



First Quarter  
**2011**

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Management's Discussion and Analysis  
For the quarter ended March 31, 2011

Atlas Financial Holdings, Inc.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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June 20, 2011

Atlas Financial Holdings, Inc. ("Atlas" or the "Company") is listed on the TSX Venture Exchange (TSXV) under the symbol AFH and began trading on January 6, 2011 having completed its reverse triangular merger with JJR VI Acquisition Corp. ("JJR VI") a wholly-owned subsidiary of JJR VI on December 31, 2010.

The following Management's Discussion and Analysis ("MD&A"), which was approved by the Atlas Board of Directors for the quarter ended March 31, 2011, is intended to enable the reader to assess the Company's results of operations and financial conditions for the three-month period ended March 31, 2011, compared to the corresponding period in 2010. It should be read in conjunction with the Company's unaudited consolidated financial statements and accompanying notes as of and for the quarter ended March 31, 2011, as well as the MD&A and the audited consolidated financial statements in the Company's 2010 Annual Report. All amounts herein are expressed in United States dollars.

Because the Company was formed through a reverse triangular merger, the consolidated financial statements are those of Atlas and its subsidiaries and have been prepared in accordance with *IFRS 3 – Business Combinations* and *IAS 27 – Consolidated and Separate Financial Statements*. Accordingly, and as a result of the December 31, 2010 merger date, shareholder's equity and earnings per share information provided herein reflect the common shares outstanding at the date of the merger as well as the ordinary common voting shares, restricted common voting shares and preferred shares that were issued in connection with the merger, as if such capitalization structure were in place during each of the periods for which financial information is being provided.

Atlas developed and is implementing a strategic business plan that focuses on target lines of business. These core lines of business historically produced an underwriting profit prior to the most recent years and are expected to produce profits post-merger based on the Company's going forward business model. Although actions were taken to terminate or transition non-core lines of business, the Company's loss ratio will continue to reflect the results of these lines during 2011 while gross premium written in the past become net premium earned. The impact of terminated non-core lines of business will be reduced as net premium earned related to these lines continue to shrink and become marginally smaller as a percentage of overall net premium earned. This positive affect should accelerate as the volume of net premium earned related to core business increases. In the first quarter 2011, non-recurring expenses in the amount of \$627,000 related to the reverse merger and transition related activities were incurred. These expenses will not continue. A primary objective of Atlas' business plan is to re-capture core business which was lost during the two years prior to the merger. Atlas' distribution channel and customer base are responding positively to the execution of the Company's strategic plan; however, it will take time for the Company to re-energize and rebuild business volumes to levels that optimize operational efficiency and profitability.

In the insurance business, premiums charged for various products are set without certainty of the benefit and claim costs that will be incurred, often many years after issuance or expiration of the related policies. Management therefore conducts the business with a primary focus on achieving favorable underwriting results over the long term. To achieve these objectives, adherence to insurance risk management principles is stressed, and asset diversification and quality are emphasized.

In addition to income from underwriting and claim related functions, significant investment income is earned from investing funds generated by those activities and from shareholders' equity. Investment management aims for stability of income from interest and dividends, protection of capital, and managing liquidity to meet underwriting and other obligations as they become payable in the future. Securities trading and the realization of capital gains are not in the strategic plan. The investment philosophy emphasizes value and credit quality.

Despite the fact that the Company first began operations in its current form on December 31, 2010, management of the Company is seasoned in the industry and the insurance subsidiaries have a long history of operations under previous ownership. Company affairs are managed for the long run. The Company's operating results and financial condition will best be evaluated by observing operating performance trends over the next five to ten years. This time

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# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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frame will likely encompass one or two underwriting cycles, providing appropriate time for those cycles to run their course and for reserved claim costs to be quantified with greater certainty.

### Caution Regarding Forward Looking Statements

This MD&A contains “forward-looking information” which may include, but is not limited to, statements with respect to estimates of future expenses, revenue and profitability; trends affecting financial condition and results of operations; the availability and terms of additional capital; dependence on key suppliers, manufacturers and strategic partners; industry trends and the competitive and regulatory environment; the impact of losing one or more senior executives or failing to attract additional key personnel; and other factors referenced in this MD&A.

Often, but not always, forward-looking statements can be identified by the use of words such as “plans”, “expects”, “is expected”, “budget”, “scheduled”, “estimates”, “forecasts”, “intends”, “anticipates”, or “believes” or variations (including negative variations) of such words and phrases, or state that certain actions, events or results “may”, “could”, “would”, “might” or “will” be taken, occur or be achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Such factors include, among others, general business, economic, competitive, political, regulatory and social uncertainties.

Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results to differ from those anticipated, estimated or intended. Forward-looking statements contained herein are made as of the date of this MD&A and the Company disclaims any obligation to update any forward-looking statements, whether as a result of new information, future events or results or otherwise. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements due to the inherent uncertainty in them.

Additional information relating to the Company is available on SEDAR at [www.sedar.com](http://www.sedar.com) or from the Company’s website at [www.atlas-fin.com](http://www.atlas-fin.com). The information contained on the Company’s website is not incorporated by reference in this MD&A and should not be considered a part of this MD&A.

# Atlas Financial Holdings, Inc.

Management Discussion and Analysis – Q1 2011

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## Table of Contents

Section	Description	Page
I	Corporate Overview	5
II	Consolidated Performance	10
III	U.S. Commercial Property and Casualty Industry Outlook	11
IV	Business Development and Operating Environment	13
V	Operating Results	14
VI	Financial Condition	21
VII	Accounting and Disclosure Matters	31
VIII	Related Party Transactions	34
IX	Risk Management	35
X	Subsequent Events	35
XI	Outlook	36

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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### I. CORPORATE OVERVIEW

#### Formation of the Company

The Company was formed on December 31, 2010 through a business combination structured as a reverse triangular merger (the “merger”) amongst:

- a) JJR VI, a “Capital Pool Company” within the meaning of TSXV policies incorporated under the laws of the Province of Ontario, Canada, and continued under the laws of the Cayman Islands;
- b) American Insurance Acquisition Inc. (“American Acquisition”), a wholly-owned indirect subsidiary of Kingsway Financial Services Inc. incorporated under the laws of Delaware by Kingsway America Inc.; and,
- c) Atlas Acquisition Corp., a wholly-owned subsidiary of JJR VI incorporated under the laws of Delaware,

Pursuant to the merger, Atlas Acquisition Corp. merged with and into American Acquisition and American Acquisition as the surviving company became a wholly-owned subsidiary of JJR VI. The merger constituted the “Qualifying Transaction” for JJR VI pursuant to TSXV policies. Prior to closing, JJR VI was continued under the laws of the Cayman Islands and became subject to the Companies Law of the Cayman Islands (as amended) as if it had been originally incorporated as a corporation under the laws of the Cayman Islands, and was renamed Atlas Financial Holdings, Inc. on closing of the merger.

The Company commenced operations under its current structure on December 31, 2010. Atlas ordinary voting common shares and restricted voting common shares (collectively the “voting common shares”) began trading on the TSXV under the symbol “AFH” on January 6, 2011.

Prior to the merger, Kingsway America, Inc. transferred 100% of the capital stock of its insurance subsidiaries, American Service Insurance Company (“American Service”) and American Country Insurance Company (“American Country”) to American Acquisition in exchange for \$35.1 million of American Acquisition common shares, \$18.0 million of American Acquisition preferred shares and promissory notes aggregating C\$7.9 million payable by American Acquisition. In addition, American Acquisition raised C\$7.9 million through a private placement offering of subscription receipts to qualified investors at a price of C\$2.00 per subscription receipt. American Country and American Service are sometimes referred to in this document as the Company’s “Operating Insurance Subsidiaries”.

In the merger, Kingsway America Inc. received 13.8 million restricted voting shares valued at \$27.4 million, 18 million non-voting preferred shares valued at \$18.0 million, and C\$7.9 million in cash from the private placement in exchange for 100% of the outstanding shares of American Acquisition and full payment of the promissory notes. Investors in the American Acquisition subscription receipt private placement received approximately 4 million ordinary voting shares plus warrants to purchase one ordinary voting share for each subscription receipt at C\$2.00 at any time until December 31, 2013 (three years after the closing of the merger). As part of the merger, JJR VI common shares held by former shareholders of JJR VI were consolidated on the basis of one post-consolidation JJR VI common share for every ten pre-consolidation JJR VI common shares, which post-consolidation JJR VI common shares were then exchanged on a one-for-one basis for 570,000 Atlas ordinary voting shares, with the surviving corporation surviving under the name Atlas.

Pursuant to Atlas’ Articles of Association, if the number of outstanding restricted voting shares exceeds 30% of the total number of all issued and outstanding voting shares, the votes attached to each restricted voting share will

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

decrease automatically without further act or formality to equal the maximum permitted vote per restricted voting share such that the restricted voting shares as a class shall not carry more than 30% of the votes eligible to be voted at a general meeting of Atlas shareholders.

Based on the foregoing limitation, voting rights of the remaining Atlas shareholders were leveraged up by 2.82X immediately following the merger. The approximate voting control is illustrated below:

**Table 1 Voting Control**

	Voting Shares Ownership	
	Economic Interest	Voting Interest
Kingsway America, Inc.	75.2%	30.0%
Atlas Investors LLC	6.2%	17.6%
Other Investors (includes Atlas Management)*	15.5%	43.6%
Original JJR VI Acquisition Corporation Shareholders*	3.1%	8.8%
	100.0%	100.0%

*\*Each individual investor in these groups controls less than 10% of voting rights of the Company after applying voting leverage created by the Restricted Voting Shares.*

The business is exclusively in the U.S. at this time and the Company's operating headquarters is 150 Northwest Point Boulevard, Elk Grove Village, IL 60007. Atlas maintains a registered office at Cricket Square, Hutchins Drive, PO Box 2681, Grand Cayman, KY1-1111, Cayman Islands.

### Adoption of IFRS

The Company adopted IFRS commencing with the presentation of its interim consolidated financial statements (unaudited) for the three months ended March 31, 2011. Comparative results and balances for 2010 have been restated to comply with IFRS. The Company previously presented its financial statements in accordance with U.S. generally accepted accounting principles.

The outstanding preferred shares are entitled accrued dividends on a cumulative basis whether or not declared by the Board of Directors. In accordance with IAS-32, *Financial Instruments: Presentation*, because of their mandatory dividend feature the preferred shares are deemed to contain both a liability and an equity component. The liability component is the estimated fair value of the future dividends the Company estimates will accrue beginning on December 31, 2010 through the date on which the preferred shares are either redeemed, at the option of the Company, or converted into ordinary restricted voting common shares, at the option of the holder. The liability component, classified as a present value liability for preferred dividends, is \$2,647, and the preferred equity component, classified in shareholders' equity, is \$15,353 at January 1, 2010, December 31, 2010 and March 31, 2011, respectively, in the accompanying balance sheet. The liability component is recognized at fair value with a corresponding charge to interest expense at the rate of 8.6% per year.

Other than what is described above, there was no impact on the Company's opening balance sheet, as of January 1, 2010, the transition date to IFRS; nor were there any significant reconciling items to report in shareholders' equity as of January 1, March 31 or December 31, 2010 or comprehensive income for the three months ended March 31, 2010 or the year ended December 31, 2010. See section 'IX. Accounting and Disclosure Matters' below for additional information related to the adoption of IFRS

### Outstanding Shares

Table 2 below illustrates the amount of outstanding shares, options and warrants of the Company at March 31, 2011 and at December 31, 2010:

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

**Table 2 Outstanding shares**

	<b>Outstanding At March 31, 2011</b>	<b>Outstanding At December 31, 2010</b>
Ordinary voting common shares	4,569,205	4,553,502
Restricted voting common shares	13,804,861	13,804,861
Total voting common shares	18,374,066	18,358,363
Preferred shares	18,000,000	18,000,000
Stock options	464,646	110,600
Warrants	3,983,502	3,983,502

### Stock Options

On January 3, 2011, Atlas adopted a 10% rolling stock option plan (the “Stock Option Plan”) in order to advance the interests of the Company by providing eligible persons with incentives. The maximum number of common shares reserved under the Stock Option Plan together with all other security-based compensation arrangements of the Company is equal to 10% of the issued and outstanding ordinary voting common shares at the dates of grant. Options cancelled, expired or forfeited are available for grant.

On January 18, 2011 Atlas granted options to purchase 369,749 ordinary voting common shares to directors and officers of the Company at an exercise price of C\$2.00 per share. The options vest 25% at the date of grant and 25% on each of the next three anniversary dates of the grant date and expire on January 18, 2021. These options will be accounted for under *International Financial Reporting Standard – 2 Share-based Payments*. The fair value of these options was \$450,389 using the Black-Scholes option pricing model. Compensation expense will be charged to income over the vesting period based on the number of options expected to vest.

On February 1, 2011, 15,703 of the options issued during 2010 were exercised.

As at the date of this MD&A, there are 464,646 Atlas options outstanding with a weighted average exercise price of C\$1.80.

### Warrants

In connection with and at the date of the merger, Atlas issued 3,983,502 new ordinary voting common shares. Each shareholder of these newly issued ordinary voting common shares was also issued non-transferable warrants equal to the amount of ordinary voting common shares held. The warrants provide the holder the right to purchase Atlas ordinary voting common shares at a purchase price of C\$2.00. These warrants expire on December 31, 2013. From the date of grant through March 31, 2011 no warrants have been exercised.

### Operating Insurance Subsidiaries

The business of the Company is carried on through the Operating Insurance Subsidiaries. The Operating Insurance Subsidiaries distribute their insurance products through a network of retail independent agents. Together, American Country and American Service are licensed to write P&C insurance in 47 states in the United States. The management of American Country and American Service is fully integrated with a single operating infrastructure supporting both.

With roots dating back to 1925 selling insurance for taxi cabs, American Country is one of the oldest insurers of the

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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U.S. taxi and livery business. For more than 75 years, American Country expanded its expertise in this and other areas of specialty insurance. American Country was a wholly-owned subsidiary of Kingsway America Inc. prior to the merger.

For over 25 years, American Service developed expertise in the area of specialty auto insurance. It was incorporated under the laws of the state of Illinois on March 11, 1983 and commenced operations on April 18, 1983 as a non-standard personal and commercial auto insurer writing business in the Chicago, Illinois area.

Effective January 1, 2009, American Service and American Country formed a statutory pool (the “American Service Pool”), pursuant to which American Country cedes 100% of its net premium written, related liabilities and certain operating expenses to American Service. American Service then retrocedes 30% of the pooled net premium written, related liabilities and certain operating expenses to American Country and retains the remaining 70% of the pool.

As a result of the successful completion of the merger, on January 6, 2011, A.M. Best Co. upgraded the Financial Strength Rating of the Operating Insurance Subsidiaries to “B” from “B-”. Simultaneous to the upgrades for the Operating Insurance Subsidiaries, A.M. Best Co. also upgraded the American Service Pool to “B” from “B-”. A.M. Best Co. assigned an outlook of “stable” to the Financial Strength Ratings of the Operating Insurance Subsidiaries and eliminated the status of “under review with developing implications”. A.M. Best Co. also upgraded the Issuer Credit Ratings of the Operating Insurance Subsidiaries to “bb” from “bb-”, and issued an Issuer Credit Rating of “b-” to Atlas. The outlook assigned to the Issuer Credit Ratings was “stable”.

### Continuation Accounting

As previously indicated, the Company was formed through a reverse triangular merger and these consolidated financial statements are those of Atlas and subsidiaries and have been prepared in accordance *with IFRS 3 – Business Combinations* and *IAS 27 Consolidated and Separate Financial Statements*. Under these standards the financial statements prepared following the reverse merger are presented in the name of the legal parent acquirer, Atlas, but are a continuation of the financial statements of the accounting acquirer, American Acquisition, with an adjustment for the capital structure (that is the number and type of equity interests, including equity instruments issued to effect the merger) of Atlas, as the legal parent acquirer and accounting acquiree. Accordingly, and as a result of the December 31, 2010 merger date, shareholders’ equity at December 31, 2010 and January 1, 2010 each reflect the common shares outstanding at the date of the merger together with the ordinary voting common shares, restricted voting common shares and preferred shares that were issued to effect the merger, and also reflect the historical retained earnings (retained deficit) balances of American Acquisition, as the accounting acquirer.

For more information with respect to the impacts of the merger on the Company, see the Filing Statement to the qualifying transaction dated December 16, 2010 that includes the pro forma financial statements which can be accessed on SEDAR at [www.sedar.com](http://www.sedar.com).

### Go-Forward Earnings

The business activities pre-merger and costs and impacts of prior ownership structure negatively impacted historical results and thus the financial statements for the three months ended March 31, 2010 and for the year ended December 31, 2010 for the Company will not provide an accurate overview of likely future results of the operations for the following reasons:

- Results of operations for the three months ended March 31, 2010 and for the year ended December 31, 2010

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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include significant non-recurring expenses relating to the close of the merger and transition to Atlas' go-forward business model.

- Business mix and volume will be different in the future, consistent with the Company's business strategy. A number of non-profitable and non-strategic lines of business have been discontinued. Some previously profitable lines of business which were de-emphasized under the former owner's business strategy are the Company's go-forward focus. As they become a relatively larger portion of the Company's book of business, the underwriting results from these lines will trend towards go-forward business.
- Cost savings are being achieved as a result of combining the Operating Insurance Subsidiaries' operations coupled with other expense reduction initiatives. Non-recurring costs were incurred in 2010 and early 2011 relating to strategic reorganization and realignment of the operations.

### **Merger Impact on Income Taxes**

The change in ownership from the merger triggered certain considerations with respect to the U.S. tax laws and their impact to the Company. First, the U.S. tax laws allow the selling company, in this case Kingsway America Inc., to retain certain tax assets of the departing company. In addition, to discourage the sale of a company with tax losses solely due to value of the future tax deduction for the tax loss, U.S. tax law generally provides for limits on the amounts of tax losses that can be utilized after such a sale. These tax law limitations, and related provisions within the merger agreement executed as part of the merger, limit the amount of the Company's prior tax losses that can be used after the merger. As a result of the two aforementioned U.S. tax laws, the Company has written down its deferred tax asset related to loss carry-forwards to the amount that can be realized against future taxable income. Prior to the merger and while under the management of its prior ownership, the Company had partially reduced the value of tax assets related to loss carry-forwards to their anticipated realizable value, also, the Company has reassessed its future utilization of the remaining deferred tax assets and has further reduced realizable deferred tax assets for certain items thereon, and, correspondingly had recorded this adjustment through income in the fourth quarter of 2010. As of March 31, 2011, there were \$12.1 million of tax affected net operating loss carry-forwards that are available to the Company of which \$2.2 million are carried on the March 31, 2011 as realizable.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

### II. CONSOLIDATED PERFORMANCE

#### First Quarter Highlights

The following financial data is derived from the Company's unaudited consolidated financial statements for the quarters ended March 31, 2011 and 2010:

**Table 3 Selected financial information**

(in thousands of dollars except percentages)

Quarter ended March 31,	2011	2010
<i>Gross premium written</i>	\$14,166	\$18,686
Net premium earned	8,809	19,301
Losses on claims	6,889	15,345
Acquisition costs	1,779	4,015
Other underwriting expenses	2,411	4,575
Net underwriting (loss)	(2,270)	(4,634)
Net investment and other income	1,381	2,240
Loss before tax	(889)	(2,394)
Income tax benefit	-	(811)
Loss attributable to common shareholders	(\$889)	(\$1,583)
<b>Key Financial Ratios:</b>		
Loss ratio	78.2%	79.5%
Acquisition cost ratio	20.2%	20.8%
Other Underwriting Expense ratio (net of fee income of \$236 for Q1 '11 and \$573 for Q1'10)	24.7%	20.7%
Combined operating ratio	123.1%	121.0%
Return on equity for quarter	(1.4%)	(3.0%)
(Loss) per common voting share (basic & diluted)	(\$0.05)	(\$0.09)
Book value per common voting share	\$2.19	\$2.30

*Note: Net of fee income which was included in the "other income" line, net underwriting results for the first quarters of 2011 and 2010 were (\$2.0) million and (\$4.1) million, respectively.*

- Shareholders' equity was \$55.7 million at March 31, 2011, factoring in the Company's convertible preferred shares, common shareholders' equity was \$40.2 million or \$2.19 per voting common share.
- Provision against deferred tax asset currently deemed unrealizable in the amount of \$0.54 per common share at March 31, 2011.
- Gross premium written was \$14.2 million for the quarter ended March 31, 2011 representing a 52.8% increase over the fourth quarter of 2010 and a 24.3% decrease as compared to the first quarter of 2010.
- The core commercial automobile gross premium written in the first quarter 2011 was \$6.6 million, representing an increase of 113% over Q4 of 2010 and a decrease of 37.1% over first quarter 2010.
- Including \$627,000 of non-recurring charges related to the merger and costs related to the Company's "go-forward" infrastructure, the Company reported a net loss of \$889,000 or \$0.05 per voting common share diluted as compared to a loss of \$1,583,000 or \$0.09 per voting common share diluted for the first quarter of 2010 and a

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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loss of \$11,430,000 or \$0.62 per voting common share for the fourth quarter of 2010. Excluding these non-recurring charges, the first quarter 2011 loss would have been \$205,000 or \$0.01 per diluted share.

- The Company's loss and loss adjustment expense ratio was 78.2% in the first quarter 2011 as compared with 79.5% in the first quarter of 2010 and 87.0% in the fourth quarter of 2010. This improvement was due to core lines of business becoming an increasingly larger percentage of total net premium earned.
- Other underwriting expenses in the first quarter 2011 were \$2.4 million, lower by 47.3% from the first quarter of 2010 and lower by 45.8% from the fourth quarter 2010. Expense reductions were the result of strategic activities and contract renegotiations undertaken to align the Company's infrastructure with its business plans, as well as the elimination of management fees and other costs allocated by the Company's previous parent to the Operating Insurance Subsidiaries.
- Including non-recurring costs, the Company's combined operating ratio was 123.1% for the first quarter 2011 as compared with 140.7% in the prior quarter and 121.0% from the first quarter of 2010. Excluding non-recurring costs, the Company's combined operating ratio would have been 116.0% in the first quarter of 2011.

### **III. U.S. COMMERCIAL PROPERTY AND CASUALTY OUTLOOK**

The primary business of the Company is commercial automobile insurance in the United States, with a niche market orientation and focus on insurance for the "light" commercial automobile sector including taxi cabs, non-emergency paratransit, limousine, livery and business auto. Automobile insurance products provide coverage in three major areas: liability, accident benefits and physical damage. Liability insurance provides coverage where the insured is responsible for an automobile accident, for the payment of claims for injuries and property damage to third parties. Accident benefit policies or personal injury protection policies provide coverage for loss of income, medical and rehabilitation expenses for insured persons who are injured in an automobile accident, regardless of fault. Physical damage coverage provides for the payment of damages to an insured automobile arising from a collision with another object or from other risks such as fire or theft. In the short run, automobile physical damage and liability coverage generally provide more predictable results than automobile accident benefit or personal injury insurance. The distinct coverage types discussed in this section may or may not be provided in each of the various jurisdictions in which the Company operates, subject to the Company's business strategy and any applicable statutory, legal or regulatory requirements.

Commercial automobile insurance is typically positively correlated with both the U.S. economy and the property and casualty ("P&C") insurance market cycle. Gross premium written experienced declines for the past few years generally from the weakness in both the U.S. economy and the P&C market. Management expects market conditions to result in a constriction of capacity deployed into the Company's niche lines of business, reducing competition and allowing for rate increases. The business plan assumes flat to moderate "hardening" in the insurance sector within the next four years.

The Company's primary market risk relates to the current soft insurance market, which risk is mitigated through pricing discipline and consistent focus on underwriting profit as opposed to top-line growth.

The U.S. commercial automobile industry can be divided into the passenger transportation business line and the business automobile business line. The passenger transportation business line can be further segmented into distinct groups including: (i) taxi cab operators, (ii) limousine operators, including sedans, limousines, chartered buses, airport shuttles and NY car service, and (iii) non-emergency paratransit and contracting. The business automobile business line is comprised of light vehicle weight, including cars, vans and pick-up trucks, owner operation or small fleet (1 – 5 vehicles), all with local driving radius. These groups have many similarities, but each business line has its own set of determining factors. The following information is based on the Company's market knowledge coupled

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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with industry information and publications including those of the Taxi, Limousine and Paratransit Association and the New York City Taxi and Limousine Commission.

### *Taxi cab*

The taxi cab business line is shifting with large dispatchers acquiring mid-sized companies resulting in an increased number of very large and very small insureds. Increased costs in fuel, insurance and depreciation have contributed to reduced revenues for the industry. Municipal and state regulation has increased the cost of doing business. Nationwide, the number of taxi permits or medallions has decreased almost 10% in the past ten years. Despite this trend, the available market is estimated at minimum \$350 million in written premium. While the overall taxi cab business line is shrinking, the owner operations and small fleets business line is expanding on a relative basis.

### *Limousine*

There are over 13,000 chauffeur or limousine companies, with an estimated 125,000 limousines operating in the U.S. Industry growth has been stable to positive, with the average hourly rate charged for sedans increasing 54% over the last 16 years and the average hourly rate charged for a limousine increasing 75% over the last 16 years. Geographic distribution of operators shows the largest concentration in the Mid-Atlantic States (25%), followed by the South (23%), Midwest (15%) and Pacific (13%). The limousine business line is not experiencing the consolidation seen in the taxi cab business line. There are relatively few very large accounts.

### *NY Car Service*

Car service vehicles are defined as for hire vehicles other than a black car, New York City Medallion taxi cab or New York City limousine, operating from an authorized New York City Taxi and Limousine Commission radio base station. The vehicles are older model sedans and vans which are not in the pristine condition of a black car.

There are approximately 20,000 car service vehicles in New York City, approximately 9,000 of these are black car vehicles. Overall, the NY Car Service business line is growing. The main writers for this business line are New York-based insurance companies.

### *Paratransit and Contracting*

The paratransit (non-emergency) business line is an emerging and expanding market with many experienced taxi cab operators and drivers converting to this business. Contracting revenue sources are Medicaid compliant transit agencies, school districts, private health care, local social service agencies and doctors' offices. Issues facing this business line are contract insurance requirements and increases in costs, labor issues and regulatory controls. There is also a concern regarding operators who are not being regulated by municipal, state or federal government. As the U.S. population ages, this business line is expected to grow. The expansion of special needs programs in schools also creates increased demand for paratransit operators. Understanding exposure related to geographic areas of operation and risks relating to the use of special equipment customarily used in this business line are critical to underwriting success in this area.

### *Business Automobile*

This is an expansion line which includes businesses of many types that utilize light vehicles such as cars, vans or pick-up trucks in the course of their business. As with other classes of business on which the Company focuses, these vehicles often have special equipment. The Company has access to a large network of non-metro personal line agents to approach in connection with marketing efforts relating to this line. These agents tend not to be specialized in a

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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particular area and often have limited markets to write commercial auto. As with any expansion line, research will be necessary to understand specific markets. Growth will be deliberate with underwriting profit in mind.

### **IV. BUSINESS DEVELOPMENT AND OPERATING ENVIRONMENT**

The Operating Insurance Subsidiaries have a diversified network consisting of independent retail agents. Within this channel the Operating Insurance Subsidiaries have a committed, but relatively small, group of cornerstone agents in each state in which the Company operates. Cornerstone agents are producers who focus on commercial automobile insurance and are considered strategic partners. Illinois is the most developed state in terms of current distribution with a large number of smaller agents located throughout the state in addition to Cornerstone agents who tend to focus on business in major metro areas.

Going forward, the Operating Insurance Subsidiaries distribution strategy is to develop a producer network similar to the one in Illinois for all states in which they write. The Company will establish specific business objectives with each cornerstone agent, including an expectation that the Company will represent one of such agent's top three insurance markets and set minimum annual written premium targets. Underwriting profit will be measured as a primary metric of success with respect to each agent's book of business.

#### **Government Regulation**

The Operating Insurance Subsidiaries are regulated at the state level, with the Illinois Department of Insurance being the primary (domestic) regulator. American Service is also licensed by the U.S. Treasury to provide insurance/surety where the U.S. Federal Government is the beneficiary.

The Operating Insurance Subsidiaries pay premium tax in all states where premium is written. On average, they pay tax equal to 2.1% of written premium.

A primary metric used by insurance regulators is the National Association of Insurance Commissioners' ("NAIC") risk based capital ("RBC") ratio. The Operating Insurance Subsidiaries are required to maintain certain minimum RBC ratios as provided for by insurance statutes in the states in which they write business. The Operating Insurance Subsidiaries are above the 200% minimum RBC ratio threshold. The March 31, 2011 RBC ratios based on the unaudited statutory financial statements of 235% and 366% for American Country and American Service, respectively, and have estimated aggregate capital in excess of the 200% level of approximately \$17.8 million.

Legislative or industry developments can lead to increased competition in the markets in which the Operating Insurance Subsidiaries operate or reduce their ability to price risks appropriately. New competition from these potential changes could cause the prices for insurance to fall, adversely affecting underwriting profitability or volume of business written.

#### **Assigned Risk**

In the United States, automobile insurers are generally required to participate in various involuntary residual market pools and assigned risk plans that provide automobile insurance coverage to individuals or other entities that are unable to purchase such coverage in the voluntary market. Participation in these pools in most jurisdictions is in proportion to voluntary writings of selected lines of business in that jurisdiction. The Company's participation in these involuntary markets was \$18,000 and \$28,000 in assumed premium written for the first quarter of 2011 and 2010, respectively.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

### V. OPERATING RESULTS

#### Total Revenues

Revenues are derived from net premium earned, insurance investment income, net realized gains (losses), and miscellaneous income. Total revenue from operations in the first quarter 2011 was \$ 10.3 million, a decrease of 53.6% as compared to the \$22.2 million in revenue from operations in the first quarter of 2010 and a decrease of 21.7% over the \$13.1 million in revenue in the fourth quarter 2010. The table below provides the comparison detail of the total revenue.

**Table 4 Total Revenue**

(in millions of dollars, except for percentages)

Quarter ended March 31,	2011	2010	Change	%
Net premium earned	\$ 8.8	\$19.3	(\$10.5)	(54.4%)
Net investment income	0.8	1.5	(0.7)	(48.5%)
Net realized gains (losses)	0.4	0.2	0.2	100.8%
Miscellaneous income	0.3	1.2	(0.9)	(75.0%)
<b>Total revenue</b>	<b>\$10.3</b>	<b>\$22.2</b>	<b>(\$11.9)</b>	<b>(53.6%)</b>

#### Gross Premium Written

For the quarter ended March 31, 2011, gross premium written were \$14.2 million compared to \$18.7 million in the first quarter of 2010 and \$9.3 million in the fourth quarter of 2010 and representing a 24.3% decrease and 52.8% increase, respectively. Table 5 below summarizes our gross premium written by line of business for the periods indicated.

**TABLE 5 Gross premium written by line of business**

(in millions of dollars, except for percentages)

Quarter ended March 31,	2011	2010	Change	
	Amount	Amount	\$	%
Commercial automobile	\$ 6.6	\$ 10.5	(\$ 3.9)	(37.1%)
Non-standard Automobile	5.9	5.7	0.2	3.5
Other	1.7	2.5	(0.8)	(30.3)
<b>Total Gross Premium Written</b>	<b>\$ 14.2</b>	<b>\$ 18.7</b>	<b>(\$ 4.5)</b>	<b>(24.3%)</b>

#### Commercial Automobile

Commercial automobile policies provide coverage for light weight, individual unit or small fleet commercial vehicles typically with the minimum limits prescribed by statute, municipal or other regulatory requirements. In the quarter ended March 31, 2011, gross premium written from commercial automobile was \$6.6 million, representing a 37.1% decrease and 112.9% increase relative to first quarter 2010 and fourth quarter 2010, respectively. The decrease relative to first quarter 2010 was primarily a result of the actions related to the Operating Insurance Subsidiaries' former parent company's strategy which focused on private passenger automobile insurance. This downward trend began to reverse by the end of 2010 as plans for Atlas' going forward strategy were communicated publicly, as seen in the increase from fourth quarter 2010 to first quarter 2011. As a percentage of the Operating Insurance Subsidiaries' overall book of business, commercial auto gross premium written represented 46.5% of gross premium

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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written in the first quarter 2011 compared to 30.8% and 33.5% for the quarters ended March 31, 2010 and December 31, 2010, respectively.

Commercial automobile insurance has outperformed the overall P&C industry in each of the past ten years based on data compiled by the NAIC. Each of the specialty business lines on which the Company's strategy is focused is a subset of this historically profitable industry subset.

Because there are a limited number of competitors specializing in these lines of business, a strong value proposition is very important and can result in desirable retention levels as policies renew on an annual basis. There are also a relatively limited number of agents who specialize in these lines of business. As a result, strategic relationships are important to ensure efficient distribution.

There is a positive correlation between the economy and commercial automobile insurance in general. However, operators of commercial automobiles may be less likely than other business segments within the commercial auto line to take vehicles out of service as their businesses and business reputations rely heavily on availability. With respect to certain business lines, such as the taxi line, there are also other factors such as the cost and limited supply of medallions which may discourage a policy holder from taking vehicles out of service in the face of reduced demand for the use of the vehicle.

Maintaining continuous insurance on all vehicles under dispatch is an important aspect of our target policyholders' businesses.

### **Non-Standard Automobile**

Non-standard automobile insurance is principally provided to individuals who do not qualify for standard automobile insurance coverage because of their payment history, driving record, place of residence, age, vehicle type or other factors. Such drivers typically represent higher than normal risks and pay higher insurance rates for comparable coverage.

Consistent with Atlas' focus on commercial automobile insurance, the Company is transitioning away from the non-standard auto line.

### **Other**

The Company wrote \$1.7 million of surety business in the first quarter of 2011 versus \$2.5 million in the first quarter 2010 and \$1.8 million in the fourth quarter 2010. This business is 100% reinsured and has an immaterial effect on the Company's results.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

### Geographic Concentration

**Table 6 Gross premium written by state**  
(in millions of dollars, except for percentages)

Quarter ended March 31,	2011			2010		
	Amount	%		Amount	%	
Illinois	\$ 10.2	72.2	%	\$ 8.5	45.8	%
Indiana	1.2	8.4		2.0	10.5	
Michigan	0.9	6.7		0.4	1.9	
New York	0.8	5.7		1.9	10.3	
Minnesota	0.5	3.8		0.1	0.7	
Texas	0.2	1.5		0.2	0.8	
Wisconsin	0.2	1.4		0.1	0.3	
Other	0.2	0.3		5.5	29.6	
Total Gross Premium Written	14.2	100.0	%	18.7	100.0	%

As illustrated by the data in the Table 6, 72.2% of the Company's first quarter 2011 gross premium written came from the state of Illinois and 87.3% came from the top 3 states (factoring in Indiana and Michigan). The Company's future business success is primarily dependent upon the health of the economy and business climate in those areas coupled with opportunities in areas where the Company is licensed and intends to expand or begin writing business.

As described earlier, a significant aspect of the Company's business plan is to increase business writings in both states where 2010 gross premium written were below target levels and in states where the Operating Insurance Subsidiaries have licenses which were not utilized. The pace and focus of these expansion plans will be driven by pricing and competitive analyses performed by the Company.

### Ceded Premium Written

Ceded premium written is equal to premium ceded under the terms of the Company's in force reinsurance treaties. Ceded premium written decreased 63.3% to \$1.8 million for the quarter ended March 31, 2011 compared with \$4.9 million for the quarter ended March 31, 2010 and decreased 5.3% as compared to the \$1.9 million of ceded premium written in the fourth quarter 2010. These decreases are attributed to the reduction of the Company's surety gross premium written.

### Net Premium Written

Net premium written is equal to gross premium written less the ceded premium written under the terms of the Company's in force reinsurance treaties. Net premium written decreased 10.1% to \$12.4 million for the quarter ended March 31, 2011 compared with \$13.8 million for the quarter ended March 31, 2010 and increased 69.9% compared to \$7.3 million net premium written in the fourth quarter 2010. These changes are attributed to the same factors as described in the 'Gross Premium Written' and the 'Ceded Premium Written' sections above.

### Net Premium Earned

Premiums are earned ratably over the term of the underlying policy. Net premium earned was \$8.8 million for the quarter ended March 31, 2011, a 54.4% decrease compared with first quarter of 2010 and a 24.0% decrease as compared to the fourth quarter 2010, respectively. These decreases are attributed to the factors described in the

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

'Gross Premium Written' and 'Ceded Premium Written' sections above. Although gross premium written increased in the first quarter 2011 as compared to the fourth quarter of 2010, net premium earned will be affected more gradually. The effect of increased gross premium written will be seen ratably over the policy periods of business written. These policy periods are typically twelve months.

### Net Investment Income

**Table 7 Investment results before the effect of income taxes**  
(in millions of dollars)

Quarter ended March 31,	2011		2010	
Average securities at cost	\$	165.5	\$	217.0
Investment income after expenses	\$	0.8	\$	1.5
Percent earned on average investments (annualized)		1.9 %		2.7 %
Net realized gains (losses)	\$	0.4	\$	0.2
Total investment income	\$	1.2	\$	1.7
Total realized yield (annualized)		2.9 %		3.1 %

Investment income, excluding net realized gains, decreased by 48.5% to \$0.8 million in the first quarter of 2011, compared to \$1.5 million in the first quarter of 2010. The change is primarily due to the decrease in the portfolio size from \$197.7 million as of March 31, 2010 to \$149.3 million of invested assets held by the Company at March 31, 2011. This decrease is attributable to payout patterns from the Company's loss and loss adjustment expense reserves and the decrease in gross premium written during 2010.

Interest income, net of investment expenses, relating to the Company's invested assets was \$0.8 million for the first quarter of 2011 compared to \$1.5 million and \$1.6 million for the first and fourth quarters of 2010, respectively.

During June of 2010, the Company's previous parent contributed its current headquarters building to American Service. In conjunction with this contribution, certain floor space leases with then affiliated entities were assigned to American Service. In the first quarter of 2011, American Service terminated these assigned leases and executed new leases for space within its current headquarters building. The terminated leases were accounted for by the straight line method of accounting for leases. As a result of the termination, amounts previously accrued or incurred were written off. American Country recorded a benefit to underwriting expense of \$194,000 related to the elimination of previous straight line expensing of its lease obligation and American Service recorded an investment expense of \$244,000 related to the elimination of previously recorded straight-line income. The \$244,000 of American Service expense is a component of the net investment income for the first quarter of 2011, accounting for the difference between interest income and investment income overall.

### Net Realized Investment Gains (Losses)

Net realized investment gains in the first quarter of 2011 were \$0.4 million compared to \$0.2 million and \$0.2 million in first quarter 2010 and fourth quarter 2010, respectively. The net realized investment gains in the first quarter of 2011 are due to rebalancing investments within the portfolio.

### Miscellaneous (Loss) Income

The Company recorded miscellaneous income in the first quarter 2011 of \$250,000 as compared with a miscellaneous income of \$559,000 for first quarter 2010 and miscellaneous income of \$20,000 for fourth quarter of 2010, respectively.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

Included in this category is fee income of \$236,000 for the first quarter 2011 and \$573,000 and \$293,000 for the first and fourth quarters of 2010, respectively. These fees include installment payment fees, policy fees, non-sufficient funds fees and certain required regulatory report filing and preparation fees received from insurance customers. The Company nets these fees against other underwriting expenses when computing its expense and combined ratios.

### Claims Incurred

The loss ratio relating to the claims incurred for the first quarter of 2011 was 78.2% compared to 79.5% for first quarter 2010 and 87.0% for fourth quarter 2010. The change in loss ratio is due to the elimination of unprofitable programs during 2010 and the decrease in unallocated loss adjustment expenses as a result of the spin-off from the Company's prior parent.

### Acquisition Costs

Acquisition costs represent commissions and taxes incurred on net premium earned. Acquisition costs were \$1.8 million for the first quarter of 2011 or 20.2% of net premium earned, as compared to 20.8% and 17.9% for the quarters ended March 31, 2010 and December 31, 2010.

### Other Underwriting Expenses

The other underwriting expense ratio (net of fee income of approximately \$232,000, \$573,000 and \$293,000 for first quarter 2011, first quarter 2010 and fourth quarter 2010, respectively) was 24.7% in first quarter 2011 compared to 20.7% in first quarter of 2010 and 35.8% in fourth quarter of 2010. As a result of the merger, the Company incurred additional expenses of approximately \$627,000 in first quarter 2011 that are deemed "non-recurring" in nature, which increased the expense ratio in first quarter 2011 by 7.1 points. The table below highlights these "non-recurring" expenses.

**Table 8 "Non-recurring" Expenses**

(in whole dollars)

Expense Item	Description	"Non-recurring" Expense/(Benefit)
Licenses, taxes and assessments	Amounts paid in Q1 2011	\$198,000
Professional fees	Legal and Accounting fees	121,000
Salary and Benefits	Q1 staff reduction impacts	174,000
EDP expense	Decommissioning software expenses previously capitalized	84,000
Occupancy	Straight-line lease adjustment (See 'Net Investment Income' section)	(194,000)
Net investment income	Straight-line lease adjustment (See 'Net Investment Income' section)	244,000
<b>Total "Non-recurring" expenses</b>		<b>\$627,000</b>

### Combined Ratio

The combined ratio was 123.1% in first quarter 2011 compared with 121.0% and 140.7% in first quarter 2010 and fourth quarter 2010, respectively, which produced an underwriting loss (net of fee income as previously indicated) of \$2.0 million in first quarter 2011 compared with a losses of \$4.6 million in first quarter 2010 and \$5.0 million in fourth quarter. The underwriting loss is attributable to the factors described in the 'Claims Incurred', 'Acquisition Costs',

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

and 'Other Underwriting Expenses' sections above. Excluding non-recurring expenses, the combined ratio in first quarter 2011 would have been 116.0%.

### Loss before Income Taxes

The Company generated a loss before income taxes of \$0.9 million, \$2.4 million and \$3.5 million for the quarters ended March 31, 2011, March 31, 2010 and December 31, 2010, respectively, the components of which are discussed above.

### Income Tax Expense (Benefit)

An income tax benefit on losses incurred for the quarter ended March 31, 2011 was not provided because the deferred tax asset otherwise attributable to these quarterly losses are not considered realizable compared to a tax benefit of \$811,000 in the first quarter of 2010.

The following table reconciles tax benefit from applying the statutory U.S. tax rate of 34% to the actual percentage of pre-tax losses provided for the three months ended March 31, 2011 and 2010.

**Table 9 Income tax expense (benefit) reconciliation**

(in thousands of dollars)

Quarter Ended March 31,	2011		2010	
	Tax expense (benefit)	% of Pre-tax Income	Tax expense (benefit)	% of Pre-tax Income
<b>Provision for taxes at U.S. statutory marginal income tax rate of 34% in 2011 and 2010</b>	<b>(\$283)</b>	<b>(34.0)%</b>	<b>(\$814)</b>	<b>(34.0)%</b>
<b>Provision for deferred tax assets deemed unrealizable</b>	<b>283</b>	<b>34.0</b>	<b>-</b>	<b>-</b>
<b>Other</b>	<b>-</b>	<b>-</b>	<b>3</b>	<b>0.1</b>
<b>Income tax expense (benefit)</b>	<b>\$0</b>	<b>0.0%</b>	<b>(\$811)</b>	<b>(33.9)%</b>

In 2010 the merger resulted in a yearly limitation (the U.S. tax law Section 382 limitation that applies to changes in ownership) on the future utilization of the Company's net operating loss carry-forwards. Furthermore as part of the merger, the Company's prior parent has retained certain tax assets of the Company previously reported as part of the Company's deferred tax asset. Due to these aspects of the merger, the Company's ability to recognize future tax benefits associated with a portion of its deferred tax assets generated during prior years and the current year have been permanently limited. These limitations resulted in a maximum expected net deferred tax asset the Company would have available after the merger and which would more-likely-than-not be utilized in the future. The result was a permanent write-down of a portion of the deferred tax asset in Q4 of 2010. Due to the size of the write-down of deferred tax assets, the Company reported a tax expense for 2010 of \$2.6 million despite the fact that the Company had a pre-tax loss for the year.

### Net Loss and Loss per Share

A net loss was reported for first quarter 2011 in the amount of \$889,000 as compared to net losses of \$1,583,000 and

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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\$11,430,000 for the first and fourth quarters 2010, respectively. After taking the impact of the preferred shares into consideration, the basic and diluted loss per common share computed under continuation accounting rules was \$0.05 for first quarter 2011 compared to a loss per common share of \$0.09 and \$0.62 for first and fourth quarters of 2010, respectively.

There were 18,368,483 weighted average voting common shares outstanding during the first quarter of 2011. For the comparable 2010 quarter 18,358,363 were used to compute earnings per voting common share, the number of voting common shares at the merger date as required by continuation accounting rules.

### **Book Value per Common Share**

Book value per voting common share was \$2.19 at March 31, 2011 as compared to \$1.96 at March 31, 2010 and \$2.30 at December 31, 2010. (See section entitled "Continuation Accounting" for discussion on presentation of capital structure prior to merger date.)

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

### VI. FINANCIAL CONDITION

**Table 10 IFRS Balance Sheet**  
**Interim Consolidated Balance Sheet (unaudited)**

(in thousands of US dollars, except for share amounts)

As at	March 31, 2011	December 31, 2010	January 1, 2010
<b>Assets</b>			
Investments			
Cash and cash equivalents	\$ 8,713	\$ 19,037	\$ 6,695
Securities	149,294	154,011	214,910
	158,007	173,048	221,605
Accrued investment income	1,296	1,293	1,710
Accounts receivable and other assets	13,909	13,340	28,109
Due from reinsurers and other insurers	11,573	11,276	5,811
Income taxes receivable	0	0	271
Deferred Policy acquisition costs	4,153	3,804	9,399
Deferred tax asset	6,399	6,399	9,273
Office equipment	1,182	1,274	1,423
Assets held for sale	15,004	15,004	0
<b>Total Assets</b>	<b>\$ 211,523</b>	<b>\$ 225,438</b>	<b>\$ 277,601</b>
<b>Liabilities</b>			
Claims liabilities	\$ 119,604	\$ 132,579	\$ 169,515
Unearned premiums	20,096	17,061	34,286
Notes Payable	0	0	13,500
Due to reinsurers and other insurers	8,559	9,614	640
Accounts payable and other liabilities	7,531	8,662	9,761
	155,790	167,916	227,702
<b>Shareholders' equity</b>			
Ordinary voting common shares, par value \$0.001, 800,000,000 shares authorized, 4,569,205 shares issued and outstanding at March 31, 2011	8,010	8,010	8,010
Restricted voting common shares, par value \$0.001, 100,000,000 shares authorized, 13,804,861 shares issued and outstanding at March 31, 2011	27,760	27,760	27,760
Preferred shares, par value \$0.001, 18,000,000 shares authorized, issued and outstanding at March 31, 2011	15,353	15,353	15,353
Contributed surplus	116,730	116,714	46,923
Retained deficit	(114,260)	(113,371)	(47,714)
Accumulated other comprehensive income (loss), net of tax	2,140	3,056	(433)
	55,733	57,522	49,899
<b>Total liabilities and shareholders' equity</b>	<b>\$ 211,523</b>	<b>\$ 225,438</b>	<b>\$ 277,601</b>

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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### Investments

#### Investments Overview and Strategy

We manage our securities portfolio to support the liabilities of the Operating Insurance Subsidiaries, to preserve capital and to generate investment returns. We invest predominantly in corporate and government bonds with relatively short durations that correlate with the payout patterns of our claims liabilities. The securities are managed by a third-party investment management firm pursuant to the Company's investment policies and guidelines as approved by its Board of Directors. The Company monitors the third-party investment manager's performance and their compliance with both their individual mandate and the Company's investment policies and guidelines.

Our investment guidelines stress the preservation of capital, market liquidity to support payment of our liabilities and the diversification of risk. With respect to fixed income securities, we generally purchase securities with the expectation of holding them to their maturities; however, the securities are available for sale if liquidity needs arise.

#### Portfolio Composition

At March 31, 2011, the Company held cash and securities with a fair value of \$158.0 million. As of March 31, 2011, the securities portfolio was comprised primarily of fixed income securities. Operating Insurance Subsidiaries' securities must comply with applicable regulations that prescribe the type, quality and concentration of securities. These regulations in the various jurisdictions in which our Operating Insurance Subsidiaries are domiciled permit investments in government, state, municipal and corporate bonds, preferred and common equities, and other high quality investments, within specified limits and subject to certain qualifications.

The following table summarizes the fair value of the securities portfolio, including cash and cash equivalents, as of the dates indicated.

**Table 11 Fair value of securities portfolio**  
(in millions of dollars)

	As of March 31, 2011	As of December 31, 2010
<b>Type of security:</b>		
Term deposits	\$ 16.9	\$ 7.9
Government bonds	65.6	69.5
Corporate	56.2	65.4
Commercial mortgage backed	8.6	8.7
Other asset backed	2.0	2.5
Subtotal	\$ 149.3	\$ 154.0
Cash and cash equivalents	8.7	19.0
Total	\$ 158.0	\$ 173.0

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

**Table 12 Net Change in unrealized gains/losses on available-for-sale securities**  
(in millions of dollars)

	As of March 31, 2011		As of December 31, 2010		Change
<b>Type of security:</b>					
Term deposits	\$	-	\$	-	\$ -
Government bonds		2.0		2.1	(0.1)
Corporate		2.3		3.0	(0.7)
Commercial mortgage backed		0.2		0.3	(0.1)
Other asset backed		0.1		0.1	-
<b>Total</b>	\$	<b>4.6</b>	\$	<b>5.5</b>	<b>(0.9)</b>

### Liquidity and Cash Flow Risk

The following table summarizes the fair value by contractual maturities of the fixed income securities portfolio excluding cash and cash equivalents at the dates indicated.

**Table 13 Fair value by contractual maturity date**  
(in millions of dollars)

	As of March 31, 2011			As of December 31, 2010		
	Amount	%		Amount	%	
Due in less than one year	\$ 40.2	26.9	%	\$ 21.6	14.0	%
Due in one through five years	71.6	48.0		88.6	57.5	
Due after five through ten years	19.6	13.1		24.0	15.6	
Due after ten years	17.9	12.0		19.8	12.9	
<b>Total</b>	\$ 149.3	100.0	%	\$ 154.0	100.0	%

At March 31, 2011, 74.9% of the fixed income securities, including treasury bills, bankers' acceptances, government bonds and corporate bonds had contractual maturities of five years or less. Actual maturities may differ from contractual maturities because certain issuers have the right to call or prepay obligations with or without call or prepayment penalties. The Company holds cash and high grade short-term assets which, along with fixed income security maturities, management believes are sufficient for the payment of claims on a timely basis. In the event that additional cash is required to meet obligations to our policyholders, we believe that the high quality, liquid securities portfolio provides us with sufficient liquidity.

### Market Risk

Market risk is the risk that the Company will incur losses due to adverse changes in interest rates, currency exchange rates or equity prices. Having disposed of a majority of its asset backed securities, its primary market risk exposures in the fixed income securities portfolio are to changes in interest rates. Because the Company's securities portfolio is comprised of primarily fixed income securities that are usually held to maturity, periodic changes in interest rate levels generally impact its financial results to the extent that the securities in its available for sale portfolio are recorded at market value. Also, reinvestment yields on maturing securities are different than the original yields. During periods of rising interest rates, the market value of the existing fixed income securities will generally decrease and realized gains on fixed income securities will likely be reduced. The reverse is true during periods of declining interest rates.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

### Credit Risk

Credit risk is defined as the risk of financial loss due to failure of the other party to a financial instrument to discharge an obligation. The Company is exposed to credit risk principally through its investments and balances receivable from policyholders and reinsurers. It monitors concentration and credit quality risk through policies to limit and monitor its exposure to individual issuers or related groups (with the exception of U.S. government bonds) as well as through ongoing review of the credit ratings of issuers in the securities portfolio. Credit exposure to any one individual policyholder is not material. Its policies, however, are distributed by agents who may manage cash collection on its behalf pursuant to the terms of their agency agreement. The Company has policies to evaluate the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurers' insolvency.

The following table summarizes the composition of the fair value of the fixed income securities portfolio, excluding cash and cash equivalents, as of the dates indicated, by ratings assigned by S&P or Moody's Investors Service. The fixed income securities portfolio consists of predominantly very high quality securities in corporate and government bonds with 97.1% rated 'A' or better at March 31, 2011 compared to 97.4% as of December 31, 2010.

**Table 14 Credit ratings of fixed income securities portfolio**

<b>Rating</b>	<b>As of March 31, 2011</b>	<b>As of December 31, 2010</b>
AAA/Aaa	65.2 %	57.6 %
AA/Aa	8.3	17.1
A/A	23.6	22.7
<b>Percentage rated A/A or better</b>	<b>97.1 %</b>	<b>97.4 %</b>
BBB/Baa	2.8	2.5
Not rated	0.1	0.1
<b>Total</b>	<b>100.0 %</b>	<b>100.0 %</b>

### Other-than-temporary impairment

The Company recognizes losses on securities for which a decline in market value was deemed to be other-than-temporary. Management performs a quarterly analysis of the securities holdings to determine if declines in market value are other-than-temporary. The Company did not recognize charges for securities impairments that were considered other-than-temporary for the quarters ended March 31, 2011 and March 31, 2010.

The length of time securities may be held in an unrealized loss position may vary based on the opinion of the appointed investment manager and their respective analyses related to valuation and to the various credit risks that may prevent us from recapturing the principal investment. In cases of securities with a maturity date where the appointed investment manager determines that there is little or no risk of default prior to the maturity of a holding, we would elect to hold the security in an unrealized loss position until the price recovers or the security matures. In situations where facts emerge that might increase the risk associated with recapture of principal, the Company may elect to sell securities at a loss. As of March 31, 2011, the Company had no material gross unrealized losses in its portfolio.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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### **Accounts Receivable and Other Assets, Deferred Policy Acquisition Costs**

The increases in accounts receivable and deferred policy acquisition costs are consistent with the increase in gross premium written during the first quarter of 2011.

### **Due from Reinsurers and Other Insurers**

The Company purchases reinsurance from third parties in order to reduce its liability on individual risks and its exposure to large losses. Reinsurance is insurance purchased by one insurance company from another for part of the risk originally underwritten by the purchasing (ceding) insurance company. The practice of ceding insurance to reinsurers allows an insurance company to reduce its exposure to loss by size, geographic area, and type of risk or on a particular policy. An effect of ceding insurance is to permit an insurance company to write additional insurance for risks in greater number or in larger amounts than it would otherwise insure independently, having regard to its statutory capital, risk tolerance and other factors.

The Company generally purchases reinsurance to limit our net exposure to a maximum amount on any one loss of \$0.5 million with respect to commercial automobile liability claims. The Company also purchases reinsurance to protect against awards in excess of its policy limits. In addition, in 2010 the Operating Insurance Subsidiaries were part of a larger group of insurance companies that purchased catastrophe reinsurance providing coverage in the event of a series of claims arising out of a single occurrence, limiting exposure to \$2.0 million per occurrence with a maximum coverage of \$38.0 million. This catastrophic coverage was deemed appropriate at the time based on the insurance subsidiaries being part of a larger group of companies. However, this exposure is much more limited due to the Operating Insurance Subsidiaries' relatively low limits of first party physical damage coverage and the geographic regions in which the Company operates on a go forward basis resulting in the determination that catastrophe reinsurance is not required and therefore was not renewed for the Company at the end of 2010. The Company will continue to evaluate and adjust its reinsurance needs based on business volume, mix, and supply levels.

Reinsurance ceded does not relieve the Company of its ultimate liability to its insureds in the event that any reinsurer is unable to meet their obligations under its reinsurance contracts. Therefore, the Company enters into reinsurance contracts with only those reinsurers who we believe have sufficient financial resources to provide the requested coverage. Reinsurance treaties are generally subject to cancellation by the reinsurers or the Company on the anniversary date and are subject to renegotiation annually. The Company regularly evaluates the financial condition of its reinsurers and monitors the concentrations of credit risk to minimize its exposure to significant losses as a result of the insolvency of a reinsurer. The Company believes that the amounts it has recorded as reinsurance recoverables are appropriately established. Estimating amounts of reinsurance recoverables, however, is subject to various uncertainties and the amounts ultimately recoverable may vary from amounts currently recorded. As of March 31, 2011, the Company had \$11.6 million recoverable from third party reinsurers and other insurers as compared to \$11.3 million as of December 31, 2010.

Estimating amounts of reinsurance recoverables is also impacted by the uncertainties involved in the establishment of provisions for unpaid claims. As underlying reserves potentially develop, the amounts ultimately recoverable may vary from amounts currently recorded. The Company's reinsurance recoverables are generally unsecured. The Company regularly evaluates its reinsurers, and the respective amounts recoverable, and an allowance for uncollectible reinsurance is provided for, if needed.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

### Deferred Tax Asset

Deferred tax assets reflects no change from year end 2010 resulting from the establishment of a provision for deferred tax assets deemed unrealizable which offsets the first quarter of 2011 income tax provision (see section entitled 'Income Tax Expense (Benefit)').

**Table 15 Components of deferred tax assets and liabilities**

(in thousands of dollars)

	March 31, 2011	December 31, 2010
<b>Deferred tax assets:</b>		
Unpaid claims and unearned premium	\$ 4,103	\$ 4,218
Loss carry-forwards	2,167	1,964
Pension expense	841	847
Bad debts	1,335	1,356
Other	1,266	1,394
<b>Total gross deferred tax assets</b>	<b>9,712</b>	<b>9,773</b>
<b>Deferred tax liabilities:</b>		
Investment securities	1,570	1,863
Deferred policy acquisition costs	1,445	1,293
Other	298	218
<b>Total gross deferred tax liabilities</b>	<b>3,313</b>	<b>3,374</b>
<b>Net deferred tax assets</b>	<b>\$ 6,399</b>	<b>\$ 6,399</b>

A deferred tax asset of \$2,167 has been recognized for \$6,374 (on a tax effected basis) of the total net operating loss carry-forwards totaling \$35,415 as of March 31, 2011 based on management's assessment of the probable amount of future taxable income that will be available against which the net operating loss carry-forwards can be utilized before expiration.

The Company has \$35.4 million in total net operating loss carry-forwards as of March 31, 2011 with the indicated expiry.

**Table 16 Net operating loss carry-forward by expiry**

(in thousands of dollars)

Year of Occurrence	Year of Expiration	Amount
2008	2028	\$ 3,808
2009	2029	20,723
2010	2030	10,884
<b>Total</b>		<b>\$ 35,415</b>

### Assets Held for Sale

As of March 31, 2011 the Company had five properties held for sale with an aggregate book value of \$15.0 million. All of the properties individual book values were below their respective 2010 appraised amounts less reasonably estimated selling costs. All were listed for sale through brokers at those appraised values as of March 31, 2011. Book value of assets under contract was adjusted to reflect expected net proceeds based on actual terms of sale less transaction costs.

The two largest properties held for sale, representing 97% of the total book value of assets held for sale, were the

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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Company's headquarters building in Elk Grove Village, Illinois with a book value of \$12.5 million and an office building in Mobile, Alabama with a book value of \$2.0 million (adjusted to reflect sale contract terms). The remaining three properties are vacant land parcels in areas surrounding Mobile, Alabama with an aggregate book value of \$0.5 million.

The Elk Grove Village building is in a major office park in a good location and includes approximately 176,844 square feet of net rentable area and 7.2 acres of land.

The Mobile, Alabama office building has approximately 29,386 square feet of usable office space, 23.1 acres of land, and was written down by \$0.4 million on December 31, 2010 to an estimated selling price less costs to sell. A contract for the sale of this property at \$2.1 million was executed on January 24, 2011. The sale was consummated in June of 2011.

### Claims Liabilities

Claims management is the procedure by which an insurance company determines the validity and amount of a claim. An important part of claims management is verifying the accuracy of the information provided to the insurance company at the time the policy is underwritten. The nature of the insurance the Company writes typically requires more specialized claims management and in particular, more thorough investigative procedures, greater defense costs than many other types of insurance, and thorough understanding of the vehicles, usage and equipment insured. Insurance claims on our policies are investigated and settled by our local claims adjusters, and we may also employ independent adjusters, private investigators, various experts and legal counsel to adjust claims. We believe that claims management is fundamental to our operations.

A provision for unpaid claims includes several components: a provision for unpaid claims based on estimated liability on individual reported claims (more commonly known as case reserves), an estimated provision for claims that have not yet been reported and expected future development on case reserves, collectively known as the incurred but not reported claims provision ("IBNR"). The provision for unpaid claims also includes an estimate of allocated loss adjustment expenses (primarily defense costs) and unallocated loss adjustment expenses (primarily the adjustment handling costs by claims personnel) which we expect to incur in the future.

The establishment of a provision for unpaid claims represents management's best estimate of the ultimate cost of both reported but unsettled claims and unreported claims. The provision for unpaid claims does not represent an exact calculation of the liability but instead represents management's best estimate at a given date utilizing actuarial and statistical procedures. The provision for unpaid claims represents the undiscounted estimates of the ultimate net cost of all unpaid claims and loss adjustment expenses. Management continually reviews its estimates and adjusts as experience develops and new information becomes available. In establishing the provision for unpaid claims, the Company also takes into account estimated recoveries, reinsurance, salvage and subrogation.

The process for establishing the provision for unpaid claims reflects the uncertainties and significant judgmental factors inherent in predicting future results of both known and unknown claims. As such, the process is inherently complex and imprecise and estimates are constantly refined. The process of establishing the provision for unpaid claims relies on the judgment and opinions of a large number of individuals, including the opinions of the independent appointed actuary.

Factors affecting the provision for unpaid claims include the continually evolving and changing regulatory and legal environments, actuarial studies, professional experience and the expertise of our claims personnel and independent

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# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

adjustors retained to handle individual claims. A change in claims handling procedures and changes in individuals involved in the reserving process can also affect the provision for unpaid claims. The quality of the data used for projection purposes, existing claims management practices, including claims handling and settlement practices, the effect of inflationary trends on future claims settlement costs, court decisions, economic conditions and public attitudes, all affect the provision for unpaid claims.

In addition, time can be a critical consideration when determining a provision, because the longer the span between the incidence of a loss and the payment or claim settlement, the more variable the ultimate settlement amount can be. Accordingly, short-tailed claims, such as property claims, tend to be more predictable than long-tailed claims such as general liability and automobile accident benefit claims. Short-tail claims are reported and settled quickly, resulting in less estimation variability. Our provision for unpaid claims is not discounted to reflect the time value of expected future payouts of claims.

The table below shows the amounts of total case reserves and incurred but not reported (“IBNR”) claims provision as of March 31, 2011 and December 31, 2010. The provision for unpaid claims decreased by 9.8% to \$119.6 million at the end of the first quarter of 2011 compared to \$132.6 million at the end of 2010. During the first quarter of 2011, case reserves decreased by 10.0% compared to December 31, 2010, while IBNR reserves decreased by 9.5% generally due to the earned premium reductions from 2010 levels and the pattern of claims payment during the first quarter of 2011. No changes were made to the Company’s prior year expected ultimate loss ratios in the first quarter 2011.

**Table 17 Provision for unpaid claims by type**  
(in millions of dollars)

	As of March 31, 2011		As of December 31, 2010		% Change
<b>Case Reserves</b>	\$	78.4	\$	87.1	(10.0%)
<b>IBNR</b>		41.2		45.5	( 9.5%)
<b>Total</b>	\$	119.6	\$	132.6	( 9.8%)

**Table 18 Provision for unpaid claims by line of business - gross**  
(in millions of dollars)

Line of Business	As of March 31, 2011		As of December 31, 2010	
<b>Non-Standard Auto</b>	\$	25.4	\$	28.9
<b>Commercial Auto</b>		83.6		92.7
<b>Other</b>		10.6		11.0
<b>Total</b>	\$	119.6	\$	132.6

**Table 19 Provision for unpaid claims - net of reinsurance recoverables**  
(in millions of dollars)

Line of Business	As of March 31, 2011		As of December 31, 2010	
<b>Non-Standard Auto</b>		\$25.4		\$28.9
<b>Commercial Auto</b>		82.1		92.1
<b>Other</b>		5.0		5.1
<b>Total</b>		\$112.5		\$126.1

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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### Notes Payable

At January 1, 2010 the Company's Operating Insurance Subsidiaries had surplus notes payable to Kingsway America Inc., their former parent, aggregating \$13.5 million. With approval of the Illinois Department of Insurance, these notes, including a \$1.0 million note brought into the Company in the Southern United Fire Insurance merger in February 2010, were forgiven on December 2, 2010 by Kingsway America Inc. and this amount was recorded as additional paid-in capital. Accrued interest of \$1.0 million from inception to the date of forgiveness was paid by the Company to Kingsway America Inc. during the first quarter of 2011.

As it relates to the surplus notes, the Operating Insurance Subsidiaries were not restricted from incurring any future indebtedness, policy claims, or prior claims.

### Due to Reinsurers

The decrease in due to reinsurers is consistent with the payout patterns of the underlying claims liabilities.

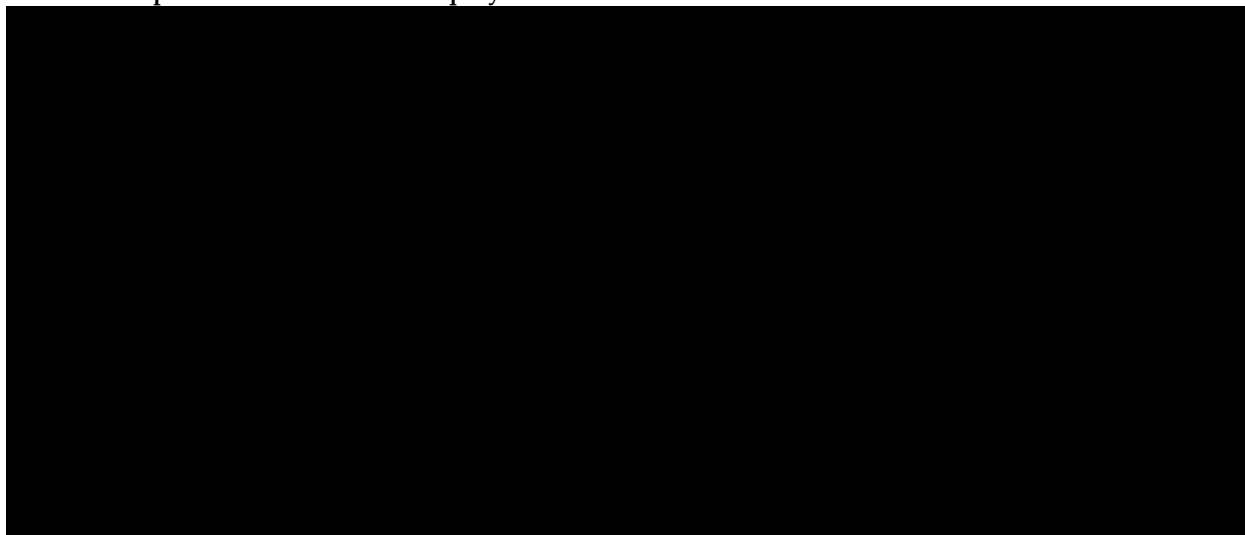
### Accounts Payable and Other Liabilities

The decrease in accounts payable and other liabilities is consistent with the decrease in operating expenses as a result of the reverse merger.

### Shareholders' Equity

The table below identifies the changes in shareholders' equity for the quarters ended March 31, 2011 and March 31, 2010.

**Table 20 Comparison of Shareholders' Equity**



The restricted voting common shares are convertible to ordinary voting common shares at the option of the holder in the event that an offer is made to purchase all or substantially all of the restricted voting common shares.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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All of the issued and outstanding restricted voting common shares are beneficially owned or controlled by Kingsway Financial Services Inc. or its affiliated entities. In the event that such shares are disposed of such that Kingsway Financial Services Inc.'s beneficial interest is less than 10% of the issued and outstanding restricted common voting shares, the restricted voting common shares shall be mandatorily converted into fully paid and non-assessable ordinary voting shares.

The restricted voting shares are entitled to vote at all meetings of shareholders, except at meetings of holders of a specific class that are entitled to vote separately as a class. Voting by restricted voting common shareholders is limited to 30% of the issued and outstanding restricted voting common shares.

Preferred shares are not entitled to vote. They accrue dividends on a cumulative basis whether or not declared by the Board of Directors at the rate of U.S. \$0.045 per share per year (4.5%) and may be paid in cash or in additional preferred shares at the option of the Company. In liquidation, dissolution or winding-up of the Company, receive the greater of US\$1.00 per share plus all declared and unpaid dividends or the amount it would receive in liquidation if the preferred shares had been converted to restricted voting shares or ordinary voting shares immediately prior to liquidation. Preferred shares are convertible into ordinary voting shares at the option of the holder at any date that is after the fifth year after issuance at the rate of 0.3808 ordinary voting common shares for each preferred share. The conversion rate is subject to change if the number of ordinary voting common shares or restricted voting common shares changes. The preferred shares are redeemable at the option of the Company at a price of US\$1.00 per share plus accrued and unpaid dividends commencing at the earlier of two years from issuance date or the date at which Kingsway Financial Services Inc.'s beneficial interest is less than 10%.

The outstanding preferred shares are entitled accrued dividends on a cumulative basis whether or not declared by the Board of Directors. In accordance with IAS-32, *Financial Instruments: Presentation*, because of their mandatory dividend feature the preferred shares are deemed to contain both a liability and an equity component. The liability component is the estimated fair value of the future dividends the Company estimates will accrue beginning on December 31, 2010 through the date on which the preferred shares are either redeemed, at the option of the Company, or converted into ordinary restricted voting common shares, at the option of the holder. The liability component, classified as a present value liability for preferred dividends, is \$2,647, and the preferred equity component, classified in shareholders' equity, is \$15,353 at January 1, 2010, December 31, 2010 and March 31, 2011, respectively, in the accompanying balance sheet. The liability component is recognized at fair value with a corresponding charge to interest expense at the rate of 8.6% per year.

### Liquidity and Capital Resources

The purpose of liquidity management is to ensure there is sufficient cash to meet all financial commitments and obligations as they become due. The liquidity requirements of the Company's business have been met primarily by funds generated from operations, asset maturities and income and other returns received on securities. Cash provided from these sources is used primarily for payment of claims and operating expenses. The timing and amount of catastrophe claims are inherently unpredictable and may create increased liquidity requirements.

As a holding company, Atlas may derive cash from its subsidiaries generally in the form of dividends and in the future may charge management fees to the extent allowed by statute or other regulatory approval requirements to meet its obligations. Atlas' Operating Insurance Subsidiaries fund their obligations primarily through premium and investment income and maturities in the securities portfolio. These Operating Insurance Subsidiaries require regulatory approval for the return of capital and, in certain circumstances, payment of dividends. In the event that dividends and management fees available to the holding company are inadequate to service its obligations, Atlas would need to raise capital, sell assets or incur debt obligations. At March 31, 2011, the Company did not have any outstanding debt, and therefore, no near term debt service obligations.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

In 2010 the Operating Insurance Subsidiaries paid dividends of \$16.7 million, respectively, to Kingsway America Inc. as their parent during that time period.

In 2010 the Operating Insurance Subsidiaries incurred losses, as did Atlas. The result of the losses by the Operating Insurance Subsidiaries reduces Atlas's capital flexibility by limiting the dividend capacity of the Operating Insurance Subsidiaries.

For further details on the capital adequacy of the Operating Insurance Subsidiaries, see the 'Capital Requirements' narrative in the MD&A for fiscal year 2010.

### Financial Strength and Credit Rating

As a result of the successful completion of the merger, on January 6, 2011, A.M. Best upgraded the Financial Strength Rating of the Operating Insurance Subsidiaries, American Country and American Service, to "B" from "B-". Both companies are members of the American Service Pool and had previously been downgraded from "B" to "B-" on November 24, 2009. Upon completion of the Atlas transaction, A.M. Best assigned an outlook of "stable" to all Financial Strength Ratings of the Operating Insurance Subsidiaries and has eliminated the "under review with developing implications" status. A.M. Best also upgraded the Issuer Credit Ratings of the Operating Insurance Subsidiaries to "bb" from "bb-", and issued an Issuer Credit Rating of "b-" to Atlas. The outlook assigned to the Issuer Credit Ratings was also "stable". These ratings have remained in effect through March 31, 2011.

### Risk Based Capital ("RBC")

In the United States, a RBC formula is used by the NAIC to identify P&C insurance companies that may not be adequately capitalized. The NAIC requires that capital and surplus not fall below 200% of the authorized control level. As of March 31, 2011, the Operating Insurance Subsidiaries are above the required 200% RBC threshold, with RBC ratios based on the unaudited statutory financial statements of 235% and 366% for American Country and American Service, respectively, and have estimated aggregate capital in excess of the 200% level of approximately \$17.8 million.

**Table 21 RBC**  
(in millions of dollars)

	Estimated as of March 31, 2011		Actual as of December 31, 2010	
	RBC (%)	Excess over Minimum <sup>1</sup>	RBC (%)	Excess over Minimum <sup>1</sup>
<b>American Service</b>	366	\$16.2	536	\$22.4
<b>American Country</b>	235	1.6	322	3.7
<b>Total Consolidated</b>		\$17.8		\$26.1

<sup>1</sup> Excess over regulatory minimum expressed in millions of dollars.

## VII. ACCOUNTING AND DISCLOSURE MATTERS

### Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the President and Chief Executive Officer (one person) and

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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the Chief Financial Officer of the Company, on a timely basis so that appropriate decisions can be made regarding public disclosure.

An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures was conducted as of March 31, 2011, by and under the supervision of the Company's management, including the Chief Executive Officer and Chief Financial Officer. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that such disclosure controls and procedures, as defined in National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings were effective as of such date to ensure that information relating to the Company required to be disclosed in reports that are filed or submitted under Canadian securities legislation are processed, summarized and reported within the time periods specified by those laws.

### **Internal Control over Financial Reporting**

Management designed and is responsible for maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

No significant changes were made to the Company's on-going internal controls over financial reporting during the period ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect the Company's internal controls over financial reporting.

All control systems contain inherent limitations, no matter how well designed. As a result, the Company's management acknowledges that its internal controls over financial reporting will not prevent or detect all misstatements due to error or fraud. In addition, management's evaluation of controls can provide only reasonable, not absolute, assurance that all control issues that may result in material misstatements, if any have been detected.

### **Critical Accounting Estimates**

The preparation of financial statements in conformity with IFRS requires management to make certain estimates and assumptions, some of which may relate to matters that are uncertain. As more information becomes known, these estimates and assumptions could change and thus have a material impact on the Company's financial condition and results of operations in the future.

### **Adoption of International Financial Reporting Standards (IFRS)**

The Canadian Accounting Standards Board requires all Canadian public companies to present financial statements in accordance with IFRS for interim and annual periods beginning January 1, 2011. Accordingly, the Company has presented its quarterly unaudited consolidated financial statements commencing with the quarter ended March 31, 2011 in accordance with IFRS, including comparative prior period results and balances restated to comply with IFRS. An opening IFRS statement of financial position has been presented as of January 1, 2010, the transition date to IFRS, together with a comparison to the December 31, 2010 balances.

The Company previously presented its consolidated financial statements in accordance with U.S. GAAP. IFRS is based on a conceptual framework similar to U.S. GAAP. There are differences in recognition; measurement and disclosure between IFRS and U.S. GAAP.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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The outstanding preferred shares are entitled accrued dividends on a cumulative basis whether or not declared by the Board of Directors. In accordance with *IAS-32, Financial Instruments: Presentation*, because of their mandatory dividend feature the preferred shares are deemed to contain both a liability and an equity component. The liability component is the estimated fair value of the future dividends the Company estimates will accrue beginning December 31, 2010 before the preferred shares are either redeemed, at the option of the Company, or converted into ordinary restricted voting common shares, at the option of the holder. The liability component, classified in accounts payable and other liabilities is \$2,647, and the equity component, classified in shareholders' equity, is \$15,353 at January 1, 2010, December 31, 2010 and March 31, 2011, respectively, in the accompanying balance sheet. The liability component is recognized at fair value with a corresponding charge to interest expense at the rate of 8.6% per year.

The IFRS include the International Financial Reporting Standards and International Accounting Standards ("IAS") issued or adopted by the International Accounting Standards Board ("IASB") together with interpretations issued by the International Financial Reporting Interpretations Committee (prefixed "IFRIC") or interpretation issued by its predecessor organization the Standards Interpretations Committee (prefixed "SIC").

The Company established a changeover plan to transition its financial statement reporting, presentation and disclosure to IFRS to meet the January 1, 2011 deadline. The Company's IFRS transition plan and all activities necessary for the adoption of IFRS were substantially completed in March, 2011.

The following describes the impact of adopting IFRS on the Company's accounting, processes, information systems and internal controls:

Except for the impact of applying *IAS-32, Financial Instruments: Presentation* with respect to the liability and equity components of the preferred shares, there was no other impact on the Company's opening IFRS consolidated balance sheet as of January 1, 2010, the transition date to IFRS, or the consolidated balance sheet as of December 31, 2010. Additionally, there was no other adoption impact to the Company's consolidated statement of comprehensive income, or statement of changes in shareholders' equity for the three months ended March 31, 2010 and the year ended December 31, 2010. According there are no reconciling items between U.S. GAAP and IFRS to present.

*IFRS-1* provides guidance on first-time adoption and generally requires the retrospective application of all IFRS at the end of the first annual reporting period. However, the standard does require certain mandatory exceptions and provides for certain optional exemptions to full retrospective application upon first-time adoption.

**Mandatory exception** - In preparing these financial statements the Company applied the mandatory exception that requires that hindsight not be used to revise estimates made under GAAP and accordingly estimates previously made are consistent with their application under IFRS. The other mandatory exceptions are not applicable to the Company.

**Optional Exemption** – The Company elected to apply the transitional provisions of *IFRS 4 Insurance Contracts* which allows insurance companies adopting IFRS to continue with their existing accounting policies and to continue to apply their existing policies for measuring insurance liabilities, subject to a liability adequacy test.

*IFRS 4* introduces new disclosures, which will be included in the Company's annual consolidated financial statements for the year ending December 31, 2011. These disclosures require (a) an insurance risk sensitivity analysis that discloses the estimated impact on income and equity resulting from changes in relevant insurance risk variables

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

and assumptions, and (b) a concentration of insurance risk describing the basis of determining insurance risk concentration. IFRS 4 does not permit off-setting of insurance liabilities against related insurance assets nor income and expenses to be offset from reinsurance amounts.

There was no impact on the Company's financial statements from the adoption of this optional election.

### Impact on processes, information systems and controls of IFRS Adoption

There are no significant changes in the Company's processes, information systems and internal controls as a result of adopting IFRS.

### Future Modifications to IFRS

In November 2009 *IFRS 9 Financial Instruments* was issued as the first phase of a three-phase project to *replace IAS 39 Financial Instruments: Recognition and Measurement*. The objective of the standard is to reduce complexity by replacing the many different rules in *IAS 39*.

The first Phase addresses the measurement and classification of financial assets and retains but simplifies the measurement model by establishing two primary methods – amortized cost and fair value. The method selected is dependent on the entity's business model and the contractual cash flows of the asset. In October 2010 the phase was issued covering the measurement and classification of financial liabilities. This chapter provides for the option to measure debt issued by an entity at fair value. The portion of the fair value adjustment attributable to an entities own credit risk is classified in other comprehensive income (loss) and the balance in income. The final third unissued phase of the project is expected to address hedge accounting.

The standard *IFRS 9* is effective for accounting periods commencing on or after January, 2013 with earlier adoption permitted. The Company is assessing the impact of these this pronouncements on its results and financial position.

## VIII. RELATED PARTY TRANSACTION

As a result of its current ownership interest in the Company, Kingsway and its affiliates remain classified as related parties to Atlas. Related party transactions, including services provided to or received by the Company's subsidiaries, are carried out in the normal course of operations and are measured at the amount of consideration paid or received as established and agreed by the parties. Management believes that consideration paid for such services approximates fair value.

**Table 22 Related party balances**

(in thousands of dollars)

Balances receivable from (payable to) affiliates:	March 31, 2011	December 31, 2010
Kingsway America Inc.	\$ 531	\$ 2,058
Universal Casualty Company	(676)	0
Kingsway Amigo Insurance Company	(33)	(13)
Hamilton Risk Management Inc.	(1)	(1)
<b>Total</b>	<b>\$ (179)</b>	<b>\$ 2,045</b>

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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In 2010 the Company's Operating Insurance Subsidiaries remitted management fees monthly to Kingsway America Inc. for managerial services and rent for the Company's Elk Grove Village headquarters building. That building was contributed to the Company in June 2010 and rental payments ceased at that time. Management fees were paid to Kingsway America Inc. totaling approximately \$0 and \$660,690 for the three months ended March 31, 2011 and 2010, respectively.

The Company received \$0 and \$78,959 in mortgage payments for the three months ended March 31, 2011 and 2010, respectively under a mortgage loan agreement with Kingsway America Inc. which was terminated in June of 2010.

For the three months ended March 31, 2011 and 2010, the Company paid \$639,126 and \$1,021,324, respectively, as commissions to Avalon Risk Management, Inc. In the three months ended March 31, 2011 and 2010, they also paid Avalon \$26,000 and \$46,875, respectively, for marketing services. Avalon Risk Management, Inc. was a Kingsway subsidiary through October 2009, and has investors and directors in common with Atlas.

During the three months ended March 31, 2010, dividends of \$14,300,000 were paid to Kingsway America Inc. by the Operating Insurance Subsidiaries of the Company.

### **IX. RISK MANAGEMENT**

The Company has not significantly changed its risk management strategy presented in the 2010 annual Management Discussion & Analysis.

#### **Estimated impact of changes in interest rates and securities prices**

For the Company's AFS fixed income securities, a 100 basis point increase in interest rates would increase income before taxes by approximately \$192,000. A 100 basis point increase would also decrease other comprehensive income by approximately \$3.5 million due to "mark-to-market" requirements; however, holding investments to maturity would mitigate this impact. Conversely, a 100 basis point decrease in interest rates would decrease income before taxes and increase other comprehensive income by the same amounts, respectively. The impacts described here are approximately linearly related to the change in interest rates.

### **X. SUBSEQUENT EVENTS**

On January 24, 2011, a contract for the sale of the office building in Mobile, Alabama with a December 31, 2010 net book value of \$2.0 million was executed. The sale consummated on June 8, 2011.

In the second quarter of 2011 the Company initiated the Atlas Employee Stock Purchase Plan to encourage continued employee interest in the operation, growth and development of the Company and to provide an additional investment opportunity to employees. Beginning in June 2010, full time and permanent part time employees working more than 30 hours per week will be allowed to invest up to 5% of adjusted salary in Company stock. The Company will match contributions at 50% of the employee investment amounts up to 2.5% of adjusted salary. Employees signing up for the program by May 30, 2011 will receive an additional 100 shares of stock as an initial participation incentive. The Company will also pay administrative costs related to this plan.

Events have been evaluated through June 17, 2011, the date the Atlas Board of Directors approved the financial statements for issuance.

# Atlas Financial Holdings, Inc.

## Management Discussion and Analysis – Q1 2011

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### XI. OUTLOOK

Over the past two years, through dispositions and by placing certain lines of business into run-off, the Operating Insurance Subsidiaries have streamlined operations to focus on the lines of business they believe will produce favorable underwriting results. Significant progress has also been made in aligning the cost base to this reduced revenue base. The core functions of the Operating Insurance Subsidiaries were integrated into a common operating platform. Management believes that both Operating Insurance Subsidiaries are well positioned to return to historic volumes with better than industry level profitability. They have a long heritage with respect to their go forward lines of business and will benefit from the efficient operating infrastructure established in the past twelve months.

Management believes that the most significant opportunities going forward are: (i) re-energizing distribution channels with the objective of recapturing the volume of business generated prior to 2009, (ii) expanding into geographic markets where licensed, but not currently active, and (iii) opportunistically acquiring books of business provided market conditions support this activity. Primary risks related to these activities include: (i) insurance market conditions remaining “soft” for a sustained period of time, (ii) not being able to achieve the expected support from distribution partners, and (iii) the Operating Insurance Subsidiaries not successfully maintaining improved ratings from A.M. Best.

In 2011, the Company’s focus is the underwriting of non-standard automobile insurance in the U.S. complimented by low limit commercial automobile insurance for light weight, individual units or small fleets.

The Company will seek to deploy its capital to maximize the return for its shareholders, either by investing in growing the operations or other capital initiatives, depending upon insurance and capital market conditions. The Company will use historic and current data to analyze and assess future business market areas.