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ASSURANCEAMERICA CORP
Form 10QSB
November 15, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-QSB

(Mark one)

QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2004

TRANSITION REPORT UNDER SECTION 13 OR 15 (D) OF THE EXCHANGE ACT OF 1934 for the transition period from _____ to _____

Commission File Number: 0-06334

AssuranceAmerica Corporation
(Exact name of small business issuer as specified in its charter)

Nevada
(State of Incorporation)

87-0291240
(IRS Employer ID Number)

5500 Interstate North Parkway, Suite 600
(Address of principal executive offices)

30328
(Zip Code)

(770) 952-0200
(Issuer's telephone number, including area code)

(Former name, former address and former fiscal year,
if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or 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

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 46,577,090 shares, \$.01 par value, as of November 1, 2004.

Transitional Small Business Disclosure Format (check one): Yes No

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements
AssuranceAmerica Corporation
(Unaudited) Consolidated Balance Sheets
September 30, 2004 and December 31, 2003

Assets	September 30, 2004 -----	December 31, 2003 -----
Short term investments	\$ 2,662,924	\$ 2,625,000
Cash and cash equivalents	6,613,965	3,130,553
Investment Income due and accrued	734	20,971
Receivable from insureds	5,020,292	4,332,942
Reinsurance recoverable (including \$2,791,055 and \$1,490,218 on paid losses)	9,911,830	4,639,626
Prepaid reinsurance premium	5,514,134	4,048,201
Deferred acquisition costs	213,928	124,505
Property and equipment (net of accumulated depreciation of \$1,054,162 and \$827,078)	913,201	1,035,975
Due from related party	30,783	30,783
Prepaid expenses	134,351	157,632
Intangibles (net of accumulated amortization of \$1,130,063 and \$1,097,563)	4,589,622	3,322,122
Security deposits	74,094	70,016
	-----	-----
Total assets	\$ 35,679,858 =====	\$ 23,538,326 =====
 Liabilities and equity		
Accounts payable and accrued expenses	\$ 2,378,341	\$ 2,036,386

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Unearned premium	8,156,616	5,861,591
Unpaid losses and loss adjustment expenses	10,214,306	4,499,152
Reinsurance payable	6,026,527	3,879,340
Provisional commission reserve	930,143	1,504,929
Long term debt, related party	6,521,378	7,043,378
Dividends payable	33,300	--
Capital lease obligations	91,600	91,600
	-----	-----
Total liabilities	34,352,211	24,916,376
Stockholders' equity		
Common stock, .01 par value (authorized 80,000,000, outstanding 46,577.090)	465,771	452,111
Preferred stock (authorized 5,000,000, outstanding 426,000)	4,260	--
Surplus-paid in	17,177,071	14,456,255
Accumulated deficit	(16,319,455)	(16,286,416)
	-----	-----
Total stockholders' equity	1,327,647	(1,378,050)
	-----	-----
Total liabilities and stockholders' equity	\$ 35,679,858	\$ 23,538,326
	=====	=====

See accompanying notes to consolidated financial statements

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ASSURANCEAMERICA CORP
(UNAUDITED) CONSOLIDATED STATEMENTS OF INCOME

Period ended September 30,	Three Month		2004
	2004	2003	
Revenue:			
Gross premiums written	\$7,188,610	\$5,827,181	\$23,525,816
Gross premiums ceded	(4,843,586)	(4,058,820)	(16,029,472)
Net premiums written	2,345,024	1,768,361	7,496,344
Decrease (increase) in unearned premiums, net of prepaid reinsurance premiums	83,844	(460,335)	(829,091)
Net premiums earned	2,428,868	1,308,026	6,667,253
Commission income	2,511,388	2,279,766	8,066,268
Managing general agent fees	844,069	629,965	2,536,996
Net investment income	6,741	5,988	17,794
Other fee Income	193,803	226,866	687,052
	-----	-----	-----
Total revenue	5,984,869	4,450,611	17,975,363
Expenses:			
Losses and loss adjustment expenses	1,790,091	1,064,345	5,122,048
Selling expenses	2,559,106	1,972,327	7,751,925
General and administrative expense	1,530,810	1,481,655	4,485,248
Depreciation and amortization expense	92,987	41,127	220,864

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Interest expense	144,683	130,000	428,317
Total operating expenses	6,117,677	4,689,454	18,008,402
Loss before provision for income tax expense	(132,808)	(238,843)	(33,039)
Income tax provision	--	--	--
Net loss	(132,808)	(238,843)	(33,039)
Dividends on preferred stock	(33,300)	--	(33,300)
Net loss attributable to common stockholders	(\$166,108)	(\$238,843)	(\$66,339)
Earnings per common share			
Basic	(0.004)	(0.005)	(0.001)
Diluted	(0.004)	(0.005)	(0.001)
Weighted average shares outstanding-basic	45,498,718	45,498,718	45,498,718
Weighted average shares outstanding-diluted	45,498,718	45,498,718	45,498,718

See accompanying notes to consolidated financial statements

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AssuranceAmerica Corporation
(Unaudited) Consolidated Statement of Cash Flows

For the nine months ended September 30,	2004	2003
	-----	-----
Operating activities		
Net loss	(\$33,039)	(\$546,081)
Adjustments to reconcile net loss income to net cash provided by operating activities:		
Depreciation and amortization	220,864	158,159
Deferred acquisition costs	(89,423)	(160,335)
Prepaid expenses and other assets	19,203	(190,496)
Reinsurance recoverable	(5,272,204)	(2,594,351)
Prepaid reinsurance premiums	(1,465,933)	(4,008,429)
Unearned premiums	2,295,025	5,703,920
Unpaid loss and loss adjustment expense	5,715,154	2,327,031
Other liabilities	(232,831)	803,983
Receivable from insureds	(687,350)	(4,031,164)
Reinsurance payable	2,147,187	3,942,817
Net cash provided by operating activities	2,616,653	1,405,054
Investing activities		
(Acquisitions)/Disposals	(1,300,000)	--
Investment income due and accrued	(17,687)	(18,031)
(Purchase)/disposal of fixed assets	(65,590)	(399,987)
Purchase of short term investments	--	(2,625,000)

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Net cash used by investing activities	(1,383,277)	(3,043,018)
	-----	-----
Financing activities		
Capital Contribution	2,090,536	74,223
Payment of accrued interest	(700,000)	--
Note payable, related party	178,000	3,340,454
	-----	-----
Common stock issued	681,500	--
	-----	-----
Net cash provided by financing activities	2,250,036	3,414,677
	-----	-----
Net change in cash	3,483,412	1,776,713
Cash beginning of period	3,130,553	477,197
	-----	-----
Cash end of period	\$6,613,965	\$2,253,910
	=====	=====

See accompanying notes to consolidated financial statements

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ASSURANCEAMERICA CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE A - THE COMPANY AND BASIS OF PRESENTATION

AssuranceAmerica Insurance Company ("Carrier"), AssuranceAmerica Managing General Agency, LLC ("MGA") Trustway Insurance Agencies, LLC ("Agencies"), each indirect wholly-owned subsidiaries of AssuranceAmerica Corporation, a Nevada corporation (the "Company"), were organized to solicit, underwrite, and retain risks associated with private passenger nonstandard automobile insurance.

The accompanying unaudited, consolidated, financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated. These unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and in accordance with the instructions to Form 10-QSB for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, such statements include all adjustments (consisting of normally recurring accruals) considered necessary for fair presentation. Operating results for the quarter and nine months ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. For further information refer to the financial statements and footnotes thereto included in the Company's Form 10-KSB for the year ended December 31, 2003. Footnote disclosures, which would substantially duplicate the disclosure contained in those documents, have been omitted.

Net income per share is computed in accordance with SFAS No. 128 "Earnings per Share."

Contingencies

In the normal course of business, the Company is named as a defendant in lawsuits related to claims and other insurance policy issues. Some of the

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actions request extra-contractual and/or punitive damages. These actions are vigorously defended unless a reasonable settlement appears appropriate. In the opinion of management, the ultimate outcome of litigation is not expected to be material to the Company's financial condition, results of operations, or cash flows.

Income Recognition

Commission income is generally recognized on the effective date of the policies. Commissions on premiums billed and collected directly by insurance companies are recorded as revenue when received. Premium adjustments, including policy cancellations, are recorded as they occur. An estimated reserve is carried for income that will not be earned due to anticipated policy cancellations.

Recognition of Premium Reserves

Property and liability premiums are generally recognized on a pro rata basis over the policy term. The portion of premiums that will be earned in the future are deferred and reported as unearned premiums.

Deferred Policy Acquisition Costs

Commissions and other costs of acquiring insurance that vary with and are primarily related to the production of new and renewal business, less ceding commissions allowed by reinsurers, are deferred and charged or credited to earnings proportionate to premiums earned. Historical and current loss and loss adjustment expense experience are considered in determining the recoverability of deferred policy acquisition costs.

Start-Up Costs

Start-up costs are expensed when incurred.

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Property and Equipment

Items capitalized as property and equipment are carried at historical cost. Depreciation is computed over the estimated useful lives of the assets using straight-line and accelerated methods. Depreciation expense was approximately \$60,000 and \$41,000 for the three months ended September 30, 2004 and 2003, respectively and \$188,000 and \$158,000 for the nine months ended September 30, 2004 and 2003 respectively.

Improvements, additions and major renewals which extend the life of an asset are capitalized. Repairs are expensed in the year incurred.

Amortization of Intangible Assets

Intangible assets consist of noncompetition agreements and goodwill. Intangible assets are stated at cost. Effective January 1, 2002, the Company adopted the Financial Accounting Standards Board ("FASB")'s Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets". SFAS 142 requires that goodwill and certain intangibles with indefinite lives no longer be amortized, but instead be tested for impairment at least annually. Amortization expense for the three months ending September 30, 2004 and 2003 was \$32,000 and -0- respectively and \$32,000 and -0- for the nine months ended September 30, 2004 and 2003 respectively.

Cash Flows

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For the purpose of the statements of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of twelve months or less to be cash and cash equivalents.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of 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 period. Actual results could differ from those estimates.

Some material estimates that are particularly sensitive are:

Return commission incurred on policies originated by MGA and Agencies - The Company has calculated a provision for return commission due to cancellation of policies before all premiums written are fully earned. This estimate is based on past Company history.

The Company maintains a liability for unpaid losses and loss adjustment expense based on management's estimate of the ultimate cost to settle claims currently in process. In addition a reserve for claims that have occurred but have not been reported is also carried as a liability. The ultimate costs to settle these claims may vary from the current estimates. The Company does not discount the liability for unpaid losses and loss adjustment expense.

Advertising Costs

Advertising costs are expensed as incurred.

Concentration of Risk

The Company operates in Florida, Georgia and South Carolina and is dependent upon the economy in those states. Automobiles insured through the Carrier are principally in South Carolina and Georgia. Premium increases generally must be approved by state insurance commissioners.

Income taxes

The Company files a consolidated federal income tax return. The tax liability of the group is apportioned among the members of the group in accordance with the ratio, which that portion of the consolidated taxable income attributable to each member of the group having taxable income bears to the consolidated income.

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Each entity within the consolidated group calculates its own tax provision and is directly responsible for its own tax benefits and/or expense.

The Company has loss carry-forwards that may be offset against future taxable income and tax credits that may be used against future income taxes. If not used, the carry-forwards will expire between now and December 31, 2022. The loss carry-forwards at December 31, 2003 were approximately \$2,710,000 and are subject to limitations each year under Section 382 of the Internal Revenue Code. After the Company's merger with AssuranceAmerica Corporation, a Georgia corporation, the Company had a net operating loss for the nine months ended December 31, 2003 of approximately \$1,220,000. There was no benefit recorded for the quarter due to management's uncertainty as to the realization of the net

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operating loss.

As a result of the net operating loss carry-forwards, the Company had a deferred tax asset of approximately \$575,000 with a 100% valuation allowance for the quarter ended September 30, 2004. The Company has established the valuation allowance for its net deferred tax assets due to the uncertainty regarding the realization of these deferred income tax assets.

Stock Based Compensation

Under the Company's 2000 Stock Option Plan, the aggregate number of common shares authorized is currently 5,000,000. As of September 30, 2004, the Company had issued options to purchase an aggregate of 2,882,918 shares of common stock. Prior to the merger with AssuranceAmerica Corporation, a Georgia corporation, the Company had issued options to purchase 948,918 shares of common stock and AssuranceAmerica had issued options to purchase 1,300,000 shares of common stock. In connection with such merger, the outstanding options to purchase shares of AssuranceAmerica common stock were exchanged on a one-for-one basis for options to purchase shares of the Company's common stock under the Company's 2000 Stock Option Plan. The weighted-average exercise price for all options outstanding at September 30, 2004 is \$1.61.

The Company has adopted SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"). The provisions of SFAS 123 allow companies to either expense the estimated fair value of employee stock options or to continue to follow the intrinsic value method set forth in Accounting Principles Board ("APB") Option No.25, "Accounting for Stock Issued to Employees" ("APB No. 25"), but disclose the pro forma effects on net income had the fair value of the options been expensed. The Company has elected to apply APB No.25 in accounting for its employee stock option plan.

	For the three months ending September 30,		For the nine months ending September 30,	
	2004	2003	2004	2003
Net income (loss) as reported	\$(132,808)	\$(238,843)	\$ (33,039)	\$(546,081)
Compensation effect	(21,131)	(10,686)	(63,393)	(32,060)
Pro forma net income (loss)	\$(153,939)	\$(249,529)	\$ (96,432)	\$(578,141)

The weighted average fair value of options granted during the nine months ended September 30, 2004, estimated on the date of grant using the Black-Scholes option-pricing model, was \$0.3214. The weighted average fair value of options granted during 2003, estimated on the date of grant using the Black-Scholes option-pricing model, was \$0.1607. The fair value of options granted is estimated on the date of grant using the following assumptions:

	September 30, 2004	December 31, 2003
Expected volatility	80%	80%
Risk-free interest rate	1.5%	1.5%
Expected life (in years)	5.0	5.0

Reclassifications

Certain reclassifications have been made to the 2003 financial statements to conform to the 2004 presentation.

Related Party Transactions

The Company has issued certain unsecured promissory notes payable to Guy W. Millner, the Chairman of the Company's Board of Directors, and Lawrence (Bud) Stumbaugh, the Company's President and Chief Executive Officer. The promissory notes accrue interest at a rate of 8.0% per annum. As of September 30, 2004, the amount of outstanding principal and accrued interest under such promissory notes totaled approximately \$6.3 million. The promissory notes provide for the repayment of principal beginning in December 2004 in an amount equal to the greater of \$1.0 million or an amount equal to 25% of the Company's net income after tax, plus non-cash items, less working capital. However, the promissory notes also permit the Company to postpone any and all payments under the promissory notes without obtaining the consent of, and without giving notice or paying additional consideration. In addition, as part of the purchase agreement of Thomas-Cook Holding Company, the Company issued a promissory note in the amount of \$178,000 with annual installments beginning August 1, 2005, and carrying an interest rate of 8%. Thomas-Cook Holding Company's sole shareholder is James C. Cook. As part of the transaction Mr. Cook agreed to be employed by the company as President of Agencies.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

The following discussion and analysis should be read in conjunction with the consolidated financial statements and notes thereto included as Item 1 of this report. This document contains "forward-looking statements" relating to future events or the Company's future financial performance within the meaning of Section 21E of the Securities Exchange Act of 1934 and that are intended to be covered by the safe harbor created thereby. These forward-looking statements are based on the beliefs of management as well as assumptions made by and information currently available to management. These statements contain the words "anticipate", "believe," "expect" and words or phrases of similar import, as they relate to the Company or management. You should be aware that these "forward-looking" statements are subject to certain risks, uncertainties and assumptions related to certain factors including, without limitation, risks relating to the significant competitive pressures that the Company faces, the extensive governmental regulation of the Company's business, the availability of reinsurance, the Company's limited experience in underwriting nonstandard automobile insurance, the Company's ability to respond to future business opportunities and other risks and difficulties generally experienced by growth stage businesses. The Company undertakes no obligation to update these forward-looking statements.

On April 1, 2003, a wholly-owned subsidiary of the Company merged with and into AssuranceAmerica Corporation, a Georgia corporation ("AAC"), a property and casualty-oriented holding company, focusing on the nonstandard automobile insurance markets. As a result of the merger, AAC became the surviving subsidiary of the Company. Following the merger, the Company has three operating entities, each of which is a wholly-owned subsidiary of AAC: Agencies, which owns 30 independent agencies located primarily in Florida, writing nonstandard automobile insurance, MGA, which writes nonstandard automobile insurance in Georgia and South Carolina, and Carrier, which underwrites the business written by MGA and is licensed in South Carolina, Georgia and Arkansas. Carrier commenced operations in April 2003.

Financial Condition

Investments and cash as of September 30, 2004 increased \$3.5 million compared to

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December 31, 2003. On June 30, 2004, the Company issued 240,000 shares of its Series A Convertible Preferred Stock for an aggregate consideration of \$1.2 million. On August 13, 2004, the Company issued an additional 186,000 of Series A Convertible Preferred Stock for \$930,000. The Series A Convertible Stock pays a semi-annual dividend of \$0.20 per share. The Company's investments are currently in money market accounts and bank Certificates of deposit. Other than the securities of its wholly owned subsidiaries, the Company has no investment in equity securities as of September 30, 2004.

Receivables from insureds as of September 30, 2004 increased approximately \$687,000 or 16% compared to December 31, 2003. The increase results from Carrier's increase in written premiums over the past nine months.

Prepaid reinsurance premiums as of September 30, 2004 increased \$1.5 million or 36%, compared to December 31, 2004. This amount represents premiums ceded by Carrier to its reinsurer that have not been fully earned. The increase results from an increase in Carrier's written premium over the past nine months.

Reinsurance recoverables as of September 30, 2004, increased by approximately \$5.3 million compared to December 31, 2003. The amount represents loss and loss adjustments expense, both paid and reserved, due from Carrier's reinsurer. The increase is the result of increasing loss and loss adjustment expense incurred by Carrier.

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Intangibles, net of accumulated amortization, increased \$1.3 million as the result of the purchase of substantially all of the assets of Thomas-Cook Holding Company.

Accounts payable and accrued expense as of September 30, 2004, increased approximately \$342,000 compared to December 31, 2003. The increase is primarily related to the accrual of agent's commission in MGA.

Unearned premiums as of September 30, 2004, increased \$2.3 million compared to December 31, 2003. The amount represents premiums written by Carrier which have not been earned and the increase is the result of an increase in written premium.

Unpaid losses and loss adjustments expense as of September 30, 2004, increased \$5.7 million compared to December 31, 2003. The amount represents reserves for losses and loss adjustments expense for claims that have been reported and incurred as well as a reserve for claims incurred but not reported. The increase is the result of a significant increase in Carrier's claim activity.

Reinsurance payables as of September 30, 2004 increased \$2.1 million compared to December 31, 2003. The increase is the result on increase in Carrier's written premium and represents amounts due its reinsurer under a 70% quota share reinsurance treaty.

Provisional commission reserve as of September 30, 2004 decreased \$575,000 compared to December 31, 2003. MGA/Carrier receives a provisional commission from Carrier's reinsurer based on written premium and is adjusted based on loss and loss adjustment expense ratios. MGA/Carrier book the difference between the minimum and provisional commissions as a liability. The decrease is the result of the return of a portion of the provisional commission.

Long term debt as of September 30, 2004 decreased \$522,000 compared to December 31, 2003. The decrease results from payment of \$700,000 to the Company's Chairman related to the promissory note payable to him. In addition, as the

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result of the purchase of Thomas-Cook Holding Company, the Company issued a promissory note in the amount of \$178,000.

Liquidity and Capital Resources

Net cash provided by operating activities for the nine month period ended September 30, 2004 was approximately \$2.6 million compared to \$1.4 million for the same period in 2003. The increase is primarily related to Carrier beginning operations in April 2003 resulting in only six months of operating activity in 2003 compared to nine months in 2004.

Investing activities for the nine months ended September 30, 2004 consisted primarily of the purchase of substantially all of the assets of Thomas-Cook Holding Company.

Financing activities for the nine month period ended September 30, 2004 included payments of accrued interest of \$700,000 to the Company's Chairman and the issuance of preferred stock resulting in additional capital of approximately \$2.1 million.

The Company's liquidity and capital needs have been met in the past through premium, commission and fee income and debt from its Chairman and President. The Company's debt consists of unsecured promissory notes payable to its Chairman and President. The promissory notes carry an interest rate of 8% per annum and provide for the repayment of principal beginning in December 2004 in an amount equal to the greater of \$1.0 million or an amount equal to 25% of the Company's net income after tax, plus non-cash items less working capital.

On June 30, 2004, the Company closed on an initial capital raise of approximately \$1.2 million through a private placement of equity. The Company issued 240,000 shares of Series A Preferred Stock with a semi-annual dividend of \$0.20 per share. The Company issued an additional 186,000 shares of Series A Preferred on August 13, 2004.

The growth of the Company has and will continue to strain its liquidity and capital resources. Carrier is required by the state of South Carolina to maintain minimum Capital and Surplus of \$3.0 million. As of September 30, 2004, Carrier's Capital and Surplus was approximately \$3.7 million.

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Results of Operations

The Company's net loss for the three months ended September 30, 2004 was \$133,000 compared to a net loss of \$238,000 for the same period in 2003. MGA had a net loss of \$93,000 for the three month period ending September 30, 2004 compared to a net loss of \$280,000 for the same period in 2003. MGA's improvement is the result of higher premium written for the three month period generating a 13% increase in revenue with only a 4% increase in expenses. Carrier had a pre-tax profit of \$204,000 for the three month period ending September 30, 2004 compared to a \$14,000 pre-tax profit for the same period in 2003. Carrier's improvement is the result of an improvement in its loss and loss adjustment expense ratio from 81.3% in 2003 to 73.7% in the three month period ending September 30, 2004. Agencies had a net loss of \$316,000 for the three month period ending September 30, 2004 compared to a pre-tax profit of \$35,000 for the same period in 2003. Agencies results were affected by the opening of four new offices which have not yet generated revenues sufficient to cover their expenses. In addition, the hurricane activity during September caused the closing of several locations for a number of days resulting in a decline in revenue for the period.

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	For the nine months ended September 30,	
	2004	2003
MGA revenue	\$ 8,006,361	\$ 7,000,798
MGA expense	7,903,733	7,863,691
MGA pre-tax income (loss)	\$ 102,628	\$ (862,893)
Carrier revenue	\$ 7,273,188	\$ 2,139,042
Carrier expense	7,016,274	2,262,111
Carrier pre-tax income (loss)	\$ 256,914	\$ (123,069)
Agencies revenue	\$ 5,032,947	\$ 4,788,940
Agencies expense	5,504,253	4,484,782
Agencies pre-tax income (loss)	\$ (471,306)	\$ 304,158
GAAP adjustment & intercompany elimination	78,725	135,723
Net loss	\$ (33,039)	\$ (546,081)

Net premiums written for the three and nine month periods ended September 30, 2004 increased 33% and 110% respectively. Net premiums written are premiums written by Carrier after deducting premiums ceded to its reinsurer pursuant to the reinsurance agreement. Carrier began operations in April 2003 and therefore recorded no premium for the first three months of 2003.

Net premiums earned for the three and nine month periods ended September 30, 2004 increased significantly compared to the corresponding periods in 2003. Premiums written are earned over the life of the policy, typically six months, and net earned premium represents Carrier's portion, net of reinsurance, of the net premiums written less the increase in unearned premiums.

Commission income for the three and nine month periods ended September 30, 2004 increased 10% and 6% respectively. MGA and Agencies received commissions from the carrier whose policies they sell. Commission rates vary between carriers and are applied to written premium to determine commission income.

Managing general agent fees increased 34% and 29% for the three and nine month periods ended September 30, 2004 compared to 2003 respectively. The increase in fees is the result of an increase in the number of policies sold and an increase in retention rate.

Other fee income decreased 15% for the three month period ended September 30, 2004 compared to the same period in 2003. For the nine month period ending September 30, 2004, other fee income increased 17% compared to the same period in 2003. Agencies collect fees for various services performed and for additional products sold to insureds. Hurricane activity in the state of Florida during September 2004 caused the closing of several offices for a number of days resulting in a decline in fee income. In addition, Agencies have begun to write more direct bill policies which have a lower potential for fee income.

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Losses and loss adjustment expense increased significantly for the three and nine month periods ended September 30, 2004 as compared to 2003. Carrier began operations in April 2003 and therefore had relatively few losses reported by insureds during its early months of operations. Carrier's loss and loss adjustment expense ratio for the three and nine month periods ended September 30, 2004 was 73.7% and 76.8% respectively. The ratios for the corresponding periods in 2003 was 81.3% and 81.2%.

Selling expenses increased 30% and 19% for the three and nine month periods ended September 30, 2004 compared to the same periods in 2003. Increases are the result of increases in written premiums for both Agencies and MGA.

General and administrative expense increased 3% and 11% for the three and nine month periods ended September 30, 2004 compared to the same periods in 2003. Generally the increases are the result of moderate increases in the Company's general operating expenses.

Interest expense increased 11% for the three month and 10% for the nine month periods ended September 30, 2004 compared to corresponding periods in 2003. The majority of the increase resulted from interest charged on interest expense accrued but not paid in 2003.

Market Risk

Market risk is the risk of loss from adverse changes in market prices and interest rates. Currently, the Company's investments are in money market accounts and bank certificates of deposit, both of which minimize market risk.

ITEM 3. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures in accordance with Rule 13a-15 under the Securities Exchange Act of 1934 (the "Exchange Act"). Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective for gathering, analyzing and disclosing the information that the Company is required to disclose in the reports it files under the Exchange Act, within the time periods specified in the SEC's rules and forms. The Company's Chief Executive Officer and Chief Financial Officer also concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company required to be included in its periodic SEC filings.

There have been no significant changes in the Company's internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES

On August 13, 2004, the Company sold 186,000 shares of its Series A Preferred Stock to Heritage Assurance Partners, LP ("Heritage") for \$930,000 in cash. Each share of Series A Preferred Stock is convertible into shares of common stock, at the option of the holder thereof, at any time. Each share of Series A Preferred Stock is convertible into the number of shares of common stock that results from dividing the "Conversion Value" per share by the "Conversion Price" per share in effect at the time of conversion. The number of shares of common stock into

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which a share of Series A Preferred Stock is convertible is referred to as the "Conversion Rate." The Conversion Price per share of Series A Preferred Stock initially in effect is \$0.50 and the Conversion Value per share of Series A Preferred Stock initially in effect is equal to \$5.00. The initial Conversion Price of Series A Preferred Stock is subject to adjustment in the event of issuances of common stock or securities convertible into common stock for consideration per share less than the Conversion Price in effect immediately prior to such issuance. All accrued and unpaid dividends owed to a holder of Series A Preferred Stock may be converted into a number of shares of common stock equal to the aggregate amount of such accrued but unpaid dividends owed such holder, divided by \$0.50.

Each share of Series A Preferred Stock will automatically convert into shares of common stock at its then effective

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Conversion Rate on August 13, 2006. Each share of Series A Preferred Stock will automatically convert into shares of common stock at its then effective Conversion Rate immediately prior to the closing of any public offering pursuant to an effective registration statement under the Securities Act of 1933, as amended, covering any of the Company's equity securities with aggregate proceeds to the Company, at the public offering price, of at least \$20 million, before underwriting commissions and expenses, and at a per share price of at least three times the then-current Conversion Price.

The Company issued the Series A Preferred Stock in reliance on the exemption from registration contained in Section 4(2) of the Securities Act of 1933, as amended.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.

- 31.1 Certification of the Company's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Company's Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K.

- 1. 8K dated August 13, 2004
- 2. 8K dated September 14, 2004
- 3. 8K dated October 15, 2004

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ASSURANCEAMERICA CORPORATION

By: /s/ Lawrence Stumbaugh

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Lawrence Stumbaugh
President and CEO

Dated: November 15, 2004

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