HALLMARK FINANCIAL SERVICES INC
Form 8-K/A
February 14, 2003

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

FORM 8-K/A

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): December 3, 2002

HALLMARK FINANCIAL SERVICES, INC.
(Exact name of registrant as specified in its charter)

Nevada	0-16090	87-0447375
(State or other jurisdiction of incorporation)	(Commission File Number)	(IRS Employer Identification No.)

14651 Dallas Parkway, Suite 900, Dallas, Texas	75254
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (972) 404-1637

Not Applicable
(Former name or former address, if changed since last report.)

The Registrant hereby amends Item 7(a) and Item 7(b) of its Current Report on Form 8-K filed on December 4, 2002, for the purpose of providing financial statements required in connection with the Registrant's acquisition of Millers General Agency, Inc., Financial and Actuarial Resources, Inc. and Effective Litigation Management, Inc.

Item 7. Financial Statements and Exhibits.
a) Financial statements of business acquired.

Report of Independent Accountants

To the Boards of Directors and Stockholders of
Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.

In our opinion, the accompanying combined balance sheets and the related combined statements of operations, stockholders' equity and cash flows present fairly, in all material respects, the financial position of Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc. at December 31, 2001, and the results of their operations and their cash flows for the eleven months ended November 30, 2002 and the year ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Companies' management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP
Dallas, Texas
February 12, 2003

Report of Independent Accountants

To the Boards of Directors and Stockholder of
Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.

In our opinion, the accompanying combined balance sheet and the related combined statement of operations, stockholders' equity and cash flows present fairly, in all material respects, the financial position of Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc. at December 31, 2002, and the results of their operations and their cash flows for the month ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Companies' management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1 to the combined financial statements, Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc. were acquired by Hallmark Financial Services, Inc. effective December 1, 2002 in a purchase business combination recorded under the push-down method of accounting, resulting in a new basis of accounting for the successor period beginning December 1, 2002.

/s/ PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP
Dallas, Texas
February 12, 2003

Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc.
COMBINED BALANCE SHEETS

	December 31, 2002 (Successor)	December 31, 2001 (Predecessor)
ASSETS		
Cash and cash equivalents	$ 825,876	$ -
Accounts receivable	2,128,942	1,411,393
Prepaid agent commission	3,899,393	2,622,819
Other current assets	15,788	8,173
Total current assets	6,869,999	4,042,385
Furniture, fixtures and equipment, net	486,398	143,265
Profit sharing commission receivable	866,663	-
Deferred tax asset	642,129	889,542
Goodwill	2,434,049	-
Other intangible assets	540,319	-
Total assets	$ 11,839,557	$ 5,075,192
LIABILITIES AND STOCKHOLDERS' EQUITY		
Unearned revenue	$ 6,871,690	$ 4,478,238
Accounts payable	406,970	212,326
Commission payable	593,821	-
Accrued agent profit sharing	449,789	341,777
Payable to Phoenix Indemnity Insurance Co.	480,000	-
Current portion of long term notes payable	83,517	315,959
Other current liabilities	410,059	387,584
Total current liabilities	9,295,846	5,735,884
Commitments and contingencies		
Long term notes payable	-	83,517
Pension liability	603,863	-
Total long term liabilities	603,863	83,517
Total liabilities	9,899,709	5,819,401

Common stock	2,100	2,100
Additional paid-in capital	2,097,900	900
Retained earnings (accumulated deficit)	1,796	(747,209)
Accumulated other comprehensive income (loss)	(161,948)	-
Total stockholders' equity	1,939,848	(744,209)
Total liabilities and stockholders' equity	$ 11,839,557	$ 5,075,192

The accompanying notes are an integral part
of these financial statements

Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.
COMBINED STATEMENTS OF OPERATIONS

	Eleven Months Ending November 30, 2002 (Predecessor)	One Month Ending December 31, 2002 (Successor)	Twelve Months Ending December 31, 2001 (Predecessor)
Revenues			
Commissions and fees	$ 10,863,314	$ 1,560,798	$ 9,417,949
Interest and other income	13,992	500	12,993
Total revenues	10,877,306	1,561,298	9,430,942
Expenses			
Commissions and other selling expenses	6,649,989	740,636	5,648,707
Salaries and employee benefits	1,256,885	423,108	1,382,514
General and administrative	1,945,318	356,177	1,780,833
Depreciation and amortization	72,243	37,425	140,354
Interest expense	22,298	832	50,228
Total expenses	9,946,733	1,558,178	9,002,636
Income before taxes	930,573	3,120	428,306
Federal income tax expense	344,896	1,324	161,890
Net income	$ 585,677	$ 1,796	$ 266,416

The accompanying notes are an integral part
of these financial statements

Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.
COMBINED STATEMENTS OF STOCKHOLDERS' EQUITY

	Additional	Retained Earnings	Accumul Other Comprehe

	Number of Shares	Par Value	Paid in Capital	(Accumulated Deficit)	Incom (Loss
December 31, 2000 (Predecessor)	2,100	$ 2,100	$ 900	$ (1,013,625)	$
Net income				266,416	
December 31, 2001 (Predecessor)	2,100	$ 2,100	$ 900	$ (747,209)	$
Predecessor net income for the eleven months ending November 30, 2002				585,677	
November 30, 2002 (Predecessor)	2,100	$ 2,100	$ 900	$ (161,532)	$
December 1, 2002 (Successor)	2,100	$ 2,100	$2,097,900	$ -	$
Comprehensive loss:					
Successor net income for the one month ending December 31, 2002				1,796	
Other comprehensive loss:					
Minimum pension liability					(255,
Tax effect of minimum pension liability					93,
Net minimum pension liability					(161,
Total comprehensive loss					
December 31, 2002 (Successor)	2,100	$ 2,100	$2,097,900	$ 1,796	$ (161,

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

Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.
COMBINED STATEMENTS OF CASH FLOWS

	Eleven Months Ending November 30, 2002 (Predecessor)	One Month Ending December 31, 2002 (Successor)	Twelve Months Ending December 31, 2001 (Predecessor)
Cash flows from operating activities:			
Net income	$ 585,677	$ 1,796	$ 266,416
Adjustments to reconcile net income to cash provided by (used in) operating activities:			

Depreciation and amortization	72,243	37,425	140,354
Gain on sale of office furniture	(9,000)	-	-
Change in accounts receivable	21,126	(170,051)	(829,181)
Change in prepaid commissions	(1,240,372)	(36,203)	(363,761)
Change in profit sharing receivable	(803,002)	(63,661)	-
Change in deferred tax asset	2,929	(1,215)	164,725
Change in unearned revenue	1,641,599	183,229	297,564
Change in commission payable	-	593,821	-
Change in accrued agent profit sharing	35,730	72,281	(449,608)
Change in other current assets	-	(7,614)	-
Change in other current liabilities	275,675	271,200	94,355
Net cash provided by (used in) operating activities	582,605	881,008	(679,136)
Cash flows from investing activities:			
Purchases of furniture, fixtures and equipment	(1,022)	-	(72,304)
Proceeds from sales of furniture, fixtures and equipment	9,000	-	3,075
Net cash provided by (used in) investing activities	7,978	-	(69,229)
Cash flows from financing activities:			
Book overdraft	(302,041)	(27,707)	329,756
Repayment of borrowings	(288,534)	(27,425)	(288,862)
Net cash provided by (used in) financing activities	(590,583)	(55,132)	40,894
Net increase (decrease) in cash and cash equivalents	-	825,876	(707,471)
Cash at beginning of period	$ -	$ -	$ 707,471
Cash at end of period	$ -	$ 825,876	$ -
Supplemental cash flow information:			
Interest paid	$ 22,298	$ 832	$ 49,887
Income taxes paid	$ -	$ -	$ 10,718

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

Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc.
Notes to Combined Financial Statements

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Millers General Agency, Inc., Effective Litigation Management, Inc. and

Financial and Actuarial Resources, Inc. (hereinafter collectively referred to as the "Company") are a regional managing general agency, a third party claims administrator and a financial administrative service company, respectively. The Company markets through an independent agency force low hazard commercial insurance policies primarily in the rural areas of Texas, New Mexico, Idaho, Oregon and Washington. The Company also underwrites and administers the claims on these insurance policies. On December 1, 2002, the Company was acquired by Hallmark Financial Services, Inc. ("HFS") in a purchase business combination recorded under the "push down" method of accounting, resulting in a new basis of accounting for the "Successor" period beginning December 1, 2002. Information relating to all "Predecessor" periods prior to the acquisition is presented using the Company's historical basis of accounting.

Basis of Combination

The accompanying combined financial statements include the accounts of Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc. Combined financial statements are presented due to the related operations and management of the Company. All significant intercompany accounts and transactions have been eliminated in the combined financial statements.

Revenue Recognition

Commission revenue and commission expense related to insurance policies serviced by the Company are recognized during the period covered by the policy. Profit sharing commission is recognized when the ratio of ultimate losses and loss expenses incurred to earned premium ("loss ratio") as determined by a qualified actuary fall below contractual thresholds. The profit sharing commission is an estimate that varies with the estimated loss ratio and is sensitive to changes in that estimate. For each 0.5% change in the loss ratio, the profit sharing commission changes by approximately $120,000.

Claim servicing fees are recognized during the period covered by the insurance policy with a portion of the fees related to casualty claims deferred and recognized over two years following the expiration of the policy.

Furniture, Fixtures and Equipment

Furniture, fixtures and equipment are carried at cost, less accumulated depreciation. Depreciation is provided on the straight-line method over the useful lives of 5 years for office furniture and equipment, 3 years for software and 10 years for leasehold improvements. Gains and losses on dispositions are shown on the statement of operations as other income.

Cash and Cash Equivalents

Cash and cash equivalents includes an overnight investment sweep account at Bank of America, N.A. used to fund the operations of the Millers General Agency, Inc.

Agent Profit Sharing Commission

The Company annually pays a profit sharing commission to its independent agency force based upon the results of the business produced by each agent. The Company estimates and accrues this liability to commission expense in the year the business is produced.

Federal Income Taxes

The Company accounts for taxes (including deferred taxes) utilizing the asset and liability method, as required by Statement of Financial Accounting Standards No. 109 ("FAS 109"). Under this method, balance sheet amounts for deferred income taxes are computed based on the tax effect of the differences between the financial reporting and federal income tax bases of assets and liabilities using tax rates which are expected to be in effect when these differences are anticipated to reverse.

In accordance with FAS 109, total tax expense (or benefit) is the amount of income taxes expected to be paid (or received) for the current year plus (or minus) the deferred income tax expense (or benefit) represented by the change in deferred income tax accounts at the beginning and end of the year. The effect of changes in tax rates and federal income tax laws are reflected in income in the period such changes are enacted.

The tax effect of future taxable temporary differences (liabilities) and future deductible temporary differences (assets) are separately calculated and recorded when such differences arise. A valuation allowance, reducing any recognized deferred tax asset, must be recorded if it is determined that it is more likely than not that such deferred tax will not be realized.

Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions. This affects amounts reported in the financial statements and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

2. FURNITURE, FIXTURES AND EQUIPMENT

Furniture, fixtures and equipment consist of the following:

	December 31, 2002	December 31, 2001
Office furniture and equipment	$ 377,564	$ 265,922
Software	389,696	79,648
Leasehold improvements	19,850	-
	787,110	345,570
Accumulated depreciation	(300,712)	(202,305)
	$ 486,398	$ 143,265

Depreciation expense was $47,906 for the eleven months ending November 30, 2002 and $8,748 for the one month ending December 31, 2002, as compared to $51,806 for the twelve months ending December 31, 2001. Amortization expense was $24,337 for the eleven months ending November 30, 2002 and $28,677 for the one month ending December 31, 2002, as compared to $88,548 for the twelve months ending December 31, 2001.

3. FEDERAL INCOME TAXES

The components of federal income tax expense (benefit) are as follows:

	Eleven Months Ending November 30, 2002 (Predecessor)	One Month Ending December 31, 2002 (Successor)	Twelve Months Ending December 31, 2001 (Predecessor)
Current	$ 341,967	$ 2,538	$ (2,836)
Deferred	2,929	(1,214)	164,726
	$ 344,896	$ 1,324	$ 161,890

Total income tax expense (benefit) is different from the amount computed using statutory tax rates applied to pre-tax income for the following reasons:

	Eleven Months Ending November 30, 2002 (Predecessor)	One Month Ending December 31, 2002 (Successor)	Twelve Months Ending December 31, 2001 (Predecessor)
Tax expense at statutory rates	$ 316,395	$ 1,062	$ 145,624
Meals and entertainment	794	98	164
Nondeductible dues	-	58	30
State tax	27,707	106	16,072
Total income tax expense	$ 344,896	$ 1,324	$ 161,890

Deferred tax assets are attributable to the following temporary differences:

	December 31, 2002	December 31, 2001
Unearned commissions	$ 2,303,576	$ 1,655,605
Goodwill	(2,200)	290,313
Prepaid commissions	(1,441,606)	(969,656)
Accrued agent profit sharing	-	(164,241)
Profit sharing commission receivable	(320,405)	-
Agency relationship amortization	(199,756)	-
Pension liability	221,014	-
Federal NOL	77,071	77,071
All others	4,435	450
	$ 642,129	$ 889,542
Valuation allowance	-	-
	$ 642,129	$ 889,542

As of December 1, 2002, the Company had a tax net operating loss carryforward of approximately $226,679 for income tax purposes which expires between 2019 and 2021. There are certain limitations that could be imposed by the Internal Revenue Code regarding the amount of carryforwards that may be utilized each year. The Company had a current tax payable (receivable) balance of $308,456 and ($36,050) as of December 31, 2002 and 2001, respectively.

4. INTANGIBLE ASSETS

The Company's intangible assets are composed of $2,434,049 of goodwill and $540,319 for the Company's relationships with its independent agents. These assets were acquired on December 1, 2002 with the acquisition of the Company by Hallmark Financial Services, Inc. The Company's agency relationships are valued at $542,580 and are being amortized over twenty years. The Company recognized $2,261 of amortization expense for the one month ending December 31, 2002 and will recognize $27,129 in amortization expense for each of the next five years and $404,674 for the remainder of the asset's life.

5. NOTES PAYABLE

The Company's notes payable balance of $83,517 as of December 31, 2002 consists of two notes payable to Millers Insurance Company. Each of these notes carries an interest rate of 9% and matures in March 2003.

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6. RETIREMENT PLANS

Certain employees of the Company were participants in a defined benefit cash balance plan covering all full-time employees who had completed at least 1,000 hours of service. This plan was frozen in March 2001 in anticipation of distribution of plan assets to members upon plan termination. All participants were vested when the plan was frozen.

	11 month Ending 11/30/02 (Predecessor)	1 month Ending 12/31/02 (Successor)	Year Ending 12/31/01 (Predecessor)
Assumptions (end of period)			
Discount rate used in determining benefit obligation	6.50%	6.50%	7.25%
Rate of compensation increase	N/A	N/A	N/A
Reconciliation of funded status (end of period):			
Vested benefit obligation	$(11,792,123)	$(11,755,854)	$(10,793,748)
Accumulated benefit obligation	(11,794,169)	(11,757,910)	(10,830,974)
Projected benefit obligation	(11,794,169)	(11,757,910)	(10,830,974)
Fair value of plan assets	11,445,744	11,154,047	12,528,900
Funded status	$ (348,425)	$ (603,863)	$ 1,697,926
Unrecognized net obligation/(asset)	-	-	-

Unrecognized prior service cost	-	-	-
Unrecognized actuarial (gain)/loss	2,450,806	267,798	228,554
Prepaid/(accrued) pension cost	$ 2,102,381	$ (336,065)	$ 1,926,480
Changes in projected benefit obligation:			
Benefit obligation as of beginning of period	$ 10,830,974	$ 11,794,169	$ 9,419,143
Service cost	-	-	18,672
Interest cost	710,763	63,625	757,443
Plan amendments	-	-	-
Actuarial liability (gain)/loss	1,213,134	(3,994)	1,756,078
Effect of curtailment (plan freeze)	-	-	(170,729)
Benefits paid	(960,702)	(95,890)	(949,633)
Benefit obligation as of end of period	$ 11,794,169	$ 11,757,910	$ 10,830,974

	11 month Ending 11/30/02 (Predecessor)	1 month Ending 12/31/02 (Successor)	Year Ending 12/31/01 (Predecessor)
Change in plan assets:			
Fair value of plan assets as of beginning of period	$ 12,528,900	$ 11,445,744	$ 14,542,959
Actual return on plan assets (net of expenses)	(122,454)	(195,807)	(1,064,426)
Employer contributions	-	-	-
Benefits paid	(960,702)	(95,890)	(949,633)
Fair value of plan assets as of end of period	$ 11,445,744	$ 11,154,047	$ 12,528,900
Net periodic pension cost:			
Service cost - benefits earned during the period	$ -	$ -	$ 18,672
Interest cost on projected benefit obligation	710,763	63,625	757,443
Expected return on plan assets	(886,664)	(75,985)	(1,044,192)
Amortizations			
Net obligation/(asset)	-	-	9,385
Unrecognized prior service cost	-	-	(12,518)
Unrecognized (gain)/loss	-	-	(24,155)
Net periodic pension cost (credit)	$ (175,901)	$ (12,360)	$ (295,365)
Discount rate (beginning of year)	7.25%	6.50%	7.75%
Expected return on plan assets	8.00%	8.00%	8.00%
Rate of compensation increase	N/A	N/A	5.00%

As of December 31, 2002, the fair value of the plan assets was composed of cash and cash equivalents of $740,031, bonds and notes of $5,661,985 and equity securities of $4,752,031.

The Company sponsors a defined contribution profit sharing plan whereby all employees are eligible to participate on the first day of the quarter following their employment date and are considered fully-vested after five years of service. Participants are permitted to contribute 1% to 15% of their annual compensation on a tax deferred basis and the Company has matched 50% on the first 6% contributed by each employee. Employer contributions approximated $23,318 for the first eleven months of 2002 and $2,034 for the one month ending December 31, 2002, as compared to $15,497 contributed for the twelve months ending December 31, 2001. Profit sharing contributions are based on the Company's performance and are authorized annually at the discretion of the Board of Directors. There were no profit sharing contributions made to the plan in 2002 or 2001.

7. COMMON STOCK

Common stock consists of the following:

	December 31, 2002	December 31, 2001
Millers General Agency, Inc. common stock, $1.00 par value, 100 shares authorized and issued	$ 100	$ 100
Effective Litigation Management, Inc. common stock $1.00 par value, 1,000 shares authorized and issued	1,000	1,000
Financial and Actuarial Resources, Inc. common stock $1.00 par value, 1,000 shares authorized and issued	1,000	1,000
	$ 2,100	$ 2,100

8. COMMITMENTS AND CONTINGENCIES

The Company was self-insured for medical and dental coverage for its employees, with stop-loss coverage for individual claims exceeding $50,000. As of January 1, 2003, the Company is fully insured for medical claims of its employees. Total expense for medical claims were $82,362 for the first eleven months of 2002 and $21,979 for the one month ending December 31, 2002 as compared to $130,700 for the twelve months ending December 31, 2001.

The Company currently reimburses its former parent, Millers American Group ("MAG") for rent under MAG's operating lease. MAG leases office space under an operating lease that expires in 2009 with an option to terminate the lease in 2005. The lease provides for increasing rents over the lease term. Rental expense on space formerly occupied by the Company, and space currently occupied under the MAG lease was $143,234 for the first eleven months of 2002 and $48,362 for the one month ending December 31, 2002 as compared to $126,302 for the twelve months ending December 31, 2001. The Company intends to either have this lease assigned to it or to sublease this space from MAG at its current terms.

Future minimum lease payments as of December 31, 2002 are as follows:

2003	$491,475
2004	$486,798
2005	$506,892
2006	$500,151

2007	$494,148
Thereafter	$947,117

Item 7. Financial Statements and Exhibits.
b) Pro forma financial information

The following unaudited Pro Forma Consolidated Balance Sheet of Hallmark Financial Services, Inc. ("HFS") is presented as if the acquisition of Millers General Agency, Inc. ("MGA"), Effective Litigation Management, Inc. ("ELM") and Financial and Actuarial Resources, Inc. ("FAR") had occurred on September 30, 2002. The following unaudited Pro Forma Consolidated Statements of Operations of HFS for the nine months ended September 30, 2002 and for the year ended December 31, 2001 assume these transactions as described above had occurred as of January 1, 2001. The Pro Forma Consolidated Balance Sheet was derived from the Consolidated Balance Sheet of HFS and its subsidiaries filed with HFS' Quarterly Report on Form 10-QSB as of and for the nine months ended September 30, 2002. The Pro Forma Consolidated Statements of Operations were derived from the Consolidated Statements of Operations of HFS and its subsidiaries filed with HFS' Quarterly Report on Form 10-QSB as of and for the nine months ended September 30, 2002 and Annual Report on Form 10-KSB as of and for the year ended December 31, 2001. In management's opinion, all of the material adjustments necessary to reflect the effects of the acquisition transactions have been made. The Pro Forma Consolidated Balance Sheet is not necessarily indicative of what the actual financial position would have been assuming such transactions had been completed as of September 30, 2002, nor does it purport to present the future financial position of HFS. Additionally, the Pro Forma Consolidated Statements of Operations are not necessarily indicative of what the actual results of operations of HFS would have been assuming such transactions had been completed at the beginning of the periods presented, nor do they purport to present the results of operations for future periods. Further, the Pro Forma Consolidated Statement of Operations for the interim period ended September 30, 2002 is not necessarily indicative of the results of operations for a full year.

The Acquisition

On December 3, 2002, HFS acquired from Millers American Group, Inc. ("Millers") all of the outstanding stock of two inactive subsidiaries, ELM and FAR. HFS simultaneously acquired from The Millers Insurance Company ("MIC"), an indirect subsidiary of Millers, all of the outstanding stock of MGA, an active Texas managing general agency, as well as certain contracts and fixed assets. Immediately following these transactions, the newly acquired subsidiaries of HFS employed all MIC personnel and began providing fee-based claims and financial administrative services to MIC. The effective date of the above transactions is December 1, 2002.

The aggregate purchase price for the acquired subsidiaries and assets was $2,580,000, consisting of $2,100,000 in cash and MGA's assumption of $480,000 in debt owed by MIC to Phoenix Indemnity Insurance Company ("Phoenix"), another indirect subsidiary of Millers. The purchase price was determined through negotiations between HFS and Millers. HFS funded the cash portion of the purchase price from an interim financing facility previously provided by Newcastle Partners, L.P., an affiliate of Mark E. Schwarz, Chairman of HFS.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition.

At December 1, 2002
($000s)

Current assets	$ 5,234
Furniture, fixtures and equipment	522
Deferred tax asset, net	547
Other non-current assets	803
Intangible assets	543
Goodwill	2,434
Total assets acquired	10,083
Current liabilities	7,635
Additional minimum pension liability	348
Total liabilities assumed	7,983
Net assets acquired	$ 2,100

The acquired intangible assets of $543,000 represent the estimated fair value of MGA's relationship with its independent agents. These assets are being amortized over twenty years.

The Company is considering an election under Internal Revenue Code Section 338(h)(10) that would, if made, cause the tax basis of the assets acquired to increase from historic carrying value to fair market value, resulting in some amount of tax deductible goodwill. The balance of the deferred tax asset as of the date of acquisition would be reduced to zero with a corresponding increase to goodwill.

Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.
UNAUDITED CONSOLIDATED PRO FORMA BALANCE SHEET
($ in thousands)

	Hallmark Financial Services, Inc. September 30, 2002	MGA, ELM and FAR September 30, 2002	Combined Historical September 30, 2002	Pro fo Adjust
Assets				
Investments:				
Debt securities, held to maturity, at amortized cost	$ 8,280		$ 8,280	
Equity securities, available for sale, at market value	93		93	

Short-term investments, at cost which approximates Market value	6,442		6,442	
Total investments	14,815	-	14,815	
Cash and cash equivalents	6,361	27	6,388	
Restricted cash	1,607		1,607	
Prepaid reinsurance premiums	9,068		9,068	
Premiums receivable from lender for financed premiums (net of allowance for doubtful accounts of $172)	11,510		11,510	
Premiums receivable	891		891	
Reinsurance recoverable	13,272		13,272	
Commission and fee receivable	-	1,859	1,859	
Deferred policy acquisition costs	1,246		1,246	
Prepaid commissions	-	3,835	3,835	
Excess of cost over net assets acquired	4,431		4,431	2,
Current federal income taxes recoverable	-	(81)	(81)	
Deferred federal income taxes	279	893	1,172	
Accrued investment income	69		69	
Other assets	733	103	836	
Total assets	$ 64,282	$ 6,636	$ 70,918	$ 4,

Millers General Agency, Inc., Effective Litigation Management, Inc. and
Financial and Actuarial Resources, Inc.
UNAUDITED CONSOLIDATED PRO FORMA BALANCE SHEET
($ in thousands)

	Hallmark Financial Services, Inc. September 30, 2002	MGA, ELM and FAR September 30, 2002	Combined Historical September 30, 2002	Pro fo Adjust
Liabilities and stockholders' equity				
Liabilities:				
Notes payable	$ 12,317	$ 165	$ 12,482	$ 2,
Unpaid losses and loss adjustment expense	17,202		17,202	
Unearned premiums	15,367		15,367	
Unearned commissions and fees	-	5,953	5,953	
Accrued agent profit sharing	-	643	643	
Reinsurance balances payable	3,217		3,217	
Drafts outstanding	610		610	
Accrued ceding commission refund	2,217		2,217	
Accounts payable and other accrued expenses	2,506	427	2,933	
Pension liability			-	
Current federal income taxes payable	67		67	
Total liabilities	53,503	7,188	60,691	3,
Stockholders' equity:				
Common stock	356	2	358	
Capital in excess of par value	10,875	1	10,876	1,

Retained earnings	591	(555)	36	
Accumulated other comprehensive income			-	
Treasury stock	(1,043)	-	(1,043)	
Total stockholders' equity	10,779	(552)	10,227	1,
Total liabilities and stockholders' equity	$ 64,282	$ 6,636	$ 70,918	$ 4,

(a) Recognition of claim fee receivable and unearned claim fee revenue of $569 for the assignment of a claims administration agreement to the Company.
(b) Recognition of fixed assets acquired separately from the acquisition of MGA, ELM and FAR from Millers Insurance Company of $450.
(c) Recognition of $2,434 of goodwill from the Hallmark Financial Services, Inc. acquisition of the Company.
(d) Recognition of $543 of agency relationship intangible asset from the Hallmark Financial Services, Inc. acquisition of the Company.
(e) Recognition of a minimum pension liability of $349 and resulting tax effect of $128 from the frozen defined benefit cash balance plan.
(f) Recognition of $2,100 of 11.75% fixed rate debt incurred to complete the acquisition.

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Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc.
UNAUDITED CONSOLIDATED PRO FORMA STATEMENTS OF OPERATIONS
($ in thousands)

	Hallmark Financial Services, Inc. 12 Months Ending December 31, 2001	MGA, ELM and FAR 12 Months Ending December 31, 2001	Combined Historic Twelve Months Ending December 31, 200
Gross premiums written	$ 49,614		$ 49,614
Ceded premiums written	(33,822)		(33,822)
Net premiums written	$ 15,792		$ 15,792
Revenues			
Gross premiums earned	$ 49,525	$ -	$ 49,525
Ceded premiums earned	(33,149)		(33,149)
Net premiums earned	16,376	-	16,376
Commission income	-	9,297	9,297
Investment income, net of expenses	1,043		1,043
Finance charges	3,095		3,095
Processing and service fees	1,120	120	1,240
Other income	368	13	381
Total revenue	22,002	9,430	31,432

Benefits, losses and expenses:

Losses and loss adjustment expenses	43,735		43,735
Reinsurance recoveries	(27,857)		(27,857)
Net losses and loss adjustment expenses	15,878	-	15,878
Acquisition costs, net	(399)		(399)
Other acquisition and underwriting expenses (net of ceding commission)	3,673	5,649	9,322
Operating expenses	3,346	3,303	6,649
Interest expense	1,021	50	1,071
Amortization of intangible assets	157		157
Litigation costs	-		-
Total benefits, losses and expenses	23,676	9,002	32,678
Loss from operations before federal income	(1,674)	428	(1,246)
Federal income tax benefit	(544)	162	(382)
Net (loss) income	$ (1,130)	$ 266	$ (864)
Basic and diluted (loss) earnings per share (11,049,133 shares outstanding)	$ (0.10)	$ 0.02	$ (0.08)

(a) Includes twelve months of depreciation expense of $344 of acquired fixed assets from Millers Insurance Company separate from the acquisition of MGA, ELM and FAR.
(b) Includes twelve months amortization expense of $27 of agency relationships.
(c) Includes twelve months of interest expense of $247 related to debt incurred to complete the acquisition.

Millers General Agency, Inc., Effective Litigation Management, Inc. and Financial and Actuarial Resources, Inc.
UNAUDITED CONSOLIDATED PRO FORMA STATEMENTS OF OPERATIONS
($ in thousands)

	Hallmark Financial Services, Inc. 9 Months Ending September 30, 2002	MGA, ELM and FAR 9 Months Ending September 30, 2002	Combined Historic Nine Months Ending September 30, 20
Gross premiums written	$ 37,542		$ 37,542
Ceded premiums written	(22,131)		(22,131)
Net premiums written	$ 15,411		$ 15,411
Revenues			
Gross premiums earned	$ 38,682	$ -	$ 38,682
Ceded premiums earned	(24,388)		(24,388)
Net premiums earned	14,294	-	14,294
Commission income	-	8,435	8,435

Investment income, net of expenses	417		417
Finance charges	1,804		1,804
Processing and service fees	335	215	550
Other income	257	13	270
Total revenue	17,107	8,663	25,770
Benefits, losses and expenses:			
Losses and loss adjustment expenses	26,584		26,584
Reinsurance recoveries	(15,908)		(15,908)
Net losses and loss adjustment expenses	10,676	-	10,676
Acquisition costs, net	(486)		(486)
Other acquisition and underwriting expenses (net of ceding commission)	4,001	5,642	9,643
Operating expenses	1,662	2,695	4,357
Interest expense	630	20	650
Amortization of intangible assets	-		-
Litigation costs	-		-
Total benefits, losses and expenses	16,483	8,357	24,840
Loss from operations before federal income	624	306	930
Federal income tax benefit	213	114	327
Net income (loss)	$ 411	$ 192	$ 603
Basic and diluted earnings (loss) per share (11,049,133 shares outstanding)	$ 0.04	$ 0.02	$ 0.05

(a) Includes nine months of depreciation expense of $258 of acquired fixed assets from Millers Insurance Company separate from the acquisition of MGA, ELM and FAR.
(b) Includes nine months of amortization expense of $20 of agency relationships.
(c) Includes nine months of interest expense of $185 related to debt incurred to complete the acquisition .

Item 7. Exhibits.

Exhibits.

2(a) * Purchase Agreement dated November 26, 2002, among Hallmark Financial Services, Inc., Millers American Group, Inc. and The Millers Insurance Company.

2(b) * Assumption Agreement dated December 1, 2002, among The Millers Insurance Company, Millers General Agency, Inc. and Phoenix Indemnity Insurance Company.

* Previously filed with the Company's Form 8-K filed with the Commission on December 4, 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

HALLMARK FINANCIAL SERVICES, INC.

Date: February 13, 2003

By: /s/ Timothy A. Bienek

Timothy A. Bienek, President and
Chief Operating Officer