

## **AMENDED FILING COVER SHEET**

Amended File Title	Amended Explanation
Notes to Financial Statements	Domiciliary state requires additional information to the Notes



19530201120100105

## ANNUAL STATEMENT

**For the Year Ended December 31, 2011**  
**OF THE CONDITION AND AFFAIRS OF THE**

## Hallmark National Insurance Company

NAIC Group Code	3478 (Current Period)	3478 (Prior Period)	NAIC Company Code	19530	Employer's ID Number	31-1334827
Organized under the Laws of	Ohio		, State of Domicile or Port of Entry		Ohio	
Country of Domicile	United States of America					
Incorporated/Organized	October 4, 1991			Commenced Business		January 10, 1992
Statutory Home Office	41 South High Street Suite 1700 (Street and Number)			Columbus, OH	43215 (City or Town, State and Zip Code)	
Main Administrative Office	777 Main Street Suite 1000 (Street and Number)			Fort Worth, TX	76102 (City or Town, State and Zip Code)	817-348-1600 (Area Code) (Telephone Number)
Mail Address	777 Main Street Suite 1000 (Street and Number or P.O. Box)			Fort Worth, TX	76102 (City or Town, State and Zip Code)	
Primary Location of Books and Records	777 Main Street Suite 1000 (Street and Number)			Fort Worth, TX	76102 (City or Town, State and Zip Code)	817-348-1600 (Area Code) (Telephone Number)
Internet Web Site Address	www.hallmarkgrp.com					
Statutory Statement Contact	Felicia M Smith (Name)			817-348-1887 (Area Code) (Telephone Number)	(Extension)	
	fsmith@hallmarkgrp.com (E-Mail Address)			817-348-1820 (Fax Number)		

## OFFICERS

OFFICERS		
	Name	Title
1.	Kevin Troy Kasitz #	President
2.	Jeffrey Ray Passmore	Chief Financial Officer & Treasurer
3.	Cecil Randolph Wise	Secretary

## VICE-PRESIDENTS

## **DIRECTORS OR TRUSTEES**

State of Texas

County of Tarrant ss

The officers of this reporting entity being duly sworn, each depose and say that they are the described officers of said reporting entity, and that on the reporting period stated above, all of the herein described assets were the absolute property of the said reporting entity, free and clear from any liens or claims thereon, except as herein stated, and that this statement, together with related exhibits, schedules and explanations therein contained, annexed or referred to, is a full and true statement of all the assets and liabilities and of the condition and affairs of the said reporting entity as of the reporting period stated above, and of its income and deductions therefrom for the period ended, and have been completed in accordance with the NAIC Annual Statement Instructions and Accounting Practices and Procedures manual except to the extent that: (1) state law may differ; or, (2) that state rules or regulations require differences in reporting not related to accounting practices and procedures, according to the best of their information, knowledge and belief, respectively. Furthermore, the scope of this attestation by the described officers also includes the related corresponding electronic filing with the NAIC, when required, that is an exact copy (except for formatting differences due to electronic filing) of the enclosed statement. The electronic filing may be requested by various regulators in lieu of or in addition to the enclosed statement.

(Signature)  
Kevin T. Kasitz  
(Printed Name)  
1.  
President  
(Title)

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(Signature)  
Jeffrey R. Passmore  
(Printed Name)  
2.  
Chief Financial Officer & Treasurer  
(Title)

---

(Signature)  
Cecil R. Wise  
(Printed Name)  
3.  
Secretary  
(Title)

Subscribed and sworn to (or affirmed) before me on this  
22nd day of May , 2012, by

## **NOTES TO FINANCIAL STATEMENTS**

### **1. Significant Accounting Policies**

#### **A. Accounting Practices**

In 1998, the National Association of Insurance Commissions (NAIC) adopted the Codification of Statutory Accounting Principles (the Codification) guidance, which replaced the prior Accounting and Practice Procedures manuals as the NAIC's primary guidance on statutory accounting. The Codification provides guidance where statutory accounting has been silent and changes current statutory accounting in some areas, (e.g. deferred income taxes are recorded). Effective January 1, 2001, the Ohio Department of Insurance (the OHDOI) adopted the NAIC Accounting Practices and Procedures Manual (the Manual). The Manual, previously known as Codification contains Statements of Statutory Accounting Principles (SSAP). The accompanying financial statements have been prepared in conformity with the Manual and accounting practices prescribed or permitted by the OHDOI.

#### **B. Use of Estimates**

The preparation of statutory financial statements requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

#### **C. Accounting policies**

Premiums are earned over the terms of the related insurance policies and reinsurance contracts. Unearned premium reserves are established to cover the unexpired portion of premiums written. Such reserves are computed by pro rata methods for direct business and are based on reports received from ceding companies for reinsurance assumed.

Expenses incurred in connection with acquiring new insurance business, including acquisition costs such as sales commissions, are charged to operations as incurred.

In addition, the Company uses the following accounting policies:

1. Money market investments are reflected at cost.
2. Bonds not backed by other loans are stated at amortized cost using the scientific interest method.
3. Common stocks are stated at fair value.
4. Preferred stocks: Book adjusted carrying value.
5. Mortgage loans: Not applicable.
6. Loan-backed: Not applicable.
7. Investments in subsidiaries and affiliated companies: Statutory surplus.
8. Investments in joint ventures, partnerships and limited liability companies: Not applicable.
9. Derivatives: Not applicable.
10. The Company anticipates investment income as a factor in the premium deficiency calculation, except accident and health business, in accordance with SSAP No. 53 - *Property-Casualty Contracts - Premiums*.
11. Unpaid losses and loss adjustment expenses include an amount determined from individual case estimates and loss reports and an amount, based on past experience, for losses incurred but not reported. Such liabilities are necessarily based on assumptions and estimates, and, while management believes the amount is adequate, the ultimate liability may be in excess of or less than the amount provided. The methods for making such estimates and for establishing the resulting liability are continually reviewed, and any adjustments are reflected in the period determined.
12. The Company has not modified its capitalization policy from the prior period.
13. Pharmaceutical rebate receivables: Not applicable.

### **2. Accounting Changes and Correction of Errors**

## NOTES TO FINANCIAL STATEMENTS

Not applicable.

### **3. Business Combinations and Goodwill**

Not applicable.

### **4. Discontinued Operations**

Not applicable.

### **5. Investments**

Not applicable.

### **6. Joint Venture, Partnerships, and Limited Liability Companies**

Not applicable.

### **7. Investment Income**

A. Accrued Investment Income: The Company nonadmits investment income due and accrued if amounts are over 90 days past due.

B. Amounts Nonadmitted: Not applicable.

### **8. Derivative Instruments**

Not applicable.

### **9. Income Taxes**

The Company files a consolidated Federal income tax return with Hallmark Financial Services Inc., ("HFS") (EIN 87-0447375) and its affiliates with the exception of Hallmark County Mutual Insurance Company. Pursuant to a written tax sharing agreement, the Company's provision for income taxes, if any, equals or approximates tax expense or benefit computed on a separate return basis.

The Company has not elected to admit additional DTA's pursuant to SSAP 10R, paragraph e. The current period election does not differ from the prior reporting period.

A. The net deferred tax asset/(liability) at December 31, 2011 and the change from the prior year are comprised of the following components:

	12/31/2011			12/31/2010			Change
	Ordinary	Capital	Total	Ordinary	Capital	Total	
(1) Total gross deferred tax assets	916,928	-	916,928	247,502	-	247,502	669,426
Adjusted gross deferred tax assets	916,928	-	916,928	247,502	-	247,502	669,426
(2) Total gross deferred tax liabilities	-	-	-	-	(201)	(201)	201
(3) Net deferred tax assets/(liabilities)	916,928	-	916,928	247,502	(201)	247,301	669,627
(4) Total Deferred tax assets nonadmitted	(253,904)	-	(253,904)	(247,022)	201	(246,821)	(7,083)
(5) Net admitted deferred tax assets/ (liabilities)	663,024	-	663,024	480	-	480	662,544

(6) The Company has not elected to admit deferred tax assets pursuant to SSAP10R.

## NOTES TO FINANCIAL STATEMENTS

(7) The amount of adjusted gross deferred tax assets under each component of SSAP 10R:

	12/31/11	12/31/10		Change
	Ordinary	Capital	Ordinary	Capital
	Total	Total	Total	Change
Admitted under paragraph 10.a.	663,024	-	663,024	480
Paragraph 10.b., lesser of:	-	-	-	-
Admitted under paragraph 10.b.i	-	-	-	-
Admitted under paragraph 10.b.ii	1,871,626	-	1,871,626	-
Admitted under paragraph 10.b. (lesser of b.i. or b.ii)	-	-	-	-
Admitted under paragraph 10.c.	-	-	-	-
Total admitted from the application of paragraph 10.a.-10.c.	663,024	-	663,024	480
Admitted under paragraph 10.e.i.	-	-	-	-
Paragraph 10.e.ii., lesser of:	-	-	-	-
Admitted under paragraph 10.e.ii.a	-	-	-	-
Admitted under paragraph 10.e.ii.b	-	-	-	-
Admitted under paragraph 10.e.ii. (lesser of e.ii.a or e.ii.b)	-	-	-	-
Admitted under paragraph 10.e.iii.	-	-	-	-
Total admitted from the application of paragraph 10.e.	-	-	-	-
Total admitted adjusted gross deferred tax assets	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>480</u>
	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>480</u>
	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>480</u>

(8) The change in deferred income taxes reported in surplus before consideration of nonadmitted assets is comprised of the following components:

	12/31/11	12/31/10	Change
Net adjusted deferred tax asset (liabilities)	916,928	247,301	669,627
Tax-effect of unrealized gains and losses	-	-	-
Net tax effect without unrealized gains and losses	<u>916,928</u>	<u>247,301</u>	<u>669,627</u>
Change in deferred income taxes	<u>(669,627)</u>		

B. Unrecognized deferred tax liabilities: None

C. Current income taxes incurred consist of the following major components:

	12/31/11	12/31/10	
Current year tax expense (benefit)	130,039	(682,312)	
Tax expense on capital gains (losses)	8,787	419,801	
Benefits of operating loss carry forwards	-	-	
Prior year adjustments	-	-	
Current income taxes incurred	<u>138,826</u>	<u>(262,511)</u>	

Deferred income tax assets and liabilities consist of the following major components:

	12/31/11	12/31/10		Change
	Ordinary	Capital	Ordinary	Capital
	Total	Total	Total	Change
Deferred tax assets:				
Uneamed Premium Reserve	477,081	-	477,081	-
Capital loss carryforward	-	-	-	-
Loss Reserve Discounting	439,847	-	439,847	-
NOL carryforward	-	-	-	-
Impairments	-	-	-	-
Goodwill	-	-	-	-
Nonadmitted asset	-	-	-	-
Other	-	-	247,502	-
Total gross deferred tax assets	<u>916,928</u>	<u>-</u>	<u>916,928</u>	<u>247,502</u>
Valuation Allowance Adjustment	-	-	-	-
Total adjusted gross deferred tax assets	<u>916,928</u>	<u>-</u>	<u>916,928</u>	<u>247,502</u>
Nonadmitted deferred tax assets	<u>(253,904)</u>	<u>-</u>	<u>(253,904)</u>	<u>(246,821)</u>
Admitted deferred tax assets	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>681</u>
Deferred tax Liabilities:				
Deferred market discount	-	-	-	-
Unrealized <Gains> Losses	-	-	-	-
Other	-	-	(201)	(201)
Total deferred tax liabilities	<u>-</u>	<u>-</u>	<u>-</u>	<u>(201)</u>
Net admitted deferred tax asset (liabilities)	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>681</u>
	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>681</u>
	<u>663,024</u>	<u>-</u>	<u>663,024</u>	<u>681</u>

## NOTES TO FINANCIAL STATEMENTS

D. The Company's income tax incurred and change in deferred income tax differs from the amount obtained by applying the federal statutory rate of 35% to income before income taxes as follows:

	12/31/11	12/31/10
Current income taxes incurred	138,826	(262,511)
Capital gains tax	8,787	419,801
Changes in deferred income tax (without tax on unrealized gains and losses)	(669,627)	2,391,232
 Total income tax reported	 <hr/>	 <hr/>
Income before taxes	(1,832,288)	7,310,689
	35%	35%
Expected Income tax expense (benefit) at 35% statutory rate	(641,301)	2,558,741
 Increase (decrease) in actual tax reported resulting from:		
a. State taxes	-	-
b. Tax-exempt income	(128,014)	(271,595)
c. Change in deferred taxes on nonadmitted assets	-	-
d. DRD	-	(10,628)
e. Other	-	194,289
f. Prior year true-up	247,301	77,715
 Total income tax reported	 <hr/>	 <hr/>

E. Operating loss carryforward

- (1) As of December 31, 2011, there is no operating loss and no tax credit carryforwards for tax purposes.
- (2) The amount of Federal income taxes incurred that are available for recoupment in the event of future net losses are:

	Ordinary	Capital	Total
2011	147,613	0	147,613
2010	-	0	-
2009	-	0	-

- (3) The aggregate amount of deposits admitted under Section 6603 of the Internal Revenue Code are \$ 0.

F. Consolidated federal income tax return

- (1) The Company's federal income tax return is consolidated with all the companies shown in Schedule Y with the exception of Hallmark County Mutual Insurance Company.

### 10. Information Concerning Parent, Subsidiaries and Affiliates

A. Nature of Relationships:

See Schedule Y - Information Concerning Activities of Insurer Members of a Holding Company Group, Part 1 Organizational Chart.

Effective March 8, 2011 the name of the Company changed to Hallmark National Insurance Company from State Auto National Insurance Company.

On August 3, 2011 Hallmark Insurance Company ("HIC") received approval from the Arizona DOI and has made an \$11 million capital contribution to the Company consisting of cash and securities.

B. The Company paid a processing and claims service fee directly to American Hallmark General Agency (AHGA) under the terms of an administrative services agreement which had been in place since January 1, 2011. Under this agreement, the Company paid processing fees to AHGA in the amount of \$1,076,436 and claims service fees of \$675,724 during 2011.

C. Effective November 1, 2011 the Company entered into a management agreement with AHGA. Under the terms of the agreement the Company incurred expenses of \$160,000 payable to AHGA.

### 11. Debt

Not applicable.

## **NOTES TO FINANCIAL STATEMENTS**

### **12. Retirement Plans, Deferred Compensation, Post Employment Benefits and Compensated Absences and Other Post Retirement Benefit Plans**

Not applicable.

### **13. Capital Surplus, Dividend Restrictions and Quasi Reorganizations**

#### **A. Capital Stock Authorized, Issued and Outstanding as of the Balance Sheet Date:**

The Company has 100,000 shares of \$40 par value common stock authorized and 60,000 shares issued and outstanding. The Company has no preferred stock authorized, issued or outstanding.

#### **B. Dividend Rate of Preferred Stock: Not applicable.**

#### **C. Dividend Restrictions:**

Dividends on common stock are paid as declared by the Board of Directors of the Company. Under the insurance regulations of Ohio, the maximum amount of dividends that the Company may pay out of earned surplus in any year without prior regulatory approval is limited to the greater of 10% of the most recent year end adjusted policyholders' surplus or net income for the prior year end. Due to the Company's earned surplus position, no distributions will be allowed during 2012 without prior approval of the insurance regulatory authorities.

#### **D. Dates and Amounts of Dividends Paid:**

The Company did not pay dividends during 2011.

In 2010 under the former parent company, State Auto Financial Corporation, dividends were paid. On September 30, 2010, the Board of Directors of the Company declared an extraordinary dividend to be paid to State Auto Financial Corporation pursuant to the terms of the stock purchase agreement between HIC and State Auto Financial Corporation in order to reduce the Company's capital and surplus to \$10,000,000. This dividend was approved by the OHDOI on November 8, 2010, and was paid in a combination of cash and securities in the amount of \$16,367,601 on December 31, 2010.

On March 5, 2010, the Board of Directors of the Company declared a \$40,000,000 extraordinary stockholder dividend to be paid to State Auto Financial Corporation. This dividend was approved by the OHDOI on April 14, 2010 and was paid in a combination of cash and securities on May 10, 2010.

#### **E. Portion of the Company's Profits that may be paid as Ordinary Dividends to Stockholders:**

Within the limitations of (C) above, there are no restrictions placed on the portion of Company profits that may be paid as ordinary dividends to shareholders.

#### **F. Restrictions Placed on the Unassigned Funds, Including for Whom the Surplus is Being Held:**

Not applicable.

#### **G. Mutual Surplus Advances: Not applicable.**

#### **H. Company Stock Held for Special Purposes: Not applicable.**

#### **I. Changes in Special Surplus Funds: Not applicable.**

#### **J. Changes in Unassigned Funds:**

Net deferred income taxes	\$ 669,627
Nonadmitted asset values	\$ (7,083)
Paid in	\$11,000,000

#### **K. Surplus Notes: Not applicable.**

#### **L. Impact of Restatement Due to Quasi Reorganizations: Not applicable.**

#### **M. Effective Date of Quasi Reorganizations: Not applicable.**

### **14. Contingencies**

#### **A. Contingent Commitments:**

The Company has no commitments or contingent commitments to affiliates or other entities. The Company has made no guarantees on behalf of affiliates.

## **NOTES TO FINANCIAL STATEMENTS**

### B. Guaranty Fund and Other Assessments:

The Company is subject to guaranty fund and other assessments by the states in which it writes business. Guaranty fund assessments should be accrued at the time of insolvencies. The Company has not received any guaranty fund assessments.

### C. Gain Contingencies: Not applicable.

### D. Claims Related Extra Contractual Obligation and Bad Faith Losses Stemming from Lawsuits: Not applicable.

### E. All Other Contingencies:

The Company is involved in litigation and may become involved in potential litigation arising in the ordinary course of business. Additionally, the Company may be impacted by adverse regulatory actions and adverse court decisions where insurance coverages are expanded beyond the scope originally contemplated in the policies. In the opinion of management, the effects, if any, of such litigation and published court decisions are not expected to be material to the financial statements.

### **15. Leases**

Not applicable.

### **16. Information about Financial Instruments with Off-Balance Sheet Risk and Financial Instruments with Concentration of Credit Risk**

Not applicable.

### **17. Sales, Transfer and Servicing of Financial Assets and Extinguishment of Liabilities**

Not applicable.

### **18. Gain or Loss to the Reporting Entity from Uninsured A&H Plans and the Underinsured Portion of Partially Insured Plan**

Not applicable.

### **19. Direct Premium Written/Produced by Managing General Agents/Third Party Administrators**

Name and Address of Managing General Agent or Third Party Administrator	FEIN Number	Exclusive Contract	Types of Business Written	Type of Authority Granted	Direct Premiums Written/ Produced by
American Hallmark G.A., Inc. 6500 Pinecrest, Suite 100 Plano, TX 75024	75-2341879	No	Personal and Commercial property/casualty	C,CA,B,P,*U	\$ 16,024,357

### **20. Fair Value Measurement**

Not applicable.

### **21. Other Items**

Not applicable.

### **22. Events Subsequent**

Not applicable.

### **23. Reinsurance**

A. Under the intercompany pooling agreement the Company has reinsurance recoverable of \$12,249,000 with American Hallmark Insurance Company of Texas (“AHIC”) which exceeds 3% of surplus.

B. The Company has no reinsurance recoverable in dispute.

## NOTES TO FINANCIAL STATEMENTS

C. Assuming that all reinsurance contracts were caused to be cancelled effective December 31, 2011, the amounts of unearned premium and related commission that would have been due to/from reinsurers on both assumed and ceded reinsurance programs are summarized below:

	Assumed Reinsurance		Ceded Reinsurance		Net Reinsurance	
	Premium	Comm	Premium	Comm	Premium	Comm
	<u>Reserve</u>	<u>Equity</u>	<u>Reserve</u>	<u>Equity</u>	<u>Reserve</u>	<u>Equity</u>
Affiliates	\$ 6,815,437	\$ 7,676,535	\$ 5,779,628	\$ 4,349,504	\$ 1,035,809	\$ 3,327,031
All Others:		\$ -	\$ 98,187		\$ (98,187)	\$ -
Total	\$ 6,815,437	\$ 7,676,535	\$ 5,877,815	\$ 4,349,504	\$ 937,622	\$ 3,327,031

D. The Company believes all reinsurance balances are collectible.

E. Commutation of Ceded Reinsurance: Not applicable.

F. As part of the sale transaction of the Company from State Auto to Hallmark at year end 2010, a Loss Portfolio Transfer Reinsurance Contract (LPT) was put in place to transfer all existing Loss and Loss Adjustment Expenses Liabilities to State Auto Property & Casualty Insurance Company. This LPT was put in place subsequent to the issuance of policies 2010 and prior. The balance sheet reserves (lines 1 and 3 of the Liabilities, Surplus and Other Funds page) are shown on a gross basis. That is, the LPT is treated as a write-in item. The LPT resulted in no special surplus gain or loss.

G. The Company does not have reinsurance accounted for as a deposit.

### 24. Retrospective Rated Contracts and Contracts Subject to Redetermination

No changes.

### 25. Changes in Incurred Loss and Adjustment Expenses

Reserves for incurred losses and loss adjustment expense attributable to insured events of prior years has increased by \$11.0 million from \$223.4 million in 2010 to \$234.4 million in 2011 as a result of re-estimation of unpaid losses and loss adjustment expenses principally on auto physical damage and private passenger auto liability lines of insurance. This increase is generally the result of ongoing analysis of recent loss development trends. There are no additional premiums or return premiums as a result of these prior year effects.

### 26. Intercompany Pooling Arrangements

Effective January 1, 2011, HNIC was added to the intercompany pool. The lead company of the pool is AHIC. Under the terms of the arrangement, the underwriting risk for all lines of business of the intercompany pool participants are reinsured with AHIC. The pool or net underwriting risk remaining after reinsurance is transacted with third parties by AHIC is then retro ceded to the pool participants based on pool participation percentages. The provision for reinsurance and the write-off of uncollectible reinsurance are reported in the statutory financial statements of AHIC and are not allocated to the other pool participants.

Effective July 1, 2011, the pooling percentages were changed to reflect a capital contribution from HIC to the Company.

The names, NAIC company codes and intercompany pooling percentages are as follows:

<u>Pool Participant</u>	<u>NAIC Company Code</u>	<u>Pool Participation%</u>
American Hallmark Insurance Company of Texas	43494	32.5
Hallmark Insurance Company	34037	28.4
Hallmark Specialty Insurance Company	26808	27.6
Hallmark National Insurance Company	19530	11.5

All of the above pool companies are party to reinsurance agreements with non-affiliated reinsurers covering business subject to the pooling agreement and have contractual rights of direct recovery from the non-affiliated reinsurers under the terms of such reinsurance agreements.

### 27. Structured Settlements

Not applicable.

### 28. Health Care Receivables

Not applicable.

## **NOTES TO FINANCIAL STATEMENTS**

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### **29. Participating Policies**

Not applicable.

### **30. Premium Deficiency Reserves**

As of December 31, 2011 the Company evaluated the need for a premium deficiency reserve and determined a reserve is not required. The Company considered anticipated investment income when evaluating this liability.

### **31. High Deductibles**

Not applicable.

### **32. Discounting of Liabilities for Unpaid Losses or Unpaid Loss Adjustment Expenses**

Not applicable.

### **33. Asbestos/Environmental Reserves**

Not applicable.

### **34. Subscriber Savings Accounts**

Not applicable.

### **35. Multiple Peril Crop Insurance**

Not applicable.

### **36. Financial Guaranty Insurance**

Not applicable.