Amtrust Financial Services, Inc.
Form 10-Q
August 04, 2011

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

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2011

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

For the transition period from ___________________ to ___________________

Commission file no. 001-33143

AmTrust Financial Services, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	04-3106389 (IRS Employer Identification No.)
59 Maiden Lane, 6th Floor, New York, New York (Address of principal executive offices)	10038 (Zip Code)

(212) 220-7120
(Registrant’s telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x 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:

Large accelerated filer ¨ Accelerated filer x

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

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

As of July 29, 2011, the Registrant had one class of Common Stock ($.01 par value), of which 59,930,452 shares were issued and outstanding.

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PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements

AMTRUST FINANCIAL SERVICES, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(in thousands, except par value)

(Amounts in Thousands)	June 30, 2011 (Unaudited)	December 31, 2010 (Audited)
ASSETS		
Investments:		
Fixed maturities, available-for-sale, at market value (amortized cost $1,191,390; $1,192,844)	$ 1,222,419	$ 1,208,813
Equity securities, available-for-sale, at market value (cost $19,204; $18,577)	19,367	17,412
Short-term investments	98,480	32,137
Equity investment in unconsolidated subsidiary – related party	86,633	77,136
Other investments	22,008	21,514
Total investments	1,448,907	1,357,012
Cash and cash equivalents	256,446	201,949
Accrued interest and dividends	10,050	7,979
Premiums receivable, net	877,047	727,561
Reinsurance recoverable (related party $426,930; $386,932)	1,006,410	775,432
Prepaid reinsurance premium (related party $320,720; $283,899)	507,999	484,960
Prepaid expenses and other assets	495,296	163,905
Federal income tax receivable	2,009	10,269
Deferred policy acquisition costs	258,557	224,671
Property and equipment, net	44,779	30,889
Goodwill	107,731	106,220
Intangible assets	120,366	91,606
	$ 5,135,597	$ 4,182,453
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Loss and loss expense reserves	$ 1,688,737	$ 1,263,537
Unearned premiums	1,212,703	1,024,965
Ceded reinsurance premiums payable (related party $152,869; $95,629)	310,894	266,314
Reinsurance payable on paid losses	10,855	11,343
Funds held under reinsurance treaties	55,324	3,217
Securities sold but not yet purchased, at market	141	8,847
Securities sold under agreements to repurchase, at contract value	211,867	347,617
Accrued expenses and other current liabilities	296,406	195,060
Deferred income taxes	67,428	9,883
Note payable on collateral loan – related party	167,975	167,975
Revolving credit facility	98,200	—
Secured term loan	10,413	—
Non-interest bearing note payable – net of unamortized discount of $303; $600	7,197	14,400
Term loan	—	6,667
Junior subordinated debt	123,714	123,714

Total liabilities	4,261,854	3,443,539
Commitments and contingencies		
Redeemable non-controlling interest	600	600
Stockholders' equity:		
Common stock, $.01 par value; 100,000 shares authorized, 84,713 and 84,314 issued in 2011 and 2010, respectively; 59,913 and 59,565 outstanding in 2011 and 2010, respectively	847	844
Preferred stock, $.01 par value; 10,000 shares authorized	—	—
Additional paid-in capital	554,994	548,731
Treasury stock at cost; 24,800 and 24,816 shares in 2011 and 2010, respectively	(300,365)	(300,489)
Accumulated other comprehensive income (loss)	16,404	(266)
Retained earnings	553,478	467,694
Total AmTrust Financial Services, Inc. equity	825,358	716,514
Non-controlling interest	47,785	21,800
Total stockholders' equity	873,143	738,314
	$ 5,135,597	$ 4,182,453

See accompanying notes to unaudited condensed consolidated statements.

AmTrust Financial Services, Inc.
Condensed Consolidated Statements of Income
(Unaudited)
(in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Revenues:				
Premium income:				
Net written premium	$ 375,681	$ 196,394	$ 609,700	$ 385,808
Change in unearned premium	(127,399)	(133)	(161,080)	(41,447)
Net earned premium	248,282	196,261	448,620	344,361
Ceding commission – primarily related party	35,414	32,958	71,098	65,206
Service and fee income (related parties – three months $4,459; $2,880 and six months $7,898; $5,548)	24,542	9,121	49,731	17,087
Net investment income	13,167	14,686	27,359	28,285
Net realized gain (loss) on investments	616	(6,544)	1,031	(4,759)
Total revenues	322,021	246,482	597,839	450,180
Expenses:				
Loss and loss adjustment expense	170,008	121,510	298,704	211,331
Acquisition costs and other underwriting expenses	89,580	79,579	170,814	140,925
Other	18,564	9,336	38,760	15,570
Total expenses	278,152	210,425	508,278	367,826
Income before other income (expense), income taxes and equity in earnings of unconsolidated subsidiaries	43,869	36,057	89,561	82,354
Other income (expense):				
Foreign currency gain	2,520	755	2,236	38
Interest expense	(4,334)	(3,063)	(8,088)	(6,635)
Net gain on investment in life settlement contracts	22,638	—	41,524	—
Total other income (expense)	20,824	(2,308)	35,672	(6,597)
Income before income taxes and equity in earnings of unconsolidated subsidiaries	64,693	33,749	125,233	75,757
Provision for income taxes	12,126	8,839	24,468	24,007
Income before equity earnings of unconsolidated subsidiaries and non-controlling interest	52,567	24,910	100,765	51,750
Equity in earnings of unconsolidated subsidiaries – related parties	4,077	5,913	7,200	17,773
Net income	56,644	30,823	107,965	69,523
Net income attributable to non-controlling interest of subsidiaries	(6,482)	—	(12,620)	—
Net income attributable to AmTrust Financial Services, Inc.	50,162	30,823	95,345	69,523
Earnings per common share:				
Basic earnings per common share	$ 0.84	$ 0.52	$ 1.60	$ 1.17
Diluted earnings per common share	$ 0.81	$ 0.51	$ 1.55	$ 1.15
Dividends declared per common share	$ 0.08	$ 0.07	$ 0.16	$ 0.14

Net realized gain (loss) on investments:				
Total other-than-temporary impairment loss	$ (345)	$ (12,007)	$ (345)	$ (17,145)
Portion of loss recognized in other comprehensive income	—	—	—	—
Net impairment losses recognized in earnings	(345)	(12,007)	(345)	(17,145)
Other net realized gain on investments	961	5,463	1,376	12,386
Net realized investment gain (loss)	$ 616	$ (6,544)	$ 1,031	$ (4,759)

See accompanying notes to unaudited condensed consolidated financial statements.

AmTrust Financial Services, Inc.
Consolidated Statements of Cash Flows
(Unaudited)
(in thousands)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Cash flows from operating activities:		
Net income	$ 107,965	$ 69,523
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	31,764	7,945
Equity earnings and gain on investment in unconsolidated subsidiaries	(7,200)	(17,773)
Gain on investment in life settlement contracts	(41,524)	—
Realized gain marketable securities	(1,376)	(12,386)
Non-cash write-down of marketable securities	345	17,145
Discount on notes payable	298	450
Stock compensation expense	2,827	1,860
Bad debt expense	4,167	3,510
Foreign currency (gain) loss	(2,236)	(38)
Changes in assets - (increase) decrease:		
Premiums and note receivables	(130,990)	(162,419)
Reinsurance recoverable	(82,829)	(53,216)
Deferred policy acquisition costs, net	(33,886)	(42,340)
Prepaid reinsurance premiums	(23,039)	(35,907)
Prepaid expenses and other assets	(35,908)	(739)
Changes in liabilities - increase (decrease):		
Reinsurance premium payable	44,580	94,480
Loss and loss expense reserve	57,179	62,671
Unearned premiums	165,925	88,653
Funds held under reinsurance treaties	52,107	(70)
Deferred tax liability, net	(20,344)	(4,170)
Accrued expenses and other current liabilities	87,070	(10,896)
Net cash provided in operating activities	174,895	6,283
Cash flows from investing activities:		
Net (purchases) sales of securities with fixed maturities and short term investments	(72,409)	95,734
Net (purchases) sales of equity securities	(176)	4,502
Net (purchases) sales of other investments	(451)	(577)
Investment in ACAC	—	(53,055)
Acquisition of and capitalized premiums for life settlement contracts	(26,504)	—
Acquisition of subsidiaries, net of cash obtained	30,874	(3,553)
Purchase of property and equipment	(18,315)	(1,677)
Net cash (used in) provided by investing activities	(86,981)	41,374
Cash flows from financing activities:		
Repurchase agreements, net	(135,750)	65,478
Revolving credit facility borrowings	98,200	—
Secured loan agreement borrowings	10,800	—
Secured loan agreement repayment	(387)	—

Term loan payment	(6,667)	(6,667)
Capital contribution to subsidiary	12,515	—
Stock option exercise and other	3,563	790
Dividends distributed on common stock	(9,551)	(7,713)
Non-interest bearing note payment	(7,500)	(7,500)
Debt financing fees	(1,394)	—
Net cash (used in) provided by financing activities	(36,171)	44,388
Effect of exchange rate changes on cash	2,754	(9,446)
Net increase in cash and cash equivalents	54,497	82,599
Cash and cash equivalents, beginning of the period	201,949	233,810
Cash and cash equivalents, end of the period	$ 256,446	$ 316,409
Supplemental Cash Flow Information		
Income tax payments	$ 6,280	$ 7,258
Interest payments on debt	6,566	8,434

See accompanying notes to unaudited condensed consolidated financial statements.

Notes to Unaudited Condensed Consolidated Financial Statements
(Unaudited)
(dollars in thousands, except share data)

1. Basis of Reporting

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial statements and with the instructions to Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all of the information and footnotes required by GAAP for complete financial statements. These interim statements should be read in conjunction with the financial statements and notes thereto included in the AmTrust Financial Services, Inc. ("AmTrust" or the "Company") Annual Report on Form 10-K for the year ended December 31, 2010, previously filed with the Securities and Exchange Commission ("SEC") on March 15, 2011. The balance sheet at December 31, 2010 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements.

These interim consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary for a fair presentation of the results for the interim period and all such adjustments are of a normal recurring nature. The results of operations for the interim period are not necessarily indicative, if annualized, of those to be expected for the full year. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

A detailed description of the Company's significant accounting policies and management judgments is located in the audited consolidated financial statements for the year ended December 31, 2010, included in the Company's Form 10-K filed with the SEC.

All significant inter-company transactions and accounts have been eliminated in the consolidated financial statements. To facilitate period-to-period comparisons, certain reclassifications have been made to prior period consolidated financial statement amounts to conform to current period presentation. There was no effect on net income from the change in presentation.

2. Recent Accounting Pronouncements

With the exception of those discussed below, there have been no recent accounting pronouncements or changes in accounting pronouncements during the six months ended June 30, 2011, as compared to those described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2010, that are of significance, or potential significance, to the Company.

In June 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-05 Comprehensive Income (Topic 220). This update requires that all non-owner charges in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-step approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. The updated guidance is effective for fiscal years and interim periods beginning on or after December 15, 2011 and is to be applied on a retrospective basis to the beginning of the annual period of adoption. Early adoption is permitted and the amendment does not require any transition disclosure. The Company is currently assessing the impact of the adoption of this guidance, but does not anticipate any material impact on its results of operations, financial position or liquidity.

In May 2011, the FASB issued ASU No. 2011-04, Fair Value Measurement (Topic 820). The ASU generally aligns the principles for fair value measurements and the related disclosure requirements under GAAP and International Financial Reporting Standards ("IFRS"). ASU 2011-04 changes certain fair value measurement principles and enhances the disclosure requirements, particularly for Level 3 fair value measurements. The amendment is effective on a prospective basis for interim and annual reporting periods beginning after December 15, 2011 and early adoption is not permitted. The Company is currently assessing the impact of the adoption of this guidance, but does not anticipate any material impact on its results of operations, financial position or liquidity.

On April 29, 2011, the FASB amended its guidance on accounting for repurchase agreements. The amendments eliminate the criteria to assess whether a transferor must have the ability to repurchase or redeem the financial assets in order to demonstrate effective control over the transferred asset. Under the amended guidance, a transferor maintains effective control over transferred financial assets (and thus accounts for the transfer as a secured borrowing) if there is an agreement that both entitles and obligates the transferor to repurchase the financial assets before maturity and if all of the following conditions previously required are met: (i) financial assets to be repurchased or redeemed are the same or substantially the same as those transferred; (ii) repurchase or redemption date before maturity at a fixed or determinable price; and (iii) the agreement is entered into contemporaneously with, or in contemplation of, the transfer. As a result, more arrangements could be accounted for as secured borrowings rather than sales. The updated guidance is effective on a prospective basis for interim and annual reporting periods beginning on or after December 15, 2011, and early adoption is prohibited. The Company is currently evaluating the impact of the adoption of this new guidance on its consolidated results of operations and financial condition.

In April 2011, the FASB issued updated guidance to clarify whether a modification or restructuring of a receivable is considered a troubled debt restructuring, i.e., whether the creditor has granted a concession and whether the debtor is experiencing financial difficulties. A modification or restructuring that is considered a troubled debt restructuring will result in the creditor having to account for the receivable as being impaired and will also result in additional disclosure of the creditors' troubled debt restructuring activities. The updated guidance is effective for the first interim period beginning on or after June 15, 2011 and is to be applied on a retrospective basis to the beginning of the annual period of adoption. The adoption of this guidance is not expected to have a material impact on the Company's results of operations, financial position or liquidity.

In December 2010, the FASB issued authoritative guidance on disclosure of supplementary pro forma information for business combinations. The new guidance specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period. The new guidance became effective for the Company on January 1, 2011. The adoption of this guidance is not expected to have a material impact on the Company's results of operations, financial position or liquidity.

In October 2010, the FASB issued updated guidance to address the diversity in practice for the accounting for costs associated with acquiring or renewing insurance contracts. This guidance modifies the definition of acquisition costs to specify that a cost must be directly related to the successful acquisition of a new or renewal insurance contract in order to be deferred. If application of this guidance would result in the capitalization of acquisition costs that had not previously been capitalized by a reporting entity, the entity may elect not to capitalize those costs. The updated guidance is effective on either a retrospective or prospective basis for interim and annual reporting periods beginning after December 15, 2011, with early adoption permitted as of the beginning of a company's annual period. The Company is currently evaluating the impact of the adoption of this new guidance on its consolidated results of operations and financial condition.

3. Investments

(a) Available-for-Sale Securities

The original cost, estimated market value and gross unrealized appreciation and depreciation of available-for-sale securities as of June 30, 2011, are presented in the table below:

(Amounts in Thousands)	Original or amortized cost	Gross unrealized gains	Gross unrealized losses	Market value
Preferred stock	$ 6,029	$ 357	$ 42	$ 6,344
Common stock	13,175	1,456	1,608	13,023
U.S. treasury securities	92,204	1,928	328	93,804
U.S. government agencies	18,224	1,651	—	19,875
Municipal bonds	84,923	1,214	821	85,316
Corporate bonds:				
Finance	425,108	13,295	9,500	428,903
Industrial	50,663	2,241	56	52,848
Utilities	39,177	2,019	126	41,070
Commercial mortgage backed securities	1,568	111	—	1,679
Residential mortgage backed securities:				
Agency backed	470,641	18,658	131	489,168
Non-agency backed	7,868	848	4	8,712
Asset-backed securities	1,014	30	—	1,044
	$ 1,210,594	$ 43,808	$ 12,616	$ 1,241,786

In June 2011, the Company, through a subsidiary, purchased $12,500 of an aggregate $107,500 principal amount of 8.25% Senior Notes issued by Maiden Holdings North America, Ltd. that are fully guaranteed by Maiden Holdings, Ltd. ("Maiden"), both related parties. The Company has classified this fixed security in corporate finance bonds and its market value at June 30, 2011 was $12,500. For a further description of this transaction see Note 11. "Related Party Transactions".

Proceeds from the sale of investments in available-for-sale securities during the six months ended June 30, 2011 and 2010 were approximately $738,742 and $369,726, respectively.

A summary of the Company's available-for-sale fixed securities as of June 30, 2011, by contractual maturity, is shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Amounts in Thousands)	Amortized Cost	Fair Value
Due in one year or less	$ 8,544	$ 8,774
Due after one through five years	172,070	172,512
Due after five through ten years	403,511	413,724
Due after ten years	126,174	126,806
Mortgage backed securities	481,091	500,603
Total fixed maturities	$ 1,191,390	$ 1,222,419

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(b) Investment Income

Net investment income for the three and six months ended June 30, 2011 and 2010 was derived from the following sources:

(Amounts in Thousands)	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Fixed maturities	$ 12,302	$ 11,666	$ 25,976	$ 23,370
Equity maturities	120	32	286	359
Cash and cash equivalents	966	1,910	1,572	2,755
Note receivable – related party	—	1,204	—	2,049
	13,388	14,812	27,834	28,533
Less: Investment expenses and interest expense on securities sold under agreements to repurchase	221	126	475	248
	$ 13,167	$ 14,686	$ 27,359	$ 28,285

(c) Other-Than-Temporary Impairment

Other-than-temporary impairment ("OTTI") charges of our fixed-maturities and equity securities for the three and six months ended June 30, 2011 and 2010 are presented in the table below:

(Amounts in Thousands)	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Equity securities	$ 345	$ 1,467	$ 345	$ 6,605
Fixed maturities	-	10,540	-	10,540
	345	12,007	345	17,145

The table below summarizes the gross unrealized losses of our fixed maturity and equity securities by length of time the securities have continuously been in an unrealized position as of June 30, 2011:

	Less Than 12 Months			12 Months or More			Total	
(Amounts in Thousands)	Fair Market Value	Unrealized Losses	No. of Positions Held	Fair Market Value	Unrealized Losses	No. of Positions Held	Fair Market Value	Unrealized Losses
Common and preferred stock	$ 948	$ 581	7	$ 4,665	$ 1,069	58	$ 5,613	$ 1,650
U.S. treasury securities	51,590	328	8	—	—	—	51,590	328
Municipal bonds	51,387	821	15	—	—	—	51,387	821
Corporate bonds:								
Finance	116,309	2,768	28	94,203	6,732	13	210,512	9,500
Industrial	7,871	56	4	—	—	—	7,871	56
Utilities	23,401	126	3	—	—	—	23,401	126
Commercial Mortgage backed securities	—	—	—	—	—	—	—	—
Residential mortgage backed securities:								
Agency backed	112,605	131	11	—	—	—	112,605	131
Non-agency backed	—	—	—	25	4	1	25	4
	$ 364,111	$ 4,811	76	$ 98,893	$ 7,805	72	$ 463,004	$ 12,616

Total temporarily
impaired securities

There are 148 securities at June 30, 2011 that account for the gross unrealized loss, none of which is deemed by the Company to be OTTI. Significant factors influencing the Company's determination that unrealized losses were temporary included the magnitude of the unrealized losses in relation to each security's cost, the nature of the investment and management's intent not to sell these securities and it being not more likely than not that the Company will be required to sell these investments before anticipated recovery of fair value to the Company's cost basis.

The Company from time to time invests in a limited amount of derivatives and other financial instruments as part of its investment portfolio to manage interest rate changes or other exposures to a particular financial market. The Company records changes in valuation on its derivative positions not designated as a hedge as a component of net realized gains and losses. The Company records changes in valuation on its hedge positions as a component of other comprehensive income. As of June 30, 2011, the Company has two interest rate swaps that were entered into in June 2011 related to the Company's trust preferred securities and will take effect in September 2011 and June 2012.

(d) Other

Securities sold but not yet purchased represent obligations of the Company to deliver the specified security at the contracted price and, thereby, create a liability to purchase the security in the market at prevailing prices. The Company's liability for securities to be delivered is measured at their fair value and as of June 30, 2011 was $0 for corporate bonds and $141 related to equity securities. These transactions result in off-balance sheet risk, as the Company's ultimate cost to satisfy the delivery of securities sold but not yet purchased may exceed the amount reflected at June 30, 2011. Subject to certain limitations, all securities owned, to the extent required to cover the Company's obligations to sell or repledge the securities to others, are pledged to the clearing broker.

The Company enters into repurchase agreements, which are accounted for as collateralized borrowing transactions and are recorded at contract amounts. The Company receives cash or securities that it invests or holds in short term or fixed income securities. As of June 30, 2011, there were $211,867 principal amount outstanding at interest rates between 0.17% and 0.3%. Interest expense associated with these repurchase agreements for the three months ended June 30, 2011 and 2010 was $221 and $125, respectively, of which $0 was accrued as of June 30, 2011. Interest expense associated with the repurchase agreements for the six months ended June 30, 2011 and 2010 was $474 and $248, respectively. The Company has approximately $215,607 of collateral pledged in support of these agreements.

4. Fair Value of Financial Instruments

The following table presents the level within the fair value hierarchy at which the Company's financial assets and financial liabilities are measured on a recurring basis as of June 30, 2011:

(Amounts in Thousands)	Total	Level 1	Level 2	Level 3
Assets:				
U.S. treasury securities	$ 93,804	$ 93,804	$ —	$ —
U.S. government agencies	19,875	—	19,875	—
Municipal bonds	85,316	—	85,316	—
Corporate bonds:				
Finance	428,903	—	428,903	—
Industrial	52,848	—	52,848	—
Utilities	41,070	—	41,070	—
Commercial mortgage backed securities	1,679	—	1,679	—
Residential mortgage backed securities:				
Agency backed	489,168	—	489,168	—
Non-agency backed	8,712	—	8,712	—
Asset-backed securities	1,044	—	1,044	—
Equity securities	19,367	19,367	—	—
Short term investments	98,480	98,480	—	—
Other investments	22,008	—	—	22,008
Life settlement contracts	108,710	—	—	108,710
	$ 1,470,984	$ 211,651	$ 1,128,615	$ 130,718

Liabilities:								
Equity securities sold but not yet purchased, market	$	141	$	141	$	—	$	—
Securities sold under agreements to repurchase, at contract value		211,867		—		211,867		—
Life settlement contract profit commission		9,267		—		—		9,267
	$	221,275	$	141	$	211,867	$	9,267

The Company classifies its financial assets and liabilities in the fair value hierarchy based on the lowest level input that is significant to the fair value measurement. This classification requires judgment in assessing the market and pricing methodologies for a particular security. The fair value hierarchy includes the following three levels:

Level 1 – Valuations are based on unadjusted quoted market prices in active markets for identical financial assets or liabilities;

Level 2 – Valuations of financial assets and liabilities are based on prices obtained from third party pricing services, dealer quotations of the bid price using observable inputs, or through consensus pricing of a pricing service; and

Level 3 – Valuations are based on unobservable inputs for assets and liabilities where there is little or no market activity. Management's assumptions are used in internal valuation pricing models to determine the fair value of financial assets or liabilities.

For additional discussion regarding techniques used to value the Company's investment portfolio, refer to Note 2. "Significant Accounting Policies" in Item 8. "Financial Statements and Supplementary Data" in its 2010 Form 10-K.

The following table provides a summary of changes in fair value of the Company's Level 3 financial assets for the three and six months ended June 30, 2011 and 2010:

(Amounts in Thousands)	Balance as of March 31, 2011	Net income	Other comprehensive income	Purchases and issuances	Sales and settlements	Net transfers into (out of) Level 3	Balance as of June 30, 2011
Other investments	$ 22,512	$ —	$ (875)	$ 786	$ (415)	$ —	$ 22,008
Life settlement contracts	63,686	33,842	—	11,182	—	—	108,710
Life settlement contract profit commission	(5,589)	(3,678)	—	—	—	—	(9,267)
Total	$ 80,609	$ 30,164	$ (875)	$ 11,968	$ (415)	$ —	$ 121,451

(Amounts in Thousands)	Balance as of December 31, 2010	Net income	Other comprehensive income	Purchases and issuances	Sales and settlements	Net transfers into (out of) Level 3	Balance as of June 30, 2011
Other investments	$ 21,514	$ 661	$ (377)	$ 866	$ (656)	$ —	$ 22,008
Life settlement contracts	22,155	57,962	—	28,593	—	—	108,710
Life settlement contract profit commission	(4,711)	(4,556)	—	—	—	—	(9,267)
Total	$ 38,958	$ 54,067	$ (377)	$ 29,459	$ (656)	$ —	$ 121,451

(Amounts in Thousands)	Balance as of March 31, 2010	Net income	Other comprehensive income	Purchases and issuances	Sales and settlements	Net transfers into (out of) Level 3	Balance as of June 30, 2010

Other investments	$ 14,019	$ —	$ (685)	$ 108	$ (119)	$ —	$ 13,323
Derivatives	(353)	133	—	—	—	—	(220)
Total	$ 13,666	$ 133	$ (685)	$ 108	$ (119)	$ —	$ 13,103

(Amounts in Thousands)	Balance as of December 31, 2009	Net income	Other comprehensive income	Purchases and issuances	Sales and settlements	Net transfers into (out of) Level 3	Balance as of June 30, 2010
Other investments	$ 12,746	$ 277	$ 296	$ 123	$ (119)	$ —	$ 13,323
Derivatives	(1,893)	133	—	—	1,540	—	(220)
Total	$ 10,853	$ 410	$ 296	$ 123	$ 1,421	$ —	$ 13,103

The Company had no transfers between levels during the three and six months ended June 30, 2011 and 2010.

The Company uses the following methods and assumptions in estimating its fair value disclosures for financial instruments:

- Equity and Fixed Income Investments: Fair value disclosures for these investments are disclosed above in this note. The carrying values of cash, short term investments and investment income accrued approximate their fair values;

- Premiums Receivable: The carrying values reported in the accompanying balance sheets for these financial instruments approximate their fair values due to the short term nature of the asset;

- Subordinated Debentures and Debt: The carrying values reported in the accompanying balance sheets for these financial instruments approximate fair value. Fair value was estimated using projected cash flows, discounted at rates currently being offered for similar notes.

5. Debt

Junior Subordinated Debt

The Company has established four special purpose trusts for the purpose of issuing trust preferred securities. The proceeds from such issuances, together with the proceeds of the related issuances of common securities of the trusts, were invested by the trusts in junior subordinated debentures issued by the Company. In accordance with FASB ASC 810-10-25, the Company does not consolidate such special purpose trusts, as the Company is not considered to be the primary beneficiary. The equity investment, totaling $3,714 as of June 30, 2011 on the Company's consolidated balance sheet, represents the Company's ownership of common securities issued by the trusts. The debentures require interest-only payments to be made on a quarterly basis, with principal due at maturity. The debentures contain covenants that restrict declaration of dividends on the Company's common stock under certain circumstances, including default of payment. The Company incurred $2,605 of placement fees in connection with these issuances, which is being amortized over thirty years. The Company recorded $2,552 of interest expense for the three months ended June 30, 2011 and 2010 and $5,104 of interest expense for the six months ended June 30, 2011 and 2010, respectively, related to these trust preferred securities.

The table below summarizes the Company's trust preferred securities as of June 30, 2011:

(Amounts in Thousands) Name of Trust	Aggregate Liquidation Amount of Trust Preferred Securities	Aggregate Liquidation Amount of Common Securities	Aggregate Principal Amount of Notes	Stated Maturity of Notes	Per Annum Interest Rate of Notes	
AmTrust Capital Financing Trust I	$ 25,000	$ 774	$ 25,774	3/17/2035	8.275%	(1)
AmTrust Capital Financing Trust II	25,000	774	25,774	6/15/2035	7.710	(1)
AmTrust Capital Financing Trust III	30,000	928	30,928	9/15/2036	8.830	(2)
AmTrust Capital Financing Trust IV	40,000	1,238	41,238	3/15/2037	7.930	(3)
Total trust preferred securities	$ 120,000	$ 3,714	$ 123,714			

(1) The interest rate will change to three-month LIBOR plus 3.40% after the tenth anniversary in 2015.
(2) The interest rate will change to LIBOR plus 3.30% after the fifth anniversary in 2011.
(3) The interest rate will change to LIBOR plus 3.00% after the fifth anniversary in 2012.

In June 2011, the Company entered into two interest rate swap agreements related to these junior subordinated debentures. Each agreement is for a period of five years and will commence upon their respective tranche's interest rate changing from a fixed rate to a variable rate on their fifth anniversary in 2011 and 2012.

Revolving Credit Agreement

On January 28, 2011, the Company entered into a three-year, $150,000 credit agreement (the "Credit Agreement"), among JPMorgan Chase Bank, N.A., as Administrative Agent, The Bank of Nova Scotia, as Syndication Agent, SunTrust Bank, as Documentation Agent, and the various lending institutions party thereto. The credit facility is a revolving credit facility with a letter of credit sublimit of $50,000 and an expansion feature not to exceed $50,000. Proceeds of borrowings under the Credit Agreement may be used for working capital, acquisitions and general corporate purposes. In connection with entering into the Credit Agreement, the Company terminated the then existing Term Loan and Uncommitted Line of Credit Letter Agreement with JPMorgan Chase Bank, N.A.

ABR borrowings (which are borrowings bearing interest at a rate determined by reference to the Alternate Base Rate) under the Credit Agreement will bear interest at (x) the greatest of (a) the Administrative Agent's prime rate, (b) the federal funds effective rate plus 0.5 percent or (c) the adjusted LIBO rate for a one month interest period on such day plus 1 percent, plus (y) a margin that is adjusted on the basis of the Company's consolidated leverage ratio. Eurodollar borrowings under the credit agreement will bear interest at the adjusted LIBO rate for the interest period in effect plus a margin that is adjusted on the basis of the Company's consolidated leverage ratio.

The Credit Agreement contains certain restrictive covenants customary for facilities of this type (subject to negotiated exceptions and baskets), including restrictions on indebtedness, liens, acquisitions and investments, restricted payments and dispositions. There are also financial covenants that require the Company to maintain a minimum consolidated net worth, a maximum consolidated leverage ratio, a minimum fixed charge coverage ratio, a minimum risk-based capital and a minimum statutory surplus. The Company was in compliance with all covenants as of June 30, 2011.

Effective June 30, 2011, the "Company entered into a Waiver and Amendment No. 1 ("Amendment") to its Credit Agreement. The Amendment modifies certain restrictive covenants (indebtedness, liens and acquisitions) to permit the Company's acquisition of certain assets and liabilities of Majestic Insurance Company ("Majestic"), as described in Note 12. "Acquisitions" and provides for a waiver of the Company's compliance with a December 31, 2010 requirement under Section 6.15(d), a financial covenant.

As of June 30, 2011, the Company had outstanding borrowings of $98,200 under this Credit Agreement. The Company has outstanding letters of credit in place under the agreement at June 30, 2011 for $48,237, which reduced the availability on the line of credit for letters of credit to $1,763 and the availability under the facility to $3,563 as of June 30, 2011. The Company did not record a gain or loss on the extinguishment of its previous term loan. The Company recorded approximately $1,140 of deferred financing costs related to the Credit Agreement. Fees payable by the Company under the Credit Agreement include a letter of credit participation fee (which is the margin applicable to Eurodollar borrowings and was 2.25% at June 30, 2011), a letter of credit fronting fee with respect to each letter of credit (.125%) and a commitment fee on the available commitments of the lenders (a range of .35% to .45% based on the Company's consolidated leverage ratio and was .40% at June 30, 2011). On July 1, 2011, the Company repaid $90,000 of its outstanding borrowings under the Credit Agreement, which had been set aside for the Company's acquisition of a Luxembourg domiciled captive insurance company, reducing its outstanding borrowings amount to $8,200.

The interest rate on the credit facility as of June 30, 2011 was 2.50%. The Company recorded interest expense of approximately $1,023 and $1,418 for the three and six months ended June 30, 2011, respectively, under the Credit Agreement. The Company recorded interest expense of approximately $0 and $33 for the three months ended June 30, 2011 and 2010, respectively, and $72 and $65 for the six months ended June 30, 2011 and 2010, respectively, related to the term loan.

Secured Loan Agreement

During February 2011, the Company entered into a seven-year secured loan agreement with Bank of America Leasing & Capital, LLC in the aggregate amount of $10,800 to finance the purchase of an aircraft. The loan bears interest at a fixed rate of 4.45%, requires monthly installment payments of approximately $117 commencing on March 25, 2011 and ending on February 25, 2018, and a balloon payment of $3,240 at the maturity date. The Company recorded approximately $70 of deferred financing costs related to this agreement. The Company recorded interest expense of approximately $119 and $170 for the three and six months ended June 30, 2011, respectively, related to this agreement. The loan is secured by an aircraft that a Company subsidiary acquired in February 2011.

The agreement contains certain covenants that are similar to the Company's revolving credit facility. Additionally, subsequent to February 25, 2012, but prior to payment in full, if the outstanding balance of this loan exceeds 90% of the fair value of the aircraft, the Company is required to pay the lender the entire amount necessary to reduce the outstanding principal balance to be equal to or less than 90% of the fair value of the aircraft. The agreement allows the Company, under certain conditions, to repay the entire outstanding principal balance of this loan without penalty.

Promissory Note

In connection with the stock and asset purchase agreement with a subsidiary of Unitrin, Inc. ("Unitrin"), the Company, on June 1, 2008, issued a promissory note to Unitrin in the amount of $30,000. The note is non-interest bearing and requires four annual principal payments of $7,500. The first three annual principal payments were paid between 2009 and 2011, and the remaining principal payment is due on June 1, 2012. Upon entering into the promissory note, the Company calculated imputed interest of $3,155 based on interest rates available to the Company, which was 4.5%. Accordingly, the note's carrying balance was adjusted to $26,845 at the acquisition. The note is required to be paid in full, immediately, under certain circumstances including a default of payment or change of control of the Company. The Company included $135 and $210 of amortized discount on the note in its results of operations for the three months ended June 30, 2011 and 2010, respectively, and $298 and $450 for the six months ended June 30, 2011 and 2010, respectively. The note's carrying value at June 30, 2011 was $7,197.

Other Letters of Credit

In addition to the aforementioned letters of credit, the Company, through certain subsidiaries, has additional stand-by letters of credit as of June 30, 2011 in the amount of $2,962.

Maturities of Debt

Maturities of the Company's debt subsequent to June 30, 2011 are as follows:

(Amounts in Thousands)	2011	2012	2013	2014	2015	Thereafter
Junior subordinated debt	$ —	$ —	$ —	$ —	$ —	$ 123,714
Revolving credit facility	—	—	—	98,200	—	—
Secured loan	395	977	1,021	1,068	1,116	5,836
Promissory note	—	7,197	—	—	—	—
Total	$ 395	$ 8,174	$ 1,021	$ 99,268	$ 1,116	$ 129,550

6.Acquisition Costs and Other Underwriting Expenses

The following table summarizes the components of acquisition costs and other underwriting expenses for the three and six months ended June 30, 2011 and 2010:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Amounts in Thousands)	2011	2010	2011	2010
Policy acquisition expenses	$ 56,499	$ 50,122	$ 103,316	$ 75,413
Salaries and benefits	31,969	23,062	59,891	48,415
Other insurance general and administrative expenses	1,112	6,395	7,607	17,097
	$ 89,580	$ 79,579	$ 170,814	$ 140,925

7. Earnings Per Share

Effective January 1, 2009, the Company adopted ASC subtopic 260-10, Determining Whether Instruments Granted in Share-Based Payments Transactions Are Participating Securities. ASC 260-10 provides that unvested share-based

payment awards that contain nonforfeitable rights to dividends or dividend equivalents, whether paid or unpaid, are participating securities and are to be included in the computation of earnings per share under the two-class method. The Company's unvested restricted shares contain rights to receive nonforfeitable dividends and are participating securities, requiring the two-class method of computing earnings per share.

The following table is a summary of the elements used in calculating basic and diluted earnings per share for the three and six months ended June 30, 2011 and 2010:

(Amounts in Thousands except per share)	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Basic earnings per share:				
Net income attributable to AmTrust Financial Services, Inc. shareholders	$ 50,162	$ 30,823	$ 95,345	$ 69,523
Less: Net income allocated to participating securities and redeemable non-controlling interest	39	26	64	32
Net income allocated to AmTrust Financial Services, Inc. common shareholders	$ 50,123	$ 30,797	$ 95,281	$ 69,491
Weighted average common shares outstanding –				