ATLANTIC AMERICAN CORP
Form 10-Q
May 11, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018
OR

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

Commission File Number 0-3722

ATLANTIC AMERICAN CORPORATION
(Exact name of registrant as specified in its charter)

Georgia	58-1027114
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

4370 Peachtree Road, N.E., Atlanta, Georgia	30319
(Address of principal executive offices)	(Zip Code)

(404) 266-5500
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company)
Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The total number of shares of the registrant's Common Stock, $1 par value, outstanding on May 7, 2018 was 20,264,477.

ATLANTIC AMERICAN CORPORATION

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ATLANTIC AMERICAN CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share data)

ASSETS

	Unaudited March 31, 2018	December 31, 2017
Cash and cash equivalents	$ 8,438	$ 24,547
Investments:		
Fixed maturities, available-for-sale (cost: $222,428 and $212,544)	217,848	215,108
Equity securities (cost: $10,918 and $10,918)	18,936	23,355
Other invested assets (cost: $5,663 and $5,626)	5,663	5,626
Policy loans	2,105	2,146
Real estate	38	38
Investment in unconsolidated trusts	1,238	1,238
Total investments	245,828	247,511
Receivables:		
Reinsurance	20,883	17,613
Insurance premiums and other (net of allowance for doubtful accounts: $223 and $209)	7,896	13,241
Deferred income taxes, net	2,271	-
Deferred acquisition costs	33,163	32,694
Other assets	4,787	5,089
Intangibles	2,544	2,544
Total assets	$ 325,810	$ 343,239
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Insurance reserves and policyholder funds:		
Future policy benefits	$ 84,368	$ 82,435
Unearned premiums	16,887	23,449
Losses and claims	70,120	65,689
Other policy liabilities	1,577	2,010
Total insurance reserves and policyholder funds	172,952	173,583
Accounts payable and accrued expenses	17,396	22,342
Deferred income taxes, net	-	593
Junior subordinated debenture obligations, net	33,738	33,738
Total liabilities	224,086	230,256
Commitments and contingencies (Note 9)		
Shareholders’ equity:		
Preferred stock, $1 par, 4,000,000 shares authorized; Series D preferred, 55,000 shares issued and outstanding; $5,500 redemption value	55	55
Common stock, $1 par, 50,000,000 shares authorized; shares issued: 22,400,894; shares outstanding: 20,372,444 and 20,449,531	22,401	22,401
Additional paid-in capital	57,431	57,495
Retained earnings	33,188	30,993
Accumulated other comprehensive income (loss)	(3,618)	9,751
Unearned stock grant compensation	(387)	(579)

Treasury stock, at cost: 2,028,450 and 1,951,363 shares	(7,346)	(7,133)
Total shareholders' equity	101,724	112,983
Total liabilities and shareholders' equity	$ 325,810	$ 343,239

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

ATLANTIC AMERICAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited; Dollars in thousands, except per share data)

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
Revenue:		
Insurance premiums	$ 42,202	$ 40,782
Investment income	2,359	2,159
Realized investment gains, net	370	883
Unrealized losses on equity securities, net	(4,419)	-
Other income	28	35
Total revenue	40,540	43,859
Benefits and expenses:		
Insurance benefits and losses incurred	33,172	29,997
Commissions and underwriting expenses	10,019	10,614
Interest expense	462	409
Other expense	3,238	3,186
Total benefits and expenses	46,891	44,206
Loss before income taxes	(6,351)	(347)
Income tax benefit	(1,327)	(126)
Net loss	(5,024)	(221)
Preferred stock dividends	(99)	(99)
Net loss applicable to common shareholders	$ (5,123)	$ (320)
Loss per common share (basic and diluted)	$ (.25)	$ (.02)

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

ATLANTIC AMERICAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited; Dollars in thousands)

	Three Months Ended March 31,	
	2018	2017
Net loss	$ (5,024)	$ (221)
Other comprehensive income (loss):		
Available-for-sale securities:		
Gross unrealized holding gain (loss) arising in the period	(6,774)	4,243
Related income tax effect	1,422	(1,485)
Less: reclassification adjustment for net realized gains included in net loss	(370)	(883)
Related income tax effect	78	309
Total other comprehensive income (loss), net of tax	(5,644)	2,184
Total comprehensive income (loss)	$ (10,668)	$ 1,963

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

ATLANTIC AMERICAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Unaudited; Dollars in thousands)

Three Months Ended March 31, 2018	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Unearned Stock Grant Compensation	Treasury Stock	Total
Balance, December 31, 2017	$ 55	$ 22,401	$ 57,495	$ 30,993	$ 9,751	$ (579)	$ (7,133)	$ 112,983
Cumulative effect of adoption of updated accounting guidance for equity financial instruments at January 1, 2018	-	-	-	9,825	(9,825)	-	-	-
Reclassification of certain tax effects from accumulated other comprehensive income at January 1,2018	-	-	-	(2,100)	2,100	-	-	-
Net loss	-	-	-	(5,024)	-	-	-	(5,024)
Other comprehensive loss, net of tax	-	-	-	-	(5,644)	-	-	(5,644)
Dividends declared on common stock	-	-	-	(407)	-	-	-	(407)
Dividends accrued on preferred stock	-	-	-	(99)	-	-	-	(99)
Restricted stock grants	-	-	(68)	-	-	115	(47)	-
Amortization of unearned compensation	-	-	-	-	-	77	-	77
Purchase of shares for treasury	-	-	-	-	-	-	(169)	(169)
Issuance of shares under stock plans	-	-	4	-	-	-	3	7
Balance, March 31, 2018	$ 55	$ 22,401	$ 57,431	$ 33,188	$ (3,618)	$ (387)	$ (7,346)	$ 101,724
Three Months Ended March 31, 2017								
Balance, December 31, 2016	$ 55	$ 22,401	$ 57,114	$ 27,272	$ 5,830	$ (428)	$ (6,738)	$ 105,506
Net loss	-	-	-	(221)	-	-	-	(221)
Other comprehensive income, net of tax	-	-	-	-	2,184	-	-	2,184
Dividends declared on common stock	-	-	-	(408)	-	-	-	(408)
Dividends accrued on preferred stock	-	-	-	(99)	-	-	-	(99)
Amortization of unearned compensation	-	-	-	-	-	116	-	116
	-	-	-	-	-	-	(105)	(105)

Purchase of shares for treasury								
Issuance of shares under stock plans	-	-	5	-	-	-	3	8
Balance, March 31, 2017	$ 55	$ 22,401	$ 57,119	$ 26,544	$ 8,014	$ (312)	$ (6,840)	$ 106,981

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

ATLANTIC AMERICAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited; Dollars in thousands)

	Three Months Ended March 31, 2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(5,024)	$(221)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization of deferred acquisition costs	3,719	3,399
Acquisition costs deferred	(4,188)	(5,036)
Realized investment gains, net	(370)	(883)
Unrealized losses on equity securities, net	4,419	-
Compensation expense related to share awards	77	116
Depreciation and amortization	273	387
Deferred income tax benefit	(1,363)	(126)
Decrease in receivables, net	1,567	4,671
Decrease in insurance reserves	(631)	(4,276)
Decrease in other liabilities	(5,453)	(4,281)
Other, net	98	102
Net cash used in operating activities	(6,876)	(6,148)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from investments sold	13,373	19,782
Proceeds from investments matured, called or redeemed	1,529	5,842
Investments purchased	(23,955)	(21,870)
Additions to property and equipment	(18)	(83)
Net cash (used in) provided by investing activities	(9,071)	3,671
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from shares issued under stock plans	7	8
Purchase of shares for treasury	(169)	(105)
Net cash used in financing activities	(162)	(97)
Net decrease in cash and cash equivalents	(16,109)	(2,574)
Cash and cash equivalents at beginning of period	24,547	13,252
Cash and cash equivalents at end of period	$8,438	$10,678
SUPPLEMENTAL CASH FLOW INFORMATION:		
Cash paid for interest	$452	$408

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

ATLANTIC AMERICAN CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited; Dollars in thousands, except per share amounts)

Note 1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Atlantic American Corporation (the "Parent") and its subsidiaries (collectively with the Parent, the "Company"). The Parent's primary operating subsidiaries, American Southern Insurance Company and American Safety Insurance Company (together known as "American Southern") and Bankers Fidelity Life Insurance Company and Bankers Fidelity Assurance Company (together known as "Bankers Fidelity"), operate in two principal business units. American Southern operates in the property and casualty insurance market, while Bankers Fidelity operates in the life and health insurance market. All significant intercompany accounts and transactions have been eliminated in consolidation. The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 8 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for audited annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. The unaudited condensed consolidated financial statements included herein and these related notes should be read in conjunction with the Company's consolidated financial statements, and the notes thereto, included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017 (the "2017 Annual Report"). The Company's financial condition and results of operations and cash flows as of and for the three month period ended March 31, 2018 are not necessarily indicative of the financial condition or results of operations and cash flows that may be expected for the year ending December 31, 2018 or for any other future period.

The Company's significant accounting policies have not changed materially from those set out in the Company's 2017 Annual Report, except as noted below for the adoption of new accounting standards.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

Note 2. Recently Issued Accounting Standards

Adoption of New Accounting Standards

In February 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2018-02, Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income ("ASU 2018-02"). The FASB issued this guidance for the effect on deferred tax assets and liabilities related to items recorded in accumulated other comprehensive income ("AOCI") resulting from legislated tax reform enacted on December 22, 2017. The tax reform reduced the federal tax rate applied to the Company's deferred tax balances from 35% to 21% on enactment. Under current GAAP, the Company recorded the total effect of the change in enacted tax rates on deferred tax balances in the income tax expense component of net income. ASU 2018-02 permits the Company to reclassify out of AOCI and into retained earnings the "stranded" tax effects that resulted from recording the tax effects of unrealized investment gains at a 35% tax rate because the 14% reduction in tax rate was recognized in net income instead of other comprehensive income. The Company adopted ASU 2018-02 as of January 1, 2018. As a result, on January 1, 2018, the Company reclassified $2,100 of stranded tax effects related to continuing operations which increased AOCI and reduced retained earnings.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). ASU 2016-15 is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. The issues addressed in ASU 2016-15 are: 1) debt prepayment or debt extinguishment costs, 2) settlement of zero-coupon debt instruments, 3) contingent consideration payments made after a business combination, 4) proceeds from the settlement of insurance claims, 5) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, 6) distributions received from equity method investees, 7) beneficial interests in securitization transactions and 8) separately identifiable cash flows and application of the predominance principle. The Company adopted ASU 2016-15 as of January 1, 2018. The adoption of this ASU did not have an impact on the Company’s consolidated statements of cash flows.

Table of Contents

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments – Overall (Subtopic 825-10) (“ASU 2016-01”). ASU 2016-01 provides updated guidance for the recognition and measurement of financial instruments. The guidance requires investments in equity securities to be measured at fair value with any changes in valuation reported in net income except for investments that are consolidated or are accounted for under the equity method of accounting. The guidance also requires a deferred tax asset resulting from net unrealized losses on available-for-sale (AFS) fixed maturities that are recognized in AOCI to be evaluated for recoverability in combination with the Company’s other deferred tax assets. Under previous guidance, the Company measured investments in equity securities at fair value with any changes in fair value reported in other comprehensive income. The Company adopted ASU 2016-01 as of January 1, 2018. The adoption of this guidance resulted in the recognition of $9,825 of net after tax unrealized gains on equity securities as a cumulative effect adjustment that increased retained earnings as of January 1, 2018 and decreased AOCI by the same amount. The Company elected to report changes in the fair value of equity securities in a separate line item on the Company’s consolidated statements of operations. At December 31, 2017, equity securities were classified as AFS in the Company’s consolidated balance sheets. However, upon adoption, the updated guidance eliminated the AFS balance sheet classification for equity securities.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) (“ASU 2014-09”). ASU 2014-09, as modified, provides guidance for recognizing revenue which excludes insurance contracts and financial instruments. Revenue is to be recognized when, or as, goods or services are transferred to customers in an amount that reflects the consideration that an entity is expected to be entitled in exchange for those goods or services. For the three months ended March 31, 2018, approximately $28, or less than one-tenth of 1% of the Company's total revenues, were within the scope of this updated guidance. The Company adopted ASU No. 2014-09 as of January 1, 2018. The adoption of this ASU did not have an impact on the Company’s consolidated financial statements.

Table of Contents

Note 3. Investments

The following tables set forth the carrying value, gross unrealized gains, gross unrealized losses and cost or amortized cost of the Company's investments, aggregated by type and industry, as of March 31, 2018 and December 31, 2017.

Investments were comprised of the following:

	March 31, 2018			
	Carrying Value	Gross Unrealized Gains	Gross Unrealized Losses	Cost or Amortized Cost
Fixed maturities:				
Bonds:				
U.S. Treasury securities and obligations of U.S. Government agencies and authorities	$29,978	$ 87	$ 966	$30,857
Obligations of states and political subdivisions	10,666	476	50	10,240
Corporate securities:				
Utilities and telecom	18,592	1,262	487	17,817
Financial services	54,061	1,394	1,412	54,079
Other business – diversified	49,639	491	2,366	51,514
Other consumer – diversified	54,720	266	3,275	57,729
Total corporate securities	177,012	3,413	7,540	181,139
Redeemable preferred stocks:				
Other consumer – diversified	192	-	-	192
Total redeemable preferred stocks	192	-	-	192
Total fixed maturities	217,848	3,976	8,556	222,428
Equity securities:				
Common and non-redeemable preferred stocks:				
Utilities and telecom	1,434	470	-	964
Financial services	5,500	716	-	4,784
Other business – diversified	299	252	-	47
Other consumer – diversified	11,703	6,580	-	5,123
Total equity securities	18,936	8,018	-	10,918
Other invested assets	5,663	-	-	5,663
Policy loans	2,105	-	-	2,105
Real estate	38	-	-	38
Investments in unconsolidated trusts	1,238	-	-	1,238
Total investments	$245,828	$ 11,994	$ 8,556	$242,390

Table of Contents

	December 31, 2017			
	Carrying Value	Gross Unrealized Gains	Gross Unrealized Losses	Cost or Amortized Cost
Fixed maturities:				
Bonds:				
U.S. Treasury securities and obligations of U.S. Government agencies and authorities	$31,155	$ 149	$ 511	$31,517
Obligations of states and political subdivisions	10,809	630	1	10,180
Corporate securities:				
Utilities and telecom	21,882	1,709	130	20,303
Financial services	53,686	2,049	453	52,090
Other business – diversified	44,184	1,024	1,349	44,509
Other consumer – diversified	53,200	924	1,477	53,753
Total corporate securities	172,952	5,706	3,409	170,655
Redeemable preferred stocks:				
Other consumer – diversified	192	-	-	192
Total redeemable preferred stocks	192	-	-	192
Total fixed maturities	215,108	6,485	3,921	212,544
Equity securities:				
Common and non-redeemable preferred stocks:				
Utilities and telecom	1,588	624	-	964
Financial services	5,634	851	-	4,783
Other business – diversified	297	250	-	47
Other consumer – diversified	15,836	10,712	-	5,124
Total equity securities	23,355	12,437	-	10,918
Other invested assets	5,626	-	-	5,626
Policy loans	2,146	-	-	2,146
Real estate	38	-	-	38
Investments in unconsolidated trusts	1,238	-	-	1,238
Total investments	$247,511	$ 18,922	$ 3,921	$232,510

Bonds having an amortized cost of $11,209 and $11,178 and included in the tables above were on deposit with insurance regulatory authorities at March 31, 2018 and December 31, 2017, respectively, in accordance with statutory requirements.

The carrying value and amortized cost of the Company’s investments in fixed maturities at March 31, 2018 and December 31, 2017 by contractual maturity were as follows. Actual maturities may differ from contractual maturities because issuers may call or prepay obligations with or without call or prepayment penalties.

	March 31, 2018		December 31, 2017	
	Carrying Value	Amortized Cost	Carrying Value	Amortized Cost
Due in one year or less	$1,498	$1,502	$1,653	$1,655
Due after one year through five years	16,936	17,402	13,738	14,056
Due after five years through ten years	127,271	130,853	112,847	112,116
Due after ten years	53,646	53,539	67,328	64,928
Varying maturities	18,497	19,132	19,542	19,789
Totals	$217,848	$222,428	$215,108	$212,544

Table of Contents

The following tables present the Company's unrealized loss aging for securities by type and length of time the security was in a continuous unrealized loss position as of March 31, 2018 and December 31, 2017.

	March 31, 2018					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government agencies and authorities	$15,379	$ 445	$ 12,018	$ 521	$27,397	$ 966
Obligations of states and political subdivisions	4,029	50	-	-	4,029	50
Corporate securities	97,572	4,118	29,050	3,422	126,622	7,540
Total temporarily impaired securities	$116,980	$ 4,613	$ 41,068	$ 3,943	$158,048	$ 8,556

	December 31, 2017					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government agencies and authorities	$12,175	$ 162	$ 12,737	$ 349	$24,912	$ 511
Obligations of states and political subdivisions	999	1	-	-	999	1
Corporate securities	40,108	653	32,667	2,756	72,775	3,409
Total temporarily impaired securities	$53,282	$ 816	$ 45,404	$ 3,105	$98,686	$ 3,921

The evaluation for an other than temporary impairment is a quantitative and qualitative process, which is subject to risks and uncertainties in the determination of whether declines in the fair value of investments are other than temporary. Potential risks and uncertainties include, among other things, changes in general economic conditions, an issuer's financial condition or near term recovery prospects and the effects of changes in interest rates. In evaluating a potential impairment, the Company considers, among other factors, management's intent and ability to hold the securities until price recovery, the nature of the investment and the expectation of prospects for the issuer and its industry, the status of an issuer's continued satisfaction of its obligations in accordance with their contractual terms, and management's expectation as to the issuer's ability and intent to continue to do so, as well as ratings actions that may affect the issuer's credit status.