Asset held for sale	—	—	8,737	—	8,737
Total assets	65,645	465,182	727,146	(885,173)	372,800
Liabilities and Equity:					
Liabilities:					
Unpaid loss and loss adjustment expenses:	—	—	106,564	—	106,564
Unearned premiums	—	—	45,047	—	45,047
LROC preferred units	—	—	13,655	—	13,655
Senior unsecured debentures	—	23,730	—	—	23,730
Subordinated debt	—	23,774	—	—	23,774
Notes payable	—	70,222	(70,222)	—	—
Other liabilities	231	16,374	92,145	(14,134)	94,616
Total liabilities	231	134,100	187,189	(14,134)	307,386
Equity:					
Common stock	296,621	829,681	572,079	(1,401,760)	296,621
Additional paid-in capital	15,757	—	—	—	15,757
Accumulated deficit	(262,069)	(474,768)	(35,045)	509,813	(262,069)
Accumulated other comprehensive income (loss)	14,762	(23,831)	2,923	20,908	14,762
Shareholders' equity attributable to common shareholders	65,071	331,082	539,957	(871,039)	65,071
Noncontrolling interests in consolidated subsidiaries	343	—	—	—	343
Total equity	65,414	331,082	539,957	(871,039)	65,414
Total liabilities and equity	$65,645	$465,182	$727,146	$(885,173)	$372,800

KINGSWAY FINANCIAL SERVICES INC.
Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

Condensed Consolidating Statement of Cash Flows
For the six months ended June 30, 2013

	KFSI (a "Guarantor")	KAI (an "Issuer")	Other subsidiaries (the "Non-Guarantor subsidiaries")	Consolidation adjustments	Total
Cash provided by (used in):					
Operating activities:					
Net (loss) income	$(27,003)	$(26,225)	$ (8,403)	$34,626	$(27,005)
Equity in undistributed net income (loss) of subsidiaries	25,941	8,685	—	(34,626)	—
Loss on change in fair value of debt	—	6,063	550	—	6,613
Other	1,047	4,431	(10,678)	—	(5,200)
Net cash used in operating activities	(15)	(7,046)	(18,531)	—	(25,592)
Investing activities:					
Proceeds from sales and maturities of fixed maturities, equity investments and investment in investee	—	13,638	11,255	—	24,893
Purchase of investments	—	(1,056)	(5,803)	—	(6,859)
Acquisition of business	—	—	(1,052)	—	(1,052)
Other	—	(4,453)	4,184	—	(269)
Net cash provided by investing activities	—	8,129	8,584	—	16,713
Financing activities:					
Redemption of senior unsecured debentures	—	(583)	—	—	(583)
Net cash (used in) provided by financing activities	—	(583)	—	—	(583)
Net (decrease) increase in cash and cash equivalents	(15)	500	(9,947)	—	(9,462)
Cash and cash equivalents at beginning of period	1,932	6,371	72,510	—	80,813
Cash and cash equivalents at end of period	$1,917	$6,871	$ 62,563	$—	$71,351

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Notes to Consolidated Financial Statements (Unaudited) June 30, 2013

	Condensed Consolidating Statement of Cash Flows For the six months ended June 30, 2012				
	KFSI	KAI	Other subsidiaries	Consolidation adjustments	Total
	(a "Guarantor")	(an "Issuer")	(the "Non-Guarantor subsidiaries")		
Cash provided by (used in):					
Operating activities:					
Net (loss) income	$(17,939)	$(18,656)	$ (5,240)	$21,596	$(20,239)
Equity in undistributed net income (loss) of subsidiaries	15,850	5,746			