

ASSURANCEAMERICA CORP

Form 10-Q

November 14, 2008

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-Q**

(Mark one)

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

For the quarterly period ended September 30, 2008

TRANSITION REPORT PURSUANT TO 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 smaller reporting company as specified in its charter)

Nevada
(State of Incorporation)

87-0281240
(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)

Check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the preceding 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

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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

There were 64,953,881 shares of the Registrant's \$.01 par value Common Stock outstanding as of November 8, 2008.

ASSURANCEAMERICA CORPORATION
Index to Form 10-Q

	Page
<u>PART I FINANCIAL INFORMATION</u>	
<u>Item 1 Financial Statements</u>	
<u>Consolidated Balance Sheets as of September 30, 2008 and December 31, 2007</u>	3
<u>Consolidated Statements of Operations for the Three Months and Nine Months Ended September 30, 2008 and September 30, 2007</u>	4
<u>Consolidated Statements of Comprehensive Income for the Three Months and Nine Months Ended September 30, 2008 and September 30, 2007</u>	5
<u>Consolidated Statements of Cash Flows for Nine Months ended September 30, 2008 and September 30, 2007</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
<u>Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	14
<u>Item 3 Quantitative and Qualitative Disclosures about Market Risk</u>	18
<u>Item 4 Controls and Procedures</u>	20
<u>PART II OTHER INFORMATION</u>	
Item 1 - Legal Proceedings	N/A
<u>Item 1 - A Risk Factors</u>	20
<u>Item 2 - Unregistered Sales of Equity Securities</u>	26
Item 3 - Defaults Upon Senior Securities	N/A
Item 4 - Submission of Matters to A Vote of Security Holders	N/A
Item 5 - Other Information	N/A
<u>Item 6 - Exhibits</u>	27
<u>Signatures</u>	28
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32.1</u>	

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements**

ASSURANCEAMERICA CORPORATION
CONSOLIDATED BALANCE SHEETS
September 30, 2008 and December 31, 2007

	September 30, 2008 (Unaudited)	December 31, 2007 (Audited)
Assets		
Cash and cash equivalents	\$ 4,605,317	\$ 5,511,842
Short-term investments	650,849	642,924
Long-term investments, available for sale at fair value	8,048,731	14,838,738
Marketable equity securities	2,315,562	2,563,040
Other securities	155,000	155,000
Investment income due and accrued	133,719	158,981
Receivable from insureds	31,732,984	28,802,125
Reinsurance recoverable (including \$14,428,845 and \$6,077,396 on paid losses)	41,174,765	29,327,012
Prepaid reinsurance premiums	23,814,634	21,145,161
Deferred acquisition costs	2,431,606	2,130,323
Property and equipment (net of accumulated depreciation of \$3,382,440 and \$2,737,288)	2,706,630	2,360,747
Other receivables	3,760,538	2,966,287
Prepaid expenses	1,079,115	861,588
Intangibles (net of accumulated amortization of \$2,559,414 and \$2,240,233)	11,104,655	11,368,383
Security deposits	94,687	86,438
Prepaid income tax	479,949	148,677
Deferred tax assets	2,182,449	1,824,453
Other assets	351,710	361,419
Total assets	\$ 136,822,900	\$ 125,253,138
Liabilities and stockholders equity		
Accounts payable and accrued expenses	\$ 9,208,051	\$ 7,184,132
Unearned premium	34,103,588	30,991,565
Unpaid losses and loss adjustment expenses	38,468,909	33,660,814
Reinsurance payable	30,194,813	25,174,138
Provisional commission reserve	2,971,594	2,963,308
Notes payable, related party	1,996,967	4,482,862
Junior subordinated debentures payable	4,973,518	4,968,519
Total liabilities	121,917,440	109,425,338
Commitments and contingencies		
Stockholders equity		
Common stock, .01 par value (authorized 120,000,000, outstanding 64,953,881 and 64,803,881)	649,539	648,039

Edgar Filing: ASSURANCEAMERICA CORP - Form 10-Q

Surplus-paid in	16,904,933	16,782,588
Accumulated deficit	(2,058,751)	(1,673,332)
Accumulated other comprehensive income:		
Net unrealized gains (losses) on investment securities, net of taxes	(590,261)	70,505
Total stockholders equity	14,905,460	15,827,800
Total liabilities and stockholders equity	\$ 136,822,900	\$ 125,253,138

See accompanying notes to consolidated financial statements.

3

Table of Contents

ASSURANCEAMERICA CORPORATION
(Unaudited) CONSOLIDATED STATEMENTS OF OPERATIONS
For the Three and Nine Months Ended September 30, 2008 and 2007

	Three Months		Nine Months	
	Ended September 30,		Ended September 30,	
	2008	2007	2008	2007
Revenue:				
Gross premiums written	\$ 22,168,416	\$ 21,535,015	\$ 71,336,281	\$ 69,964,867
Gross premiums ceded	(15,263,051)	(14,553,205)	(49,304,392)	(47,230,864)
Net premiums written	6,905,365	6,981,810	22,031,889	22,734,003
Decrease (Increase) in unearned premiums, net of prepaid reinsurance premiums	473,519	(185,972)	(442,549)	(3,985,676)
Net premiums earned	7,378,884	6,795,838	21,589,340	18,748,327
Commission income	5,117,743	4,498,414	16,501,325	16,302,203
Managing general agent fees	2,962,309	2,871,324	9,080,139	8,109,556
Net investment income	159,597	209,132	549,410	602,935
Net investment gains (losses) on securities	(92,312)	(9,573)	(149,035)	16,666
Other fee income	112,680	49,578	370,298	297,794
Total revenue	15,638,901	14,414,713	47,941,477	44,077,481
Expenses:				
Losses and loss adjustment expenses	6,360,258	4,726,493	17,494,409	13,593,464
Selling, general and administrative expenses	9,713,440	9,021,080	29,434,351	27,003,762
Stock option expense	527	110,888	42,346	329,000
Depreciation and amortization expense	325,933	256,016	964,781	904,665
Interest expense	154,074	255,785	569,010	775,161
Total operating expenses	16,554,232	14,370,262	48,504,897	42,606,052
Income (loss) before provision for income tax expense	(915,331)	44,451	(563,420)	1,471,429
Income tax provision (benefit)	(296,845)	89,942	(178,001)	752,777
Net income (loss) before minority interest	(618,486)	(45,491)	(385,419)	718,652
Minority interest		(1,971)		2,655
Net income (loss)	\$ (618,486)	\$ (43,520)	\$ (385,419)	\$ 715,997
Earnings per common share				
Basic	\$ (0.009)	\$ (0.001)	\$ (0.006)	\$ 0.012
Diluted	\$ (0.009)	\$ (0.001)	\$ (0.006)	\$ 0.012
Weighted average shares outstanding-basic	64,941,381	64,731,908	64,911,655	60,939,646
Weighted average shares outstanding-diluted	64,941,381	65,475,724	64,911,655	61,732,488

See accompanying notes to consolidated financial statements.

Table of Contents

ASSURANCEAMERICA CORPORATION AND SUBSIDIARIES
(Unaudited) CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the Three and Nine Months Ended September 30, 2008 and 2007

	Three Months		Nine Months	
	Ended September 30,		Ended September 30,	
	2008	2007	2008	2007
Net income (loss)	\$ (618,486)	\$ (43,520)	\$ (385,419)	\$ 715,997
Other comprehensive income (loss):				
Change in unrealized gains (losses) of investments arising during the period	(568,256)	215,191	(1,206,261)	12,605
Reclassification adjustment for realized losses (gains) recognized during the year	92,312	9,573	149,035	(16,666)
Net change in unrealized (losses) gains	(475,944)	224,764	(1,057,226)	(4,061)
Deferred tax (loss) benefit on above changes	178,479	(84,287)	396,460	1,523
Other comprehensive losses	(297,465)	140,477	(660,766)	(2,538)
Comprehensive income (loss)	\$ (915,951)	\$ 96,957	\$ (1,046,185)	\$ 713,459

See accompanying notes to consolidated financial statements.

Table of Contents

ASSURANCEAMERICA CORPORATION
(Unaudited) CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Nine Months Ending September 30, 2008 and 2007

	Nine Months Ended	
	September 30,	
	2008	2007
Cash flows from operating activities:		
Net income (loss)	\$ (385,419)	\$ 715,997
Adjustments to reconcile net income to net cash provided by operating activities:		
Net investment losses (gains) on securities	149,035	(16,666)
Depreciation and amortization	964,781	909,663
Stock-based compensation options	42,348	329,000
Stock-based compensation director fees	81,500	116,600
Deferred tax provision	38,464	442,563
Changes in assets and liabilities:		
Investment income due and accrued	25,262	(82,494)
Receivables	(3,731,831)	(13,855,635)
Prepaid expenses and other assets	(216,067)	(97,242)
Unearned premiums	3,112,023	12,298,713
Unpaid loss and loss adjustment expenses	4,808,095	5,847,610
Ceded reinsurance payable	5,020,675	12,808,182
Reinsurance recoverable	(11,847,753)	(9,446,962)
Prepaid reinsurance premiums	(2,669,473)	(8,313,037)
Accounts payable and accrued expenses	2,023,919	2,962,225
Prepaid income taxes	(331,272)	303,187
Deferred acquisition costs	(301,283)	(1,117,101)
Provisional commission reserve	8,286	314,534
Net cash provided by operating activities	(3,208,710)	4,119,137
Cash flows from investing activities:		
Purchases of property and equipment, net	(998,615)	(548,839)
Proceeds from sales, call and maturities of investments	10,570,879	1,433,650
Purchases of investments	(4,734,320)	(5,898,942)
Cash paid for acquisition of agencies, net of cash acquired	(55,200)	(400,000)
Net cash provided (used) by investing activities	4,782,744	(5,414,131)
Cash flows from financing activities:		
Repayments of notes payable	(2,480,559)	(1,178,804)
Repayments on capital lease obligation		(64,759)
Net used provided by financing activities:	(2,480,559)	(1,243,563)
Net decrease in cash and cash equivalents	(906,525)	(2,538,557)
Cash and cash equivalents, beginning of period	5,511,842	8,185,539

Cash and cash equivalents, end of period	\$ 4,605,317	\$ 5,646,982
---	--------------	--------------

See accompanying notes to consolidated financial statements.

6

Table of Contents

ASSURANCEAMERICA CORPORATION AND SUBSIDIARIES
Notes to Consolidated Financial Statements
September 30, 2008 and 2007

(1) Description of Business

AssuranceAmerica Corporation, a Nevada corporation (the Company) is an insurance holding company whose business is comprised of AssuranceAmerica Insurance Company (AAIC), AssuranceAmerica Managing General Agency, LLC (MGA) and TrustWay Insurance Agencies, LLC (TrustWay), each wholly-owned. The Company solicits and underwrites nonstandard private passenger automobile insurance. The Company is headquartered in Atlanta, Georgia.

(2) Summary of Significant Accounting Policies

Basis of Consolidation and Presentation

The accompanying unaudited consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Such financial statements do not include all of the information and disclosures required by GAAP for complete financial statements. In our opinion, all adjustments (consisting solely of normal recurring accruals) necessary for a fair presentation have been included in the accompanying financial statements. Certain items in prior period financial statements have been reclassified to conform to the current presentation. For further information, please refer to our audited consolidated financial statements appearing in the Form 10-K for the year ended December 31, 2007.

Estimates

A discussion of our significant accounting policies and the use of estimates is included in the notes to the consolidated financial statements included in the Company's Financial Statements for the year ended December 31, 2007 as filed with the Securities and Exchange Commission in the 2007 Form 10-K.

New Accounting Standards Adopted

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements (SFAS 157) which defines fair value, establishes a framework for measuring fair value, and expands disclosures about the information used to measure fair value. SFAS 157 applies whenever other accounting pronouncements require, or permit, assets or liabilities to be measured at fair value; it does not require any new fair value measurements. The adoption of SFAS 157 did not have a material impact on the results of operations or financial position of the Company (See Note 10 for required disclosures).

Effective January 1, 2008, the Company adopted SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No. 115 (SFAS 159) which permits entities to voluntarily choose to measure many financial instruments at fair value. The election is made on an instrument-by-instrument basis and is irrevocable. If the fair value is elected for an instrument, the statement specifies that entities report in earnings unrealized gains and losses at each subsequent reporting date. The Company did not elect the fair value option for any of its financial assets or liabilities.

(3) Losses and Loss Adjustment Expenses

The estimated liabilities for losses and loss adjustment expenses (LAE) include the accumulation of estimates for losses for claims reported prior to the balance sheet dates (case reserves), estimates (based upon actuarial analysis of historical data) of losses for claims incurred but not reported (IBNR) and for the development of case reserves to ultimate values, and estimates of expenses for investigating, adjusting and settling all incurred claims. Amounts reported are estimates of the ultimate costs of settlement, net of estimated salvage and subrogation. These estimated liabilities are subject to the outcome of future events, such as changes in medical and repair costs as well as economic and social conditions that impact the settlement of claims. Management believes that, given the inherent variability in any such estimates, the aggregate reserves are within a reasonable and acceptable range of adequacy. The methods of making such estimates and for establishing the resulting reserves are reviewed and updated quarterly and any resulting adjustments are reflected in current operations.

Table of Contents

A summary of unpaid losses and loss adjustment expenses, net of reinsurance ceded, is as follows:

	September 30, 2008	December 31, 2007
Case basis	\$ 4,077,396	\$ 4,200,577
IBNR	7,645,593	6,210,621
Total	\$ 11,722,989	\$ 10,411,198

(4) Reinsurance

In the normal course of business, the Company seeks to reduce its overall risk levels by obtaining reinsurance from other insurance enterprises or reinsurers. Reinsurance premiums and reserves on reinsured business are accounted for on a basis consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

Reinsurance contracts do not relieve the Company from its obligations to policyholders. The Company periodically reviews the financial condition of its reinsurers to minimize its exposure to losses from reinsurer insolvencies. Reinsurance assets include balances due from other insurance companies under the terms of reinsurance agreements. Amounts applicable to ceded unearned premiums, ceded loss payments and ceded claims liabilities are reported as assets in the accompanying balance sheets. The Company believes the fair value of its reinsurance recoverables approximates their carrying amounts.

The impact of reinsurance on the statements of operations for the three and nine-month periods ended September 30, 2008 and 2007 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Premiums written:				
Direct	\$ 21,948,630	\$ 21,145,204	\$ 70,425,262	\$ 68,784,027
Assumed	219,786	389,811	911,019	1,180,840
Ceded	15,263,051	14,553,205	49,304,392	47,230,864
Net	\$ 6,905,365	\$ 6,981,810	\$ 22,031,889	\$ 22,734,003
Premiums earned:				
Direct	\$ 23,344,385	\$ 20,348,021	\$ 67,111,079	\$ 56,885,146
Assumed	303,812	369,866	1,113,178	781,009
Ceded	16,269,313	13,922,049	46,634,917	38,917,828
Net	\$ 7,378,884	\$ 6,795,838	\$ 21,589,340	\$ 18,748,327
Losses and loss adjustment expenses incurred:				
Direct	\$ 20,868,196	\$ 14,686,373	\$ 56,229,573	\$ 43,410,668
Assumed	287,861	312,760	982,042	543,172
Ceded	14,795,799	10,272,640	39,717,266	30,360,376
Net	\$ 6,360,258	\$ 4,726,493	\$ 17,494,409	\$ 13,593,464

The impact of reinsurance on the balance sheets as of September 30, 2008 and December 31, 2007 is as follows:

	September 30, 2008	December 31, 2007
Unpaid losses and loss adjustment expense:		
Direct	\$ 38,189,103	\$ 33,391,172
Assumed	279,806	269,642
Ceded	26,745,920	23,249,616
Net	\$ 11,722,989	\$ 10,411,198
Unearned premiums:		
Direct	\$ 33,809,372	\$ 30,495,191
Assumed	294,216	496,374
Ceded	23,814,634	21,145,161
Net	\$ 10,288,954	\$ 9,846,404

Table of Contents

The Company received \$3,968,393 and \$12,819,142 in commissions on premiums ceded during the three and nine month periods ended September 30, 2008, respectively. Had all of the Company's reinsurance agreements been cancelled at September 30, 2008, the Company would have returned \$6,191,805 in reinsurance commissions to its reinsurers and its reinsurers would have returned \$23,814,634 in unearned premiums to the Company.

(5) Income Taxes

The provision for federal and state income taxes for the period ended September 30, 2008 and 2007 were as follows:

	Three Months		Nine Months	
	Ended September 30, 2008	2007	Ended September 30, 2008	2007
Current	\$ (289,689)	\$ (79,368)	\$ (216,465)	\$ 310,214
Deferred	(7,156)	169,310	38,464	442,563
Total provision for income taxes	\$ (296,845)	\$ 89,942	\$ (178,001)	\$ 752,777

(6) Capital Stock**Common Stock**

During the first nine months of 2007, 840,000 shares of preferred stock converted to 8,400,000 shares of common stock. During the first nine months of 2008, the Company issued 120,000 shares of common stock, \$.01 par value to its board of directors.

Stock-Based Compensation

The weighted-average grant date fair value of options granted during the nine months ended September 30, 2008 and September 30, 2007, using the Black-Scholes-Merton option-pricing model, was \$0.4499 and \$0.7844, respectively. The total intrinsic value of options exercised during the nine months September 30, 2007 was \$162,000 respectively. There were no options exercised during the nine months ended September 30, 2008.

Total compensation cost for share-based payment arrangements recognized for the three and nine months periods ended September 30, 2008 was \$527 and \$42,346, respectively. Total compensation cost for share-based payment arrangements recognized for the three and nine months periods ended September 30, 2007 was \$110,888 and \$329,000 respectively. The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton option-pricing model using the assumptions noted in the following table.

	September 30, 2008	September 30, 2007
Weighted-average-grant-date fair value	\$ 0.4499	\$ 0.7844
Expected volatility	108% - 110%	106% - 120%
Weighted average volatility	109%	113%
Risk-free interest rate	3.45% - 3.85%	2.00% - 2.70%
Expected term (in years)	7.4	5.0

Table of Contents

A summary of all stock option activity during the nine months ending September 30, 2008 and 2007 follows:

	September 30, 2008		September 30, 2007	
	Number of	Weighted	Number of	Number of
Options Outstanding	Shares	Average	Shares	Shares
		Exercise		
		Price		
January 1	4,946,665	\$ 0.80	5,347,225	\$ 0.85
Add (deduct):				
Granted	462,500	\$ 0.55	330,000	\$ 1.06
Exercised			(50,000)	\$ 0.25
Forfeited	(109,040)	\$ 0.82	(416,750)	\$ 0.78
Expired				
March 31	5,300,125	\$ 0.75	5,210,475	\$ 0.87
Add (deduct):				
Granted			1,091,000	\$ 0.96
Exercised			(120,000)	\$ 0.60
Forfeited	(18,500)	\$ 0.83	(1,099,510)	\$ 0.83
Expired			(20,000)	\$ 0.75
June 30	5,281,625	\$ 0.75	5,061,965	\$ 0.91
Add (deduct):				
Granted	677,943	\$ 0.50	235,000	\$ 0.91
Exercised	(50,000)	\$ 0.25	(144,000)	\$ 0.46
Forfeited	(651,060)	\$ 0.78	(170,000)	\$ 0.92
Expired			(80,000)	\$ 5.25
September 30	5,258,508	\$ 0.83	4,902,965	\$ 0.86
Exercisable, September 30,	1,810,900	\$ 0.68	1,166,183	\$ 0.57

(7) Commitments and Contingencies***Contractual Commitments***

The Company leases office space for its corporate headquarters in Atlanta, Georgia under a 12-year lease that commenced on May 1, 2003. The Company leases retail office space at various locations in Georgia, Florida and Alabama under short to medium term commercial leases. The Company also leases office equipment for use in its various locations. Rent expense for long-term leases with predetermined minimum rental escalations is recognized on a straight-line basis, and the difference between the recognized rental expense and amounts payable under the leases, or deferred rent, is included in other liabilities. The Company has a software license agreement with a term greater than one year.

The Company also has contractual commitments in association with long-term debt owed to current and former owners of the Company and in connection with a Junior Subordinated Debentures issued in December 2005. Please refer to Note 6 of the *Notes to Consolidated Financial Statements*, as of December 31, 2007 included in our Annual Report on Form 10-K for additional information about the long-term debt arrangements.

Minimum amounts due under the Company's noncancelable commitments at September 30, 2008 are as follows:

Payments due by period	Long-Term Debt Obligations	Operating Lease Obligations	Total
Less than 1 year	\$ 296,921	\$ 503,533	\$ 800,454
1-3 years	1,581,242	2,995,330	4,576,572
4-5 years	115,468	2,528,579	2,644,047
More than 5 years	4,976,854	1,912,321	6,889,175
Total	\$ 6,970,485	\$ 7,939,763	\$ 14,910,248

Table of Contents**Defined Contribution Plan**

The Company's associates participate in the AssuranceAmerica Corporation 401(k) defined contribution retirement plan. Under the plan, the Company can elect to make discretionary contributions. Effective January 1, 2008, the Company elected to match 33% of employee contributions up to 6% of gross earnings. Matching contributions during the first nine months of 2008 and 2007 were \$72,394 and \$37,054, respectively. The eligibility requirements are 21 years of age, 6 months of service and full time employment.

(8) Net Income Per Share

Basic and diluted income per common share is computed using the weighted average number of common shares outstanding during the period. Potential common shares not included in the calculations of net income per share for the periods ended September 30, 2008 and 2007, because their inclusion would be anti-dilutive, are as follows:

	Three Months		Nine Months	
	Ended September 30, 2008	2007	Ended September 30, 2008	2007
Stock options	5,258,500	3,576,965	5,258,500	3,576,965

The reconciliation of the amounts used in the computation of both basic earnings per share and diluted earnings per share for the periods ended September 30, 2008 and 2007 are as follows:

	Net Income (Loss)	Average Shares Outstanding	Per Share Amount
For the three months ended September 30, 2008:			
Net income - basic	\$ (618,486)	64,941,381	(0.009)
Effect of dilutive stock warrants and options			
Net income - diluted	\$ (618,486)	64,941,381	(0.009)
For the three months ended September 30, 2007:			
Net income - basic	\$ (43,520)	64,731,908	(0.001)
Effect of dilutive stock warrants and options		743,816	
Net income - diluted	\$ (43,520)	65,475,724	(0.001)
For the nine months ended September 30, 2008:			
Net income - basic	\$ (385,419)	64,911,655	(0.006)
Effect of dilutive stock warrants and options			
Net income - diluted	\$ (385,419)	64,911,655	(0.006)
For the nine months ended September 30, 2007:			
Net income - basic	\$ 715,997	60,939,646	0.012
Effect of dilutive stock warrants and options		792,842	

Net income diluted	\$	715,997	61,732,488	0.012
--------------------	----	---------	------------	-------

(9) Supplemental Cash Flow Information

	2008	2007
Cash paid during the nine months ended September 30:		
Interest	\$ 569,011	\$ 775,158
Income taxes	\$ 114,807	\$ 7,025

The Company recorded net unrealized losses on investment securities in the amount of \$660,766 and \$2,538, net of taxes, for the nine month period ended September 30, 2008 and 2007, respectively.

On January 3, 2007, the Company purchased the assets of Frontline Insurance Group, LLC. As part of the purchase agreement, the Company issued a note payable in the amount of \$114,400.

On January 16, 2008 the Company purchased the assets of Alabama One Stop, LLC for cash.

Table of Contents

On August 5, 2008, the Company purchased the remaining minority interest in TW Partners Agencies for cash. The following table illustrates the composition of acquisitions for the nine months ended September 30, 2008 and 2007:

	2008	2007
Fair value of assets acquired	\$ 55,200	\$ 604,400
Cash paid to sellers	(55,200)	(400,000)
Liabilities assumed	\$	\$ 204,400

During the first nine months of 2008, the Company issued 120,000 shares of common stock, \$.01 par value, to members of its board of directors pursuant to the director compensation program in lieu of cash directors' fees.

(10) Fair Value Disclosures

The fair value of our investments in fixed income and equity securities is based on observable market quotations, other market observable data, or is derived from such quotations and market observable data. We utilize third party pricing services, brokers and internal valuation models to determine fair value. We gain assurance of the overall reasonableness and consistent application of the assumptions and methodologies and compliance with accounting standards for fair value determination through our ongoing monitoring of the fair values received or derived internally. Level 1 inputs are unadjusted, quoted prices in active markets for identical instruments at the measurement date (e.g., U.S. Government securities and active exchange-traded equity securities). Level 2 securities are comprised of securities whose fair value was determined by a nationally recognized pricing service using observable market inputs. Level 3 securities are comprised of (i) securities for which the pricing service is unable to provide a fair value, (ii) securities whose fair value is determined by the pricing service based on unobservable inputs and (iii) securities, other than securities backed by the U.S. Government, that are not rated by a Nationally Recognized Statistical Rating Organization.

The following table illustrates the fair value measurements as of September 30, 2008:

Description:	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Available for sale securities	\$ 2,932,223	\$ 5,116,508	\$
Marketable equity securities	2,315,562		
Total	\$ 5,247,785	\$ 5,116,508	\$

(11) Segment Reporting

The Company's subsidiaries are each unique operating entities performing a separate business function. AAIC, a property and casualty insurance company focuses on writing nonstandard automobile business in the states of Georgia, Alabama, Arizona, Florida, Louisiana, Indiana, Mississippi, South Carolina and Texas. MGA markets AAIC's policies through more than 1,800 independent agencies in these states. MGA provides all of the underwriting, accounting, product management, legal, policyholder administration and claims functions for AAIC and for two unaffiliated insurers that retain the non-standard automobile insurance policies produced by MGA in Florida and Texas. MGA receives various fees related to insurance transactions that vary according

Table of Contents

to state insurance laws and regulations. TrustWay is comprised of 49 retail insurance agencies that focus on selling nonstandard automobile policies and related coverages in Georgia, Florida and Alabama. TrustWay receives commissions and various fees associated with the sale of the products and services from its appointing insurance carriers.

The Company evaluates profitability based on pretax income. Pretax income for each segment is defined as the revenues less the segment's operating expenses including depreciation, amortization and interest.

Following are the operating results for the Company's various segments and an overview of segment assets:

(\$ in thousands)	MGA	TrustWay	AAIC	Company	Eliminations	Consolidated
<u>THIRD QUARTER</u>						
<u>2008</u>						
Revenues						
External customer	\$ 6,499	\$ 1,669	\$ 7,471	\$	\$	\$ 15,639
Intersegment	1,643	614	749	699	(3,705)	
Income						
Segment pretax income(loss)	779	(1,556)	(182)	44		(915)
Assets						
Segment assets	12,292	4,634	116,859	26,922	(23,884)	136,823
<u>THIRD QUARTER</u>						
<u>2007</u>						
Revenues						
External customer	\$ 6,539	\$ 877	\$ 6,998	\$	\$	\$ 14,414
Intersegment	1,620	813	743	743	(3,919)	
Income						
Segment pretax income(loss)	354	(1,475)	1,358	(192)		45
Assets						
Segment assets	8,168	11,155	110,531	23,047	(22,799)	130,102
<u>FIRST NINE</u>						
<u>MONTHS 2008</u>						
Revenues						
External customer	\$ 20,557	\$ 5,260	\$ 22,124	\$	\$	\$ 47,941
Intersegment	5,188	2,379	2,363	2,097	(12,062)	
Income						
Segment pretax income(loss)	2,973	(3,690)	98	56		(563)
Assets						
Segment assets	12,292	4,634	116,859	26,922	(23,884)	136,823
<u>FIRST NINE</u>						
<u>MONTHS 2007</u>						
Revenues						
External customer	\$ 20,632	\$ 4,074	\$ 19,371	\$	\$	\$ 44,077

Edgar Filing: ASSURANCEAMERICA CORP - Form 10-Q

Intersegment	5,335	3,372	2,412	2,228	(13,347)	
Income						
Segment pretax income(loss)	966	(1,954)	3,190	(730)		1,472
Assets						
Segment assets	8,168	11,155	110,531	23,047	(22,799)	130,102

13

Table of Contents**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Financial Condition**

Investments and cash as of September 30, 2008, decreased \$7.9 million to \$15.8 million from investments and cash of \$23.7 million as of December 31, 2007. The decrease was due in part to \$3.2 million decline in cash and income related to operating activities. This increase was offset by \$5.8 million in net sales of investments, \$1.0 million in purchases of property and equipment and \$2.5 million in principal payments on notes payable. The Company continues to invest in upgrading its retail stores and invest in technology to strengthen our infrastructure and support expansion. The Company's investments of \$11.1 million are primarily in direct obligations of the U.S. Treasury as well as those securities unconditionally guaranteed as to the payment of principal and interest by the United States government or any agency thereof and in high-quality corporate and municipal bonds of Georgia-based issuers. The Company's investment activities are made in accordance with the Company's Investment Policy. The objectives of the Investment Policy are to obtain favorable after-tax returns on investments through a diversified portfolio of fixed income, equity and real estate holdings. The Company's investment criteria and practices reflect the short-term duration of its contractual obligations with policyholders and regulators. Tax considerations include federal and state income tax as well as premium tax abatement and credit opportunities offered to insurance companies in the states where AAIC writes policies.

Premiums receivable as of September 30, 2008, increased \$2.9 million to \$31.7 million compared to December 31, 2007. The balance represents amounts due from AAIC's insureds and the increase is directly attributable to the increase in AAIC's premium writings during the first nine months of 2008. The Company's policy is to write off receivable balances immediately upon cancellation or expiration, and the Company does not consider an allowance for doubtful accounts to be necessary.

Reinsurance recoverable as of September 30, 2008, increased \$11.8 million to \$41.2 million compared to December 31, 2007. The increase is mainly attributable to AAIC's continued growth and loss experience. AAIC maintains a quota-share reinsurance treaty with its reinsurers in which it cedes 70% of the majority of premiums and losses. The \$41.1 million represents the reinsurers' portion of losses and loss adjustment expense, both paid and unpaid. All amounts are considered current.

Prepaid reinsurance premiums as of September 30, 2008, increased \$2.7 million to \$23.8 million compared to December 31, 2007. The increase results from AAIC's continued growth, and represents premiums ceded to its reinsurers which have not been fully earned.

Deferred acquisition costs as of September 30, 2008 increased \$0.3 million to \$2.4 million compared to December 31, 2007. The increase resulted from AAIC's continued growth. The amount represents agents' commissions and other variable expenses associated with acquiring the insurance policies that are being deferred to coincide with the earnings of the related policy premiums.

Intangible assets as of September 30, 2008, decreased \$0.3 million to \$11.1 million from the balance of \$11.4 million as of December 31, 2007. This decrease is directly related to the amortization of acquired assets.

Accounts payable and accrued expenses as of September 30, 2008, increased \$2.0 million from December 31, 2007 to \$9.2 million. The increase is due to \$0.2 million of accrued commissions due to agents, \$0.2 million of expenses and \$0.3 million increase in the liability for premium taxes.

Unearned premium as of September 30, 2008 increased \$3.1 million to \$34.1 million from December 31, 2007, and represents premiums written but not earned. This is directly attributable to the increase in AAIC's premium writings during the first nine months of 2008.

Unpaid losses and loss adjustment expenses increased \$4.8 million to \$38.5 million as of September 30, 2008 from \$33.7 million at December 31, 2007. This amount represents management's estimates of future amounts needed to pay claims and related expenses and the increase correlates with the increase in AAIC's writings and anticipated future losses.

Reinsurance payable as of September 30, 2008 increased \$5.0 million to \$30.2 million, compared to the balance at December 31, 2007. The amount represents premiums owed to the Company's reinsurers. AAIC maintains a quota-share reinsurance treaty with its reinsurers in which it cedes 70% of the majority of both premiums and losses.

The increase is directly attributable to the increase in AAIC's premium writings during the first nine months of 2008.

Table of Contents

Provisional commission reserves represent the difference between our minimum ceding commission and the provisional amount paid by the reinsurers. This balance as of September 30, 2008 increased \$0.01 million to \$2.9 million, compared to the balance at December 31, 2007. The increase is related to a provisional commission payment during the third quarter of 2008.

Liquidity and Capital Resources

Net cash used by operating activities for the nine months ended September 30, 2008 was \$3.2 million compared to net cash provided by operating activities of \$4.2 million for the same period of 2007.

Investing activities for the nine months ended September 30, 2008 consisted of the purchase of leasehold improvements and property and equipment in the amount of \$1.0 million in our retail stores and new technology and \$5.8 million in net sales of investments in compliance with various Departments of Insurance requirements for issuance of Certificates of Authority and general investment policies of the Company.

Financing activities for the nine months ended September 30, 2008 consisted of debt repayments for the nine months ended September 30, 2008 and 2007 of \$2.5 million, compared to \$1.2 million during the same period in 2007.

The Company's liquidity and capital needs have been met in the past through premium, commission and fee income, loan from its Chairman and issuance of its Series A Convertible Preferred Stock, common stock and debt securities. The Company's related party debt consists of unsecured promissory notes payable to its Chairman. The promissory notes carry an interest rate of 8% per annum and provide for the repayment of principal on an annual basis. On December 22, 2005, the Company, through a newly-formed Delaware statutory trust, AssuranceAmerica Capital Trust I (the Trust), consummated the private placement of 5,000 of the Trust's floating rate capital securities, with a liquidation amount of \$1,000 per capital security (the Capital Securities). In connection with the Trust's issuance and sale of the Capital Securities, the Company purchased from the Trust 155 of the Trust's floating rate common securities, with a liquidation amount of \$1,000 per common security (the Common Securities). The Trust used the proceeds from the issuance and sale of the Capital Securities and the Common Securities to purchase \$5,155,000 in aggregate principal amount of the floating rate junior subordinated debentures of the Company (the Debentures). The Capital Securities mature on December 31, 2035, but may be redeemed at par beginning December 31, 2010 if and to the extent the Company exercises its right to redeem the Debentures. The Capital Securities require quarterly distributions by the Trust to the holders of the Capital Securities, at a floating rate of three-month LIBOR plus 5.75% per annum, reset quarterly. Distributions are cumulative and will accrue from the date of original issuance but may be deferred for a period of up to 20 consecutive quarterly interest payment periods if the Company exercises its right under the Indenture to defer the payment of interest on the Debentures.

The growth of the Company has and will continue to strain its liquidity and capital resources. AAIC is required by the state of South Carolina to maintain minimum capital and surplus of \$3.0 million. As of September 30, 2008, AAIC's statutory capital and surplus was \$11.4 million.

Results of Operations

The Company reported a net loss of \$0.6 million and \$0.4 million for the three and nine month periods ended September 30, 2008 compared to net loss of \$0.01 million and net income of \$0.8 million for the three and nine month periods ended September 30, 2007, respectively. The Company reported basic losses per common share of \$0.009 and \$0.005 for the three and nine month periods ended September 30, 2008 compared to basic losses per common share of \$0.001 and basic gain per common share of \$0.012 for the three and nine month periods ended September 30, 2007. Fully diluted losses per common share was \$0.009 and \$0.012 for the three and nine month period ended September 30, 2008 compared to \$0.001 fully diluted losses per common share and \$0.012 fully diluted earnings per common share for the three and nine month periods ended September 30, 2007.

Table of Contents**Revenues***Premiums*

Gross premiums written for the three and nine month periods ended September 30, 2008 were \$22.2 million and \$71.3 million, respectively. In the comparable period for 2007, AAIC recorded \$21.5 million and \$70.0 million, respectively, in gross premiums written. 2008 gross premiums written includes insurance premiums written directly by AAIC, or direct premiums written, of \$21.9 million and \$70.4 million in the respective three and nine month periods, plus \$0.4 and \$0.9 million, in the respective three and nine month periods, of premiums associated with the insurance risk transferred to AAIC by two unaffiliated insurance companies pursuant to a reinsurance contract, referred to as assumed premiums written. 2007 gross premiums written includes direct premiums written of \$21.1 million and \$68.8 million in the respective three and nine month periods, plus \$0.4 million and \$1.2 million, in the respective three and nine month periods, of assumed premiums written. The majority of our growth occurred in Louisiana and Arizona, where AAIC began writing policies in Louisiana in 2007 and in Arizona where AAIC began writing policies in the first quarter of 2008. Entry into Louisiana accounted for \$5.9 million and Arizona was \$1.4 million of the increase during 2008 over the comparable 2007 period. As of September 30, 2008 the soft market and economic factors continues to put pressure on our writings in Georgia and Florida. The decline in Georgia premium for the nine months ended September 30, 2008 was \$2.3 million or 8% from the 2007 comparable period. Florida premium declined \$4.6 million when compared with the first nine months of 2007. Policies inforce increased 12% from December 31, 2007 to September 30, 2008. The Company cedes approximately 70% of its direct premiums written to its reinsurers and the total amount ceded for the nine months ended September 30, 2008, was \$49.3 million.

Premiums written refers to the total amount of premiums billed to the policyholder less the amount of premiums returned, generally as a result of cancellations, during a given period. Premiums written become premiums earned as the policy ages. Barring premium rate changes, if an insurance company writes the same mix of business each year, premiums written and premiums earned will be equal and the unearned premium reserve will remain constant. During periods of growth, the unearned premium reserve will increase, causing premiums earned to be less than premiums written. Conversely, during periods of decline, the unearned premium reserve will decrease, causing premiums earned to be greater than premiums written. The Company's net earned premium, after deducting reinsurance, was \$7.4 million and \$21.6 million for the three and nine month periods ended September 30, 2008 and compares to \$6.8 million and \$18.7 million, respectively, for the three and nine month periods ended September 30, 2007.

Commission and Fee Income

MGA and TrustWay produce and service non-standard personal automobile insurance business for our own carrier and other insurers. We receive service fees for agency, underwriting, policy administration, and claims adjusting services performed on behalf of these insurers. We also receive commission and service fee income in TrustWay on other insurance products produced for unaffiliated insurance companies on which we do not bear underwriting risk, including travel protection, vehicle protection and hospital indemnity insurance policies. Commission rates vary between carriers and are applied to written premium to determine commission income.

Commission income, as a result of business produced in both TrustWay and MGA, increased 14% and 1% for the three and nine month periods ended September 30, 2008, respectively, compared to the same periods ended September 30, 2007. Total commission income earned by TrustWay from the production of AAIC for the three and nine month periods ended September 30, 2008 totaled \$0.6 million and \$2.4 million, respectively and this amount is eliminated from total commission income (revenue) and commission expense. AAIC pays MGA commission on the 30% of premium which AAIC retains. This amount is subsequently eliminated upon consolidation. The amount eliminated was \$1.6 million and \$5.2 million, respectively, for the three and nine month periods ended September 30, 2008.

Managing general agent fees for the three and nine month periods ended September 30, 2008 were \$3.0 million and \$9.1 million, respectively, an increase of \$0.1 million and \$1.0 million, when compared to the same periods of 2007.

Other fee income was increased \$0.1 million for each of the three and nine month ended September 30, 2008 from the comparable periods of 2007. TrustWay collects fees for various services performed and for additional products sold to insureds. As TrustWay writes less agency bill policies, the fee income will decline slightly.

Table of Contents*Net Investment Income*

Our investment portfolio is generally highly liquid and consists substantially of readily marketable, investment-grade debt and equity securities. Net investment income is primarily comprised of interest and dividends earned on these securities, net of related investment expenses. Net investment income decreased \$50,000 and \$54,000 for the three and nine month periods ended September 30, 2008 from \$0.2 million and \$0.6 million in the comparable 2007 periods. This is primarily a result of a decrease in average invested assets.

Expenses*Insurance Loss and Loss Adjustment Expenses*

Insurance losses and loss adjustment expenses include payments made to settle claims, estimates for future claim payments and changes in those estimates for current and prior periods, as well as loss adjustment expenses incurred in connection with settling claims. Insurance losses and loss adjustment expenses are influenced by many factors, such as claims frequency and severity trends, the impact of changes in estimates for prior accident years, and increases in the cost of medical treatment and automobile repairs. The anticipated impact of inflation is considered when we establish our premium rates and set loss reserves. We perform a rolling quarterly actuarial analysis each month and establish or adjust (for prior accident quarters) reserves, based upon our estimate of the ultimate incurred losses and loss adjustment expenses to reflect loss development information and trends that have been updated for the most recent quarter's activity. Each month our estimate of ultimate loss and loss adjustment expenses is evaluated by accident quarter, by state and by major coverage grouping (e.g., bodily injury, physical damage) and changes in estimates are reflected in the period the additional information becomes known.

We have historically used reinsurance to manage our exposure to loss by ceding a portion of our gross losses and loss adjustment expenses to reinsurers. We remain obligated for amounts covered by reinsurance, however, in the event that the reinsurers do not meet their obligations under the agreements (due to, for example, disputes with the reinsurer or the reinsurer's insolvency). The Company cedes approximately 70% of its direct loss and loss adjustment expenses incurred to its reinsurers and the amount ceded for the three and nine month periods ended September 30, 2008, was \$14.8 million and \$39.7 million, respectively.

After making deductions for the effect of reinsurance, losses and loss adjustment expenses were \$6.4 million and \$17.5 million for the three and nine month periods ended September 30, 2008. As a percentage of earned premiums, this amount increased for the three month period ended September 30, 2008, from 69.5% to 86.2%, when compared with the same period in 2007. As a percentage of earned premiums, this amount decreased for the nine month period ended September 30, 2008, from 72.5% to 81.0%, when compared with the same period in 2007. The amount represents actual payments made and changes in estimated future payments to be made to or on behalf of its policyholders, including the expenses associated with settling claims. The increase in the year-over-year loss ratio is in part due to adverse loss development experienced due to storm activity and increased claim frequency in various states.

Other Expenses

Other operating expenses, including selling and general and administrative increased \$0.7 million and \$2.4 million for the three and nine month periods ended September 30, 2008 when compared to the same periods of 2007. As a percentage of revenue, selling and general and administrative expenses for the three month period ended September 30, 2008 decreased from 62.6% to 62.1% when compared to the 2007 period. As a percentage of revenue, selling and general and administrative expenses for the nine month period ended September 30, 2008 increased from 61.3% to 61.4% when compared to the 2007 period. The increase in selling expenses is primarily attributable to additional staffing costs as compared to the 2007 period.

Income Tax Expense

The provision for income taxes for the three and nine month periods ended September 30, 2008, consists of federal and state income taxes at the Company's effective tax rate. The Company had a tax benefit of \$0.3 million and \$0.2 million for the three and nine month periods ended September 30, 2008, representing an effective tax benefit rate of 31.6% for the year. This tax expense compares with \$0.1 million and \$0.8 million for the comparable 2007 periods, which was an effective tax rate of 51.25% for the year. The Company experienced a higher tax rate in 2007 due to the impact of incentive stock options compensation expense.

Table of Contents**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are primarily exposed to the impact of interest rate changes, changes in market values of investments and to credit risk.

In the normal course of business, we employ established policies and procedures to manage our exposure to changes in interest rates, fluctuations in the fair market value of debt and equity securities and credit risk. We seek to mitigate these risks by various actions described below.

Our cash flows from operations and short-term cash position generally have been more than sufficient to meet our projected obligations for claim payments, which by the nature of the personal automobile insurance business, tend to have an average duration of less than one year. As a result, it has been unnecessary for the Company to employ elaborate market risk management techniques involving complicated asset and liability duration matching or hedging strategies.

Interest Rate Risk

Investments. Our investment portfolio consists primarily of fixed-maturity debt securities, all of which are classified as available for sale. For these securities, we seek to provide for liquidity and diversification while maximizing income without sacrificing investment quality. The value of the fixed maturity securities portfolio is subject to interest rate risk where the value of the fixed maturity securities portfolio decreases as market interest rates increase, and conversely, when market interest rates decrease, the value of the fixed maturity securities portfolio increases. Duration is a common measure of the sensitivity of a fixed maturity security's value to changes in interest rates. More specifically, it is the approximate percentage change in the value of a bond or bond portfolio due to a 100 basis point change in interest rates. The higher the duration, the more sensitive a fixed maturity security is to market interest rate fluctuations. Effective duration also measures this sensitivity, but it takes into account call terms, as well as changes in remaining term, coupon rate, cash flow, and other items. We strive to limit interest rate risk by selecting investments with characteristics such as duration, yield and liquidity tailored to the anticipated cash outflow characteristics of our liabilities. Interest rate risk includes the risk from movements in the underlying market rate and in the credit spread of the respective sectors of the debt securities in our portfolio. We do not hedge our exposure to interest rate risk because we have the capacity to, and typically, hold fixed-maturity investments to maturity. The effective duration of the portfolio as of September 30, 2008 was 5.31 years. Should market interest rates increase 1.0%, our fixed income portfolio would be expected to decline in market value by \$0.9 million, or 10.8%. Conversely, a 1.0% decline in interest rates would result in approximately \$0.1 million, or 1%, depreciation in the market value of our fixed income portfolio.

Credit Facility. We also have exposure to market risk for changes in interest rates because we have variable rate debt. The interest rate we pay increases or decreases with the changes in LIBOR. Based on our borrowings under the floating rate credit agreement at September 30, 2008, a 10% increase in market interest rates would increase our annual net interest expense by approximately \$21,134. Conversely, a 10% decrease in market interest rates would decrease our annual net interest expense by approximately \$21,134.

The graphical depiction of the relationship between the yield on bonds of the same credit quality with different maturities is usually referred to as a yield curve. Because the yield on U.S. Treasury securities is the base rate (or risk free rate) from which non-government bond yields are normally benchmarked, the most commonly constructed yield curve is derived from the observation of prices and yields in the Treasury market. An upward sloping curve, where yield rises steadily as maturity increases, is referred to as a normal yield curve.

The following table shows the carrying values of our fixed maturity securities, which are reported at fair value. The table also presents estimated fair values at adjusted market rates assuming a parallel 100 basis point increase in market interest rates, given the effective duration noted above. The following sensitivity analysis summarizes only the exposure to market interest rate risk:

Estimated Carrying Value at	Change in Value as a
--	---------------------------------

(Dollar amounts in thousands)	Carrying	Adjusted Market Rates/Prices Indicated Above	Percentage of Carrying Value
September 30, 2008	Value		
Fixed maturity securities available-for-sale, at fair value	\$8,676.7	\$ 8,048.7	(7.2)%

18

Table of Contents

The discussion above provides only a limited, point-in-time view of the market risk sensitivity of our fixed rate financial instruments. The actual impact of interest rate changes on our fixed maturity securities in particular may differ significantly from those shown, as the analysis assumes a parallel shift in market interest rates. The analysis also does not consider any actions we could take in response to actual and/or anticipated changes in interest rates.

The difference between long-term Treasury yields and short-term Treasury yields are usually referred as the slope of the yield curve. If the spread between the long end of the curve, where maturities are high, and the short end of the curve, where maturities are low, narrows, the yield curve is said to be flattening. Conversely, if the spread between the long end of the curve and the short end of the curve widens, the yield curve is said to be steepening. If the yields on the long end of the curve fall below those of the short end of the curve, the yield curve is said to be inverted.

The analysis above assumes a parallel shift in interest rates. However, the curve may also steepen, flatten or become inverted. This type of behavior may affect certain sections of the curve in disproportionate amounts. For example, if short-term Treasury yields rise and the yield curve flattens, fixed maturity instruments with short duration may be impacted to a greater degree than fixed maturity instruments with longer duration. Conversely, if long-term Treasury yields rise and the yield curve steepens, fixed maturity instruments with long duration may be impacted to a greater degree than fixed maturity instruments with shorter duration.

The following summarizes the effective duration distribution of our fixed maturity securities portfolio.

September 30, 2008	Duration Ranges					
	Below 1	1 to 3	3 to 5	5 to 7	7 to 10	10 to 20
Fair value percentage of fixed maturity security portfolio	0.0%	18.0%	31.3%	25.1%	25.6%	0.0%

Equity Price Risk

Investments. The marketable equity securities portfolio of our insurance subsidiary, which is carried on our consolidated balance sheets at estimated fair value, has exposure to price risk, which is the risk of potential loss in estimated fair value resulting from adverse changes in prices. The objective of our insurance subsidiary is to earn competitive relative returns by investing in diverse portfolios of high-quality, liquid securities.

Credit Risk

Investments. The fixed maturity securities portfolio of our insurance subsidiary is subject to credit risk. This risk is the potential loss in market value resulting from adverse changes in the borrower's ability to repay the debt. We attempt to manage our credit risk through issuer and industry diversification. We regularly monitor our overall investment results and review compliance with our investment objectives and guidelines. Our investment guidelines include limitations on the minimum rating of debt securities in our investment portfolio, as well as restrictions on investments in debt securities of a single issuer. All of the debt securities in our portfolio were rated investment grade by the National Association of Insurance Commissioners, or the NAIC, and Standard & Poor's as of September 30, 2008.

Reinsurance. We place reinsurance with four major unaffiliated reinsurers. Two of the reinsurers are authorized and two are unauthorized. To the extent that a reinsurer may be unable to pay losses for which it is liable to us under the terms of its reinsurance agreement, we remain liable for such losses. The Company attempts to minimize this risk by maintaining reinsurance agreements with financially sound reinsurers. The Company maintains security trust agreements with the two unauthorized reinsurers, whereby all reinsurance receivables are pre-funded and secured. As of September 30, 2008, there were no amounts deemed uncollectible.

Table of Contents**ITEM 4. CONTROLS AND PROCEDURES****Evaluation of Disclosure Controls and Procedures**

As of the end of the period covered by this report on Form 10-Q, the Company's Chief Executive Officer and Acting Chief Financial Officer carried out an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures in accordance with Rule 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934 (the Exchange Act). Based on this evaluation, the Company's Chief Executive Officer and Acting Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure and are effective to ensure that such information is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

Management's Annual Report on Changes in Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Management assessed the effectiveness of our internal control over financial reporting as of September 30, 2008. In making this assessment, management used the criteria described in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies and procedures may deteriorate. Based on this evaluation, management determined that, as of September 30, 2008, we maintained effective internal control over financial reporting, and there were no changes in our internal control over financial reporting made during our most recent fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION**ITEM 1A. RISK FACTORS**

An investment in Company common stock involves a number of risks. Investors should carefully consider the following information, together with the other information contained in the Company's Annual Report on Form 10-K, before investing in Company common stock. Further, such factors could cause actual results to differ materially from those contained in any forward-looking statement contained in this report, statements by us in periodic press releases and oral statements by Company officials to securities analysts and stockholders during presentations about us.

We face intense competition from other automobile insurance providers.

The non-standard automobile insurance business is highly competitive and, except for regulatory considerations, there are relatively few barriers to entry. We compete with both large national insurance providers and smaller regional companies. The largest automobile insurance companies include The Progressive Corporation, The Allstate Corporation, State Farm Mutual Automobile Insurance Company, GEICO, Farmers Insurance Group, Safeco Corp., and American International Group (AIG). Our chief competitors include some of these companies as well as Mercury General Corporation, Infinity Property & Casualty Corporation, Affirmative Insurance Holdings, Inc., and Direct General Corporation. Some of our competitors have more capital, higher ratings and greater resources than we have, and may offer a broader range of products and lower prices and down payments than we offer. Some of our competitors that sell insurance policies directly to customers, rather than through agencies or brokerages as we do, may have certain competitive advantages, including increased name recognition among customers, direct relationships with policyholders and potentially lower cost structures. In addition, it is possible that new competitors will enter the non-standard automobile insurance market. Our loss of business to competitors could have a material impact on our growth and profitability. Further, competition could result in lower premium rates and less favorable policy terms and conditions, which could reduce our underwriting margins.

Table of Contents

Our concentration on non-standard automobile insurance could make us more susceptible to unfavorable market conditions.

We underwrite exclusively non-standard automobile insurance. Given this focus, negative developments in the economic, competitive or regulatory conditions affecting the non-standard automobile insurance industry could have a material adverse effect on our results of operations, financial condition and cash flows. In addition, these developments could have a greater effect on us, compared to more diversified insurers that also sell other types of automobile insurance products. Our profitability can be affected by cyclicity in the non-standard automobile insurance industry caused by price competition and fluctuations in underwriting capacity in the market, as well as changes in the regulatory environment.

Our success depends on our ability to price the risks we underwrite accurately.

Our results of operations and financial condition depend on our ability to underwrite and set rates accurately for a full spectrum of risks. Rate adequacy is necessary to generate sufficient premiums to pay losses, loss adjustment expenses and underwriting expenses and to earn a profit. If we fail to assess accurately the risks that we assume, we may fail to establish adequate premium rates, which could reduce our income and have a material adverse effect on our results of operations, financial condition or cash flows.

In order to price our products accurately, we must collect and properly analyze a substantial volume of data; develop, test and apply appropriate rating formulas; closely monitor and timely recognize changes in trends; and project both severity and frequency of losses with reasonable accuracy. Our ability to undertake these efforts successfully, and as a result price our products accurately, is subject to a number of risks and uncertainties, including, without limitation:

- availability of sufficient reliable data;
- incorrect or incomplete analysis of available data;
- uncertainties inherent in estimates and assumptions, generally;
- selection and application of appropriate rating formulas or other pricing methodologies;
- unanticipated or inconsistent court decisions, legislation or regulatory action;
- ongoing changes in our claim settlement practices, which can influence the amounts paid on claims;
- changing driving patterns, which could adversely affect both frequency and severity of claims;
- unexpected inflation in the medical sector of the economy, resulting in increased bodily injury and personal injury protection claim severity; and
- unanticipated inflation in automobile repair costs, automobile parts prices and used automobile prices, adversely affecting automobile physical damage claim severity.

Such risks may result in our pricing being based on inadequate or inaccurate data or inappropriate analyses, assumptions or methodologies, and may cause us to estimate incorrectly future increases in the frequency or severity of claims. As a result, we could underprice our products, which would negatively affect our profit margins, or we could overprice our products, which could reduce our volume and competitiveness. In either event, our results of operations, financial condition and cash flows could be materially and adversely affected.

Our losses and loss adjustment expenses may exceed our loss and loss adjustment expense reserves, which could adversely impact our results of operation, financial condition and cash flows.

Our financial statements include loss and loss adjustment expense reserves, which represent our best estimate of the amounts that we will ultimately pay on claims and the related costs of adjusting those claims as of the date of the financial statements. We rely heavily on our historical loss and loss adjustment expense experience in determining these loss and loss adjustment expense reserves. The historic development of reserves for losses and loss adjustment expenses may not necessarily reflect future trends in the development of these amounts. In addition, factors such as inflation, claims settlement patterns and legislative activities, regulatory activities, and litigation trends may also affect loss and loss adjustment expense reserves. As a result of these and other risks and uncertainties, ultimate losses and loss adjustment expenses may deviate, perhaps substantially, from our estimates of losses and loss adjustment expenses included in the loss and loss adjustment expense reserves in our financial statements. If actual losses and loss

Table of Contents

adjustment expenses exceed our expectations, our net income and our capital would decrease. Actual paid losses and loss adjustment expenses may be in excess of the loss and loss adjustment expense reserve estimates reflected in our financial statements.

We are subject to comprehensive regulation, and our ability to earn profits may be adversely affected by these regulations.

We are subject to comprehensive regulation by government agencies in the states where our insurance subsidiaries are domiciled and where these subsidiaries issue policies and handle claims. Certain states impose restrictions or require prior regulatory approval of certain corporate actions, which may adversely affect our ability to operate, innovate, obtain necessary rate adjustments in a timely manner or grow our business profitably. In addition, certain federal laws impose additional requirements on insurers. Our ability to comply with these laws and regulations, and to obtain necessary regulatory action in a timely manner, is and will continue to be critical to our success.

Required Licensing. We operate under licenses issued by various state insurance authorities. If a regulatory authority denies or delays granting a new license, our ability to enter that market quickly can be substantially impaired.

Transactions Between Insurance Companies and Their Affiliates. Transactions between our subsidiaries and their affiliates (including us) generally must be disclosed to the state regulators, and prior approval of the applicable regulator generally is required before any material or extraordinary transaction may be consummated. State regulators may refuse to approve or delay approval of such a transaction, which may impact our ability to innovate or operate efficiently.

Regulation of Insurance Rates and Approval of Policy Forms. The insurance laws of the states in which our insurance subsidiaries operate require insurance companies to file insurance rate schedules and insurance policy forms for review and/or approval. If, as permitted in some states, we begin using new rates before they are approved, we may be required to issue refunds or credits to our policyholders if the new rates are ultimately deemed excessive or unfair and disapproved by the applicable state regulator. Accordingly, our ability to respond to market developments or increased costs in that state can be adversely affected.

Restrictions on Cancellation, Non-Renewal or Withdrawal. Many states have laws and regulations that limit an insurer's ability to exit a market. For example, certain states limit an automobile insurer's ability to cancel or not renew policies. Some states prohibit an insurer from withdrawing from one or more lines of business in the state, except pursuant to a plan approved by the state insurance department. In some states, this restriction applies to significant reductions in the amount of insurance written, not just to a complete withdrawal. These laws and regulations could limit our ability to exit or reduce our writings in unprofitable markets or discontinue unprofitable products in the future.

Other Regulations. We must also comply with regulations involving, among other things:

- the use of non-public consumer information and related privacy issues;
- investment restrictions;
- the use of credit history in underwriting and rating;
- the payment of dividends;
- the acquisition or disposition of an insurance company or of any company controlling an insurance company;
- the involuntary assignments of high-risk policies, participation in reinsurance facilities and underwriting associations, assessments and other governmental charges; and
- reporting with respect to financial condition.

Compliance with laws and regulations addressing these and other issues often will result in increased administrative costs. In addition, these laws and regulations may limit our ability to underwrite and price risks accurately, prevent us from obtaining timely rate increases necessary to cover increased costs and may restrict our ability to discontinue unprofitable relationships or exit

Table of Contents

unprofitable markets. These results, in turn, may adversely affect our results of operation or our ability or desire to grow our business in certain jurisdictions. The failure to comply with these laws and regulations may also result in actions by regulators, fines and penalties, and in extreme cases, revocation of our ability to do business in that jurisdiction. In addition, we may face individual and class action lawsuits by our insureds and other parties for alleged violations of certain of these laws or regulations.

Our insurance subsidiaries are subject to minimum capital and surplus requirements. Our failure to meet these requirements could subject us to regulatory action.

The laws of the states of domicile of our insurance subsidiaries impose risk-based capital standards and other minimum capital and surplus requirements. Failure to meet applicable risk-based capital requirements or minimum statutory capital requirements could subject us to further examination or corrective action imposed by state regulators, including limitations on our writing of additional business, state supervision or liquidation. Any changes in existing risk-based capital requirements or minimum statutory capital requirements may require us to increase our statutory capital levels, which we may be unable to do.

Regulation may become more extensive in the future, which may adversely affect our business.

States may make existing insurance laws and regulations more restrictive in the future or enact new restrictive laws. In such events, we may seek to reduce our premium writings in, or to withdraw entirely from, these states. In addition, from time to time, the United States Congress and certain federal agencies investigate the current condition of the insurance industry to determine whether federal regulation is necessary. We are unable to predict whether and to what extent new laws and regulations that would affect our business will be adopted in the future, the timing of any such adoption and what effects, if any, they may have on our financial condition, results of operations, and cash flows.

Our failure to pay claims accurately could adversely affect our business, financial condition, results of operations and cash flows.

We must accurately evaluate and pay claims that are made under our policies. Many factors affect our ability to pay claims accurately, including the training and experience of our claims representatives, our claims organization's culture and the effectiveness of our management, our ability to develop or select and implement appropriate procedures and systems to support our claims functions and other factors. Our failure to pay claims accurately could lead to material litigation, undermine our reputation in the marketplace, impair our image and materially adversely affect our financial condition, results of operations and cash flows.

In addition, if we do not train new claims employees effectively or lose a significant number of experienced claims employees our claims department's ability to handle an increasing workload could be adversely affected. In addition to potentially requiring that growth be slowed in the affected markets, we could suffer in decreased quality of claims work, which in turn could lower our operating margins.

The policy service fee revenues could be adversely affected by insurance regulation.

Policy service fee revenues have provided additional revenues equivalent to approximately 12% of gross premium produced by MGA. These fees include policy origination fees and installment fees to compensate us for the costs of providing installment payment plans, as well as late payment, policy cancellation, policy rewrite and reinstatement fees. Our revenues could be reduced by changes in insurance regulation that restrict our ability to charge these fees. Those arrangements are subject to insurance holding company act regulation in the states where our insurance subsidiaries are domiciled. Continued payment of these fees could be affected if insurance regulators in these states determined that these arrangements are not permissible under the insurance holding company acts.

Table of Contents

New pricing, claim and coverage issues and class action litigation are continually emerging in the automobile insurance industry, and these new issues could adversely impact our results of operations and financial condition.

As automobile insurance industry practices and regulatory, judicial and consumer conditions change, unexpected and unintended issues related to claims, coverage and business practices may emerge. These issues can have an adverse effect on our business by changing the way we price our products, including limiting the factors we may consider when we underwrite risks, by extending coverage beyond our underwriting intent, by increasing the size or frequency of claims or by requiring us to change our claims handling practices and procedures or our practices for charging fees. The effects of these unforeseen emerging issues could negatively affect our results of operations, financial condition and cash flows.

We may be unable to attract and retain independent agents and brokers.

We distribute our products exclusively through independent agents and brokers. We compete with other insurance carriers to attract producers and maintain commercial relationships with them. Some of our competitors offer a larger variety of products, lower prices for insurance coverage or higher commissions. We may not be able to continue to attract and retain independent agents and brokers to sell our products. Our inability to continue to recruit and retain productive independent agents and brokers would have an adverse effect on our financial condition and results of operations and could impact our cash flows.

We rely on information technology and telecommunication systems, and the failure of these systems could materially and adversely affect our business.

Our business is highly dependent upon the successful and uninterrupted functioning of our information technology and telecommunications systems. We rely on these systems to process new and renewal business, provide customer service, make claims payments and facilitate collections and cancellations. These systems also enable us to perform actuarial and other modeling functions necessary for underwriting and rate development. The failure of these systems could interrupt our operations or materially impact our ability to evaluate and write new business. Because our information technology and telecommunication systems interface with and depend on third-party systems, we could experience service denials if demand for such service exceeds capacity or such third-party systems fail or experience interruptions. If sustained or repeated, a system failure or service denial could result in a deterioration of our ability to write and process new and renewal business and provide customer service or compromise our ability to pay claims in a timely manner. This outcome could result in a material adverse effect on our business and our results of operations, financial condition and cash flows.

Our ability to operate our company effectively could be impaired if we lose key personnel.

We manage our business with a number of key personnel, including our executive officers, the loss of whom could have a material adverse effect on our business and our results of operations, financial condition and cash flows. Only our Vice Chairman, Lawrence Stumbaugh and our President, Joseph Skruck, have employment agreements with us. In addition, as our business develops and expands, we believe that our future success will depend greatly on our continued ability to attract and retain highly skilled and qualified personnel. We may not be able to continue to employ key personnel and may not be able to attract and retain qualified personnel in the future. Failure to retain or attract key personnel could have a material adverse effect on our business and our results of operations, financial condition and cash flows.

Our debt service obligations could impede our operations, flexibility and financial performance.

Our level of debt could affect our financial performance. As of September 30, 2008, we had consolidated indebtedness (other than trade payables and certain other short term debt) of approximately \$7.0 million. In addition, borrowings under our trust preferred arrangement bear interest at rates that may fluctuate. Therefore, increases in interest rates on the obligations under our credit agreement would adversely affect our income and cash flow that would be available for the payment of interest and principal on the loans outstanding.

If we do not have enough money to pay our debt service obligations, we may be required to refinance all or part of our existing debt, sell assets, borrow more money or raise equity. In that event, we may not be able to refinance our debt, sell assets, borrow more money or raise equity on terms acceptable to us or at all.

Table of Contents**Adverse securities market conditions can have significant and negative effects on our investment portfolio.**

Our results of operations depend in part on the performance of our invested assets. As of September 30, 2008, 73% of our investment portfolio was invested in fixed maturity securities with the remainder in equity investments. Certain risks are inherent in connection with fixed maturity securities, including loss upon default and price volatility in reaction to changes in interest rates, credit spreads, deterioration in the financial condition of the issuers and general market conditions. An increase in interest rates lowers prices on fixed maturity securities, and any sales we make during a period of increasing interest rates may result in losses. Also, investment income earned from future investments in fixed maturity securities will decrease if interest rates decrease.

In addition, our investment portfolio is subject to risks inherent in the capital markets. The functioning of those markets, the values of our investments and our ability to liquidate investments on short notice may be adversely affected if those markets are disrupted by national or international events including, without limitation, wars, terrorist attacks, recessions or depressions, high inflation or a deflationary environment, the collapse of governments or financial markets, and other factors or events.

If our investment portfolio were impaired by market or issuer-specific conditions to a substantial degree, our financial condition, results of operations and cash flows could be materially adversely affected. Further, our income from these investments could be materially reduced, and write-downs of the value of certain securities could further reduce our profitability. In addition, a decrease in value of our investment portfolio could put us at risk of failing to satisfy regulatory capital requirements. If we were not able to supplement our subsidiaries' capital by issuing debt or equity securities on acceptable terms, our ability to continue growing could be adversely affected.

Our operations could be adversely affected if conditions in the states where our business is concentrated were to deteriorate.

For the nine months ended September 30, 2008, we generated approximately 60% of our gross written premium in our top two states, Florida and Georgia. Our revenues and profitability are therefore subject to prevailing regulatory, legal, economic, demographic, competitive and other conditions in those states. Changes in any of those conditions could have an adverse effect on our results of operations, financial condition and cash flows. Adverse regulatory developments in any of those states, which could include, among others, reductions in the rates permitted to be charged, inadequate rate increases, restrictions on our ability to reject applications for coverage or on how we handle claims, or more fundamental changes in the design or implementation of the automobile insurance regulatory framework, could have a material adverse effect on our results of operations, financial condition and cash flows.

Severe weather conditions and other catastrophes may result in an increase in the number and amount of claims filed against us.

Our business is also exposed to the risk of severe weather conditions and other catastrophes in the states in which we operate. Catastrophes include severe hurricanes, tornadoes, hail storms, floods, windstorms, earthquakes, fires and other events such as terrorist attacks and riots, each of which tends to be unpredictable. Such conditions may result in higher incidence of automobile accidents and increase the number of claims. Because many of our insureds live near the coastlines, we have potential exposure to hurricanes and major coastal storms. In addition, our business could be impaired if a significant portion of our business or systems were shut down by, or if we were unable to gain access to certain of our facilities as a result of such an event. If such events were to occur with enough severity, our results of operations, financial condition and cash flows could be materially adversely affected.

Our financial condition may be adversely affected if one or more parties with which we enter into significant contracts becomes insolvent or experiences other financial hardship.

Our business is dependent on the performance by third parties of their responsibilities under various contractual relationships, including without limitation, contracts for the acquisitions of goods and services (such as telecommunications and information technology software, equipment and support and other services that are integral to our operations) and arrangements for transferring certain of our risks (including our corporate insurance policies). If one or more of these parties were to default on the performance of their obligations under their respective contracts or determine to abandon or terminate support for a system, product or service that is significant to our business, we could suffer significant financial losses and operational problems, which could in turn adversely affect our financial condition, results of operations and cash flows.

Table of Contents

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

For 2008 directors' fees, each non-officer director may choose between (i) an amount in cash equal to \$10,000 plus the number of shares equal to \$10,000 divided by the share price on December 31, 2007, or (ii) if they accept all stock for their fee, the number of shares equal to \$30,000 divided by the share price on December 31, 2007. During the first nine months of 2008, the Company issued 120,000 shares of common stock, \$.01 par value, to members of its board of directors pursuant to this director compensation program. The shares were issued on January 29, 2008 to directors, each an accredited investor, as a private placement exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended and Regulation D. The Company received no consideration for the common stock issued.

Table of Contents

ITEM 6. EXHIBITS

(a) Exhibits.

- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Acting Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer and Acting Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Table of Contents

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.

Date: November 14, 2008

ASSURANCEAMERICA CORPORATION

By: /s/ Guy W. Millner
Guy W. Millner
Chairman and CEO

Date: November 14, 2008

/s/ Gregory D. Woods
Gregory D. Woods
Acting Chief Financial Officer