CARDINAL HEALTH INC
Form 424B2
February 20, 2013
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Filed Pursuant to Rule 424(b)(2)

Registration Statement No. 333-169073

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered	Maximum Offering Price Per Unit	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee(1)
1.700% Notes due 2018	$400,000,000	99.840%	$399,360,000	$54,473
3.200% Notes due 2023	$550,000,000	99.793%	$548,861,500	$74,865
4.600% Notes due 2043	$350,000,000	99.657%	$348,799,500	$47,576
Total	$1,300,000,000		$1,297,021,000	$176,914

(1) Calculated in accordance with Rule 457(r) under the Securities Act of 1933, as amended.

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PROSPECTUS SUPPLEMENT

February 19, 2013

(To Prospectus dated August 27, 2010)

$1,300,000,000

Cardinal Health, Inc.

$400,000,000 1.700% Notes due 2018

$550,000,000 3.200% Notes due 2023

$350,000,000 4.600% Notes due 2043

The 1.700% notes will mature on March 15, 2018 (the 2018 notes), the 3.200% notes will mature on March 15, 2023 (the 2023 notes) and the 4.600% notes will mature on March 15, 2043 (the 2043 notes and, together with the 2018 notes and the 2023 notes, the notes). Interest on the notes will accrue from February 22, 2013. Interest on the notes will be payable semi-annually on March 15 and September 15 of each year, commencing September 15, 2013. We may redeem the notes of each series in whole at any time or in part from time to time, at the applicable redemption prices described in Description of the Notes Optional Redemption.

The notes are being issued to fund a portion of the purchase price of our acquisition of AssuraMed, Inc. (the Acquisition). In the event that we do not consummate the Acquisition on or prior to October 31, 2013, or the Merger Agreement (as defined herein) is terminated at any time prior to such date, we will be required to redeem all of the notes on a special mandatory redemption date at a redemption price equal to 101% of the principal amount of the notes as described under the caption Description of the Notes Special Mandatory Redemption. If a change of control repurchase event occurs, we will be required to offer to purchase the notes from holders at a purchase price of 101% of the principal amount of the notes. See Description of the Notes Repurchase at the Option of Holders Upon a Change of Control.

The notes will be our senior unsecured obligations and will rank equally with our other senior unsecured indebtedness outstanding from time to time.

Investing in the notes involves risk. See Risk Factors beginning on page S-5 and the section entitled Risk Factors in our Annual Report on Form 10-K for the fiscal year ended June 30, 2012, as they may be amended, updated or modified periodically in our reports filed with the Securities and Exchange Commission, for a discussion of certain risks that you should consider in connection with an investment in the notes.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus supplement or the accompanying prospectus. Any representation to the contrary is a criminal offense.

	Per 2018 Note	2018 Notes Total	Per 2023 Note	2023 Notes Total	Per 2043 Note	2043 Notes Total	Total
Price to Public (1)	99.840%	$ 399,360,000	99.793%	$ 548,861,500	99.657%	$ 348,799,500	$ 1,297,021,000
Underwriting Discount	0.600%	$ 2,400,000	0.650%	$ 3,575,000	0.875%	$ 3,062,500	$ 9,037,500
Proceeds to Us Before Expenses (1)	99.240%	$ 396,960,000	99.143%	$ 545,286,500	98.782%	$ 345,737,000	$ 1,287,983,500

(1) Plus accrued interest from and including February 22, 2013.

Currently, there is no public market for the notes. We do not intend to apply for listing of the notes on a securities exchange or for inclusion of the notes on an automated dealer quotation system.

We expect that delivery of the notes will be made to investors in book-entry form only through The Depository Trust Company for the accounts of its participants, including Clearstream Banking, société anonyme, and Euroclear Bank S.A./N.V., as operator of the Euroclear System, on or about February 22, 2013.

Joint Book-Running Managers

BofA Merrill Lynch **Deutsche Bank Securities** **UBS Investment Bank**

Co-Managers

Barclays **HSBC** **Mitsubishi UFJ Securities**

Morgan Stanley **Wells Fargo Securities**

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PROSPECTUS

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ABOUT THIS PROSPECTUS SUPPLEMENT

This document is in two parts. The first part is this prospectus supplement, which describes the specific terms of the offering of the notes and other matters relating to us. The second part is the accompanying prospectus, which gives more general information about securities we may offer from time to time, some of which does not apply to the notes we are offering. The information in this prospectus supplement replaces any inconsistent information included in the accompanying prospectus. If information in the prospectus supplement differs from information in the accompanying prospectus, you should rely on the information in this prospectus supplement. Before investing in the notes, you should read carefully both this prospectus supplement and the accompanying prospectus, together with additional information described under the heading Where You Can Find More Information and Incorporation of Certain Documents by Reference below.

Unless otherwise indicated or unless the context requires otherwise, all references in this prospectus supplement to we, us, our or the Company mean Cardinal Health, Inc., an Ohio corporation, and its consolidated subsidiaries, and references to Cardinal Health refer to Cardinal Health, Inc., excluding its consolidated subsidiaries.

You should rely only on the information contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or any free writing prospectus prepared by the Company. We do not, and the underwriters and their affiliates do not, take any responsibility for, and can provide no assurance as to the reliability of, any information that others may provide to you. You should not assume that the information contained or incorporated by reference in this prospectus supplement or in the accompanying prospectus is accurate as of any date other than the date on the front of that document. Our business, financial condition, results of operations and prospects may have changed since those dates.

The distribution of this prospectus supplement and the accompanying prospectus and the offering of the notes in certain jurisdictions may be restricted by law. We are not making an offer of the notes in any jurisdiction where the offer is not permitted. Persons who come into possession of this prospectus supplement and the accompanying prospectus should inform themselves about and observe any such restrictions. This prospectus supplement and the accompanying prospectus do not constitute, and may not be used in connection with, an offer or solicitation by anyone in any jurisdiction in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful to make such offer or solicitation.

You should not consider any information in this prospectus supplement or the accompanying prospectus to be investment, legal or tax advice. You should consult your own counsel, accountant and other advisors for legal, tax, business, financial and related advice regarding the purchase of the notes. We are not making any representation to you regarding the legality of an investment in the notes by you under applicable investment or similar laws.

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WHERE YOU CAN FIND MORE INFORMATION AND INCORPORATION

OF CERTAIN DOCUMENTS BY REFERENCE

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (the SEC). The SEC allows us to incorporate by reference the information we file with them, which means that we can disclose important business and financial information to you that is not included in or delivered with this prospectus supplement and the accompanying prospectus by referring you to publicly filed documents that contain the omitted information. Our SEC filings are available on the Internet at the SEC s website at http://www.sec.gov. You may also read and copy any document we file at the SEC s public reference room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for more information on the public reference room and its copy charges. You may also inspect our SEC reports and other information at the New York Stock Exchange, 20 Broad Street, New York, New York 10005. Documents may also be available on our website at http://www.cardinalhealth.com under the heading Investors. Please note that all references to http://www.cardinalhealth.com in this prospectus supplement and the accompanying prospectus are inactive textual references only and that the information contained on our website is neither incorporated by reference into this prospectus supplement and the accompanying prospectus nor intended to be used in connection with this offering. You may also request a copy of these filings, at no cost, by writing or telephoning us as follows: Cardinal Health, Inc., 7000 Cardinal Place, Dublin, Ohio 43017, (614) 757-3996 Attention: Investor Relations. Exhibits to the filings will not be sent unless those exhibits have been specifically incorporated by reference in this prospectus supplement or the accompanying prospectus.

We have filed with the SEC an automatic shelf registration statement on Form S-3 under the Securities Act of 1933, as amended (the Securities Act), as a well-known seasoned issuer (as defined in Rule 405 under the Securities Act) covering the securities described in this prospectus supplement and the accompanying prospectus. This prospectus supplement and the accompanying prospectus do not contain all of the information included in the registration statement, some of which is contained in exhibits included with or incorporated by reference into the registration statement. The registration statement, including the exhibits contained or incorporated by reference therein, can be read at the SEC s website or at the SEC offices referred to above. Any statement made in this prospectus supplement or the accompanying prospectus concerning the contents of any contract, agreement or other document is only a summary of the actual contract, agreement or other document. If we have filed or incorporated by reference any contract, agreement or other document as an exhibit to the registration statement, you should read the exhibit for a more complete understanding of the document or matter involved. Each statement regarding a contract, agreement or other document is qualified in its entirety by reference to the actual document.

We incorporate by reference the following documents filed with the SEC by us and any future filings we make with the SEC after the date of this prospectus supplement under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act), until we complete our offering of the securities offered by this prospectus supplement and the accompanying prospectus. We are not incorporating by reference any documents or portions thereof, whether specifically listed below or filed in the future, that are not deemed filed with the SEC (including the Current Reports on Form 8-K listed below), unless otherwise specified.

SEC Filings	Period/Date
Annual Report on Form 10-K	Fiscal Year ended June 30, 2012, filed with the SEC on August 22, 2012.
Quarterly Reports on Form 10-Q	Quarters ended September 30, 2012, filed with the SEC on November 9, 2012 and December 31, 2012, filed with the SEC on February 6, 2012.
Current Reports on Form 8-K	Dated August 8, 2012, August 31, 2012 (as amended on February 7, 2013), October 26, 2012, November 2, 2012, January 25, 2013, February 13, 2013 (Items 1.01 and 8.01 only) and February 19, 2013.

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SEC Filings	Period/Date
Definitive Proxy Statement on Schedule 14A	Filed with the SEC on September 14, 2012 for the 2012 Annual Meeting of Shareholders (other than the information set forth under the headings Human Resources and Compensation Committee Report and Shareholder Performance Graph)

Any statement contained or incorporated by reference in this prospectus supplement and the accompanying prospectus shall be deemed to be modified or superseded for purposes of this prospectus supplement and the accompanying prospectus to the extent that a statement contained herein or therein, or in any subsequently filed document which also is incorporated by reference herein or therein, modifies or supersedes such earlier statement. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this prospectus supplement and the accompanying prospectus.

INFORMATION CONCERNING FORWARD-LOOKING STATEMENTS

This prospectus supplement, the accompanying prospectus, our filings with the SEC, including our Annual Report on Form 10-K for the fiscal year ended June 30, 2012 (the 2012 Form 10-K), our Annual Report to Shareholders, any of our Quarterly Reports on Form 10-Q or any of our Current Reports on Form 8-K (together with any exhibits to such reports as well as any amendments to such reports), our press releases, or any other written or oral statements made by or on behalf of us, may include directly or by incorporation by reference forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 27A of the Securities Act. These statements reflect our view (as of the date such forward-looking statement is first made) with respect to future events, prospects, projections or financial performance. The matters discussed in these forward-looking statements are subject to certain risks and uncertainties and other factors that could cause actual results to differ materially from those projected, anticipated or implied in or by such statements. These risks and uncertainties include, but are not limited to:

competitive pressures in the markets in which we operate, including pricing pressures;

increasing consolidation in the healthcare industry, which could give the resulting enterprises greater bargaining power and may increase pressure on prices for our products and services;

uncertainties due to government healthcare reform, including the impact of the 2.3 percent tax to be paid by medical device manufacturers like us on the sale price of products;

changes to the prescription drug reimbursement formula and related reporting requirements for generic pharmaceuticals under Medicaid;

the expiration, loss of, material reduction in purchases by, or default by key customers, including CVS Caremark Corporation (CVS) and Walgreens Co. (Walgreens), whose contracts with us, absent renewal, are currently scheduled to expire in June 2013 and August 2013, respectively;

actions of regulatory bodies and other governmental authorities, including the U.S. Drug Enforcement Administration (DEA), the U.S. Food and Drug Administration, the U.S. Nuclear Regulatory Commission, the U.S. Department of Health and Human Services, the U.S. Federal Trade Commission, various state boards of pharmacy, state health departments, state insurance departments or comparable agencies or foreign equivalents that could delay, limit or suspend product development, manufacturing, distribution, importation or sales or result in warning letters, recalls, seizures, injunctions and monetary sanctions;

compliance with the settlement agreement that we entered into in connection with the DEA s suspension of our Lakeland, Florida distribution center s registration to distribute controlled substances and the possibility of civil fines against us by the U.S. Department of Justice for conduct covered by the settlement agreement;

the loss of, or default by, one or more key suppliers for which alternative suppliers may not be readily available;

unfavorable changes to the terms of key customer or supplier relationships, or changes in customer mix;

changes in manufacturers pricing, selling, inventory, distribution or supply policies or practices;

changes in hospital buying groups or hospital buying practices;

changes in the frequency or magnitude of branded pharmaceutical price appreciation or generic pharmaceutical price deflation, restrictions in the amount of inventory available to us, or changes in the timing or frequency of generic launches or the introduction of branded pharmaceuticals;

uncertainties relating to market conditions for pharmaceuticals;

uncertainties relating to demand for our products and services;

changes in the distribution or outsourcing pattern for pharmaceutical and medical/surgical products and services, including an increase in direct and limited distribution;

the costs, difficulties and uncertainties related to the integration of acquired businesses, including liabilities related to the operations or activities of such businesses prior to their acquisition;

the possibility that the closing of the Acquisition may be delayed or may not occur and the uncertainties relating to our ability to achieve the expected benefits from the Acquisition;

uncertainties relating to our ability to grow our specialty pharmaceutical services and distribution business;

uncertainties relating to our ability to grow our Cardinal Health China business, including growth of the pharmaceutical market in China;

risks arising from possible violations of the Foreign Corrupt Practices Act;

risks arising from possible violations of healthcare fraud and abuse laws, including the current Department of Justice investigation regarding the structure of discounts offered or provided to our customers;

our ability to introduce and market new products and our ability to keep pace with advances in technology;

uncertainties relating to the effectiveness of our Medical segment s business transformation project;

changes in laws or in the interpretation or application of laws or regulations, as well as possible failures to comply with applicable laws or regulations as a result of possible misinterpretations or misapplications;

the continued financial viability and success of our customers, suppliers and franchisees;

costs or claims resulting from potential errors or defects in our manufacturing, compounding, repackaging, information systems or pharmacy management services that may injure persons or damage property or operations, including costs from remediation efforts or recalls;

the results, costs, effects or timing of any commercial disputes, government contract compliance matters, patent infringement claims, or other legal proceedings;

the costs, effects, timing or success of restructuring programs or plans, including the restructuring plan within the Medical segment that we announced in January 2013;

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increased costs for commodities used in the Medical segment including various components, compounds, raw materials or energy such as oil-based resins, cotton, latex and other commodities;

shortages in commodities, components, compounds, raw materials or energy used by our businesses, including supply disruptions of radioisotopes;

the risks of counterfeit products in the supply chain;

risks associated with global operations, including the effect of local economic environments, inflation, recession, currency volatility and global competition, in addition to risks associated with compliance with U.S and international laws relating to global operations;

difficulties or delays in the development, production, manufacturing, sourcing and marketing of new or existing products and services, including difficulties or delays associated with obtaining requisite regulatory consents or approvals associated with those activities;

disruption or damage to or failure of our information or controls systems or a data security breach;

disruptions to the proper functioning of our critical facilities, including our national logistics center;

uncertainties relating to general political, business, industry, regulatory and market conditions;

adverse changes in U.S. or foreign tax laws, unfavorable challenges to our tax positions and payments to settle these challenges;

risks associated with the spin-off of CareFusion Corporation, including risks of non-performance under the tax matters agreement and risks relating to adverse tax consequences to us and our shareholders; and

other factors described in Item 1A-Risk Factors of the 2012 Form 10-K.

The words expect, anticipate, intend, plan, believe, will, should, could, would, project, continue, likely, and similar exp identify forward-looking statements, which speak only as of the date the statements were made, and also include statements reflecting future results or guidance, statements of outlook and expense accruals. We undertake no obligation to update or revise any forward-looking statements, except to the extent required by applicable law.

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SUMMARY

The following summary highlights selected information contained elsewhere in this prospectus supplement, the accompanying prospectus and in the documents incorporated by reference in this prospectus supplement and does not contain all the information you will need in making your investment decision. You should read carefully this entire prospectus supplement, the accompanying prospectus and the documents incorporated by reference in this prospectus supplement. See Where You Can Find More Information and Incorporation of Certain Documents by Reference in this prospectus supplement.

The Company

Cardinal Health, Inc. is an Ohio corporation formed in 1979. We are a healthcare services company providing products and services that help pharmacies, hospitals, surgery centers, physician offices and other healthcare providers focus on patient care while reducing costs, enhancing efficiency and improving quality.

The mailing address of our executive offices is 7000 Cardinal Place, Dublin, Ohio 43017, and our telephone number is (614) 757-5000.

For additional information concerning our business and affairs and descriptions of certain laws and regulations to which we may be subject, please refer to the information in the documents incorporated by reference in this prospectus supplement and the accompanying prospectus.

Recent Developments

On February 14, 2013, we announced that we entered into an Agreement and Plan of Merger (the Merger Agreement) to acquire AssuraMed, Inc. (AssuraMed). The Merger Agreement provides that we will pay an aggregate consideration of approximately $2.07 billion in cash to acquire AssuraMed, on a cash-free, debt-free basis, subject to working capital and other adjustments. AssuraMed is a leading provider of medical supplies to patients in the home.

We intend to finance the Acquisition with a combination of the net proceeds from this offering and cash on hand. On February 13, 2013, in connection with the Merger Agreement and the funding of the Acquisition, we obtained a commitment from Bank of America, N.A., an affiliate of Merrill Lynch, Pierce, Fenner & Smith Incorporated, for a new $1.3 billion senior unsecured bridge term loan facility.

The closing of the Acquisition is subject to the satisfaction or waiver of customary closing and regulatory conditions, including, among other things, the expiration or early termination of the waiting periods under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended. We currently expect that the Acquisition will be completed by early April 2013.

This offering is expected to be consummated on or about February 22, 2013, in advance of the expected date of the closing of the Acquisition. In the event that we do not consummate the Acquisition on or prior to October 31, 2013 or the Merger Agreement is terminated at any time prior to such date, we will be required to redeem all of the notes on a special mandatory redemption date at a redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding the date of redemption. See Description of Notes Special Mandatory Redemption.

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The Offering

Issuer	Cardinal Health, Inc.
Notes Offered	$400 million aggregate principal amount of 1.700% notes due 2018. $550 million aggregate principal amount of 3.200% notes due 2023. $350 million aggregate principal amount of 4.600% notes due 2043.
Interest	1.700% per year for the 2018 notes payable on March 15 and September 15, commencing September 15, 2013. 3.200% per year for the 2023 notes payable on March 15 and September 15, commencing September 15, 2013. 4.600% per year for the 2043 notes payable on March 15 and September 15, commencing September 15, 2013.
Maturity	March 15, 2018 for the 2018 notes March 15, 2023 for the 2023 notes March 15, 2043 for the 2043 notes
Issue Date	February 22, 2013
Record Dates	March 1 and September 1
Ranking	The notes will be senior unsecured debt obligations of Cardinal Health. The notes will rank equally with all of Cardinal Health s existing and future senior unsecured debt and senior to all of Cardinal Health s existing and future subordinated debt. As of December 31, 2012, Cardinal Health had outstanding approximately $2,898 million of unsecured indebtedness and guarantees of subsidiary indebtedness for borrowed money with which the notes would rank equally. The notes will be effectively subordinated to the liabilities of Cardinal Health s subsidiaries, including trade payables. As of December 31, 2012, Cardinal Health s subsidiaries had approximately $355 million of indebtedness for borrowed money ($184 million of which is guaranteed by Cardinal Health) and Cardinal Health s subsidiaries had an aggregate of approximately $11.8 billion of trade payables, to which the notes would be effectively subordinated.
Optional Redemption	We may redeem the notes prior to maturity, in whole at any time or in part from time to time, at our option, at a redemption price equal to the greater of the principal amount of such notes and the make-whole price described under Description of the Notes in this prospectus supplement, plus, in each case, accrued and unpaid interest, if any, to, but excluding, the date of redemption. See Description of the Notes Optional Redemption.

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Special Mandatory Redemption	The offering is not conditioned upon the consummation of the Acquisition but, in the event that we do not consummate the Acquisition on or prior to October 31, 2013 or the Merger Agreement is terminated at any time prior to such date, we will be required to redeem all of the notes on a special mandatory redemption date at a redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding, the date of redemption. See Description of the Notes Special Mandatory Redemption.
Change of Control Repurchase Event	Upon the occurrence of a change of control repurchase event, we will be required to make an offer to purchase the notes at a price equal to 101% of the principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding, the date of repurchase. See Description of the Notes Repurchase at the Option of Holders Upon a Change of Control.
Form of Notes	The notes of each series will initially be represented by one or more global notes, registered in the name of Cede & Co., the nominee of The Depository Trust Company (DTC). The notes of each series will be issued in denominations of $2,000 and integral multiples of $1,000 in excess thereof.
Use of Proceeds	We estimate that the net proceeds from the sale of the notes, after deducting the underwriting discount and estimated unreimbursed offering expenses, will be approximately $1.29 billion. We plan to use the net proceeds from the offering, and cash on hand, to fund the Acquisition. See Use of Proceeds.
Further Issuances	We may from time to time, without the notice to or consent of the holders of the notes, create and issue additional notes ranking equally and ratably in all respects with the notes offered by this prospectus supplement, having the same terms and conditions (other than the issue date, the price to public, and if applicable, the first interest payment date) as each series of notes, so that such issuance shall be consolidated and form a single series with the outstanding 2018 notes, 2023 notes or 2043 notes, as the case may be.
Risk Factors	See Risk Factors beginning on page S-5 and the section entitled Risk Factors in our Annual Report on Form 10-K for the fiscal year ended June 30, 2012 for discussion of factors you should carefully consider before deciding to invest in the notes.

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Summary Financial Information

In the table below, we provide you with our summary financial information, which is derived from our consolidated financial statements. The information is only a summary and should be read together with the financial information incorporated by reference into this prospectus supplement and the accompanying prospectus. See Where You Can Find More Information and Incorporation of Certain Documents by Reference in this prospectus supplement.

	At or for the Six Months Ended December 31,		At or for the Fiscal Year Ended June 30,		
	2012	2011	2012	2011	2010
	(unaudited)				
	(in millions, except per share amounts)				
Earnings Data:					
Revenue	$ 51,121	$ 53,870	$ 107,552	$ 102,644	$ 98,503
Earnings from continuing operations	$ 575	$ 501	$ 1,070	$ 966	$ 587
Earnings/(loss) from discontinued operations (1)		(2)	(1)	(7)	55
Net earnings	$ 575	$ 499	$ 1,069	$ 959	$ 642
Basic earnings/(loss) per Common Share					
Continuing operations	$ 1.69	$ 1.45	$ 3.10	$ 2.77	$ 1.64
Discontinued operations (1)		(0.01)		(0.02)	0.15
Net basic earnings per Common Share	$ 1.69	$ 1.44	$ 3.10	$ 2.75	$ 1.79
Diluted earnings/(loss) per Common Share					
Continuing operations	$ 1.67	$ 1.44	$ 3.06	$ 2.74	$ 1.62
Discontinued operations (1)		(0.01)		(0.02)	0.15
Net diluted earnings per Common Share	$ 1.67	$ 1.43	$ 3.06	$ 2.72	$ 1.77
Cash dividends declared per Common Share	$ 0.5125	$ 0.4300	$ 0.8825	$ 0.8000	$ 0.7200
Balance Sheet Data:					
Total assets	$ 24,642	$ 24,263	$ 24,260	$ 22,846	$ 19,990
Long-term obligations, less current portion and other short-term borrowings	$ 2,423	$ 2,211	$ 2,418	$ 2,175	$ 1,896
Shareholders equity	$ 6,542	$ 5,928	$ 6,244	$ 5,849	$ 5,276

(1) On August 31, 2009, we separated the clinical and medical products businesses from our other businesses through a pro rata distribution to shareholders of 81 percent of the then outstanding common stock of CareFusion and met the criteria for classification of these businesses as discontinued operations. During the fourth quarter of fiscal 2009, we committed to plans to sell our United Kingdom-based Martindale injectable manufacturing business within our Pharmaceutical segment, and met the criteria for classification of this business as discontinued operations. For additional information regarding discontinued operations, see Note 5 of the Notes to Consolidated Financial Statements in the 2012 Form 10-K.

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RISK FACTORS

Investing in our notes involves various risks. There are a number of factors, including those described below and in our Annual Report on Form 10-K for the fiscal year ended June 30, 2012, as they may be amended, updated or modified periodically in our reports filed with the SEC, that could materially and adversely affect our results of operations, financial condition, liquidity and cash flows. You should carefully consider the risks and uncertainties described below and the other information in this prospectus supplement and the accompanying prospectus and in the documents incorporated by reference before deciding whether to purchase Cardinal Health s notes. These risks are not the only risks that we face. Our business operations could also be affected by additional factors that are not presently known to us or that we currently consider to be immaterial to our operations.

Risks Related to our Business

You should carefully review all the information under the heading Risk Factors in our Annual Report on Form 10-K for the fiscal year ended June 30, 2012 in addition to those set forth below.

We have a few large customers that generate a significant amount of our revenue. Contracts with our two largest customers will expire in June 2013 and August 2013 and if either contract is not renewed, the expiration of that contract could materially adversely affect our business.

Our sales and credit concentration is significant. CVS and Walgreens accounted for approximately 22 percent and 21 percent, respectively, of our fiscal 2012 revenue. In addition, CVS and Walgreens accounted for 19 percent and 25 percent, respectively, of our gross trade receivable balance at June 30, 2012. Our contracts with CVS and Walgreens are scheduled to expire in June 2013 and August 2013, respectively. Walgreens and CVS issued requests for proposal for pharmaceutical distribution services during August 2012 and December 2012, respectively, and we are participating in these processes. The expiration of either of these contracts will have an adverse effect, which could be material, on our results of operations and operating cash flow. In addition, if CVS or Walgreens defaults in payment or significantly reduces its purchases of our products, our results of operations and financial condition could be materially adversely affected.

The Acquisition may not provide us with the benefits we expect and may expose us to unforeseen risks. The Acquisition will lead to significant expense related to amortization of intangible assets.

An important element of our growth strategy has been to acquire other businesses that expand or complement our existing businesses, such as the planned acquisition of AssuraMed. Acquisitions involve risks: we may overpay for a business or fail to realize the synergies and other benefits we expect from the acquisition; or we may encounter unforeseen accounting, internal control, regulatory or compliance issues.

In addition, for financial accounting purposes, we amortize intangible assets with definitive lives, such as customer relationships, trademarks and patents and non-compete agreements, over their useful lives. We have not made a preliminary valuation of intangible assets relating to AssuraMed, but we expect intangible assets to be a significant portion of the AssuraMed purchase price. As a result, we expect the amortization of acquisition-related intangible assets to be a significant expense in the portion of fiscal 2013 after the Acquisition closes and in future fiscal years.

Risks Related to the Offering

The notes will be effectively subordinated to all existing and future liabilities of Cardinal Health s subsidiaries.

Cardinal Health conducts nearly all of its operations through subsidiaries and it expects that it will continue to do so. As a result, the right of Cardinal Health to participate as a shareholder in any distribution of assets of any subsidiary upon such subsidiary s liquidation or reorganization or otherwise and the ability of holders of the notes to benefit as creditors of Cardinal Health from any such distribution are subject to the prior claims of creditors of the subsidiary. As of December 31, 2012, Cardinal Health had outstanding approximately $2,898 million of indebtedness and guarantees of subsidiary indebtedness for borrowed money with which the notes would rank equally. As of such date, Cardinal Health s subsidiaries had outstanding approximately $355 million of indebtedness for borrowed money ($184 million of which is guaranteed by Cardinal Health) and Cardinal Health s subsidiaries had an aggregate of approximately $11.8 billion of trade payables to which the notes would be effectively subordinated.

Cardinal Health currently has no secured debt. To the extent Cardinal Health were to incur any secured debt, the notes would effectively rank junior in right of payment to such secured debt of Cardinal Health to the extent of the value of the assets securing such debt.

Active trading markets for the notes may not develop.

The notes are new issues of securities with no established trading market. We do not intend to apply for listing of the notes on any securities exchange or for inclusion of the notes on any automated dealer quotation system. If no active trading markets develop, you may not be able to resell your notes at their fair market value or at all. Future trading prices of the notes will depend on many factors, including, among other things, prevailing interest rates, our financial condition and the markets for similar securities. We have been informed by the underwriters that they currently intend to make a market in the notes of each series after this offering is completed. However, the underwriters may cease their market-making at any time at their discretion without notice.

We may not be able to repurchase the notes upon a change of control.

Upon the occurrence of a change of control repurchase event, we will be required to offer to repurchase all outstanding notes at 101% of the aggregate principal amount plus accrued and unpaid interest, if any, to the date of repurchase. However, it is possible that we will not have sufficient funds at the time of the change of control (as defined herein) to make the required repurchase of notes or that restrictions in our then existing debt instruments will not allow such repurchases. See Description of the Notes Repurchase at the Option of Holders Upon a Change of Control.

In the event that we do not consummate the Acquisition on or prior to October 31, 2013 or the Merger Agreement is terminated at any time prior to such date, we will be required to redeem all of the notes on a special mandatory redemption date at a redemption price equal to 101% of the aggregate principal amount of the notes, and, as a result, holders of the notes may not obtain their expected return on the notes.

We may not consummate the Acquisition within the timeframe specified under Description of the Notes Special Mandatory Redemption, or the Merger Agreement may be terminated prior to such time. Our ability to consummate the Acquisition is subject to various closing conditions, including regulatory approvals and other matters over which we have limited or no control. If we fail to consummate the Acquisition on or prior to October 31, 2013 or the Merger Agreement is terminated prior to such time, we will be required to redeem all of the notes at a redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding, the date of redemption. If we redeem the notes pursuant to the special mandatory redemption, you may not obtain your expected return on the notes. Your decision to invest in the notes is made at the time of the offering of the notes. You will have no rights under the special mandatory redemption provision if the Acquisition closes within the specified timeframe, nor will you have any right to require us to redeem your notes if, between the closing of the notes offering and the closing of the Acquisition, we experience any changes in our business or financial condition or if the terms of the Acquisition change.

We may be unable to redeem the notes in the event of a special mandatory redemption.

If we do not consummate the Acquisition on or before October 31, 2013, or the Merger Agreement is terminated any time prior to such date, we will be required to redeem all of the notes for a redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding, the date of redemption. See Description of the Notes Special Mandatory Redemption. We are not obligated to place the proceeds from the sale of the notes in escrow prior to consummation of the Acquisition or to provide a security interest in those proceeds, and there are no restrictions on our use of those proceeds during such time. Accordingly, we will need to fund any special mandatory redemption using cash on hand, proceeds of this offering that we have voluntarily retained or from other sources of liquidity. In the event of a special mandatory redemption, we may not have sufficient funds to redeem any or all of the notes.

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CAPITALIZATION

The following table sets forth our short-term obligations and capitalization at December 31, 2012 (1) on an actual basis, and (2) as adjusted to reflect the issuance and sale of the notes offered hereby. You should read this table together with our audited financial statements incorporated by reference in this prospectus supplement and the accompanying prospectus. See Where You Can Find More Information and Incorporation of Certain Documents by Reference in this prospectus supplement.

	As of December 31, 2012	
	Actual	**As Adjusted**
	(unaudited, in millions)	
Short-term obligations:		
Current portion of long-term obligations and other short-term borrowings	$ 474	$ 474
Long-term obligations:		
1.700% Notes due 2018 offered hereby		400
3.200% Notes due 2023 offered hereby		550
4.600% Notes due 2043 offered hereby		350
1.900% Notes due 2017	250	250
3.200% Notes due 2022	251	251
4.00% Notes due 2015	531	531
4.625% Notes due 2020	540	540
5.80% Notes due 2016	304	304
5.85% Notes due 2017	161	161
6.00% Notes due 2017	204	204
7.00% Debentures due 2026	124	124
7.80% Debentures due 2016	37	37
Other long-term obligations, including capital leases (1)	21	21
Total long-term obligations	$ 2,423	$ 3,723
Shareholders equity:		
Preferred Shares, without par value; Authorized 500 thousand shares; Issued none	$	$
Common Shares, without par value; Authorized 755 million shares; Issued 364 million shares	2,929	2,929
Retained earnings	4,491	4,491
Common Shares in treasury, at cost 23 million shares	(952)	(952)
Accumulated other comprehensive income	74	74
Total shareholders equity	$ 6,542	$ 6,542
Total capitalization	$ 9,439	$ 10,739

(1) In connection with the Acquisition, we obtained a commitment letter for a new $1.3 billion senior unsecured bridge term loan facility. The aggregate commitments in respect of this facility will be permanently reduced dollar-for-dollar by the net proceeds from this offering.

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USE OF PROCEEDS

We estimate that the net proceeds from the sale of the notes, after deducting the underwriting discount and estimated unreimbursed expenses, will be approximately $1.29 billion. We plan to use the net proceeds from the offering and cash on hand to consummate the Acquisition. Under the Merger Agreement, we will pay an aggregate consideration of approximately $2.07 billion in cash to acquire AssuraMed, on a cash-free, debt-free basis subject to working capital and other adjustments. In connection with the Acquisition, we obtained a commitment letter for a new $1.3 billion senior unsecured bridge term loan facility. The aggregate commitments under the commitment letter will be permanently reduced dollar-for-dollar by the net proceeds from this offering. In addition, any proceeds from borrowings under the $1.3 billion senior unsecured bridge term loan facility may only be used to consummate the Acquisition and pay for certain related expenses.

The offering is not conditioned upon the consummation of the Acquisition but, in the event that we do not consummate the Acquisition on or prior to October 31, 2013 or the Merger Agreement is terminated at any time prior to such date, we will be required to redeem all of the notes on a special mandatory redemption date at a redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding, the date of redemption. See Description of the Notes Special Mandatory Redemption. There can be no assurance that the Acquisition will be consummated or that we will be able to fund the special mandatory redemption, if it is applicable.

We will temporarily invest the net proceeds from the sale of the notes in short-term, liquid investments until they are used for their stated purpose.

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DESCRIPTION OF THE NOTES

The following information concerning the notes supplements, and should be read in conjunction with, the statements under Description of Debt Securities in the accompanying prospectus. Terms not defined herein are used as defined in the indenture referred to below. You should also read the entire indenture and the notes before you make any investment decision because they and not this description, define your rights as a holder of the notes.

The 2018 notes, the 2023 notes and the 2043 notes will be issued as separate series of senior unsecured debt securities under an indenture dated as of June 2, 2008 (the indenture) between Cardinal Health and The Bank of New York Mellon Trust Company, N.A., as trustee (the trustee). The indenture provides that the debt securities may be issued from time to time in one or more series with different terms. The indenture does not limit the aggregate amount of debt securities that may be issued or any other debt that may be incurred by Cardinal Health. A default in our obligations with respect to any other indebtedness will not constitute a default or an event of default with respect to the debt securities. The indenture does not contain any covenants or provisions that afford holders of debt securities protection in the event of a highly leveraged transaction. Reference is made to the accompanying prospectus for a description of other terms of the debt securities. The indenture and the notes are governed by New York law.

The 2018 notes will be limited initially to $400 million aggregate principal amount, the 2023 notes will be limited initially to $550 million aggregate principal amount and the 2043 notes will be limited initially to $350 million aggregate principal amount. The 2018 notes will mature on March 15, 2018, the 2023 notes will mature on March 15, 2023 and the 2043 notes will mature on March 15, 2043. Interest on the notes will accrue from February 22, 2013, and will be payable semi-annually on March 15 and September 15, commencing September 15, 2013, to the persons in whose names the notes are registered at the close of business on March 1 or September 1 prior to the payment date at the annual rate for each series set forth on the cover page of this prospectus supplement.

We may, at any time, without notice to or the consent of the holders of the notes, create and issue additional notes having the same ranking and the same interest rate, maturity and other terms as the notes of each series (other than the date of issuance, price to public, and, under certain circumstances, the first interest payment date following the issue date of such additional notes). Any such additional notes, together with the notes of the applicable series offered by this prospectus supplement, will each form a single series of the notes under the indenture.

Cardinal Health may from time to time issue other series of debt securities under the indenture consisting of notes or other unsecured evidences of indebtedness, but, unless otherwise indicated, such other series will be separate from and independent of the notes.

The notes will not be entitled to the benefit of any sinking fund.

The notes of each series will initially be represented by one or more global notes (each, a global note), in registered form, without coupons, in denominations of $2,000 or an integral multiple of $1,000 in excess thereof as described under Book-Entry System.

There is no public trading market for the notes, and we do not intend to apply for listing of the notes on a securities exchange or for inclusion of the notes on an automated quotation system.

Ranking of Notes

The notes will be senior unsecured obligations of Cardinal Health and will rank equally in right of payment with all of Cardinal Health s existing and future senior unsecured indebtedness. The notes will also effectively rank junior in right of payment to any secured debt of Cardinal Health to the extent of the value of the assets securing such indebtedness.

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Cardinal Health conducts nearly all of its operations through subsidiaries and it expects that it will continue to do so. As a result, the right of Cardinal Health to participate as a shareholder in any distribution of assets of any subsidiary upon its liquidation or reorganization or otherwise and the ability of holders of the notes to benefit as creditors of Cardinal Health from any distribution are subject to the prior claims of creditors of the subsidiary. As of December 31, 2012, Cardinal Health had outstanding approximately $2,898 million of indebtedness and guarantees of subsidiary indebtedness for borrowed money with which the notes would rank equally. As of such date, Cardinal Health s subsidiaries had outstanding approximately $355 million of indebtedness for borrowed money ($184 million of which is guaranteed by Cardinal Health) and Cardinal Health s subsidiaries had an aggregate of approximately $11.8 billion of trade payables to which the notes would be effectively subordinated.

Cardinal Health currently has no secured debt. To the extent Cardinal Health were to incur any secured debt, the notes would effectively rank junior in right of payment to such secured debt of Cardinal Health to the extent of the value of the assets securing such debt.

Optional Redemption

The notes of each series will be redeemable, in whole at any time or, in part from time to time, at the option of Cardinal Health, at a redemption price equal to the greater of:

(1) 100% of the principal amount of the notes to be redeemed, or

(2) as determined by a quotation agent, the sum of the present values of the remaining scheduled payments of principal and interest thereon (exclusive of interest accrued to the date of redemption) discounted to the date of redemption on a semi-annual basis (assuming a 360-day year consisting of twelve 30-day months) at the adjusted treasury rate plus 15 basis points for the 2018 notes, 20 basis points for the 2023 notes and 25 basis points for the 2043 notes, *plus*, in each case, accrued and unpaid interest, if any, on the amount being redeemed to, but excluding, the date of redemption.

Adjusted treasury rate means, with respect to any redemption date, the rate per year equal to the semi-annual equivalent yield to maturity of the comparable treasury issue, assuming a price for the comparable treasury issue (expressed as a percentage of its principal amount) equal to the comparable treasury price for such redemption date.

Comparable treasury issue means the United States Treasury security selected by a quotation agent as having a maturity comparable to the remaining term of the notes to be redeemed that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining terms of such notes.

Comparable treasury price means, with respect to any redemption date,

(1) the average of three reference treasury dealer quotations for such redemption date, after excluding the highest and lowest such reference treasury dealer quotations, or

(2) if the trustee obtains fewer than three such reference treasury dealer quotations, the average of all such quotations.

Quotation agent means the reference treasury dealer appointed by Cardinal Health.

Reference treasury dealer means,

(1) Merrill Lynch, Pierce, Fenner & Smith Incorporated, Deutsche Bank Securities Inc. and UBS Securities LLC and their respective successors; provided, however, that if any of the foregoing shall cease to be a primary U.S. Government securities dealer in the United States (a primary treasury dealer), Cardinal Health shall substitute therefor another primary treasury dealer, and

(2) any other primary treasury dealer selected by Cardinal Health.

Reference treasury dealer quotation means, with respect to each reference treasury dealer and any redemption date, the average, as determined by Cardinal Health, of the bid and asked prices for the comparable treasury issue (expressed in each case as a percentage of its principal amount) quoted in writing to the trustee by such reference treasury dealer at 5:00 p.m., New York City time on the third business day preceding such redemption date.

Notice to holders of notes to be redeemed will be delivered by first-class mail at least 30 and not more than 60 days prior to the date fixed for redemption. Unless Cardinal Health defaults in payment of the redemption price, on and after the redemption date interest will cease to accrue on the notes or portions thereof called for redemption.

Special Mandatory Redemption

If we do not consummate the Acquisition on or prior to October 31, 2013, or the Merger Agreement is terminated any time prior to such date, we will be required to redeem all of the outstanding notes on a special mandatory redemption date at a redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest, if any, to, but excluding, the special mandatory redemption date. The *special mandatory redemption date* means the earlier to occur of (1) December 31, 2013, if the Acquisition has not been consummated on or prior to October 31, 2013, or (2) the 60th day (or if such day is not a business day, the first business day thereafter) following the termination of the Merger Agreement for any reason. Notwithstanding the foregoing, installments of interest on any series of notes that are due and payable on interest payment dates falling on or prior to the special mandatory redemption date will be payable on such interest payment dates to the registered holders as of the close of business on the relevant record dates in accordance with the notes and the indenture.

We will cause the notice of special mandatory redemption to be mailed, with a copy to the trustee, within five business days after the occurrence of the event triggering the special mandatory redemption to each holder at its registered address. If funds sufficient to pay the special mandatory redemption price of the notes to be redeemed on the special mandatory redemption date are deposited with the trustee or a paying agent on or before such special mandatory redemption date, and certain other conditions are satisfied, on and after such special mandatory redemption date, the notes will cease to bear interest.

Repurchase at the Option of Holders Upon a Change of Control

If a change of control repurchase event occurs, unless we have exercised our right to redeem the notes in full as described above, we will make an offer to each holder of notes to repurchase all or any part (equal to $2,000 or in integral multiples of $1,000 in excess thereof) of that holder s notes at a repurchase price in cash equal to 101% of the aggregate principal amount of notes repurchased plus accrued and unpaid interest, if any, on the notes repurchased to, but excluding, the date of purchase. Within 30 days following any change of control repurchase event or, at our option, prior to any change of control, but after the public announcement of the change of control, we will mail a notice to each holder, with a copy to the trustee, describing the transaction or transactions that constitute or may constitute the change of control repurchase event and offering to repurchase notes on the payment date specified in the notice, which date will be no earlier than 30 days and no later than 60 days from the date such notice is mailed. The notice shall, if mailed prior to the date of consummation of the change of control, state that the offer to purchase is conditioned on the change of control repurchase event occurring on or prior to the payment date specified in the notice. We will comply with the requirements of Rule 14e-1 under the Exchange Act and any other securities laws and regulations under the Exchange Act to the extent those laws and regulations are applicable in connection with the repurchase of the notes as a result of a change of control repurchase event. To the extent that the provisions of any securities laws or regulations conflict with the change of control repurchase event provisions of the notes, we will comply with the applicable securities laws and regulations and will not be deemed to have breached our obligations under the change of control repurchase event provisions of the notes by virtue of such conflict.

On the change of control repurchase event payment date, we will, to the extent lawful:

- accept for payment all notes or portions of notes properly tendered pursuant to our offer;
- deposit with the paying agent an amount equal to the aggregate purchase price in respect of all notes or portions of notes properly tendered; and
- deliver or cause to be delivered to the trustee the notes properly accepted, together with an officers certificate stating the aggregate principal amount of notes being purchased by us.

The paying agent will promptly mail to each holder of notes properly tendered the purchase price for the notes, and the trustee will promptly authenticate and mail (or cause to be transferred by book-entry) to each holder a new note equal in principal amount to any unpurchased portion of any notes surrendered; provided that each new note will be in a principal amount of $2,000 or an integral multiple of $1,000 in excess thereof.

We will not be required to make an offer to repurchase the notes upon a change of control repurchase event if a third party makes such an offer in the manner, at the times and otherwise in compliance with the requirements for an offer made by us and such third party purchases all notes properly tendered and not withdrawn under its offer.

The term below investment grade rating event means the notes are rated below investment grade (defined below) by each of the rating agencies (defined below) on any date from the date of the public notice of an arrangement that could result in a change of control until the end of the 60-day period following public notice of the occurrence of a change of control (which period shall be extended so long as the rating of the notes is under publicly announced consideration for possible downgrade by any of the rating agencies).

The term change of control means the occurrence of any one of the following: (1) the direct or indirect sale, lease, transfer, conveyance or other disposition (other than by way of merger or consolidation), in one or a series of related transactions, of all or substantially all of our assets taken as a whole to any person (as that term is used in Section 13(d)(3) of the Exchange Act) other than to Cardinal Health or one of its subsidiaries; (2) the consummation of any transaction (including, without limitation, any merger or consolidation) the result of which is that any person (as that term is used in Section 13(d)(3) of the Exchange Act) becomes the beneficial owner, directly or indirectly, of more than 50% of Cardinal Health s voting stock (defined below), measured by voting power rather than number of shares; or (3) the first day on which a majority of the members of Cardinal Health s board of directors cease to be continuing directors. Notwithstanding the foregoing, a transaction will not be deemed to involve a change of control if (i) Cardinal Health becomes a wholly owned subsidiary of a holding company and (ii) the holders of the voting stock of such holding company immediately following that transaction are substantially the same as the holders of Cardinal Health s voting stock immediately prior to that transaction.

The definition of change of control includes a phrase relating to the direct or indirect sale, lease, transfer, conveyance or other disposition of all or substantially all of the properties or assets of Cardinal Health and its subsidiaries taken as a whole. Although there is a limited body of case law interpreting the phrase substantially all, there is no precise established definition of the phrase under applicable law. Accordingly, the applicability of the requirement that we offer to repurchase the notes as a result of a sale, lease, transfer, conveyance or other disposition of less than all of the assets of Cardinal Health and its subsidiaries taken as a whole to another person or group may be uncertain.

The term change of control repurchase event means the occurrence of both a change of control and a below investment grade rating event.

The term continuing director means, as of any date of determination, members of our board of directors who (1) were members of such board of directors on the date of the issuance of the notes; or (2) were

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nominated for election, elected or appointed to such board of directors with the approval of a majority of the continuing directors who were members of such board of directors at the time of such nomination, election or appointment.

Under clause (3) of the definition of change of control, a change of control will occur when a majority of the members of Cardinal Health s board of directors cease to be continuing directors. In 2009, the Delaware Court of Chancery held that the occurrence of a change of control under a similar indenture provision may nevertheless be avoided if the existing directors were to approve the slate of new director nominees, provided the incumbent directors gave their approval in the good faith exercise of their fiduciary duties owed to the corporation and its stockholders. It has not been determined under Ohio law whether Cardinal Health s board of directors could similarly approve a slate of dissident director nominees while recommending and endorsing its own slate. If so, in certain circumstances involving a significant change in the composition of Cardinal Health s board of directors, including in connection with a proxy contest where Cardinal Health s board of directors does not endorse a dissident slate of directors but approves the dissident slate as continuing directors, holders of the notes may not be entitled to require Cardinal Health to repurchase the notes.

The term Fitch, Moody s and S&P mean Fitch Ratings, Moody s Investors Service, Inc. and Standard & Poor s Ratings Services, a division of T McGraw-Hill Companies, Inc., respectively.

The term investment grade means a rating of BBB or better by Fitch (or its equivalent under any successor rating categories of Fitch), Baa3 or better by Moody s (or its equivalent under any successor rating categories of Moody s); a rating of BBB or better by S&P (or its equivalent under any successor rating categories of S&P); or the equivalent investment grade credit rating from any additional rating agency (defined below) or rating agencies selected by us.

The term rating agency means (1) each of Fitch, Moody s and S&P; and (2) if any of Fitch, Moody s or S&P ceases to rate the notes or fails to make a rating of the notes publicly available for reasons outside of our control, a nationally recognized statistical rating organization within the meaning of Rule 15c3-1(c)(2)(vi)(F) under the Exchange Act, selected by Cardinal Health as a replacement agency for Fitch, Moody s or S&P, or all of them, as the case may be.

The term voting stock of any specified person (as that term is used in Section 13(d)(3) of the Exchange Act) as of any date means the capital stock of such person that is at the time entitled to vote generally in the election of the board of directors of such person.

Unless we default in the change of control payment, on and after the change of control payment date, interest will cease to accrue on the notes or portions of the notes tendered for repurchase pursuant to the change of control offer.

Certain Covenants

The indenture contains certain covenants for the benefit of the holders of notes which limit our ability to incur liens, to incur certain subsidiary debt and to enter into certain sale and lease-back, merger, and sale of assets transactions. See Description of Debt Securities Certain Covenants in the accompanying prospectus.

Events of Default

The indenture contains certain events of default. See Description of Debt Securities Events of Default in the accompanying prospectus.

Regarding the Trustee

The Bank of New York Mellon Trust Company, N.A., as trustee under the indenture, has been appointed by us as paying agent, registrar and DTC custodian with regard to the notes. The trustee or its affiliates may from time to time in the future provide banking and other services to us in the ordinary course of their business.

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Book-Entry System

The notes of each series will be issued initially in the form of one or more global notes, in the aggregate principal amount of the issue, that will be deposited with, or on behalf of, The Depository Trust Company (DTC), which will act as securities depository for the notes. The notes will be issued as fully-registered securities registered in the name of Cede & Co. (DTC s partnership nominee) or such other name as may be requested by an authorized representative of DTC. DTC and any other depository which may replace DTC as depository for the notes are sometimes referred to herein as the depository. Except under the limited circumstances described below, notes represented by global notes will not be exchangeable for certificated notes.

So long as the depository, or its nominee, is the registered owner of a global note, such depository or such nominee, as the case may be, will be considered the sole registered holder of the individual notes represented by such global note for all purposes under the indenture. Payments of principal of and premium, if any, and any interest on individual notes represented by a global note will be made to the depository or its nominee, as the case may be, as the registered holder of such global note. Except as set forth below, owners of beneficial interests in a global note will not be entitled to have any of the individual notes represented by such global note registered in their names, will not receive or be entitled to receive physical delivery of any such note and will not be considered the registered holder thereof under the indenture, including, without limitation, for purposes of consenting to any amendment thereof or supplement thereto as described in the accompanying prospectus.

Beneficial interests in the global notes will be represented through book-entry accounts of financial institutions acting on behalf of beneficial owners as direct and indirect participants in DTC. Investors may hold interests in the global notes through either DTC (in the United States), Clearstream Banking, société anonyme, Luxembourg (Clearstream), or Euroclear Bank S.A./N.V., as operator of the Euroclear System (Euroclear), in Europe, either directly if they are participants in such systems or indirectly through organizations that are participants in such systems. Clearstream and Euroclear will hold interests on behalf of their participants through customers securities accounts in Clearstream s and Euroclear s names on the books of their United States depositaries, which in turn will hold such interests in customers securities accounts in the United States depositaries names on the books of DTC.

The following is based on information furnished by DTC:

DTC is a limited-purpose trust company organized under the New York Banking Law, a banking organization within the meaning of the New York Banking Law, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code, and a clearing agency registered pursuant to the provisions of Section 17A of the Exchange Act. DTC was created to hold securities of its participants and to facilitate the clearance and settlement of securities transactions among its participants in such securities through electronic book-entry changes in accounts of the participants, thereby eliminating the need for physical movement of securities certificates. Direct participants include securities brokers and dealers (including the underwriters), banks, trust companies, clearing corporations, and certain other organizations (Direct Participants). DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (DTCC). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to DTC s book-entry system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (Indirect Participants). The rules applicable to DTC and its Direct and Indirect Participants are on file with the SEC.

Purchases of notes under the DTC system must be made by or through Direct Participants, which will receive a credit for the notes on DTC s records. The ownership interest of each actual purchaser of each note (Beneficial Owner) is in turn to be recorded on the Direct and Indirect Participants records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are, however, expected

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to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the notes are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in notes, except in the event that use of the book-entry system for the notes is discontinued.

To facilitate subsequent transfers, all global notes deposited by Direct Participants with DTC are registered in the name of DTC s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of global notes with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the notes; DTC s records reflect only the identity of the Direct Participants to whose accounts such notes are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

The laws of some jurisdictions may require that purchasers of securities take physical delivery of those securities in definitive form. Accordingly, the ability to transfer interests in the notes represented by a global note to those persons may be limited. In addition, because DTC can act only on behalf of its participants, who in turn act on behalf of persons who hold interests through participants, the ability of a person having an interest in notes represented by a global note to pledge or transfer those interests to persons or entities that do not participate in DTC s system, or otherwise to take actions in respect of such interest, may be affected by the lack of a physical definitive security in respect of such interest.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the notes unless authorized by a Direct Participant in accordance with DTC s procedures. Under its usual procedures, DTC mails an Omnibus Proxy to Cardinal Health as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co. s consenting or voting rights to those Direct Participants to whose accounts the notes are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, interest payments and redemption proceeds on the notes will be made to Cede & Co., or such other nominee, as may be requested by an authorized representative of DTC. DTC s practice is to credit Direct Participants accounts upon DTC s receipt of funds and corresponding detail information from us or the trustee, on the payment date in accordance with their respective holdings shown on DTC s records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in street name and will be the responsibility of such Participant and not of DTC nor its nominee, any Agents, the trustee or Cardinal Health, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, interest and redemption proceeds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of Cardinal Health or the trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

None of Cardinal Health, the underwriters or the trustee will have any responsibility or liability for any aspect of the records relating to or payments made on account of notes by DTC, Clearstream or Euroclear, or for maintaining, supervising or reviewing any records of those organizations relating to the notes.

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DTC may discontinue providing its services as depository with respect to the notes at any time by giving reasonable notice to Cardinal Health or the trustee. Under such circumstances, in the event that a successor depository is not obtained, certificated notes are required to be printed and delivered in exchange for the notes represented by the global notes held by DTC.

In addition, Cardinal Health may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depositary). In that event, certificated notes will be printed and delivered in exchange for the notes represented by the global notes held by DTC.

Distributions on the notes held beneficially through Clearstream will be credited to cash accounts of its customers in accordance with its rules and procedures, to the extent received by the United States depositary for Clearstream.

Securities clearance accounts and cash accounts with the Euroclear Operator are governed by the Terms and Conditions Governing Use of Euroclear and the related Operating Procedures of the Euroclear System, and applicable Belgian law (collectively, the *Terms and Conditions*). The Terms and Conditions govern transfers of securities and cash within Euroclear, withdrawals of securities and cash from Euroclear, and receipts of payments with respect to securities in Euroclear. All securities in Euroclear are held on a fungible basis without attribution of specific certificates to specific securities clearance accounts. The Euroclear Operator acts under the Terms and Conditions only on behalf of Euroclear participants and has no record of or relationship with persons holding through Euroclear participants.

Distributions on the notes held beneficially through Euroclear will be credited to the cash accounts of its participants in accordance with the Terms and Conditions, to the extent received by the United States depositary for Euroclear.

Same-Day Settlement and Payment

Settlement for the notes will be made by the underwriters in immediately available funds. All payments of principal and interest will be made by us in immediately available funds.

Secondary trading in long-term notes of corporate issuers is generally settled in clearing-house or next-day funds. In contrast, the notes will trade in the Same-Day Funds Settlement System maintained by DTC until maturity, and secondary market trading activity in the notes will therefore be required by DTC to settle in immediately available funds. No assurance can be given as to the effect, if any, of settlement in immediately available funds on trading activity in the notes.

Cross-market transfers between persons holding directly or indirectly through DTC, on the one hand, and directly or indirectly through Clearstream customers or Euroclear participants, on the other, will be effected through DTC in accordance with DTC rules on behalf of the relevant European international clearing system by the United States depositary. Such cross-market transactions, however, will require delivery of instructions to the relevant European international clearing system by the counterparty in such system in accordance with its rules and procedures and within its established deadlines (European time). The relevant European international clearing system will, if the transaction meets its settlement requirements, deliver instructions to the United States depositary to take action to effect final settlement on its behalf by delivering or receiving the notes in DTC, and making or receiving payment in accordance with normal procedures for same-day funds settlement applicable to DTC. Clearstream customers and Euroclear participants may not deliver instructions directly to their United States depositaries.

Because of time-zone differences, credits of notes received in Clearstream or Euroclear, as a result of a transaction with a DTC participant will be made during subsequent securities settlement processing and dated the Business Day following the DTC settlement date. Such credits or any transactions in such notes settled during such processing will be reported to the relevant Clearstream or Euroclear participants on such Business Day. Cash received in Clearstream or Euroclear as a result of sales of notes by or through a Clearstream participant or a Euroclear participant to a DTC participant will be received with value on the DTC settlement date but will be available in the relevant Clearstream or Euroclear cash account only as of the Business Day following settlement in DTC.

Although DTC, Clearstream and Euroclear have agreed to the foregoing procedures in order to facilitate transfers of notes among participants of DTC, Clearstream and Euroclear, they are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time.

The information in this section concerning DTC and DTC s book-entry system has been obtained from sources that Cardinal Health believes to be reliable, but Cardinal Health takes no responsibility for the accuracy thereof.

Cardinal Health has provided the descriptions of the operations and procedures of DTC, Clearstream and Euroclear in this prospectus supplement solely as a matter of convenience, and Cardinal Health makes no representation or warranty of any kind with respect to these operations and procedures. These operations and procedures are solely within the control of those organizations and are subject to change by them from time to time. None of Cardinal Health, the underwriters, the trustee, any paying agent or the registrar for the notes will have any responsibility or liability for any aspect of the records relating to or payments made on account of beneficial ownership interests in a global note or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

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MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES

The following discussion summarizes certain U.S. federal income tax considerations that may be relevant to the acquisition, ownership and disposition of the notes. This discussion is based upon the provisions of the Internal Revenue Code of 1986, as amended (the Code), applicable Treasury regulations promulgated thereunder, judicial authority and administrative interpretations, in each case as of the date hereof, all of which are subject to change, possibly with retroactive effect, or are subject to different interpretations.

This discussion does not address all tax considerations that may be relevant to a holder in light of the holder s particular circumstances, or to certain categories of investors that may be subject to special rules, such as banks or other financial institutions, insurance companies, regulated investment companies, tax-exempt organizations, dealers in securities or currencies, U.S. Holders (as defined below) whose functional currency is not the U.S. dollar, partnerships or other pass-through entities for U.S. federal income tax purposes, former U.S. citizens or residents of the United States, or persons who hold the notes as part of a hedge, conversion transaction, straddle or other risk-reduction transaction. This summary does not consider any tax consequences arising under U.S. federal gift, estate or alternative minimum tax law or under the laws of any foreign, state, local or other jurisdiction. Except as otherwise provided, this discussion is limited to initial investors who purchased the notes for cash at the initial issue price (i.e., the initial offering price to the public, excluding bond houses and brokers, at which price a substantial amount of such notes were sold) and hold the notes as capital assets (generally, property held for investment purposes).

If a partnership (or an entity treated as a partnership for U.S. federal income tax purposes) acquires the notes, the U.S. federal income tax consequences of an investment in the notes will depend on the status of the partners and the activities of the partnership. Partnerships that invest in the notes (and partners of such partnerships) are urged to consult their independent tax advisors regarding the U.S. federal income tax consequences of investing in the notes through a partnership.

This summary is intended for general information purposes only. Potential investors are urged to consult their independent tax advisors regarding the U.S., state, local and non-U.S. tax consequences of the acquisition, ownership and disposition of the notes.

Treatment of the notes

In certain circumstances (see Description of the Notes Special Mandatory Redemption and Description of the Notes Repurchase at the Option of Holders Upon a Change of Control), we may be obligated to pay amounts in excess of stated interest or principal on the notes. These contingencies could subject the notes to the provisions of the Treasury regulations relating to contingent payment debt instruments. Under these regulations, however, one or more contingencies will not cause a debt instrument to be treated as a contingent payment debt instrument if, as of the issue date, each such contingency is remote or is considered to be incidental. We believe and intend to take the position that the foregoing contingencies should be treated as remote and/or incidental. Our position is binding on a holder, unless the holder discloses in the proper manner to the Internal Revenue Service (IRS) that it is taking a different position. However, this determination is inherently factual and we can give no assurance that our position would be sustained if challenged by the IRS. A successful challenge of this position by the IRS could affect the timing and amount of a holder s income and could cause the gain from the sale or other disposition of a note to be treated as ordinary income, rather than capital gain. The remainder of this discussion assumes that the notes will not be considered contingent payment debt instruments for U.S. federal income tax purposes.

Consequences to U.S. Holders

A U.S. Holder for purposes of this discussion is a beneficial owner of a note which, for U.S. federal income tax purposes, is:

- a U.S. citizen or U.S. resident alien;

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- a corporation, or other entity taxable as a corporation for U.S. federal income tax purposes, organized under the laws of the United States, any state thereof or the District of Columbia;

- an estate whose income is subject to U.S. federal income taxation regardless of its source; or

- a trust (i) if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust or (ii) that has a valid election in effect under applicable Treasury regulations to be treated as a U.S. person.

Interest on the notes

Interest on notes generally will be taxable to a U.S. Holder as ordinary interest income at the time it accrues or is received, in accordance with the U.S. Holder s regular method of accounting for U.S. federal income tax purposes.

Disposition of the notes

A U.S. Holder generally will recognize capital gain or loss on the sale, exchange, redemption, retirement or other taxable disposition of a note. This gain or loss will equal the difference between the amount realized by the U.S. Holder in such sale, exchange, redemption, retirement or other taxable disposition and its adjusted tax basis in the note. The amount realized by a U.S. Holder for such purposes will equal the proceeds (including cash and the fair market value of any property) received for the note, less any portion of such proceeds attributable to accrued interest on the note, which will be taxable as ordinary interest income to the extent not previously included in gross income. A U.S. Holder s adjusted tax basis in a note generally will equal the cost of the note. Any gain or loss will be long-term capital gain or loss if at the time of disposition the note has been held for more than one year. Long-term capital gains of non-corporate U.S. Holders (including individuals) currently are eligible for taxation at preferential rates. The deductibility of capital losses is subject to limitation.

Information reporting and backup withholding

Information reporting will apply to payments of interest on or the proceeds of the sale, exchange, redemption, retirement or other taxable disposition of notes held by a U.S. Holder, and backup withholding (currently at a rate of 28%) will apply to such payments unless a U.S. Holder provides its correct taxpayer identification number, certified under penalties of perjury, as well as certain other information, or otherwise establishes an exemption from backup withholding. Certain U.S. Holders (including, among others, corporations and certain tax-exempt organizations) generally are not subject to backup withholding. Backup withholding is not an additional tax. Any amount withheld under the backup withholding rules is allowable as a refund or credit against a U.S. Holder s U.S. federal income tax liability, provided that the required information or appropriate claim form is furnished to the IRS on a timely basis.

Additional Tax on Net Investment Income

Certain U.S. Holders that are individuals, estates and trusts are subject to an additional 3.8% U.S. federal income tax on, among other things, interest and capital gains from the sale or other disposition of the notes if their modified adjusted gross income exceeds certain threshold amounts. U.S. Holders should consult their own tax advisors regarding the effect, if any, of this new tax on their ownership and disposition of the notes.

Consequences to non-U.S. Holders

A non-U.S. Holder is a beneficial owner of notes that is neither a U.S. Holder nor a partnership or other pass through entity for U.S. federal income tax purposes.

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Interest on the notes

Subject to the discussion below under Income or gain effectively connected with a U.S. trade or business, payments of interest on the notes to a non-U.S. Holder generally will be exempt from U.S. federal income tax (and generally no tax will be withheld) under the portfolio interest exemption if such non-U.S. Holder properly certifies as to its foreign status as described below, and:

- such non-U.S. Holder does not own, actually or constructively, 10% or more of the combined voting power of all classes of our stock entitled to vote; and

- such non-U.S. Holder is not a controlled foreign corporation that is related to us, within the meaning of Section 864(d)(4) of the Code.

The portfolio interest exemption and several of the special rules for non-U.S. Holders described below generally apply only if a non-U.S. Holder appropriately certifies as to its foreign status. Generally a non-U.S. Holder can meet this certification requirement by providing a properly executed IRS Form W-8BEN or appropriate substitute form to us or our paying agent certifying under penalty of perjury that such non-U.S. Holder is not a U.S. person as defined in the Code. If a non-U.S. Holder holds the notes through a financial institution or other agent acting on its behalf, such holder may be required to provide appropriate certifications to the agent. Such agent will then generally be required to provide appropriate certifications to us or our paying agent, either directly or through other intermediaries.

If a non-U.S. Holder does not qualify for the portfolio interest exemption and the interest is not effectively connected with the non-U.S. Holder s conduct of a trade or business within the United States (see Income or gain effectively connected with a U.S. trade or business), payments of interest made to such non-U.S. Holder will be subject to U.S. federal withholding tax at a rate of 30% (or lower applicable treaty rate).

Disposition of the notes

A non-U.S. Holder generally will not be subject to U.S. federal income tax (and generally no tax will be withheld) on any gain realized on the sale, redemption, exchange, retirement or other taxable disposition of a note unless:

- the gain is effectively connected with the conduct by such non-U.S. Holder of a U.S. trade or business (and, if an income tax treaty applies, is attributable to a U.S. permanent establishment or fixed base of the non-U.S. Holder); or

- such non-U.S. Holder is an individual who has been present in the United States for 183 days or more in the taxable year of disposition and certain other requirements are met. Such individual non-U.S. Holder will be subject to a flat 30% U.S. federal income tax (or reduced rate under an applicable income tax treaty) on the gain derived from the sale, which may be offset by certain U.S.-source capital losses, even though that non-U.S. Holder is not considered a resident of the United States.

Income or gain effectively connected with a U.S. trade or business

If any interest on the notes or gain from the sale, exchange, redemption, retirement or other taxable disposition of the notes is effectively connected with a U.S. trade or business conducted by a non-U.S. Holder (and, if an income tax treaty applies, is attributable to a U.S. permanent establishment or fixed base of such non-U.S. Holder), then interest or gain will be subject to U.S. federal income tax on a net income basis at regular graduated income tax rates, but will not be subject to withholding tax if certain certification requirements are satisfied. A non-U.S. Holder generally can meet the certification requirements by providing a properly executed

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IRS Form W-8ECI or appropriate substitute form to us, or our paying agent. If a non-U.S. Holder is a corporation, the portion of its earnings and profits that is effectively connected with its U.S. trade or business (and, if an income tax treaty applies, is attributable to a U.S. permanent establishment or fixed base of the non-U.S. Holder) also may be subject to an additional branch profits tax at a 30% rate (or reduced rate under an applicable income tax treaty).

Information reporting and backup withholding

Payments to a non-U.S. Holder of interest on a note, and amounts withheld from such payments, if any, generally will be required to be reported to the IRS and to such non-U.S. Holder. Backup withholding generally will not apply to payments of interest and principal on a note to a non-U.S. Holder if certification, such as an IRS Form W-8BEN described above in Consequences to non-U.S. Holders Interest on the notes, is duly provided by the holder or the holder otherwise establishes an exemption, provided that we do not have actual knowledge or reason to know that the holder is a U.S. person as defined in the Code. Payment of the proceeds of a sale of a note effected by the U.S. office of a U.S. or foreign broker will be subject to information reporting requirements and backup withholding unless a non-U.S. Holder properly certifies under penalties of perjury as to its foreign status and certain other conditions are met or a non-U.S. Holder otherwise establishes an exemption. Information reporting requirements and backup withholding generally will not apply to any payment of the proceeds of the sale of a note effected outside the United States by a foreign office of a broker. However, unless such a broker has documentary evidence in its records that you are a non-U.S. Holder and certain other conditions are met, or you otherwise establish an exemption, information reporting will apply to a payment of the proceeds of the sale of a note effected outside the United States by such a broker if the broker:

- is a U.S. person;
- derives 50% or more of its gross income for certain periods from the conduct of a trade or business in the United States;
- is a controlled foreign corporation for U.S. federal income tax purposes; or
- is a foreign partnership that, at any time during its taxable year, has more than 50% of its income or capital interests owned by U.S. persons or is engaged in the conduct of a U.S. trade or business.

Backup withholding is not an additional tax. Any amount withheld under the backup withholding rules may be refunded or credited against a non-U.S. Holder s U.S. federal income tax liability, provided the proper information is furnished to the IRS on a timely basis.

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UNDERWRITING

Subject to the terms and conditions contained in an underwriting agreement among us and Merrill Lynch, Pierce, Fenner & Smith Incorporated, Deutsche Bank Securities Inc. and UBS Securities LLC, as representatives of the several underwriters, we have agreed to sell to the underwriters, and the underwriters have severally and not jointly agreed to purchase from us, the principal amount of the notes listed opposite their respective names below. The underwriters have agreed to purchase all of the notes sold pursuant to the underwriting agreement if any of these notes are purchased.

Underwriter	Principal Amount of 2018 Notes	Principal Amount of 2023 Notes	Principal Amount of 2043 Notes
Merrill Lynch, Pierce, Fenner & Smith Incorporated	$ 120,000,000	$ 165,000,000	$ 105,000,000
Deutsche Bank Securities Inc.	100,000,000	137,500,000	87,500,000
UBS Securities LLC	100,000,000	137,500,000	87,500,000
Barclays Capital Inc.	16,000,000	22,000,000	14,000,000
HSBC Securities (USA) Inc.	16,000,000	22,000,000	14,000,000
Mitsubishi UFJ Securities (USA), Inc.	16,000,000	22,000,000	14,000,000
Morgan Stanley & Co. LLC	16,000,000	22,000,000	14,000,000
Wells Fargo Securities, LLC	16,000,000	22,000,000	14,000,000
Total	$ 400,000,000	$ 550,000,000	$ 350,000,000

The underwriters are offering the notes, subject to prior sale, when, as and if issued to and accepted by them, subject to approval of legal matters by their counsel, including the validity of the notes, and other conditions contained in the underwriting agreement, such as the receipt by the underwriters of officer s certificates and legal opinions. The underwriters reserve the right to withdraw, cancel or modify offers to the public and to reject orders in whole or in part.

The underwriters have advised us that they propose initially to offer the notes to the public at the public offering prices on the cover page of this prospectus supplement, and may offer the notes to dealers at that price less a concession not in excess of 0.350% of the principal amount of the 2018 notes, 0.350% of the principal amount of the 2023 notes and 0.525% of the principal amount of the 2043 notes. The underwriters may allow, and the dealers may reallow, a discount not in excess of 0.200% of the principal amount of the 2018 notes, 0.250% of the principal amount of the 2023 notes and 0.350% of the principal amount of the 2043 notes to other dealers. After the initial public offering, the public offering price, concession and discount may be changed.

The following table shows the discounts and commissions we will pay to the underwriters in respect to this offering:

Per 2018 Note	0.600%
Per 2023 Note	0.650%
Per 2043 Note	0.875%
Total	$ 9,037,500

The notes are new issues of securities with no established trading markets. We have been advised by the underwriters that the underwriters presently intend to make a market in the notes of each series after completion of the offering. However, the underwriters are under no obligation to do so and may discontinue any market-making activities at any time without notice. We cannot assure the liquidity of the trading market for the notes or that an active public market for the notes will develop. If active public trading markets for the notes do not develop, the market prices and liquidity of the notes may be adversely affected.

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In connection with the offering, the underwriters are permitted to engage in transactions that stabilize the market prices of the notes. Such transactions consist of bids or purchases to peg, fix or maintain the prices of the notes. If the underwriters create a short position in the notes in connection with the offering, i.e., if they sell more notes than are on the cover page of this prospectus supplement, the underwriters may reduce that short position by purchasing notes in the open market. Purchases of a security to stabilize the price or to reduce a short position could cause the price of the security to be higher than it might be in the absence of such purchases.

Neither we nor the underwriters make any representation or prediction as to the direction or magnitude of any effect that the transactions described above may have on the prices of the notes. In addition, neither we nor the underwriters make any representation that the underwriters will engage in these transactions or that these transactions, once commenced, will not be discontinued without notice.

The expenses of the offering, not including the underwriting discount, are estimated to be approximately $2.5 million. The underwriters have agreed to reimburse us up to $903,750 for certain of our expenses incurred with this offering.

We have agreed to indemnify the underwriters against certain liabilities, including liabilities under the Securities Act, as amended, or, if such indemnification is not available, to contribute to payments the underwriters may be required to make in respect of these liabilities.

The underwriters and their affiliates have provided, and expect to provide in the future, certain investment banking, commercial banking and other financial services to us and our affiliates, for which they have received, and may continue to receive, customary fees and commissions. For instance, Merrill Lynch, Pierce, Fenner & Smith Incorporated served as our financial advisor in connection with the Acquisition. In addition, we have obtained a commitment from an affiliate of Merrill Lynch, Pierce, Fenner & Smith Incorporated and an affiliate of UBS Securities LLC to enter into a new senior unsecured bridge term loan facility under which we may borrow up to $1.3 billion to finance the Acquisition. Certain other underwriters or their affiliates may also be lenders under the bridge term loan facility. The amount of financing available under the bridge term loan facility will be permanently reduced and any amount drawn is subject to prepayment in certain circumstances, including for each dollar of net proceeds received by us from this offering of notes. Certain affiliates of the underwriters are also lenders under our revolving credit facility.

In addition, in the ordinary course of their business activities, the underwriters and their affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers. Such investments and securities activities may involve securities and/or instruments of ours or our affiliates. If any of the underwriters or their affiliates have a lending relationship with us, certain of those underwriters or their affiliates routinely hedge, and certain other of those underwriters may hedge, their credit exposure to us consistent with their customary risk management policies. Typically, these underwriters and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions, including potentially the notes offered hereby. Any such credit default swaps or short positions could adversely affect future trading prices of the notes offered hereby. The underwriters and their affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or financial instruments and may hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

European Economic Area

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive, as defined below (each, a Relevant Member State), and with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the Relevant Implementation Date), an offer of notes to the public may not be made in that Relevant Member State, except that an offer to the public in the Relevant Member State of any notes may, with effect from and including the Relevant Implementation Date, be made in that Relevant Member State:

(a) at any time to any legal entity which is a qualified investor as defined in the Prospectus Directive;

(b) at any time to fewer than 100 or, if the Relevant Member State has implemented the relevant provision of the 2010 PD Amending Directive, as defined below, 150 natural or legal persons (other than qualified investors as defined in the Prospectus Directive) subject to obtaining the prior consent of the underwriters; or

(c) at any time in any other circumstances falling within Article 3(2) of the Prospectus Directive,

provided that no such offer of notes referred to in (a) to (c) above shall require the publication by us or any underwriter of a prospectus pursuant to Article 3 of the Prospectus Directive, or supplement to a prospectus pursuant to Article 16 of the Prospectus Directive. For the purposes of this provision, the expression an offer to the public in relation to any notes in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the notes to be offered so as to enable an investor to decide to purchase or subscribe to the notes, as the same may be varied in that Relevant Member State by any measure implementing the Prospectus Directive in that Relevant Member State, the expression Prospectus Directive means Directive 2003/71/EC (and the amendments thereto, including the 2010 PD Amending Directive, to the extent implemented in the Relevant Member State), and includes any relevant implementing measure in the Relevant Member State and the expression 2010 PD Amending Directive means Directive 2010/73/EU.

United Kingdom

The underwriters have informed us that (a)(i) they are each a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business and (ii) they have not offered or sold and will not offer or sell the notes other than to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or as agent) for the purposes of their businesses or who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses where the issue of the notes would otherwise constitute a contravention of Section 19 of the Financial Services and Markets Act 2000 (FSMA) by them; (b) they have only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by them in connection with the issue or sale of the notes in circumstances in which Section 21(1) of the FSMA does not apply; and (c) they have complied and will comply with all applicable provisions of the FSMA with respect to anything done by them in relation to the notes in, from or otherwise involving the United Kingdom.

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LEGAL MATTERS

The validity of the notes will be passed upon for us by Shearman & Sterling LLP, New York, New York and by Rylan O. Rawlins, Esq., Associate General Counsel of Cardinal Health. Mr. Rawlins is paid a salary by Cardinal Health and he participates in various employee benefit plans offered to its employees generally. Mr. Rawlins holds equity incentive awards with respect to Common Shares of the Company valued at greater than $50,000. Hunton & Williams LLP, New York, New York is counsel for the underwriters in connection with this offering. Hunton & Williams LLP from time to time has performed and may perform legal services for us.

EXPERTS

The consolidated financial statements of Cardinal Health, Inc. and subsidiaries appearing in Cardinal Health, Inc. s Annual Report on Form 10-K for the year ended June 30, 2012 (including the schedule appearing therein) and the effectiveness of Cardinal Health Inc. s internal control over financial reporting as of June 30, 2012, have been audited by Ernst & Young LLP, independent registered public accounting firm, as set forth in their reports thereon, included therein, and incorporated herein by reference. Such consolidated financial statements are, and audited consolidated financial statements to be included in subsequently filed documents will be, incorporated herein in reliance upon the reports of Ernst & Young LLP pertaining to such consolidated financial statements and the effectiveness of our internal control over financial reporting as of the respective dates (to the extent covered by consents filed with the Securities and Exchange Commission) given on the authority of such firm as experts in accounting and auditing.

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COMMON SHARES

PREFERRED SHARES

DEBT SECURITIES

Cardinal Health may offer and sell from time to time, together or separately, the following securities:

(i) common shares,

(ii) preferred shares,

(iii) unsecured debt securities, or

(iv) any combination of these securities.

We will provide the terms of any offering and the specific terms of the securities offered in supplements to this prospectus. You should read this prospectus and any accompanying prospectus supplement carefully before you invest. This prospectus may not be used to sell any of these securities unless accompanied by a prospectus supplement or term sheet.

See Risk Factors beginning on page 3 for a discussion of certain risks that you should consider in connection with an investment in Cardinal Health s securities.

Cardinal Health s common shares are listed on the New York Stock Exchange under the symbol CAH.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is August 27, 2010.

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ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we filed with the Securities and Exchange Commission (the SEC) using a shelf registration process. Under this shelf process, Cardinal Health may sell in one or more offerings any combination of Cardinal Health s common shares, preferred shares, unsecured debt securities in one or more series, which may be senior or subordinated debt securities, or any combination of these securities. This prospectus provides you with a general description of the securities Cardinal Health may offer. Each time Cardinal Health sells securities, we will provide a prospectus supplement, which may be in the form of a term sheet, that will contain specific information about the terms of that offering and the specific terms of the securities. The prospectus supplement may also add, update or change information contained in this prospectus, and accordingly, to the extent inconsistent, information in this prospectus is superseded by the information in the prospectus supplement. You should read both this prospectus and the applicable prospectus supplement together with additional information described under the heading Where You Can Find More Information and Incorporation of Certain Documents by Reference.

Because Cardinal Health is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933, as amended (the Securities Act), Cardinal Health may add to and offer additional securities, including securities to be offered and sold by selling securityholders, by filing a prospectus supplement with the SEC at the time of the offer.

We have not authorized any person to provide you with any information or to make any representation other than as contained in this prospectus or in any prospectus supplement and the information incorporated by reference herein and therein. We do not take any responsibility for, and can provide no assurance as to the reliability of, any information that others may give you. Cardinal Health is not making an offer to sell or a solicitation of an offer to buy these securities in any jurisdiction where the offer, sale or solicitation is not permitted. The information appearing or incorporated by reference in this prospectus and any supplement to this prospectus is accurate only as of the date of this prospectus or any supplement to this prospectus or the date of the document in which incorporated information appears. Our business, financial condition, results of operations and prospects may have changed since those dates.

Unless otherwise indicated or unless the context otherwise requires, all references in this prospectus to we, us or our mean Cardinal Health, Inc. and its consolidated subsidiaries, and references to Cardinal Health or the Company refer to Cardinal Health, Inc. excluding its consolidated subsidiaries.

WHERE YOU CAN FIND MORE INFORMATION AND

INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

We file annual, quarterly and current reports, proxy statements and other information with the SEC. Our SEC filings are available on the Internet at the SEC s web site at http://www.sec.gov. You may also read and copy any document we file at the SEC s public reference room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for more information on the public reference room and its copy charges. You may also inspect our SEC reports and other information at the New York Stock Exchange, 20 Broad Street, New York, New York 10005. Documents may also be available on our web site at http://www.cardinal.com under the heading Investors. Please note that all references to http://www.cardinal.com in this registration statement and prospectus and any prospectus supplement that accompanies this prospectus are inactive textual references only and that the information contained on our website is neither incorporated by reference into this registration statement or prospectus or any accompanying prospectus supplement nor intended to be used in connection with any offering hereunder.

This prospectus is part of a registration statement on Form S-3 that we filed with the SEC, which includes exhibits and other information not included in this prospectus or a prospectus supplement. The SEC allows us to incorporate by reference in this prospectus the information we file with it. This means that we are disclosing

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important business and financial information to you by referring to other documents filed separately with the SEC that contain the omitted information. The information incorporated by reference is an important part of this prospectus, and information that we file later with the SEC will automatically update and supersede this information.

We incorporate by reference the following documents filed with the SEC by us and any future filings we make with the SEC after the date of this prospectus under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act), until we complete our offering of the securities offered by this prospectus and the accompanying prospectus supplement. We are not incorporating by reference any information furnished rather than filed under Item 2.02 or Item 7.01 of any Current Report on Form 8-K, unless otherwise specified:

SEC Filings	Period/Date
Annual Report on Form 10-K	Fiscal Year ended June 30, 2010, filed on August 26, 2010
Definitive Proxy Statement on Schedule 14A	Filed on September 24, 2009 for the 2009 Annual Meeting of Shareholders (other than the information set forth under the headings Human Resources and Compensation Committee Report and Shareholder Performance Graph)
Description of common shares contained in Registration Statement on Form 8-A	Filed August 19, 1994

Any statement contained or incorporated by reference in this prospectus shall be deemed to be modified or superseded for purposes of this prospectus to the extent that a statement contained herein, or in any subsequently filed document which also is incorporated herein by reference, modifies or supersedes such earlier statement. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this prospectus. Any statement made in this prospectus concerning the contents of any contract, agreement or other document is only a summary of the actual contract, agreement or other document. If we have filed or incorporated by reference any contract, agreement or other document as an exhibit to the registration statement, you should read the exhibit for a more complete understanding of the document or matter involved. Each statement regarding a contract, agreement or other document is qualified by reference to the actual document.

We will furnish without charge to each person (including any beneficial owner) to whom a prospectus is delivered, upon written or oral request, a copy of any or all of the foregoing documents incorporated herein by reference (other than certain exhibits). Requests for such documents should be made to:

Cardinal Health, Inc.

7000 Cardinal Place

Dublin, Ohio 43017

(614) 757-5222

Attention: Investor Relations

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RISK FACTORS

Investing in Cardinal Health s securities involves significant risks. Before you invest in Cardinal Health s securities, in addition to the other information contained in this prospectus and in the accompanying prospectus supplement, you should carefully consider the risks and uncertainties identified in Cardinal Health s reports to the SEC incorporated by reference into this prospectus and the accompanying prospectus supplement.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Cardinal Health s filings with the SEC, including Cardinal Health s Annual Report on Form 10-K for the fiscal year ended June 30, 2010 (the 2010 Form 10-K), Cardinal Health s Annual Report to Shareholders, any quarterly report on Form 10-Q or any current report on Form 8-K of Cardinal Health (along with any exhibits to such reports as well as any amendments to such reports), Cardinal Health press releases, or any other written or oral statements made by or on behalf of Cardinal Health, may include directly or by incorporation by reference forward-looking statements which reflect Cardinal Health s current view (as of the date such forward-looking statement is first made) with respect to future events, prospects, projections or financial performance. The matters discussed in these forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those projected, anticipated or implied in or by such statements. These risks and uncertainties include, but are not limited to:

- competitive pressures in the markets in which Cardinal Health operates, including pricing pressures;
- increasing consolidation in the healthcare industry, which could give the resulting enterprises greater bargaining power and may increase pressure on prices for Cardinal Health s products and services;
- uncertainties due to government healthcare reform, including the impact of the recently enacted health care reform legislation;
- legislative changes to the prescription drug reimbursement formula and related reporting requirements for generic pharmaceuticals under Medicaid;
- the loss of, or material reduction in purchases by, or default by one or more key customers;
- the loss of, or default by, one or more key suppliers for which alternative suppliers may not be readily available;
- unfavorable changes to the terms of key customer or supplier relationships, or changes in customer mix;
- changes in manufacturers pricing, selling, inventory, distribution or supply policies or practices, including policies concerning price appreciation;
- changes in hospital buying groups or hospital buying practices;
- changes in the frequency or magnitude of branded pharmaceutical price appreciation or generic pharmaceutical price deflation, restrictions in the amount of inventory available to us, or changes in the timing of generic launches or the introduction of branded pharmaceuticals;

uncertainties relating to market conditions for pharmaceuticals;

uncertainties relating to demand for our products and services;

changes in the distribution or outsourcing pattern for pharmaceutical and medical/surgical products and services, including an increase in direct distribution;

the costs, difficulties and uncertainties related to the integration of acquired businesses, including liabilities related to the operations or activities of such businesses prior to their acquisition;

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the ability to achieve the expected benefits from the acquisition of Healthcare Solutions Holding and to grow Cardinal Health s specialty distribution business;

uncertainties related to Cardinal Health s divestiture strategy, including difficulties in finding buyers or alternative exit strategies at acceptable prices and terms and in a timely manner;

Cardinal Health s ability to introduce and market new products and Cardinal Health s ability to keep pace with advances in technology;

changes in laws and regulations or in the interpretation or application of laws or regulations, as well as possible failures to comply with applicable laws or regulations as a result of possible misinterpretations or misapplications;

the continued financial viability and success of Cardinal Health s customers, suppliers and franchisees;

actions of regulatory bodies and other governmental authorities, including the U.S. Drug Enforcement Administration, the U.S. Food and Drug Administration, the U.S. Nuclear Regulatory Commission, the U.S. Department of Health and Human Services, various state boards of pharmacy, state health departments, and state insurance departments or comparable agencies that could delay, limit or suspend product development, manufacturing, distribution or sales or result in warning letters, recalls, seizures, injunctions and monetary sanctions;

costs or claims resulting from potential errors or defects in Cardinal Health s manufacturing, compounding, repackaging, information systems or pharmacy management services that may injure persons or damage property or operations, including costs from remediation efforts or recalls;

the results, costs, effects or timing of any commercial disputes, patent infringement claims, or other legal proceedings;

the costs, effects, timing or success of restructuring programs or plans;

increased costs for commodities used in the Medical segment including various components, compounds, raw materials or energy such as oil, oil-related and other commodities;

shortages in commodities, components, compounds, raw materials or energy used by Cardinal Health businesses, including supply disruptions of radioisotopes;

the risks of counterfeit products in the supply chain;

risks associated with global operations, including the effect of local economic environments, inflation, recession, currency volatility and global competition, in addition to risks associated with compliance with U.S and international laws relating to global operations;

difficulties or delays in the development, production, manufacturing, sourcing and marketing of new or existing products and services, including difficulties or delays associated with obtaining requisite regulatory consents or approvals associated with those activities;

disruption or damage to or failure of Cardinal Health s information or controls systems;

uncertainties relating to general political, business, industry, regulatory and market conditions;

risks associated with the spin-off of CareFusion Corporation (CareFusion), including risks of non-performance under spin-off agreements, and risks relating to adverse tax consequences to us and/or our shareholders;

risks associated with Cardinal Health s minority investment in CareFusion such as risks relating to CareFusion s business and risks relating to the disposition of the shares of CareFusion common stock currently held by Cardinal Health; and

other factors described in Item 1A: Risk Factors of the 2010 Form 10-K.

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The words expect, anticipate, intend, plan, believe, will, should, could, would, project, continue, and similar expressions g forward-looking statements, which speak only as of the date the statement was made, and also include statements reflecting future results or guidance, statements of outlook and tax accruals. Cardinal Health undertakes no obligation to update or revise any forward-looking statements, except to the extent required by applicable law.

THE COMPANY

Cardinal Health, Inc. is an Ohio corporation formed in 1979. We are a global healthcare solutions company providing products and services that help hospitals, physician offices and pharmacies reduce costs, improve safety and productivity, and deliver better care to patients.

On August 31, 2009, we completed the spin-off of CareFusion Corporation, our wholly-owned subsidiary, formed for the purpose of holding the majority of our clinical and medical products businesses.

For additional information concerning our business and our financial results and condition, please refer to the documents incorporated by reference in this prospectus.

The mailing address of our executive offices is 7000 Cardinal Place, Dublin, Ohio 43017, and our telephone number is (614) 757-5000.

USE OF PROCEEDS

Except as we may describe otherwise in a prospectus supplement, we will use the net proceeds from the sale of any offered securities for general corporate purposes, which may include working capital, capital expenditures, repayment or refinancing of indebtedness, acquisitions, repurchases of Cardinal Health s common shares, dividends or investments.

RATIO OF EARNINGS TO FIXED CHARGES

Our ratio of earnings to fixed charges for each of the fiscal years ended June 30, 2006 through 2010 was as follows:

	Fiscal Year Ended June 30				
	2010	**2009**	**2008**	**2007**	**2006**
Ratio of Earnings to Fixed Charges	9.4	9.4	8.4	6.7	11.4

The ratio of earnings to fixed charges is computed by dividing fixed charges of Cardinal Health and its consolidated subsidiaries into earnings before income taxes and discontinued operations plus fixed charges and capitalized interest. Fixed charges include interest expense, amortization of debt offering costs and the portion of rent expense which is deemed to be representative of the interest factor. Interest expense recorded on tax exposures has been recorded in income tax expense and has therefore been excluded from the calculation.

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DESCRIPTION OF CAPITAL STOCK

The following is a summary of Cardinal Health s capital stock. The following summary of the terms of Cardinal Health s capital stock is not meant to be complete and is qualified by reference to Cardinal Health s Amended and Restated Articles of Incorporation, as amended (the Articles), and Cardinal Health s Restated Code of Regulations, as amended (the Regulations), which are the operative documents that establish these rights. Copies of the Articles and Regulations are incorporated by reference in the registration statement of which this prospectus is a part. See Where You Can Find More Information and Incorporation of Certain Documents by Reference on page 1 of this prospectus for information on how to obtain a copy of the Articles and Regulations.

The Articles authorize Cardinal Health to issue up to 750,000,000 common shares. On June 30, 2010, approximately 363.6 million common shares were issued and outstanding and approximately 7.2 million were held in treasury. The Articles also authorize Cardinal Health to issue up to 5,000,000 Class B common shares, none of which are outstanding or reserved for issuance, and 500,000 non-voting preferred shares, none of which are outstanding or reserved for issuance.

From time to time, Cardinal Health may issue additional authorized but unissued common shares for share dividends, stock splits, employee benefit programs, financing and acquisition transactions, and other general purposes. Those common shares will be available for issuance without action by Cardinal Health s shareholders, unless action by the Cardinal Health shareholders is required by applicable law or the rules of the New York Stock Exchange or any other stock exchange on which common shares may be listed in the future.

Common Shares

All of the outstanding common shares are fully paid and nonassessable. Holders of common shares do not have preemptive rights and have no right to convert their common shares into any other security. All common shares are entitled to participate equally and ratably in dividends, when and as declared by Cardinal Health s board of directors. In the event of the liquidation of Cardinal Health, holders of common shares are entitled to share ratably in assets remaining after payment of all liabilities, subject to prior distribution rights of any preferred shares then outstanding. Holders of common shares are entitled to one vote per share in the election of directors and upon all matters on which shareholders are entitled to vote. Holders of Class B common shares (if any are issued in the future) are entitled to one-fifth of one vote per share in the election of directors and upon all matters on which shareholders are entitled to vote. Under certain circumstances, holders of Class B common shares have a right to a separate class vote. Holders of common shares do not have any rights to cumulate votes in the election of directors.

Preferred Shares

No shares of non-voting preferred shares are currently outstanding. Under the Articles, Cardinal Health s board of directors, without further action by our shareholders, is authorized to issue up to 500,000 non-voting preferred shares, without par value, in one or more series and to fix the designation, preferences, limitations and relative or other rights thereof, including the designation and authorized number of shares constituting each series, dividend rights, redemption rights, conversion rights and liquidation price. The issuance of preferred shares could adversely affect the holders of common shares. The issuance of preferred shares could also have the effect, under certain circumstances, of delaying, deferring or preventing a change of control of Cardinal Health.

Board of Directors

Cardinal Health s board of directors currently consists of twelve members. The Regulations provide that the number of directors may be increased or decreased by action of the board of directors upon the majority vote of the board, but in no case may the number of directors be fewer than nine or more than sixteen without an amendment approved by the affirmative vote of the holders of shares representing not less than a majority of the voting power with respect to that proposed amendment. The board of directors may fill any vacancy with a person who will serve until the shareholders hold an election to fill the vacancy. Each director serves until the next annual meeting of shareholders and until his or her successor is duly elected and qualified. At the 2008 annual meeting of shareholders, Cardinal Health s shareholders approved amendments to the Articles and the Regulations to implement a majority voting standard for the election of directors in uncontested elections of directors (as defined in our Articles). Director elections other than uncontested elections are governed by a plurality voting standard. Also at the 2008 annual meeting, Cardinal Health s shareholders approved amendments to our Articles and Regulations to eliminate cumulative voting in elections of directors.

Anti-takeover Protections

The following summarizes certain provisions of the Ohio Revised Code (the Ohio Law) which may have the effect of prohibiting, raising the costs of, or otherwise impeding, a change of control of Cardinal Health, whether by merger, consolidation or sale of assets or stock (by tender offer or otherwise), or by other methods. Chapter 1704 of the Ohio Law provides generally that any person who acquires 10% or more of a corporation s voting stock (thereby becoming an interested shareholder) may not engage in a wide range of business combinations with the corporation for a period of three years following the date the person became an interested shareholder, unless the directors of the corporation have approved the transactions or the interested shareholder s acquisition of shares of the corporation, in either case, prior to the date the interested shareholder became an interested shareholder of the corporation. These restrictions on interested shareholders do not apply under certain circumstances, including, but not limited to, the following: (i) if the corporation s original articles of incorporation contain a provision expressly electing not to be governed by Chapter 1704 of the Ohio Law; (ii) if the corporation, by action of its shareholders, adopts an amendment to its articles of incorporation expressly electing not to be governed by such section; or (iii) if, on the date the interested shareholder became a shareholder of the corporation, the corporation did not have a class of voting shares registered or traded on a national securities exchange. The Articles do not contain a provision electing not to be governed by Chapter 1704.

Under Section 1701.831 of the Ohio Law, unless the articles of incorporation or regulations of a corporation otherwise provide, a control share acquisition of an issuing public corporation can be made only with the prior approval of the corporation s shareholders. A control share acquisition is defined as any acquisition of shares of a corporation that, when added to all other shares of that corporation owned by the acquiring person, would enable that person to exercise levels of voting power in any of the following ranges: at least 20% but less than 331/3%, at least 331/3% but less than 50%, or 50% or more. Although Cardinal Health is an issuing public corporation, the Regulations expressly provide that the provisions of Section 1701.831 of the Ohio Law do not apply to control share acquisitions of shares of Cardinal Health.

Transfer Agent and Registrar

The transfer agent and registrar for the common shares is Computershare Trust Co., Inc. (formerly EquiServe Trust Company), Providence, Rhode Island.

DESCRIPTION OF DEBT SECURITIES

The following description summarizes the general terms and provisions of the debt securities that Cardinal Health may offer pursuant to this prospectus that are common to all series. The specific terms relating to any series of the debt securities that Cardinal Health may offer will be described in a prospectus supplement, which you should read. Because the terms of specific series of debt securities offered may differ from the general information that Cardinal Health has provided below, you should rely on information in the applicable prospectus supplement that contradicts any information below.

As required by federal law for all bonds and notes of companies that are publicly offered, the debt securities will be governed by a document called an indenture. An indenture is a contract between a financial institution, acting on your behalf as trustee of the debt securities offered, and Cardinal Health. The debt securities will be issued pursuant to an indenture, dated as of June 2, 2008, between Cardinal Health and The Bank of New York Mellon Trust Company, N.A. (formerly The Bank of New York Trust Company, N.A.), as trustee, unless otherwise indicated in the applicable prospectus supplement. When Cardinal Health refers to the indenture in this prospectus, Cardinal Health is referring to the indenture under which your debt securities are issued, as may be supplemented by any supplemental indenture applicable to your debt securities. The trustee has two main roles. First, subject to some limitations on the extent to which the trustee can act on your behalf, the trustee can enforce your rights against Cardinal Health if Cardinal Health defaults on its obligations under the indenture. Second, the trustee performs certain administrative duties for Cardinal Health with respect to the debt securities.

Unless otherwise provided in any applicable prospectus supplement, the following section is a summary of the principal terms and provisions that will be included in the indenture. This summary is not complete and is subject to, and qualified in its entirety by reference to, the terms and provisions of the indenture, which will be in the form filed as an exhibit to or incorporated by reference in the registration statement of which this prospectus is a part. If this summary refers to particular provisions in the indenture, such provisions, including the definition of terms, are incorporated by reference in this prospectus as part of this summary. Cardinal Health urges you to read the applicable indenture and any supplement thereto because these documents, and not this section, define your rights as a holder of debt securities.

In this section, Cardinal Health refers to Cardinal Health, Inc., excluding its subsidiaries, unless otherwise expressly stated or the context otherwise requires.

General

The indenture does not limit the amount of debt securities or any other debt Cardinal Health may incur. The indenture provides that the debt securities may be issued from time to time in one or more series. The debt securities may have the same or various maturities. The debt securities may be issued at par, at a premium or with original issue discount. Cardinal Health may also reopen a previous issue of securities and issue additional securities of the series. The debt securities will be unsecured obligations of Cardinal Health. Senior debt securities will rank equally in right of payment with all of Cardinal Health s existing and future unsecured and unsubordinated indebtedness. Subordinated debt securities will be unsecured and subordinated in right of payment to the prior payment in full of all of Cardinal Health s unsecured and senior indebtedness. Unless otherwise specified in a prospectus supplement, a default in Cardinal Health s obligations with respect to any other indebtedness will not constitute a default or an event of default with respect to the debt securities. The indenture does not contain any covenants or provisions that afford holders of debt securities protection in the event of a highly leveraged transaction.

Cardinal Health conducts nearly all of its operations through subsidiaries and it expects that it will continue to do so. As a result, the right of Cardinal Health to participate as a shareholder in any distribution of assets of any subsidiary upon its liquidation or reorganization or otherwise and the ability of holders of the debt securities to benefit as creditors of Cardinal Health from any distribution are subject to the prior claims of creditors of the subsidiary.

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The prospectus supplement relating to any series of debt securities will, among other things, describe the following terms, where applicable:

- The title of the debt securities and whether the debt securities will be senior securities or subordinated securities;
- The total principal amount of the debt securities and any limit on the total principal amount of the debt securities of the series;
- If not the principal amount of the debt securities, the portion of the principal amount payable upon acceleration of the maturity of the debt securities or how this portion will be determined;
- The date or dates, or how the date or dates will be determined when the principal of the debt securities will be payable;
- The interest rate or rates, which may be fixed or variable, that the debt securities will bear, if any, or how the rate or rates will be determined, the date or dates from which any interest will accrue or how the date or dates will be determined, the interest payment dates, any record dates for these payments and the basis upon which interest will be calculated if other than that of a 360-day year of twelve 30-day months;
- Any optional redemption provisions;
- Any sinking fund or other provisions that would obligate us to repurchase or otherwise redeem the debt securities;
- The form in which we will issue the debt securities; whether we will have the option of issuing debt securities in certificated form; whether we will have the option of issuing certificated debt securities in bearer form if we issue the securities outside the United States to non-U.S. persons; any restrictions on the offer, sale or delivery of bearer securities and the terms, if any, upon which bearer securities of the series may be exchanged for registered securities of the series and vice versa (if permitted by applicable laws and regulations);
- If other than U.S. dollars, the currency or currencies in which the debt securities are denominated and/or payable;
- Whether the amount of payments of principal, premium or interest, if any, on the debt securities will be determined with reference to an index, formula or other method (which could be based on one or more currencies, commodities, equity indices or other indices) and how these amounts will be determined;
- The place or places, if any, other than or in addition to The City of New York, of payment, transfer, conversion and/or exchange of the debt securities;
- If other than denominations of $1,000 or any integral multiple in the case of registered securities issued in certificated form and $5,000 in the case of bearer securities, the denominations in which the offered debt securities will be issued;

The applicability of the provisions of the indenture described under defeasance and any provisions in modification of, in addition to or in lieu of any of these provisions;

Whether the securities are subordinated and the terms of such subordination;

Any provisions granting special rights to the holders of the debt securities upon the occurrence of specified events;

Any changes or additions to the events of default or covenants contained in the indenture;

	Whether the debt securities will be convertible into or exchangeable for any other securities and the applicable terms and conditions; and	2003	2002	2001
Provision for taxes at Canadian statutory marginal income tax rate	$ 28,433	$ 27,304	$ 22,621	
Non-taxable investment income	(838)	(832)	(282)	
Foreign operations subject to different tax rates	(32,722)	(36,455)	(9,106)	
Non-deductible goodwill amortization	--	--	2,786	
Change in tax rates and other	(2,514)	1,187	(5,936)	
Provision for (recovery of) income taxes	$ (7,641)	$ (8,796)	$ 10,083	

(b) The components of future income tax balances are as follows:

	2003	2002
Future income tax assets:		
Losses carried forward	$ 30,569	$ 34,089
Unpaid claims and unearned premiums	36,382	32,663
Investments	5,926	1,713
Share issue expenses	3,920	2,985
Contingent commission accruals	4,436	--
Other	4,385	4,639
Future income tax assets	85,618	76,089
Future income tax liabilities:		
Deferred policy acquisition costs	(9,399)	(12,248)
Investments	(1,157)	(786)

Goodwill and intangible assets	(2,878)	(2,843)
Other	--	(707)
Future income tax liabilities	(13,434)	(16,584)
Net future income tax assets	$ 72,184	$ 59,505

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

7. Income taxes (continued):

(c) Amounts and expiration dates of the operating loss carryforward are as follows:

Year of net operating loss	Expiration date	Net operating loss
Canadian operations:		
2002	2009	$17,741
2003	2010	37,323
U.S. operations:		
1995	2010	961
1997	2012	2,701
1998	2018	1,153
2000	2020	402
2001	2021	21,883
2002	2022	5,737

(d) If the Company believes that all of its future income tax assets will not result in future tax benefits, it must establish a valuation allowance for the portion of these assets that it thinks will not be realized. Based predominantly upon a review of the Company s anticipated future earnings, but also including all other available evidence, both positive and negative, the Company has concluded it is more likely than not that its net future income tax assets will be realized.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

8. Unpaid claims:

(a) Nature of unpaid claims:

The establishment of the provision for unpaid claims is based on known facts and interpretation of circumstances and is therefore a complex and dynamic process influenced by a large variety of factors. These factors include the Company s experience with similar cases and historical trends involving claim payment patterns, loss payments, pending levels of unpaid claims, product mix or concentration, claims severity and claim frequency patterns.

Other factors include the continually evolving and changing regulatory and legal environment, actuarial studies, professional experience and expertise of the Company s claim departments personnel and independent adjusters retained to handle individual 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. In addition, time can be a critical part of the provision determination, since the longer the span between the incidence of a loss and the payment or settlement of the claims, the more variable the ultimate settlement amount can be. Accordingly, short-tail claims such as property claims, tend to be more reasonably predictable than long-tailed claims, such as general liability and automobile accident benefit claims which are less predictable.

Consequently, the process of establishing the provision for unpaid claims is complex and imprecise as it relies on the judgement and opinions of a large number of individuals, on historical precedent and trends, on prevailing legal, economic, social and regulatory trends and on expectations as to future developments. The process of determining the provision necessarily involves risks that the actual results will deviate, perhaps substantially, from the best estimates made.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

8. Unpaid claims: (continued)

(b) Provision for unpaid claims:

The Company completes an annual evaluation of the adequacy of unpaid claims at the end of each financial year. This evaluation includes a re-estimation of the liability for unpaid claims relating to each preceding financial year compared to the liability that was originally established. The results of this comparison and the changes in the provision for unpaid claims for the years ended December 31, 2003, 2002 and 2001 were as follows:

	2003	2002	2001
Unpaid claims - beginning of year - net	$ 1,066,356	$ 487,229	$ 342,776
Net unpaid claims of subsidiaries acquired	--	207,840	--
Provision for claims occurring:			
In the current year	1,599,196	1,152,507	588,942
In prior years	196,783	101,079	33,874
Claims paid during the year relating to:			
The current year	(644,801)	(491,352)	(303,783)
The prior years	(505,170)	(382,051)	(189,801)
Currency translation adjustment	(198,075)	(8,896)	15,221
Unpaid claims - end of year - net	1,514,289	1,066,356	487,229
	155,445	134,198	102,734

Reinsurers' and other insurers' share of unpaid claims			
Unpaid claims end of year	$ 1,669,734	$ 1,200,554	$ 589,963

The results for the years ended December 31, 2003, 2002 and 2001 were adversely affected by the evaluation of unpaid claims related to prior years. In 2002 and 2001 adverse development of Ontario automobile claims (including standard and non-standard automobile, motorcycle, commercial auto and long haul trucking) was the primary reason for the unpaid claims deficiency as well as development in non-standard automobile claims in southeastern United States. In 2003, adverse development on unpaid claims came from Ontario and Alberta automobile claims and non-standard automobile claims in southeastern United States.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

8. Unpaid claims: (continued)

Ontario Automobile

Ontario private passenger automobile contributed $32.8 million in 2003 and $26.4 million in 2002 of prior year claims development. The increase in fraudulent claims, the erosion of the tort threshold and accelerating health cost inflation contributed to the required increase in claims liabilities related to prior years. Evolving case law and the erosion of the tort threshold in Ontario has led to an extension of the reporting period during which a plaintiff may bring suit. Also, beginning in 2000, we identified significantly increased frequency and severity trends in health care cost in Ontario where we are required to offer unlimited coverage and much higher liability limits than our other markets. The estimated provisions related to automobile accident benefit claims were also increased as the assumed inflation rate and severity factors previously utilized were found to be inadequate based on actual development experienced in 2003.

Alberta Automobile

Alberta non-standard automobile business contributed $34.5 million of the prior years claims development in 2003, compared to $16.3 million in 2002. An increase in average reserves due to the continued escalation in bodily injury claim settlements was the reason for the adverse claims development in 2002 and 2003 in Alberta, where we increased existing case reserves based on actual settlement patterns.

Southeastern United States Non-Standard Automobile

Adverse development of unpaid losses incurred accounted for approximately $24.1 million and $25.3 million in 2003 and 2002 reported incurred losses, respectively. Similar to Ontario, Florida has experienced a significant acceleration in fraudulent claims activity over the last several years. Continued cost escalation of loss adjusting expenses and an increase in the number of files litigated required upward adjustments to open claims reserves for both the current and prior years as the unfavourable legal environment has resulted in the inflation of claims payments beyond our original estimates.

Canadian and U.S. Operations Trucking

Trucking business contributed $32.4 million to the 2003 prior years claims development, compared to $20.6 million in the same period in 2002. Increases in reserves were due to larger than anticipated settlements, particularly in the

U.S., which required upward adjustments to open claim files. Average claim file reserves were increased to reflect this pattern of settlement. Case reserves were increased to reflect the increased cost on injury claims similar to the development experienced on the Ontario automobile business.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

8. Unpaid claims: (continued)

(c) The fair value of unpaid claims and adjustment expenses, gross and recoverable from reinsurers, has been omitted because it is not practicable to determine fair value with sufficient reliability.

9. Acquisitions:

In 1999 the Company acquired all of the outstanding shares of Hamilton Investments, Inc. (Hamilton). All consideration was payable in cash, part of which was paid at closing, with the remaining payments based on the earnings of Hamilton for the fiscal years 1999 to 2003. The present value of the guaranteed future payments was accrued at the date of acquisition. The additional consideration payable for the years ended December 31, 2003, 2002 and 2001 was $2,163,000, $2,369,000 and $2,336,000, respectively. At December 31, 2003 no contingent consideration based on earnings was payable.

On April 5, 2002, the Company acquired all of the outstanding common and preferred shares of American Country Holdings, Inc. for a purchase price of $37.8 million. The results of American Country s operations have been included in the consolidated financial statements since March 31, 2002. American Country owns all the outstanding shares of American Country Insurance Company, an insurer of taxicabs based in Chicago, Illinois.

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

Cash and investments	$216,885
Accounts receivable	102,986
Other tangible assets	35,708
Intangible assets	
Contracts	3,782
Insurance licenses	3,553
Goodwill	20,110
Total assets	383,024
Bank indebtedness	15,794
Insurance liabilities	304,200
Accounts payable	22,454
Other liabilities	570
Total liabilities	343,018
Purchase price	$ 40,006

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

10. Segmented information:

The Company provides property and casualty insurance and other insurance related services in three reportable segments: Canada, the United States and corporate and other insurance related services. The Company s Canadian and United States segments include transactions with the Company s reinsurance subsidiaries. At the present time, other insurance related services are not significant. Results for the Company s operating segments are based on the Company s internal financial reporting systems and are consistent with those followed in the preparation of the consolidated financial statements. The segmented information for December 31, 2003 is summarized as follows:

	Canada	United States	Corporate and Other	Total
Gross premiums written	$ 654,877	$ 1,981,945	$ --	$ 2,636,822
Net premiums earned	554,334	1,827,650	--	2,381,984
Investment income (loss)	33,631	45,528	(790)	78,369
Net realized gains (losses)	12,495	42,563	(26)	55,032
Interest expense	--	13,077	7,906	20,983
Amortization of capital assets	767	5,378	1,333	7,478
Amortization of intangible assets	--	854	--	854
Net income tax expense (recovery)	(7,652)	9,685	(9,674)	(7,641)
Net income (loss)	(16,670)	95,936	6,017	85,283
Total assets	$ 1,154,646	$2,415,966	$ 59,823	$ 3,630,436
Underwriting profit (loss)	(65,383)	31,461	--	(33,922)
Claims ratio	83.7%	71.5%	--	74.3%
Expense ratio	28.1%	26.8%	--	27.1%
Combined ratio	111.8%	98.3%	--	101.4%

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

10. Segmented information (continued):

The segmented information for December 31, 2002 is summarized below:

	Canada	United States	Corporate and Other	Total
Gross premiums written	$ 490,754	$ 1,633,937	$ --	$ 2,124,691
Net premiums earned	415,227	1,322,527	--	1,737,754
Investment income (loss)	24,059	41,583	(787)	64,855
Net realized gains (losses)	(2,574)	17,084	1,749	16,259
Interest expense	--	10,508	1,766	12,274
Amortization of capital assets	748	7,529	1,081	9,358
Net income tax expense (recovery)	(6,005)	(3,751)	960	(8,796)
Amortization of intangible assets	--	716	--	716
Net income (loss)	(13,042)	88,708	3,866	79,532
Total assets	$ 1,299,918	$ 1,670,807	$ 13,709	$ 2,984,434
Additions to goodwill	--	20,110	--	20,110
Additions to intangible assets	--	7,335	--	7,335
Underwriting profit (loss)	(34,902)	37,514	--	2,612
Claims ratio	78.3%	69.2%	--	71.4%
Expense ratio	30.1%	28.0%	--	28.4%
Combined ratio	108.4%	97.2%	--	99.8%

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

10. Segmented information (continued):

The segmented information for December 31, 2001 is summarized below:

	Canada	United States	Corporate and Other	Total
Gross premiums written	$ 356,049	$ 709,213	$ --	$1,065,262
Net premiums earned	321,926	550,904	--	872,830
Investment income	25,035	27,289	229	52,553
Net realized gains	7,579	4,426	74	12,079
Interest expense	--	10,262	1,137	11,399
Amortization of capital assets	644	3,132	1,361	5,137
Net income tax expense	2,941	6,730	412	10,083
Goodwill amortization	701	5,105	50	5,856
Net income	14,925	27,080	2,926	44,931
Total assets	$ 633,545	$1,075,538	$69,661	$1,778,744
Underwriting profit (loss)	(9,826)	17,463	--	7,636
Claims ratio	73.5%	68.9%	--	70.6%
Expense ratio	29.6%	27.9%	--	28.5%

Combined ratio	103.1%	96.8%	--	99.1%

The Company s gross premiums written are derived from the following business lines and geographical areas:

	2003	2002	2001
Business Line			
Personal Lines:			
Non-Standard Auto	37%	39%	51%
Standard Auto	4%	2%	3%
Motorcycle	2%	2%	4%
Property (including Liability)	1%	2%	3%
Warranty	1%	1%	2%
Other Specialty Lines	1%	1%	1%
Total Personal Lines	46%	47%	64%
Commercial Lines:			
Trucking	31%	32%	24%
Commercial Auto	11%	8%	5%
Property (including Liability)	10%	11%	5%
Other Specialty Lines	2%	2%	2%
Total Commercial Lines	54%	53%	36%
Total Gross Premiums Written	100%	100%	100%

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

10. Segmented information (continued):

	2003	2002	2001
Geographical Area			
United States:			
California	13%	11%	4%
Florida	12%	12%	13%
Illinois	10%	11%	15%
Texas	7%	7%	6%
South Carolina	3%	4%	5%
Alabama	2%	3%	4%
Pennsylvania	2%	3%	3%
Other	26%	26%	17%
Total United States	75%	77%	67%

Canada:			
Ontario	12%	10%	16%
Alberta	6%	6%	7%
Quebec	5%	5%	8%
Other	2%	2%	2%
Total Canada	25%	23%	33%
Total Gross Premiums Written	100%	100%	100%

11. Indebtedness and subsequent events:

(a) Bank indebtedness:

On February 23, 1999, the Company entered into a U.S.$100 million unsecured credit facility with a syndicate of banks. Under this facility the Company has the option to borrow at a floating rate equivalent to the banks prime rate or for a fixed term at a fixed rate of LIBOR plus a spread based on the Company s credit rating or upon the ratio of funded debt to total capitalization, whichever is higher. The facility is for a fixed term of five years and one day and was fully drawn on March 5, 1999 for general corporate purposes. During each of the years ended December 31, 2003, 2002 and 2001 the Company repaid U.S.$5 million. The facility matures on March 5, 2004 and the Company anticipates refinancing the facility prior to its maturity.

In March, 1999, the Company entered into interest rate swap contracts whereby the Company fixed its rate on this U.S.$100 million debt at 5.91% plus a spread based on the Company s credit rating or upon the ratio of funded debt to total capitalization, whichever is higher, for the period of the facility. The fair values of the liabilities under the swap contracts at December 31, 2003, 2002 and 2001 were $1,506,000, $8,632,000 and $7,479,000, respectively.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

11. Indebtedness and subsequent events (continued):

(a) Bank indebtedness (continued):

In May, 2002, the Company entered into a $66.5 million revolving credit facility with a syndicate of banks which was renewed in May, 2003. The facility is a 364 day revolving credit facility at a floating interest rate determined based on the type of loan and the Company s senior unsecured debt rating. As at December 31, 2003, $50,275,000 (2002 $33,076,000) was outstanding under this facility with an effective interest rate of approximately 3% (2002 3%).

(b) Senior unsecured debentures:

On December 6, 2002, the Company issued $78 million of 8.25% unsecured senior debentures with a maturity date of December 31, 2007. The debentures are redeemable prior to the maturity date, at the Company s option, providing at least 30 days notice to debenture holders. Interest on the debentures is payable semi-annually in arrears. The net proceeds to the Company were $77,087,420.

(c) Subordinated indebtedness:

Between December 4, 2002 and December 16, 2003, six subsidiary trusts of the Company issued U.S.$90.5 million of 30 year capital securities to third parties in separate private transactions. In each instance, a corresponding floating rate junior subordinated deferrable interest debenture was then issued by Kingsway America Inc. to the trust in exchange for the proceeds from the private sale. The floating rate debentures bear interest at the rate of the London interbank offered interest rate for three-month U.S. dollar deposits, plus spreads ranging from 3.85% to 4.20%, but until dates ranging from December 4, 2007 to January 8, 2009, the interest rates will not exceed 12.45% to 12.75%. The Company has the right to call each of these securities at par anytime after five years from their issuance until their maturity. The net proceeds to the Company were $95,613,000 in 2003 and $22,198,000 in 2002 after deducting expenses of $6,273,000 and $1,438,000, respectively.

(d) Subsequent events:

On January 29, 2004, a subsidiary of the Company, Kingsway America Inc. completed the sale of U.S.$100 million 7.50% senior notes due 2014 in a private offering. The notes are fully and unconditionally guaranteed by the Company. The notes will be redeemable at Kingsway America s option on or after February 1, 2009. On February 4, 2004, Kingsway America repaid U.S.$34.5 million outstanding under the $66.5 million revolving credit facility described in (a) above.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

12. Contingent liabilities:

(a) Legal Proceedings:

In connection with its operations, the Company and its subsidiaries are, from time to time, named as defendants in actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the outcome of the various proceedings at this time, such actions have generally been resolved with minimal damages or expense in excess of amounts provided and the Company does not believe that it will incur any significant additional loss or expense in connection with such actions.

(b) Statutory Requirements:

Statutory policyholders capital and surplus of the Company s insurance subsidiaries was $816.2 million and $654.3 million at December 31, 2003 and 2002, respectively.

The Company s subsidiaries are subject to certain requirements and restrictions under their respective statutory insurance legislations including minimum asset requirements and dividend restrictions. For the year 2003, under the various insurance regulatory restrictions, based on the Company s December 31, 2003 financial statements, the Company s insurance and reinsurance subsidiaries would have aggregate dividend capacity of $212.9 million (2002 $180.3 million).

(c) Letters of Credit:

On October 4, 2002 the Company entered into a syndicated U.S.$350 million letter of credit facility. The letter of credit facility is principally used to collateralize inter-company reinsurance balances for statutory capital management purposes. The Company pledges securities to collateralize the utilized portion of the letter of credit facility. At December 31, 2003 and 2002 the letter of credit facility utilization was U.S.$306.3 million and U.S.$304.6 million, respectively.

Also from time to time, the Company pledges securities to third parties to collateralize liabilities incurred under its policies of insurance. At December 31, 2003 and 2002, the amount of pledged securities was U.S.$33.9 million and U.S.$49.2 million, respectively.

13. Fair value disclosure:

The fair value of financial assets and liabilities, other than investments (note 2), unpaid claims (note 8) and interest rate swaps (note 11) approximate their carrying amounts.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

14. Reconciliation of Canadian and United States Generally Accepted Accounting Principles:

The consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada. The significant differences between Canadian GAAP and U.S. GAAP, which affect the Company s consolidated financial statements, are described below:

The following table reconciles the consolidated net income as reported under Canadian GAAP with net income and other comprehensive income in accordance with U.S. GAAP:

	2003	2002	2001
Net income based on Canadian GAAP	$ 85,283	$ 79,532	$ 44,931
Impact on net income of U.S. GAAP adjustments, net of tax:			
Deferred start-up costs (a)	938	1,052	1,037
Goodwill amortization (b)	--	--	116
Equity accounting (c)	983	1,237	281
Gain on sale of USA Insurance Group (c)	(1,451)	--	--
Net income based on U.S. GAAP *	$ 85,753	$ 81,821	$ 46,365
Other comprehensive income adjustments:			
Change in unrealized gain on investments classified as available for sale (d)	19,976	20,973	11,996
Change in fair value of interest rate swaps (e)	7,126	(1,152)	(7,479)
Less: related future income taxes	6,170	4,949	2,512
Other comprehensive income adjustments	20,932	14,872	2,005
Currency translation adjustments in the period (f)	(105,403)	(4,409)	11,447
Other comprehensive income (loss)	(84,471)	10,463	13,452
Total comprehensive income	$ 1,282	$ 92,284	$ 59,817
*Basic earnings per share based on U.S. GAAP net income	$1.64	$1.68	$1.25
*Diluted earnings per share based on U.S. GAAP net income	$1.63	$1.66	$1.22

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

14. Reconciliation of Canadian and United States Generally Accepted Accounting Principles (continued):

The following table reconciles shareholders equity as reported under Canadian GAAP with shareholders equity in accordance with U.S. GAAP:

	2003	2002
Shareholders' equity based on Canadian GAAP	$ 704,959	$ 612,925
Other comprehensive income	37,490	16,558
Cumulative net income impact:		
Deferred start-up costs (a)	(1,043)	(1,981)
Goodwill amortization (b)	(1,213)	(1,213)
Equity accounting (c)	1,618	635
Gain on sale of USA Insurance Group (c)	(1,451)	--
Shareholders' equity based on U.S. GAAP	$ 740,360	$ 626,924

Statement of Financial Accounting Standards (SFAS) No. 130 Reporting Comprehensive Income requires the Company to disclose items of other comprehensive income in a financial statement and to disclose accumulated balances of other comprehensive income or loss in the equity section of the Company s consolidated balance sheet. Comprehensive income, which incorporates net income, includes all changes in equity during a period, except those resulting from investments by, and distributions to, owners. There is no requirement to disclose comprehensive income under Canadian GAAP. Total cumulative other comprehensive income (loss) amounted to $(56,823,000) and $27,648,000 as at December 31, 2003 and 2002, respectively.

(a) Deferred start-up costs:

Under Canadian GAAP, start-up costs of Avalon Risk Management, Inc. are deferred and amortized over a five year period commencing from the date the start-up period ended. Under U.S. GAAP, such costs are expensed in the periods in which the expenditures are incurred.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

14. Reconciliation of Canadian and United States Generally Accepted Accounting Principles (continued):

(b) Goodwill amortization:

As per Note 1(e), effective January 1, 2002, all existing goodwill which is currently included in the Company s Consolidated Balance Sheets ceased to be amortized to income over time for both Canadian and U.S. GAAP, and is subject to a periodic impairment review to ensure that the fair value remains greater than, or equal to, book value. Any excess of book value over fair value will be charged to income in the period in which the impairment is determined.

The Company adopted this new standard prospectively. As a result of the adoption of this new standard, no goodwill amortization was recorded in the twelve months ended December 31, 2002 and 2003.

Under Canadian GAAP, guarantee fund assessment liabilities were estimated and accrued at the date of acquisition, which resulted in an increase in the amount of goodwill recorded. Under U.S. GAAP, such costs are expenses in the periods in which the liabilities are estimated.

Prior to January 1, 2002, under Canadian GAAP, the amortization of goodwill was shown as the final item in the Statement of Operations, net of applicable taxes, whereas under U.S. GAAP this presentation was not permitted and the applicable taxes would be included in the income tax expense on the Statement of Operations. As a result, under U.S. GAAP, the applicable taxes of $818,000 for the twelve months ended December 31, 2001 would be reclassified to increase the goodwill amortization and decrease the income tax expenses. Goodwill amortization would be classified with expenses under U.S. GAAP.

(c) Equity accounting:

Under Canadian GAAP, the Company s 25% equity investment in USA Group was carried at cost as the Company did not have significant influence over the investee. Under U.S. GAAP the Company is deemed to have significant influence because the Company s equity investment exceeds 20%, and the equity method of accounting is used. This method recognizes the Company s share of net income or loss of the investee. Also, under U.S. GAAP goodwill is recognized, and prior to December 31, 2001 was being amortized over a period of 10 years.

The Company disposed of its equity investment in USA Group in November, 2003 and had to reverse a portion of the gain under U.S. GAAP due to the difference in the cost base of the investment under Canadian and U.S. GAAP.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

14. Reconciliation of Canadian and United States Generally Accepted Accounting Principles (continued):

(d) Portfolio investments:

Under Canadian GAAP, portfolio investments are carried at cost or amortized cost, and where a decline in value of an investment is considered to be other than temporary, a write-down of the investment to its estimated recoverable amount is recorded. Under U.S. GAAP, such investments would be classified as available for sale and are marked to market after write-downs for other than temporary declines in values, and the unrealized gain or loss, net of any future income taxes, is recorded as other comprehensive income, a component of shareholders equity.

(e) Accounting for Derivative Instruments and Hedging Activities:

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement No. 133, Accounting for Derivative Instruments and Hedging Activities (FAS 133), as amended by Statements No. 137 and 138, which established accounting and reporting standards for derivative instruments and for hedging activities. Under FAS 133, all derivative instruments, including certain derivative instruments embedded in other contracts, are recognized as either assets or liabilities in the balance sheet at their fair values, and changes in such fair values must be recognized immediately in earnings unless specific hedging criteria are met. The Company adopted this statement effective January 1, 2001 for purposes of its U.S. GAAP reconciliation. The Company has purchased interest rate swap contracts that are designated as cash flow hedges against the amounts borrowed under the unsecured credit facility. The terms of the swaps match those of the unsecured credit facility, and were entered into to minimize the Company s exposure to fluctuations in interest rates. The change in the fair value of interest rate swap contracts is reflected in other comprehensive income.

(f) Currency translation adjustments:

The Company reports its results in Canadian dollars. The operations of the Company s subsidiaries in the United States and Barbados are self-sustaining. These subsidiaries hold all of their assets and liabilities and report their results in U.S. dollars. As a result, the assets and liabilities of these subsidiaries are translated at the year-end rates of exchange. The unrealized gains and losses, which result from translation are deferred and included in shareholders equity under the caption currency translation adjustment . The currency translation account will change with fluctuations in the U.S. to Canadian dollar exchange rate.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

14. Reconciliation of Canadian and United States Generally Accepted Accounting Principles (continued):

(g) Future accounting pronouncements:

The Company does not expect the adoption of any known proposed accounting pronouncements to have a material impact on its consolidated financial statements.

15. Comparative figures:

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted in the current year.

16. Supplemental Condensed Consolidating Financial Information:

Kingsway America Inc. (KAI) issued senior notes which are fully and unconditionally guaranteed by the Company. The following is condensed consolidating financial information for the Company as of December 31, 2003 and 2002 and for the three years ended December 31, 2003, 2002 and 2001, with a separate column for each of KAI as Issuer, the Company (KFSI) as Guarantor and the other businesses of the Company combined (the Non-Guarantor Subsidiaries). For the purposes of the condensed consolidating financial information, the Company carries its investments under the equity method.

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Statement of Operations
For the year ended December 31, 2003

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the Non-Guarantor subsidiaries)	Consolidation adjustments	Total

Revenues					
Net premiums earned	$ --	$ --	$2,381,984	$ --	$2,381,984
Investment related income	(816)	24,255	109,962	--	133,401
Management fees	46,040	2,849	--	(48,889)	--
	45,224	27,104	2,491,946	(48,889)	2,515,385
Expenses					
Claims incurred	--	--	1,784,091	(13,954)	1,770,137
Commissions and premium taxes	--	--	503,158	--	503,158
Other expenses	40,975	11,475	125,950	(34,935)	143,465
Interest expense	7,906	--	13,077	--	20,983
	48,881	11,475	2,426,276	(48,889)	2,437,743
Income before income taxes	(3,657)	15,629	65,670	--	77,642
Income taxes	(9,674)	5,272	(3,239)	--	(7,641)
Equity in undistributed net income of subsidiaries	79,266	13,475	--	(92,741)	--
Net income	$85,283	$23,832	$ 68,909	$(92,741)	$ 85,283

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Statement of Operations
For the year ended December 31, 2002

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the Non-Guarantor subsidiaries)	Consolidation adjustments	Total
Revenues					
Net premiums earned	$ --	$ --	$1,813,208	$ (75,454)	$1,737,754
Investment related income	960	2,381	77,773	--	81,114
Management fees	38,001	2,153	--	(40,154)	--
	38,961	4,534	1,890,981	(115,608)	1,818,868
Expenses					
Claims incurred	--	--	1,323,780	(83,451)	1,240,329
Commissions and premium taxes	--	--	379,123	(7,072)	372,051
Other expenses	32,369	7,334	122,451	(38,676)	123,478
Interest expense	1,766	--	10,508	--	12,274
	34,135	7,334	1,835,862	(129,199)	1,748,132
Income before income taxes	4,826	(2,800)	55,119	13,591	70,736
Income taxes	960	(976)	(8,780)	--	(8,796)
Equity in undistributed net income of subsidiaries	75,666	(3,608)	--	(72,058)	--

Net income	$79,532	$(5,432)	$ 63,899	$ (58,467)	$ 79,532

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Statement of Operations
For the year ended December 31, 2001

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the Non-Guarantor subsidiaries)	Consolidation adjustments	Total
Revenues					
Net premiums earned	$ --	$ --	$872,830	$ --	$872,830
Investment related income	304	2,208	62,120	--	64,632
Management fees	29,516	1,762	--	(31,278)	--
	29,820	3,970	934,950	(31,278)	937,462
Expenses					
Claims incurred	--	--	623,163	(7,084)	616,079
Commissions and premium taxes	--	--	167,176	--	167,176
Other expenses	25,297	2,168	93,836	(39,363)	81,938
Interest expense	1,136	--	10,263	--	11,399
	26,433	2,168	894,438	(46,447)	876,592
Income before income taxes	3,387	1,802	40,512	15,169	60,870
Income taxes	412	612	9,059	--	10,083
Amortization of goodwill, net of applicable income tax	--	--	5,856	--	5,856
Equity in undistributed net income of subsidiaries	41,956	12,724	--	(54,680)	--
Net income	$44,931	$13,914	$ 25,597	$(39,511)	$ 44,931

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidating Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Balance Sheet
As at December 31, 2003

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the	Consolidation adjustments	Total

			Non-Guarantor subsidiaries)		
Assets					
Investments in subsidiaries	$739,653	$461,943	$ 802,724	$(2,004,320)	$ --
Cash	23,302	2,473	115,108	--	140,883
Investments	2,523	--	2,509,529	--	2,512,052
Goodwill and other intangible assets	--	--	75,800	10,040	85,840
Other assets	35,428	33,800	2,362,164	(1,539,731)	891,661
	$800,906	$498,216	$5,865,325	$(3,534,011)	$3,630,436
Liabilities and Shareholders' Equity					
Liabilities:					
Bank indebtedness	$ 16,514	$ --	$ 137,381	$ --	$ 153,895
Other liabilities	1,433	17,850	112,205	(102)	131,386
Unearned premiums	--	--	1,294,246	(517,765)	776,481
Unpaid claims	--	--	2,638,518	(968,784)	1,669,734
Senior unsecured debentures	78,000	--	--	--	78,000
Subordinated indebtedness	--	115,981	--	--	115,981
	95,947	133,831	4,182,350	(1,486,651)	2,925,477
Shareholders' equity:					
Share capital	468,668	423,911	1,519,315	(1,943,226)	468,668
Contributed surplus	678	--	--	--	678
Currency translation adjustment	(94,313)	(64,991)	(25,348)	90,339	(94,313)
Retained earnings	329,926	(5,465)	189,008	(194,473)	329,926
	704,959	364,385	1,682,975	(2,047,360)	704,959
	$800,906	$498,216	$5,865,325	$(3,534,011)	$3,630,436

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Balance Sheet
As at December 31, 2002

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the Non-Guarantor subsidiaries)	Consolidation adjustments	Total
Assets					
Investments in subsidiaries	$619,192	$347,253	$761,943	$(1,728,388)	$ --
Cash	1,402	464	243,055	--	244,921
Investments	5,139	506	1,828,099	--	1,833,744
Goodwill and other intangible assets	--	--	94,250	10,040	104,290
Other assets	87,756	(41,924)	1,856,742	(1,101,095)	801,479
	$713,489	$306,299	$4,784,089	$(2,819,443)	$2,984,434

Liabilities and Shareholders' Equity					
Liabilities:					
Bank indebtedness	$ 20,532	$ --	$ 149,858	$ --	$ 170,390
Other liabilities	2,032	1,389	120,008	(823)	122,606
Unearned premiums	--	--	1,282,603	(506,280)	776,323
Unpaid claims	--	--	1,809,608	(609,054)	1,200,554
Senior unsecured debentures	78,000	--	--	--	78,000
Subordinated indebtedness	--	23,636	--	--	23,636
	100,564	25,025	3,362,077	(1,116,157)	2,371,509
Shareholders' equity:					
Share capital	357,192	335,757	1,295,744	(1,631,501)	357,192
Currency translation adjustment	11,090	(49,051)	17,481	31,570	11,090
Retained earnings	244,643	(5,432)	108,787	(103,355)	244,643
	612,925	281,274	1,422,012	(1,703,286)	612,925
	$713,489	$306,299	$4,784,089	$(2,819,443)	$2,984,434

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Statement of Cash Flows
For the year ended December 31, 2003

	KFSI (the Guarantor)	**KAI (the Issuer)**	**Other subsidiaries (the Non-Guarantor subsidiaries)**	**Consolidation adjustments**	**Total**
Cash provided by (used in):					
Operating activities:					
Net income	$ 85,283	$ 23,832	$ 68,909	$ (92,741)	$ 85,283
Adjustments to reconcile net income to net cash used by operating activities:					
Equity in undistributed earnings in subsidiaries	(79,266)	(13,475)	--	92,741	--
Other	56,973	(84,724)	564,745	(4,353)	532,641
	62,990	(74,367)	633,654	(4,353)	617,924
Financing activities:					
Increase in share capital, net	111,476	88,154	204,906	(293,060)	111,476
Increase/(decrease) in bank indebtedness	(4,018)	--	20,095	--	16,077
Increase in mortgage loan	--	17,760	(4,016)	(13,744)	--
Increase in subordinated indebtedness	--	101,886	--	--	101,886
	107,458	207,800	220,985	(306,804)	229,439
Investing activities:					
Purchase of investments	(29,692)	(7,228)	(6,598,124)	20,015	(6,615,029)
Proceeds from sale of investments	32,408	25,732	5,642,213	--	5,700,353
Other	(151,264)	(149,928)	(26,675)	291,142	(36,725)

	(148,548)	(131,424)	(982,586)	311,157	(951,401)
Increase (decrease) in cash during the year	21,900	2,009	(127,947)	--	(104,038)
Cash, beginning of year	1,402	464	243,055	--	244,921
Cash, end of year	$ 23,302	$ 2,473	$ 115,108	$ --	$ 140,883

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Statement of Cash Flows
For the year ended December 31, 2002

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the Non-Guarantor subsidiaries)	Consolidation adjustments	Total
Cash provided by (used in):					
Operating activities:					
Net income	$ 79,532	$ (5,432)	$ 63,899	$(58,467)	$ 79,532
Adjustments to reconcile net income to net cash used by operating activities:					
Equity in undistributed earnings in subsidiaries	(75,666)	3,608	--	72,058	--
Other	(73,617)	79,919	475,094	39,456	520,852
	(69,751)	78,095	538,993	53,047	600,384
Financing activities:					
Increase in share capital, net	960	82,744	11,002	(93,746)	960
Increase/(decrease) in bank indebtedness	6,186	--	20,766	--	26,952
Increase in subordinated indebtedness	--	23,636	--	--	23,636
Increase in senior unsecured debentures	78,000	--	--	--	78,000
	85,146	106,380	31,768	(93,746)	129,548
Investing activities:					
Purchase of investments	(145,341)	(177)	(4,251,307)	--	(4,396,825)
Proceeds from sale of investments	185,651	--	3,671,399	--	3,857,050
Other	(56,402)	(184,688)	158,955	40,699	(41,436)
	(16,092)	(184,865)	(420,953)	40,699	(581,211)
Increase (decrease) in cash during the year	(697)	(390)	149,808	--	148,721
Cash, beginning of year	2,099	854	93,247	--	96,200
Cash, end of year	$ 1,402	$ 464	$ 243,055	$ --	$ 244,921

KINGSWAY FINANCIAL SERVICES INC.

Notes to Consolidated Financial Statements

(Tabular amounts in thousands of Canadian dollars, except for per share amounts)

Condensed Consolidating Statement of Cash Flows
For the year ended December 31, 2001

	KFSI (the Guarantor)	KAI (the Issuer)	Other subsidiaries (the Non-Guarantor subsidiaries)	Consolidation adjustments	Total
Cash provided by (used in):					
Operating activities:					
Net income	$ 44,931	$ 13,914	$ 25,597	$(39,511)	$ 44,931
Adjustments to reconcile net income to net cash used by operating activities:					
Equity in undistributed earnings in subsidiaries	(41,956)	(12,724)	--	54,680	--
Other	(10,432)	(8,079)	180,908	--	162,397
	(7,457)	(6,889)	206,505	15,169	207,328
Financing activities:					
Increase in share capital, net	207,751	70,610	93,664	(164,274)	207,751
Increase/(decrease) in bank indebtedness	139	--	(7,174)	--	(7,035)
	207,890	70,610	86,490	(164,274)	200,716
Investing activities:					
Purchase of investments	(129,274)	(9,682)	(2,138,687)	--	(2,277,643)
Proceeds from sale of investments	97,258	9,898	1,851,522	--	1,958,678
Other	(167,772)	(72,313)	68,261	149,105	(22,719)
	(199,788)	(72,097)	(218,904)	149,105	(341,684)
Increase (decrease) in cash during the year	645	(8,376)	74,091	--	66,360
Cash, beginning of year	1,454	9,230	19,156	--	29,840
Cash, end of year	$ 2,099	$ 854	$ 93,247	$ --	$ 96,200

MANAGEMENT S DISCUSSION AND ANALYSIS

The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this annual report. The following discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ substantially from those anticipated in these forward-looking statements as a result of several factors, including those set forth under the section entitled Risk Factors and elsewhere in this annual report.

From time to time, we make written and oral forward-looking statements, including in this annual report, in other filings with Canadian regulators or the U.S. Securities and Exchange Commission (SEC), and in other communications. Forward-looking statements include, among others, statements regarding the Company s objectives and strategies to achieve them. Forward-looking statements are typically identified by words such as believe , expect , may and could . By their very nature, these statements are subject to inherent risks and uncertainties, general and specific, which may cause actual results to differ materially from the expectations expressed in the forward-looking statements. Some of the factors that could cause such differences are discussed under the section entitled Risk Factors of this annual report and in other regulatory filings made in Canada and with the SEC. The discussion of factors under the section entitled Risk Factors is not exhaustive of all possible factors. Other factors could also adversely affect the Company s results.

All such factors should be considered carefully when making decisions with respect to the Company, and undue reliance should not be placed on the Company s forward-looking statements. The Company does not undertake to update any forward-looking statements, written or oral, that may be made from time to time by or on its behalf.

All of the dollar amounts in this annual report are expressed in Canadian dollars, except where otherwise indicated. References to Canadian dollars, dollars, C$, or $ are to Canadian dollars and any references to U.S. dollars or US$ are to U.S. dollars. As presented in this annual r our Canadian and U.S. segment information includes the results of our Bermuda and Barbados reinsurance subsidiaries, respectively.

Overview

Kingsway Financial serves as the holding company for all of our subsidiaries, Kingsway America is the holding company for all of our U.S. operating subsidiaries. Our insurance subsidiaries include Kingsway General Insurance Company, York Fire & Casualty Insurance Company, and Jevco Insurance Company in Canada and Universal Casualty Company, Southern United Fire Insurance Company, American Service Insurance Company, Inc., Lincoln General Insurance Company, U.S. Security Insurance Company and American Country Insurance Company in the United States. We also have wholly owned reinsurance subsidiaries domiciled in Bermuda and Barbados. In the year ended December 31, 2003, we generated 75% of our gross premiums written from the United States and 25% from Canada.

Kingsway is a specialty provider of personal and commercial lines of property and casualty insurance in the United States and Canada. Our principal lines of business are non-standard automobile and trucking insurance. Non-standard automobile insurance covers drivers 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. We also provide standard automobile insurance as well as insurance for commercial and public vehicles, including taxis.

In addition to automobile insurance, we provide motorcycle insurance, specialized commercial and personal property coverage, warranty insurance and other specialty coverages, such as customs and surety bonds. In the year ended December 31, 2003, we derived 37% of our gross premiums written from non-standard automobile insurance, 31% from trucking, 12% from commercial and personal property coverages, 11% from commercial automobile, 4% from standard automobile, 2% from motorcycle and 3% from other specialty lines.

We are a leading provider of non-standard automobile and motorcycle insurance in Canada and have a prominent position in several U.S. markets in which we currently operate, such as Florida, Illinois, and South Carolina, based on direct premiums written. We are the third largest writer of non-standard automobile insurance in Illinois and the fourth largest in South Carolina according to A.M. Best.

Since 1996, we have experienced significant growth through acquisitions. In Canada, we acquired York Fire in February 1996 and Jevco in March 1997. In the United States, we acquired Universal Casualty and Southern United in January 1998, American Service in March 1998, Lincoln General in December 1998, U.S. Security in January 1999, and American Country in April 2002 (using an effective date of March 31, 2002).

We accounted for these acquisitions using the purchase method of accounting. Accordingly, we included the assets and liabilities of the acquired entities in our consolidated financial statements at their fair value at the date of acquisition and the results of their operations from that date.

In 2003, our gross premiums written increased 24% to $2.64 billion, compared to $2.12 billion in 2002. Our return on equity averaged 11.2% for the fiscal years 1999 to 2003. For the year ended December 31, 2003, our return on equity was 12.9% on an annualized basis compared to 13.8% in 2002. As of December 31, 2003, we had total assets of $3.6 billion and shareholders equity of $705.0 million. During the year ended December 31, 2003, shareholders equity was negatively impacted by the unrealized currency translation adjustment of our U.S. dollar denominated assets into Canadian dollars amounting to $105.4 million, or $1.88 per share outstanding at December 31, 2003.

The insurance industry is highly competitive. However, we generally seek to identify and operate in specialty markets which present opportunities for us to compete effectively due to the narrow scope or limited size of the market or the specialty nature of the coverage or risk. These specialty markets may be defined by geographic area, type of insurance or other factors. We focus on specialty lines of automobile, property and casualty insurance where we believe competition is more limited. We emphasize underwriting profit and will not knowingly underwrite risks at rates which we believe are unprofitable in order to increase our premium volume. We believe that by executing this strategy we have been able to deliver returns that have exceeded the average in our industry in both the United States and Canada.

We use the claims ratio, the expense ratio and the combined ratio as important measures of our performance. The claims ratio is derived by dividing the amount of net claims incurred by net premiums earned. The expense ratio is derived by dividing the sum of commissions and premium taxes and general and administrative expenses by net premiums earned. The combined ratio is the sum of the claims ratio and the expense ratio. A combined ratio below 100% demonstrates underwriting profit whereas a combined ratio over 100% demonstrates an underwriting loss. We believe that underwriting profit is the true measure of performance of the core business of a property and casualty insurance company. We, therefore, emphasize underwriting profit and will not underwrite risks at rates which we believe are unprofitable in order to increase our premium volume. Management s incentive compensation is directly linked to our combined ratio and our return on equity objectives.

In recent years, the North American property and casualty insurance market, including the non-standard automobile market, has been less price competitive than in the late 1990 s. Many insurers significantly reduced premium rates from 1998 to 2000 due to higher investment returns and an over-capitalization of the industry which subsequently led to poor underwriting results, together with investment impairments, caused an erosion of capital by December 31, 2002. As a result, premium rates began to rise and continued to do so throughout 2001, 2002 and 2003. Generally, we expect the rate increase trend to continue into 2004. The industry posted better underwriting results for 2002 and 2003 due to the increase in premium rates. However, the continued trend of adverse development of prior years claims continued to minimize improvement in reported underwriting results as many companies announced material year-end increases to prior years claims reserves, including Kingsway.

At the same time, in both 2002 and 2003, the insurance industry has been adversely affected by lower interest rates and a significant drop in equity indices. Poor pricing, adverse prior years claims development and historically low investment returns have also triggered an unprecedented rise in reinsurance rates and a significant decline in available reinsurance capacity. Although there has been a series of new reinsurance companies started since late 2001, these new companies have not materially replaced the capital and corresponding reinsurance capacity lost since that time. As a result of all of the above factors taken together, we believe the insurance industry s current improved pricing environment and significant limitations due to capital constraints will continue in the U.S. and Canadian insurance markets through 2004.

Corporate Strategy

Our strategy is to build long-term shareholder value by targeting three financial measurements over a five year period: (i) a 15% average after-tax return on shareholders equity, (ii) an average combined ratio, a measurement of profitability, of 96% or lower, and (iii) average increases in net premiums earned of 15% per annum. Our strategy is characterized by the following principles:

Adhere to a strict underwriting discipline. We manage our business with a strict focus on underwriting profit rather than on premium growth or market share and have demonstrated our willingness to increase pricing or reduce or increase premium volumes based on market conditions. Over the five year period ended December 31, 2003, our combined ratio averaged 100.8%, including 106.0% for our Canadian operations and 98.8% for our U.S. operations. For the year ended December 31, 2003, our combined ratio was 101.4%, including 111.8% for our Canadian operations and 98.3% for our U.S. operations. Management s incentive compensation is directly linked to our combined ratio and return on equity objectives.

Apply a specialty focus to regional markets. We seek to identify market segments where we believe competition is more limited, presenting the potential for above average returns. We believe that the non-standard automobile insurance business, our primary business, is presently one such specialty market. Other specialty markets in which we operate include trucking, taxi, motorcycle and warranty insurance. We operate through a network of regionally based operating subsidiaries. This decentralized operating structure allows us to target specialized markets and products based on our underwriting expertise and knowledge of local market conditions.

Rigorously manage claims at the local level. We seek to protect our business through diligent claims management. Our claims are managed by our experienced personnel located in our regional operating subsidiaries and by some of our MGAs. We maintain a culture of rigorously investigating claims, preventing fraud and litigating our claims as necessary before final settlement.

Expand in the United States and Canada. We rely on our detailed understanding of our regional markets to take advantage of any favorable conditions or trends. We look for opportunities to expand our specialty focus into selected regional markets and increase the distribution of our core products in our existing territories. We may also look for opportunities to acquire books of business or other companies which are in line with our specialty focus. Since late 2001, we have also entered into new programs with several Managing General Agents (MGAs) in the United States to expand the distribution network for our core business lines. In 2003, gross premiums written from these programs were $1,290.0 million or 49% of our business, compared to $961.4 million or 45% of our business in 2002.

Maintain a strong relationship with our agents, MGAs and brokers. We are committed to our distribution network of independent agents, MGAs and brokers. We continually strive to provide the highest level of service to our agents, MGAs and brokers and build relationships at the local level in the markets in which we operate. We communicate with our network through a variety of channels and we look for opportunities to increase efficiency and further reduce our operating costs, including through the use of technology and automation. We also look for opportunities to expand our distribution relationships and enhance our product mix.

Corporate Structure

We conduct our operations through our wholly owned subsidiaries in Canada and the United States. We are licensed to write a broad range of property and casualty insurance in all Canadian provinces and territories and in all states and the District of Columbia in the United States. We distribute all of our products through independent agents, MGAs, and brokers.

We conduct our operations through these subsidiaries to, among other things:

maintain discrete brand identities; and

develop expertise and organizational cultures that best serve the individual markets in which we operate.

We believe that the markets for our insurance products differ greatly by community because regulations, legal decisions, traffic, law enforcement, cultural attitudes, insurance agents, medical services and auto repair services vary greatly by jurisdiction and by community. Our corporate structure helps to meet varied local conditions under a cohesive set of policies and procedures designed to provide underwriting discipline, consistency and control.

Critical Accounting Policies

Our significant accounting policies are described in Note 1 to the audited financial statements included in pages 60 to 61 of this annual report. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect amounts reported in the financial statements. As more information becomes known, these estimates and assumptions could change and thus impact amounts reported in the future. Management believes that the establishment of the provision for unpaid claims is the area where the degree of judgment required to determine amounts recorded in the financial statements makes the accounting policy critical. Management believes that the establishment of an other-than-temporary impairment of an investment security requires a number of judgements and estimates which makes the accounting policy critical.

Revenues

Revenues reflected in our consolidated financial statements are derived from insurance premiums earned, investment income and net realized investment gains. Our total revenues increased 38% to $2.5 billion in 2003 compared to $1.8 billion in 2002 and $0.9 billion in 2001.

Premium Income

The insurance industry is highly competitive. We compete on the basis of numerous factors such as distribution strength, pricing, agency and broker relationships, service, reputation and financial strength. In Canada, our main competitor for non-standard auto is Pembridge Insurance Company, a subsidiary of The Allstate Corporation. In the United States, we face competition in our non-standard automobile lines from Allstate, Progressive and State Farm and in our trucking lines from Associates Insurance Group, Old Republic General Group, Canal

Insurance Company and Harco National Insurance Company. We also compete in both Canada and the United States with numerous smaller insurance companies. Many of our larger competitors have greater financial and other resources than we do, have more favorable A.M. Best ratings and offer more diversified insurance coverages. Many of our competitors in the non-standard automobile markets in the United States are small companies with limited capital resources who generally have less favorable A.M. Best ratings and who have traditionally relied upon the support of reinsurers to supplement their capital by way of proportional reinsurance treaties. Current reinsurance market conditions have led to a contraction of the availability of these proportional coverages.

Our competitors include other companies that, like us, serve the independent agency market, as well as companies that sell insurance directly to customers. Direct underwriters may have certain competitive advantages over agency underwriters, including increased name recognition, loyalty of the customer base to the insurer rather than an independent agency and, potentially, reduced acquisition costs.

Additionally, our markets may attract competition from time to time from new or temporary entrants in our niche markets. In some cases, these entrants may, because of inexperience, desire for new business or other reasons, price their insurance below the rates that we believe provide an acceptable premium for the related risk. We believe that it is generally not in our best interest to compete solely on price, and may from time to time experience a loss of market share during periods of intense price competition or soft market conditions.

We attribute the growth over the last five years to our various acquisitions and to internal growth, as we have executed our strategy to diversify both by line of business and by geographic location. We believe that our ability to compete successfully in our industry will be based on:

- our ability to identify specialty markets which are more likely to produce an underwriting profit;
- our disciplined underwriting approach;
- our prudent claims management; and
- the service and competitive commissions we provide to our agents, MGAs and brokers.

Any new, proposed or potential legislative or industry developments could further increase competition in our markets. New competition from these developments could cause the prices for insurance to fall, which would adversely affect our underwriting profitability.

We employ stringent underwriting standards to develop a broad spread of risk and to receive an appropriate premium for each risk. We seek to achieve an underwriting profit, targeting a combined ratio of 96% or less. Our underwriting philosophy stresses receiving an adequate premium and spread of risks for the business we accept. Rather than attempt to select individual risks, we seek to set premium rates at levels that should generate profitable underwriting. Once we have set premium rates that we believe are adequate, we are generally willing to accept as much business within our underwriting guidelines as is available to us. We regularly monitor premium adequacy by territory and class of business and make adjustments as required. We do not reduce our pricing when competitors offer to underwrite certain classes of business at premium rates which are below what we believe is an acceptable level. Instead, we elect to maintain our premium per risk rather than write a large number of risks at premiums which we consider to be inadequate. In such instances, our premium volumes have decreased, in some cases significantly. Underwriting profitability is dependent in large part on the amount of claims incurred on the policies sold in relation to net premiums earned. At the time premium levels are established, the amount of claims to be incurred on the policies sold is unknown. The process for estimating claims is inherently uncertain and imprecise.

We regularly consider and implement various initiatives to address adverse profitability trends in our business. These initiatives vary by jurisdiction, but include tightening of underwriting requirements, price increases, reduction in agent commissions, policy non-renewals (where permitted) and other administrative changes. All companies writing insurance in Canada and in most U.S. jurisdictions must have their premium rates approved by the applicable regulatory authority. Once these rates are approved, an insurance company is prohibited from altering them without approval for new rates.

We market and distribute our automobile insurance products through a network of over 2,900 independent agents and approximately 20 MGAs in the United States and over 3,000 independent brokers across Canada. In 2003, approximately 49% of our gross written premiums was sourced through MGAs and approximately 51% was sourced through independent agents. We maintain an open market approach which allows these agents and brokers to place business with us with no minimum commitments and provides us with a broad, flexible and easily scalable distribution network. We believe that this approach is different from that generally used by automobile insurance companies.

We focus on developing and maintaining strong relationships with our independent agents, MGAs and brokers. We continually strive to provide excellent service to our agents, MGAs and brokers and build relationships in the local markets in which we operate. We communicate with our agents, MGAs and brokers through a variety of channels and we look for opportunities to increase efficiency and reduce operating costs.

We believe that the commissions we pay to our agents, MGAs and brokers are fair and competitive.

Our independent agents, MGAs and brokers generally have the authority to enter into binding policies on our behalf with respect to specified insurance coverages within prescribed underwriting guidelines, subject to compliance with our mandated procedures. These guidelines prescribe the kinds and amounts of coverage that may be written and the premium rates that may be charged for specified categories of risk. In most cases, our independent agents, MGAs and brokers do not have authority on our behalf to settle or adjust claims, establish underwriting guidelines, develop rates or enter into other transactions or commitments. Certain MGAs have greater authority than our independent agents and brokers. However, we work diligently with them to ensure that they adhere to our underwriting standards and claims handling procedures.

We write automobile insurance primarily for the non-standard automobile and trucking markets. We also write insurance in selected other lines of business for both individuals and commercial customers. Other coverages for individuals that we provide include motorcycle, homeowners and selected specialty lines. Our commercial coverages include automobile, trucking, property and selected specialty lines such as customs bonds. Our personal lines business accounted for 46.3% of our gross premiums written for the year ended December 31, 2003 and 53.7% was generated from our commercial lines.

Our automobile insurance products provide coverage in three major areas: liability, accident benefits and physical damage. Liability insurance provides coverage, where our insured is responsible for an automobile accident, for the payment for injuries and for property damage to third parties. Accident benefits 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 coverages provide 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. Automobile physical damage and liability coverages generally provide more predictable results than automobile personal injury insurance.

Our gross premiums written increased 24% in 2003 to $2.64 billion, compared to $2.12 billion in 2002. In 2003, we experienced an increase of 33% in gross premiums written for our Canadian operations and 21% for our U.S. operations.

The following table sets forth our gross premiums written by line of business for the periods indicated:

For the year ended December 31,
(in millions of Canadian dollars, except for percentages)

	2003		2002	
Non-Standard Automobile	$ 966.1	36.6%	$ 828.1	39.0%
Standard Automobile	95.2	3.6	36.5	1.7
Motorcycle	57.4	2.2	52.3	2.5
Property (including liability)	43.3	1.6	49.2	2.3
Warranty	24.8	0.9	25.8	1.2
Other Specialty Lines	34.6	1.4	15.9	0.7
Total Personal	$ 1,221.4	46.3%	$ 1,007.8	47.4%
Trucking	808.4	30.7	685.5	32.3
Commercial Automobile	296.1	11.2	158.9	7.5
Property (including liability)	260.2	9.9	237.5	11.2
Other Specialty Lines	50.7	1.9	35.0	1.6
Total Commercial	$ 1,415.4	53.7%	$ 1,116.9	52.6%
Total Gross Premiums Written	$ 2,636.8	100.0%	$ 2,124.7	100.0%

We conduct our business in the United States and Canada. The following table sets forth our gross premiums written by state and province for the periods indicated:

For the year ended December 31,
(in millions of Canadian dollars, except for percentages)

	2003		2002	
California	$ 350.4	13.3%	$ 230.1	10.8%
Florida	318.2	12.1	257.4	12.1
Illinois	270.7	10.3	224.8	10.6
Texas	192.6	7.3	149.7	7.0
South Carolina	81.4	3.1	93.1	4.4
Alabama	61.3	2.3	60.0	2.9
Pennsylvania	52.0	2.0	54.8	2.6
Other	655.3	24.8	564.0	26.5
Total United States	$1,981.9	75.2%	$1,633.9	76.9%
Ontario	$ 304.7	11.5%	$ 220.0	10.4
Alberta	146.5	5.5	122.8	5.8
Québec	128.1	4.9	109.0	5.1
Other	75.6	2.9	39.0	1.8
Total Canada	$ 654.9	24.8	$ 490.8	23.1%
Total Gross Premiums Written	$2,636.8	100.0%	$2,124.7	100.0%

Non-Standard Automobile

Non-standard automobile insurance accounted for 37% and 39% of our gross premiums written for the years ended December 31, 2003 and 2002, respectively. 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. As underwriting standards for providing standard coverages have become more restrictive and many jurisdictions now require insurance regardless of driving record, high risk individuals have been forced to seek non-standard coverage and have contributed to the increase in the size of the non-standard automobile insurance market.

Non-standard automobile insurance is generally accompanied by increased loss exposure, higher claims experience and a higher incidence of consumer fraud. However, these factors are mitigated to some extent by higher premium rates, the tendency of high-risk individuals to own low value automobiles, and generally lower limits of insurance coverage. In addition, policy renewal rates tend to be low for non-standard automobile policies as policyholders often allow their policies to lapse because of non-payment of premiums and then reapply for insurance as new policyholders. This creates an ongoing requirement to replace non-renewing policyholders with new policyholders and to react promptly to issue cancellation notices for non-payment of premiums.

The insuring of non-standard drivers is often transitory. We expect that if and when their driving records improve, these drivers will qualify for and obtain insurance in the standard market at lower premium rates. As a result, our automobile insurance policies experience a retention rate that is lower than that experienced for standard market risks. Most of our insureds pay their premiums on a monthly installment basis. We limit our risk of non-payment of premiums by requiring a deposit for two months of insurance premiums.

In the United States and Canada, automobile insurers are generally required to participate in various involuntary residual market pools that provide automobile insurance coverages to individuals or other entities that are unable to purchase such coverage in the voluntary market. For example, in Ontario, every insurer is required to be a member of the Facility Association, an entity that was created to ensure the availability of automobile insurance to every motorist in Ontario. The Facility Association selects designated carriers to provide coverage and claims handling services to drivers who are unable to purchase insurance through private carriers, in return for an administration fee. Assessments from the Facility Association in Ontario increased our underwriting loss by $6.3 million in 2003 and reduced our underwriting profit by $1.4 million in 2002. Participation in these pools in most jurisdictions is in proportion to voluntary writings of selected lines of business in that jurisdiction.

In Canada, we are the largest writer of non-standard automobile insurance and operate primarily in Ontario, Alberta and Québec, with Alberta being our largest market. The non-standard automobile insurance market in Canada is primarily focused on providing drivers with minimum levels of liability coverage with accident benefit insurance. We obtained approval for premium rate increases effective in early 2002 in Ontario of 5.7% and Alberta of 10.0%. In July 2002, we obtained approval for a further rate increase commencing September 2002 and to eliminate certain rating classes in Ontario, the effect of which was an average 22.3% increase in premiums, although many of our insureds faced increases in excess of 40%. Further rate increases of 16.4% and 2.4% were effective in January and May 2003, respectively in Alberta, and effective February 2003, we obtained approval for an additional average 7% increase in Ontario. Rate freezes on automobile insurance premiums in Ontario and Alberta were effected in October and November of 2003, respectively. In December 2003 the Ontario legislature passed the Automobile Insurance Rate Stabilization Act of 2003 (the Rate Stabilization Act) and the rate freeze was removed in January 2004. The Alberta government has indicated that its rate freezes are in anticipation of a rate reform program that will reward safe drivers while allowing rate increases to be imposed on drivers with at-fault claims and poor driving records. At this time there is no certainty as to what the final Alberta legislative provisions will be or how such legislation will impact our Ontario and Alberta automobile business. We continue to assess opportunities for additional rate increases.

In the United States, we write non-standard automobile insurance in Illinois, South Carolina, Florida, Mississippi, Alabama, Missouri, Indiana, Texas, Georgia, California, Louisiana, Ohio and Virginia. Our business in Illinois is presently concentrated in the Chicago metropolitan area, although we are expanding into other areas of Illinois. In the United States, non-standard automobile insurance policies generally have lower limits of insurance commensurate with the minimum coverage requirement under the statute of the state in which we write the business. These limits of liability are typically not greater than US$40,000 per occurrence. Consequently, we are able to retain most of our gross written premiums for our own account while minimizing our claims exposure, and only purchase reinsurance to limit our exposure to the larger and catastrophic type losses.

Standard Automobile

Standard automobile insurance provides coverage for drivers of standard-risk private passenger automobiles. Premiums for these types of policies are usually lower than premiums charged in the non-standard market. However, the frequency and severity of accidents and other loss events are also typically lower. Our standard automobile business is written in Ontario and Alberta.

Motorcycle

Motorcycle insurance primarily consists of liability, physical damage and personal injury insurance coverages. In Canada, we are the leading writer of motorcycle insurance, writing over 30% of the total market. We write motorcycle insurance in the provinces of Ontario, Alberta and Québec. We obtained approval for a 17.7% rate increase effective March 1, 2003 and a 7.1% rate increase effective March 1, 2004 in Ontario, our largest market. We also write motorcycle insurance in the United States.

Property (including liability)

We write property (including liability) insurance for businesses and individuals in Canada and the United States. This business focuses on insuring against damage to property and accidents that may occur on such property. Our commercial property and liability business consists of risks that are difficult to place due to class, age, location or occupancy of the risk. These risks are characterized by high premiums and deductibles and limited coverage. We generally limit our exposure to no more than $500,000 in Canada and US$500,000 in the United States on any one risk.

Our specialty property business includes insurance for restaurants, rental properties and garages. We also write non-hydrant protected homeowners insurance and habitational risks which do not qualify for coverage by writers of standard insurance. We provide coverage on a very itemized named perils basis with relatively high rates and high deductibles for risks that are considered substandard by other companies. We believe these risks provide us with the opportunity to achieve attractive returns.

Our strategy is to operate as a niche underwriter of classes of property business that are more difficult to underwrite and offer the potential to achieve higher levels of underwriting profitability. We underwrite this business using our carefully developed underwriting methodology based on a stringent set of criteria. This business is seldom subject to a high degree of competition and we have often been able to write these policies at relatively high rates with fairly restricted coverage.

Warranty

In our warranty insurance business, we assume the liability for performance under the terms of service contracts and limited warranties issued by retailers of automobiles, home appliances, furniture and electronics and by residential home builders. This coverage indemnifies the consumer against loss resulting from service contract claims that occur during a specified period after expiration of the manufacturer s or builder s warranty. We discontinued writing any new warranty business in Canada during 2003.

Trucking

We provide coverage for liability, accident benefits, physical damage, cargo and comprehensive general liability under a package program throughout both Canada and the United States. Since late 2000, several companies have exited this business as a result of poor performances due to severe underpricing. These market conditions have allowed us to increase our prices, expand our relationships and have led to a significant increase in our gross premiums written for trucking insurance.

In the year ended December 31, 2003, gross premiums written from trucking increased by 17.9% to $808.4 million compared to $685.5 million in 2002. Trucking insurance accounted for 31%, 32% and 24% of our gross premiums written for the years ended December 31, 2003, 2002 and 2001, respectively.

Commercial Automobile

Commercial automobile policies provide coverage for taxis, rental car fleets and garage risks. Through American Service and American Country we are the largest writer of taxi risks in the Chicago area. In the year ended December 31, 2003, gross premiums written from commercial automobile increased by 86% to $296.1 million compared to $158.9 million in 2002, primarily as a result of the acquisition of American Country in April 2002.

Other Specialty Lines

Our other specialty lines include customs and surety bonds written in both the United States and Canada. Custom bonds involve insuring the timely payment of customs duties on goods imported into the United States and Canada, as well as any penalties incurred due to late payment of the duties or administrative non-compliance. Such duties generally represent less than 5% of the face value of the imported goods. We also write contract payment and performance and other miscellaneous surety bonds.

Investments and Investment Income

Our business philosophy stresses the importance of both underwriting profits and investment returns to build shareholder value. We manage our investment portfolio primarily to support the liabilities of our insurance operations and generate investment returns. We invest predominantly in high quality corporate, government and municipal bonds with relatively short durations. We also invest in preferred and common equity securities and consider our finance premium receivables to be a part of our investment portfolio. Our overall investment strategy is aimed at maximizing returns without compromising liquidity and risk control.

Our investment guidelines stress the preservation of capital, market liquidity to support payment obligations of our insurance liabilities and the diversification of risk. As part of this strategy, we attempt to maintain an appropriate relationship between the average duration of the investment portfolio and the approximate duration of our policy claims liabilities. With respect to fixed maturity securities, we generally purchase securities with the expectation of holding them to their maturity. Insurance laws and regulations in each domiciliary state or province also place limitations on the permitted investments of property and casualty insurers.

All of our investments are managed by professional, third-party investment management firms and we monitor their performance. We have engaged Conning Asset Management to oversee the majority of the fixed income investments of our U.S., Canadian and Bermuda subsidiaries.

In addition, Burgundy Asset Management, Deans Knight Capital Management Limited, Marquest Investment Counsel, SFE Investment Counsel, Kingwest and Company, J. Zechner Associates Inc. and Royal Bank of Canada (Caribbean) have each been engaged to manage portions of our subsidiaries equity and fixed income investments.

At December 31, 2003, we held cash, investments and accrued interest with a fair value of $2.73 billion and a carrying value of $2.67 billion, resulting in a net unrealized gain of $52.5 million. Because most of our investment portfolio is comprised of fixed-income securities which are usually held to maturity, periodic changes in interest rate levels generally impact our financial results to the extent that reinvestment yields are different than the original yields on maturing securities. Our investment portfolio includes investments which are subject to changes in market values with changes in interest rates. We do not hedge any foreign currency exposure that may exist in the portfolio. Our U.S. operations generally hold investments in U.S. dollar denominated investments, and our Canadian operations in Canadian dollar investments.

With the exception of U.S. and Canadian government bonds, it is our policy to limit our investment concentration at each of our subsidiary companies in any one issuer or related groups of issuers to less than 5% of the subsidiary company s investment portfolio.

The following table summarizes the fair value of our investments, including cash and cash equivalents, at the dates indicated:

For the year ended December 31,
(in millions of Canadian dollars)

	2003	2002
Type of investment		
Term deposits	$ 285.5	$ 506.5
Government Bonds	$ 787.5	$ 454.5
Corporate debt securities	$1,112.4	$ 630.7
Subtotal	$2,185.4	$1,591.7
Preferred shares	$ 0.5	$ 2.0
Common shares	$ 297.7	$ 185.8
Finance premiums	$ 80.9	$ 86.8
Cash and cash equivalents	$ 140.9	$ 244.9
Total	$2,705.4	$2,111.2

Investment results before the effect of income taxes were as follows:

For the year ended December 31,
(in millions of Canadian dollars)

	2003	2002
Average investments at cost	$2,384.5	$1,665.1
Investment income after expenses	$ 78.4	$ 64.9
Percent earned on average investments (annualized)	3.3%	3.9%
Net realized gains	$ 55.0	$ 16.3
Total realized yield	5.6%	4.9%
Change in unrealized investment gains	$ 20.0	$ 21.0
Total return yield	6.4%	6.1%

The percentages earned on average investments shown above compare with the Lehman Brothers Global Bond Index of 12.5% and 28.7% for the S&P 500 Index for the twelve months ended December 31, 2003.

The following table summarizes the fair value by contractual maturities of our fixed maturity investment portfolio, excluding cash and cash equivalents, at the dates indicated.

For the year ended December 31,
(in millions of Canadian dollars)

	2003	2002
Due in less than one year	$ 605.5	$ 638.2
Due after one through five years	1,155.0	717.5
Due after five through ten years	319.9	188.2
Due after ten years	105.0	47.8
Total	$2,185.4	$1,591.7

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.

Currently, we maintain a liquid portfolio to ensure there is sufficient cash available for the payment of claims on a timely basis. We believe that our high quality, liquid investment portfolio and our success in underwriting provide us with sufficient liquidity to meet our obligations to our policyholders.

The following table summarizes the composition of the fair value of our fixed maturity investment portfolio, excluding cash and cash equivalents, at the dates indicated, by rating as assigned by S&P or Moody s Investors Service, using the higher of these ratings for any security where there is a split rating.

As at December 31,

	2003	2002
Rating		
AAA/Aaa	60.5%	61.5%
AA/Aa2	17.6%	23.1%
A/A2	17.2%	10.1%
Percentage rated A/A2 or better	95.3%	94.7%
BBB/Baa2	2.1%	1.8%
BB/Ba2	0.3%	0.4%
B/B2	0.5%	0.5%
CCC/Caa or lower, or not rated	1.8%	2.6%
Total	100.0%	100.0%

The fair value of our investment portfolio, including cash and premium finance receivables, amounted to $2.7 billion at December 31, 2003 and $2.1 billion at December 31, 2002. At December 31, 2003, our portfolio, other than cash and premium finance receivables, was comprised primarily of short-term securities including treasury bills, bankers acceptances, government bonds and corporate bonds. The fair value of equity investments represented 11% of our investment portfolio at December 31, 2003 and 9% of our investment portfolio at December 31, 2002. The following chart shows how the carrying value of our investment portfolio, including accrued investment income, has grown over the last seven years.

	Investment Portfolio (in $millions)	Investment Portfolio Per Share Outstanding (in $ s)	Cash Flow Generated from Operations (in $millions)
1996	$ 188	$ 7.08	$ 45
1997	$ 354	$ 9.87	$ 48
1998	$ 634	$17.65	$ 63
1999	$ 693	$20.38	$ 34
2000	$ 787	$23.12	$ 93
2001	$1,235	$25.39	$207
2002	$2,095	$42.93	$600
2003	$2,674	$47.90	$617

We historically complied with SFAS 115 related to Accounting for Certain Investments in Debt and Equity Securities and recognized losses on securities whose decline in market value was deemed to be other than temporary. Subsequent to the issuance of SAB 59 in 2001, however, we reviewed our policy for determining declines considered other than temporary against the guidance provided by the SEC and identified certain securities for which a write-down may have been appropriate, based on the more specific requirements. We disposed of those securities that fell into this category and recognized the loss. None of the capital losses realized in 2003, 2002 and 2001 were considered individually material as we limit the exposure to any one security through our investment policy.

We recognized charges of $3.5 million, $6.6 million and $1.2 million for investment value impairment that was considered other than temporary for the years ended December 31, 2003, 2002 and 2001, respectively. We perform periodic analyses of our investment holdings to determine if declines in market value are other than temporary. These periodic analyses include some or all of the following procedures:

- identifying all security holdings in an unrealized loss position that has existed for at least six months;
- obtaining a valuation analysis from third party investment managers regarding the intrinsic value of these holdings based on their knowledge, experience and other market based valuation techniques;
- reviewing the trading range of certain securities over the preceding calendar period;
- assessing if declines in market value are other than temporary for debt security holdings based on the investment grade credit rating from third party security rating agencies;
- assessing if declines in market value are other than temporary for any debt security holding with non-investment grade credit rating based on the continuity of their debt service record; and
- determining the necessary provision for declines in market value that are considered other than temporary based on the analyses performed.

The risks and uncertainties inherent in the assessment methodology utilized to determine declines in market value that are other than temporary include, but may not be limited to, the following:

- the opinion of professional investment managers could be incorrect;
- the past trading patterns of individual securities may not reflect future valuation trends;
- the credit ratings assigned by independent credit rating agencies may be incorrect due to unforeseen or unknown facts related to a company s financial situation; and
- the debt service pattern of non-investment grade securities may not reflect future debt service capabilities and may not reflect the company s unknown underlying financial problems.

The length of time securities may be held in an unrealized loss position may vary based on the opinion of our appointed investment managers and their respective analyses related to valuation and the various credit risks that may prevent us from recapturing our principal investment. In cases where our appointed investment manager determines 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, securities would be traded and losses realized. Due to the current volatility of the equity markets, we believe there are a number of securities currently trading at values below their respective intrinsic values based on historical valuation measures. In these situations, holdings may be maintained in an unrealized loss position for different periods of time based on the underlying economic assumptions driving the investment manager s valuation of the holding. In cases where the economic realities divert from the underlying assumptions driving the investment manager s valuation, securities would be traded and losses realized. In cases where the economic assumptions coincide with valuation assumptions, the holding would be maintained until the market value of the security recovers in the public markets.

At December 31, 2003, and December 31, 2002, the gross unrealized losses amounted to $14.4 million and $11.3 million, respectively. The unrealized loss attributable to non-investment grade fixed income securities at December 31, 2003 and December 31, 2002 was $0.7 million and $0.8 million, respectively. The unrealized losses at December 31, 2003 and December 31, 2002 were considered temporary declines in market value based on the review of individual holdings as indicated above.

At December 31, 2003 and December 31, 2002, unrealized losses related to government bonds and term deposits were considered temporary as there was no evidence of default risk. Corporate bonds, even those below investment grade, in a material unrealized loss position, continued to pay interest and were not subject to material changes in their respective debt ratings. We concluded that a default risk did not exist at the time and, therefore, the decline in value was considered temporary. As we have the capacity to hold these securities to maturity, no investment impairment provision was considered necessary. Common stock positions in an unrealized loss position for more than six months may not be considered impaired based on the underlying fundamentals of the respective holdings. In making our investment impairment decisions, we utilized the professional expertise of our investment advisors, analyzed independent economic indicators (such as the price of oil when evaluating an oil and gas sector holding) and reviewed stock market trends.

The following table segregates the gross unrealized losses at December 31, 2003 and December 31, 2002 by security type or industry sector:

(in thousands of Canadian Dollars)	**December 31, 2003**	**December 31, 2002**
Mortgage backed	$ (497)	$ --
Government	(4,729)	(84)
Provincial, State, Municipal	(193)	--
Financial Services	(3,206)	(1,609)
Energy	(647)	(414)
Telecommunications	(412)	(493)
Information Technology	(199)	(646)
Consumer Products	(1,628)	(1,372)
Metals & Mining	(37)	(225)
Industrials	(1,471)	(2,972)
Utilities	(313)	(9)
Media	(20)	(1,227)
Medical	(122)	(6)
Pharmaceuticals	(615)	(701)
Retail	(266)	(1,323)
Real Estate	(18)	(233)
Total	$(14,373)	$(11,314)

We may hold other non-traded securities from time to time subject to the review and approval of our Investment Committee. As at December 31, 2003 and December 31, 2002, the carrying value of non-traded securities was $nil and $22.7 million respectively and the fair value approximated the carrying value. The fair value of non-traded securities is estimated based on a multiple of earnings per share that is consistent with earnings multiples of other public entities in the same industry. The fair value of non-traded securities is reviewed at least annually to determine if any decline should be considered other than temporary.

Movements in short-term and long-term interest rates, as well as fluctuations in the value of equity securities, affect the level and timing of recognition of gains and losses on securities we hold, causing changes in realized and unrealized gains and losses. Generally, our investment income will be reduced during sustained periods of lower interest rates as higher yielding fixed income securities are called, mature, or are sold and the proceeds are reinvested at lower rates. During periods of rising interest rates, the market value of our existing fixed-income securities will generally decrease and our realized gains on fixed-income securities will likely be reduced.

We currently maintain and intend to maintain an investment portfolio comprising primarily fixed income securities. Generally, declining interest rates result in unrealized gains in the value of fixed income securities we continue to hold, as well as realized gains to the extent the relevant securities are sold. General economic conditions, stock market conditions and many other factors can also adversely affect the securities markets and, consequently, the value of the equity securities we own.

Premiums for property and casualty insurance are typically payable at the time a policy is placed in force or renewed. To assist our insureds in making their payments to us, in some instances we offer premium financing either directly or through a separate premium finance company, whereby the insured can pay a portion of the premium in monthly installments. We provide the option of monthly payments on personal automobile policies, whereby the insured is only required to pay a portion of the premium when the policy is placed in force and the balance in monthly installments. The insured pays us an additional premium for this option, reflecting handling costs and the income we would have earned on such premium, had we received the total amount at the beginning of the policy period. We typically collect sufficient premiums in advance of the period of risk which ensures that in the event of payment defaults by insured, we do not have uncollectible balances. The option of monthly premium payments is available only where permitted under the laws or regulations of the specific territory. Some jurisdictions require the option of monthly premium payments at a specific annual interest rate or monthly charge. We consider our income from our premium finance activities to be a part of investment income, because this additional premium is essentially an interest payment on the balance of unpaid premium. At December 31, 2003, the balance of our financed premiums was $80.9 million compared to $86.8 million at December 31, 2002. The fair value of financed premiums approximates their carrying amount.

Our investment income, including net realized gains, increased 64% in 2003 to $133.4 million, compared to $81.1 million in 2002. Our insurance subsidiaries investments must comply with applicable regulations which prescribe the type, quality and concentration of investments. These regulations, in the various jurisdictions in which our insurance subsidiaries are domiciled, permit investments in government, state, provincial, municipal and corporate bonds, and preferred and common equities, within specified limits and subject to certain qualifications. The majority of our investments are held by our insurance subsidiaries. Because most of our investment portfolio is comprised of fixed-income securities, which are usually held to maturity, periodic changes in interest rate levels generally impact our financial results to the extent that reinvestment yields are different than the original yields on maturing securities.

Our investment portfolio includes investments that are subject to changes in market values with changes in interest rates. Actual maturities may differ from contractual maturities because certain issuers have the right to call or prepay obligations with or without penalties.

We maintain a liquid portfolio to ensure there is sufficient cash available for the payment of claims on a timely basis. We believe that funds generated by operations and our liquid investment portfolio provide us with sufficient liquidity to meet our obligations to our policyholders.

Provisions for Unpaid Claims

Claims management is the procedure by which an insurance company determines the validity and amount of a claim. We focus on rigorous claims management, which we believe is one of our areas of expertise. We believe that effective claims management is fundamental to our operations. We investigate the actual circumstances of the incident that gave rise to the claim and the actual loss suffered. 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 non-standard automobile insurance typically requires more thorough claims management and, in particular, more thorough investigative procedures than other types of insurance. Insurance claims on our policies are investigated and settled by our local claims adjusters. If necessary, we also employ independent adjusters, private investigators, various experts and legal counsel to adjust claims. Claims are scrutinized by an appraiser, an adjuster and, as appropriate, senior management, before claims payments are made.

We establish provisions for unpaid claims to reflect the estimated ultimate cost of both reported but unsettled claims and incurred but not reported (IBNR) claims. Our provisions for unpaid claims are based on individual reported claims, for which we establish case reserves; estimated provisions for claims that have not yet been reported but we expect will be reported in the future and expected future development on existing reported claims; and internal or unallocated claims adjustment expenses. The provisions for claims not yet reported and future development on existing reported claims are sometimes referred to as provisions for IBNR. The establishment of provisions for unpaid claims is based on known facts and interpretation of circumstances and is, therefore, a complex and dynamic process influenced by a large variety of factors. These factors include our experience with similar cases and historical trends involving claim payment patterns, loss payments, pending levels of unpaid claims, product mix or concentration, claims severity, claim frequency patterns and inflation rates. Our provisions for unpaid claims are not discounted to reflect expected future payouts of claims nor do they reflect any future investment income.

The process for establishing the provisions for unpaid claims reflects the uncertainties and significant judgmental factors inherent in predicting future results of both known and unknown claims and as such, the process is inherently complex and imprecise. Factors affecting provisions for unpaid claims include the continually evolving and changing regulatory and legal environment, actuarial studies, professional experience and expertise of our claims personnel and independent adjustors retained to handle individual 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. In addition, time can be a critical part of the provisions determination, because the longer the span between the incidence of a loss and the payment or settlement of the claims, the more variable the ultimate settlement amount can be. Accordingly, short-tailed claims, such as property claims, tend to be more reasonably predictable than long-tailed claims, such as general liability and automobile accident benefit claims, which are less predictable. We do not have exposure to asbestos, environmental or other products liability exposure.

The process of establishing provisions for unpaid claims relies on the judgment and opinions of a large number of individuals, on historical precedent and trends, on prevailing legal, economic, social and regulatory trends and on expectations as to future developments. The process of determining the provision necessarily involves risks that the actual results will deviate, perhaps substantially, from the best estimates made. This evaluation includes a re-estimation of the liability for unpaid claims relating to each preceding financial year compared to the liability that we originally established. In addition, we conduct a detailed review of all open claims each quarter and consider all factors into the provisions calculation. Accordingly, as experience develops and new information becomes known, we adjust our reserves as necessary following these evaluations. Any adjustments are reflected in our consolidated statement of income in the period in which they become known and are accounted for as changes in estimates. Even after such adjustments, ultimate liability or recovery may exceed or be less than the revised estimates.

Each operating company separately establishes, maintains and evaluates its respective provisions for unpaid claims for statutory reporting purposes. The process undertaken by each operating company includes evaluating all of its respective policy coverages and paid and open claim level data to ascertain claim frequency and severity trends, as well as the effects, if any, of inflation and the impact that any premium rate action or changes in operating structure or process may have on future loss settlements. The management of each operating company works with reporting segment management to ensure IBNR reserve methodologies are appropriate, based on lines of business and geographic region. Management incorporates all of the above information to record its best estimate of liabilities for unpaid claims.

Once an amount for liabilities for unpaid claims is established by management, our independent appointed actuary reviews management s methodologies, data and work papers to ascertain whether the provision for unpaid claims as established by management is reasonably stated and within the appointed independent actuary s range of reserve estimates. The provisions for unpaid claims established by each operating company are then consolidated for public reporting purposes. In accordance with actuarial standards, in the United States the independent actuary develops a range of reserve estimates and a recommended point estimate of reserves, and in Canada develops a point estimate.

As of December 31, 2003, the range of reserve estimates for unpaid claims for our U.S. subsidiaries established by our independent appointed actuary and the actual provision for unpaid claims on a gross basis for each of our operating companies were as follows:

	Low	High	Actual
	(in millions of Canadian dollars)		
United States			
Lincoln General Insurance Company	$ 653.8	$ 832.6	$ 726.3
American Country Insurance Company	146.8	187.9	164.2
American Service Insurance Company	63.2	79.6	75.1
U.S. Security Insurance Company	76.7	87.4	81.3
Universal Casualty Insurance Company	38.9	55.5	46.1
Southern United Fire Insurance Company	34.6	41.8	37.1

Kingsway Reinsurance Corporation (Barbados)	6.7	6.7	6.7
	$ 1,020.7	$ 1,291.5	$ 1,136.8
<u>Canada</u>			
Kingsway General Insurance Company			$ 420.5
Jevco Insurance Company			48.9
York Fire & Casualty Insurance Company			63.5
Total Consolidated Provision for Unpaid Claims			$ 1,669.7

Our policy as of December 31, 2003 is, and in the future will be, that to the extent that management s estimates of reserve levels at our individual insurance subsidiaries are less than the point estimates recommended by our independent actuary, those reserve levels will be adjusted to levels that are no less than the recommended point estimate. Under Canadian actuarial practice the appointed actuary does not provide a range of reserve estimates, but provides a point estimate for estimated claims liabilities. Each of our Canadian subsidiaries recorded at least 100% of the point estimate recommended by the appointed actuary.

During 2003 we significantly strengthened both reserves on individual claim files (case reserves) and our IBNR reserves. At December 31, 2003 our U.S. operations increased case reserves by 42%, IBNR by 85% and total reserves by 61% compared to December 31, 2002 and our Canadian operations also increased case reserves by 63%, IBNR by 58% and total reserves by 61%.

The following table summarizes the provisions for unpaid claims, net of recoveries from reinsurers, established as at the end of the years 1993 through 2002 for our Canadian operations and at the end of years 1998 to 2002 for our U.S. operations. The table compares the re-estimation of those liabilities as at December 31,2003.

as at December 31, 2003.

(In thousands of Canadian dollars, except percentages)	**2003**	**2002**	**2001**	**2000**	**1999**	**1998**	**1997**	**1996**	**1995**	**1994**	**1993**
Unpaid claims - originally established - end of year, gross	1,669,734	1,200,554	589,963	435,322	444,689	446,245	198,186	--	--	--	--
Less: Reinsurance recoverable on unpaid losses	155,445	134,198	102,734	92,546	119,817	135,270	73,242	--	--	--	--
Unpaid claims - originally established - end of year, net	1,514,289	1,066,356	487,229	342,776	324,872	310,975	124,944	65,142	24,322	16,987	10,945
Cumulative paid as of:											
One year later		504,772	382,051	189,801	149,708	141,093	46,083	31,309	13,665	12,384	5,984
Two years later			438,175	301,411	239,178	217,108	74,479	42,108	19,404	18,633	8,032
Three years later				383,015	309,888	261,809	91,127	55,214	25,273	22,066	10,347
Four years later					352,025	306,748	108,391	60,230	31,738	25,456	11,739
Five years later						332,990	121,076	66,029	32,679	29,300	12,576
Six years later							125,577	68,543	35,884	29,051	14,259
Seven years later								71,209	37,419	31,068	14,147
Eight years later									35,870	32,515	14,160
Nine years later										30,393	16,834
Ten years later											14,573
Re-estimated liability as of:											

One year later	1,263,139	588,308	377,592	329,069	306,377	112,075	62,022	27,705	22,776	11,395
Two years later		677,729	423,371	346,548	309,629	114,922	65,122	27,467	25,628	12,187
Three years later			478,184	367,951	318,226	117,759	66,368	31,707	25,580	12,256
Four years later				399,910	333,109	122,578	66,508	32,254	27,589	12,164
Five years later					345,749	129,697	68,570	32,745	28,243	13,004
Six years later						135,544	71,720	34,050	28,225	13,310
Seven years later							74,315	36,520	28,892	13,219
Eight years later								36,000	32,248	13,652
Nine years later									30,239	16,387
Ten years later										14,253
As at December 31, 2003: Cumulative (redundancy) deficiency	196,783	190,500	135,408	75,038	34,774	10,600	9,173	11,678	13,252	3,308
Cumulative (redundancy) deficiency as a % of reserves originally established	18.45%	39.10%	39.50%	23.10%	11.18%	8.48%	14.08%	48.01%	78.01%	30.22%
Re-estimated liability - gross	1,408,616	764,617	547,277	460,181	434,803	203,758	--	--	--	--
Less: Re-estimated reinsurance recoverable	145,476	86,888	69,093	60,271	89,054	68,214	--	--	--	--
Re-estimated liability - net	1,263,140	677,729	478,184	399,910	345,749	135,544	--	--	--	--
Cumulative (redundancy) deficiency-gross	208,062	174,654	111,955	15,492	(11,442)	5,572	--	--	--	--
% of reserves originally established	17.33%	29.60%	25.72%	3.48%	(2.56%)	2.81%	--	--	--	--

The foregoing table presents the development of unpaid claims liabilities for 1993 through 2002. The top line of the table presents the estimated liability for unpaid claims recorded at the balance sheet date for each of the indicated years. This liability represents the estimated amount of losses and adjustment expenses for claims unpaid at the balance sheet date, including losses that had been incurred and not reported. The table also presents the re-estimated liabilities for unpaid claims on a gross basis, with separate disclosure of the re-estimated reinsurance recoverable on unpaid claims for years 1997 through 2002. Information related to gross unpaid claims development is not available for years 1996 and prior.

The development of the provisions for unpaid claims is shown by the difference between estimates of claims as of the initial year-end and the re-estimated liability at each subsequent year-end. This is based on actual payments in full or partial settlement of claims, plus re-estimates of the claims required for claims still open or claims still unreported. Favorable development (reserve redundancy) means that the original claim estimates were higher than subsequently determined. Unfavorable development (reserve deficiency) means that the original claim estimates were lower than subsequently determined.

The table presents the cumulative amount paid with respect to the previously recorded liability as of the end of each succeeding year and the re-estimated amount of the previously recorded liability based on experience as of the end of the succeeding year. The estimate is increased or decreased as more information about the claims becomes known for individual years. For example, as of December 31, 2003, we had paid $71.2 million of the currently estimated $74.3 million of claims that had been incurred through the end of 1996; thus an estimated $3.1 million of losses incurred through 1996 remain unpaid as of the current financial statement date.

The cumulative development represents the aggregate change in the estimates over all prior years. For example, unpaid claims at December 31, 1993 have developed adversely by $3.3 million over the ten subsequent years and unpaid claims at December 31, 1995 have developed adversely by $11.7 million over the eight subsequent years. The effects on income during the past three years due to changes in estimates of unpaid claims is shown in note 8(b) to the Consolidated Financial Statements as the prior years contribution to incurred losses.

Each cumulative development amount includes the effects of all changes in amounts during the current year for prior periods and the impact of currency translation. For example, the amount of the development related to losses settled in 2003, but incurred in 1998, will be included in the cumulative development amounts for years 1998, 1999, 2000, 2001 and 2002. In addition, the deficiency identified during the year 2003 of $196.8 million was attributable to unpaid claims as at December 31, 2002 for unpaid claims for the year 2002 and all prior years. Of this deficiency, $107.4 million related to claims occurring in accident year 2002, $34.6 million to claims occurring in 2001, $22.9 million to claims in 2000, $19.3 million to claims occurring in 1999 and $6.8 million to claims occurring in 1997 and prior years.

The following table is derived from the unpaid claims re-estimates table above and summarizes the effect of re-estimates, net of reinsurance, on calendar year operations for the nine-year period ended December 31, 2003. The total of each column details the amount of reserve re-estimates made in the indicated calendar year and shows the accident years to which the re-estimates are applicable. The amounts in the total accident year column represent the cumulative reserve re-estimates for the indicated accident year.

(in millions of Canadian dollars)

By Accident Year	**2003**	**2002**	**2001**	**2000**	**1999**	**1998**	**1997**	**1996**	**1995**	**1994 & Prior**
By Calendar Year										
2003	(196,783)	107,362	34,608	22,854	19,318	6,794	3,252	3,115	1,489	(2,009)
2002		(101,079)	55,301	24,374	6,521	7,765	3,969	680	(886)	3,355
2001			(33,874)	13,695	8,483	7,173	2,783	757	638	345
2000				3,386	(6,651)	423	2,697	(351)	509	(13)
1999					6,377	(9,224)	1,601	699	(107)	654
1998						12,869	(15,969)	(1,140)	2,231	2,009
1997							3,120	(3,358)	190	48
1996								(3,383)	531	2,852
1995									(5,789)	5,789
Total	(196,783)	6,283	56,035	64,309	34,048	25,800	1,453	(2,981)	(1,194)	13,030
Combined Ratio										
As reported	101.4%	99.8%	99.1%	101.0%	102.6%	93.9%	95.8%	95.6%	96.6%	
Net reserve re-estimates	(8.3)%	0.4%	6.4%	11.9%	7.6%	8.2%	0.8%	(2.8)%	(2.6)%	
Accident year combined ratio	93.1%	100.2%	105.5%	112.9%	110.2%	102.1%	96.6%	92.8%	94.04%	

Information with respect to our liability for unpaid claims and the subsequent development of those claims is presented in the following tables.

	Liability for Unpaid Claims December 31,	
Line of Business	**2003**	**2002**
	(in thousands of Canadian dollars)	
Non-Standard Auto	$ 518,423	$401,976
Standard Auto	55,856	26,967
Commercial Auto	187,363	197,705
Trucking	567,326	320,708
Motorcycle	56,521	54,191
Property & Liability	223,775	192,023
Other	60,470	6,984
Total	$1,669,734	$1,200,554

Line of Business	Liability for Unpaid Claims Net of Reinsurance Recoverables December 31, 2003	2002
	(in thousands of Canadian dollars)	
Non-Standard Auto	$509,606	$380,193
Standard Auto	50,801	25,024
Commercial Auto	178,389	175,097
Trucking	518,242	291,739
Motorcycle	44,434	45,583
Property & Liability	165,876	143,786
Other	46,941	4,934
Total	$1,514,289	$1,066,356

These increases (decreases) in prior year incurred claims, net of reinsurance, for the years ended December 31, 2003, 2002 and 2001 were $196.8 million, $101.1 million and $33.9 million, respectively. The following tables identify the relative contribution of the increases (decreases) in incurred claims attributable to the respective products and incurred loss years.

Year Ended December 31, 2003
(in thousands of Canadian dollars)

	Motorcycle	Trucking	Standard Auto	Non-Standard Auto	Property & Liability	Other	Total
1998 and prior	$ 152	$ 3,531	$ 1,224	$ 6,045	$ 1,958	$ (269)	$ 12,641
1999	278	821	1,623	13,614	2,102	880	19,318
2000	1,929	1,732	4,875	11,719	2,253	346	22,854
2001	394	14,547	2,648	18,642	1,908	(3,531)	34,608
2002	(766)	11,813	3,327	60,346	7,817	24,825	107,362
Total	$ 1,987	$32,444	$13,697	$110,366	$16,038	$ 22,251	$196,783

Year Ended December 31, 2002
(in thousands of Canadian dollars)

	Motorcycle	Trucking	Standard Auto	Non-Standard Auto	Property & Liability	Other	Total
1997 and prior	$ 3,210	$ (487)	$ (108)	$ 4,402	$ 104	$ (3)	$ 7,118
1998	(71)	3,346	2,675	1,068	614	133	7,765
1999	396	1,177	1,692	2,212	1,036	8	6,521
2000	1,864	3,107	6,096	13,654	173	(520)	24,374
2001	336	4,575	6,051	42,981	1,385	(27)	55,301
Total	$ 5,735	$ 11,718	$ 16,406	$64,317	$3,312	$(409)	$101,079

Year Ended December 31, 2001
(in thousands of Canadian dollars)

	Motorcycle	Trucking	Standard Auto	Non-Standard Auto	Property & Liability	Other	Total
1996 and prior	$ 35	$ (9)	$ (120)	$ 1,256	$ 540	$ 38	$ 1,740
1997	66	385	303	1,868	171	(10)	2,783
1998	1,480	255	470	4,881	76	11	7,173
1999	1,447	1,919	(161)	4,942	295	41	8,483
2000	553	1,923	1,991	9,119	399	(290)	13,695
Total	$3,581	$ 4,473	$ 2,483	$22,066	$1,481	$(210)	$33,874

The results for the year ended December 31, 2003 and 2002 were adversely affected by the evaluation of unpaid claims related to prior years that identified a net deficiency of $196.8 million and $101.1 million, respectively related to claims incurred during prior years.

The following table shows the sources of the prior years development in the U.S. and Canada by line of business.

Increase (decrease) in claims incurred for unpaid claims arising from prior periods

Net of External Reinsurance (in millions of Canadian dollars)	2003	2002
United States Operations		
MGA program non-standard automobile	$ 21.1	$ 1.3
Florida non-standard automobile	19.2	9.5
Trucking	18.4	14.2
Commercial automobile	15.3	1.7
Southern United non-standard automobile	4.9	16.3
Other	13.9	(7.7)
Subtotal U.S. operations	92.8	35.3
Canadian Operations		
Alberta non-standard automobile	34.5	16.3
Ontario private passenger automobile	32.8	26.4
Trucking	14.0	6.4
Commercial automobile	18.6	8.7
Other	4.1	8.0
Subtotal Canadian operations	104.0	65.8
Total increases in claims incurred for unpaid claims occurring prior to December 31, 2002	$196.8	$101.1

United States Operations

MGA Programs Non-Standard Automobile

Lincoln General Insurance Company experienced adverse development on its MGA non-standard automobile programs of $21.1 million in 2003 and $1.3 million in 2002. The adverse development was related to the accident year 2002 and primarily related to the trend of liability settlements in the California market.

Florida Non-Standard Automobile

In 2002 and 2003, the increase in personal injury protection litigation in Florida gave rise to increased estimates for allocated loss adjustment expenses. The increase in litigation was caused in part by plaintiffs attorneys bringing separate actions for each clinic or claimant, rather than consolidating cases, and by delays in claims handling due to difficulty in hiring enough qualified claims adjusters. Staffing issues have been alleviated resulting in a 33% decline in monthly suit counts since September 2002. At December 31, 2003, the provision for unpaid claims for non-standard automobile in Florida was $81.3 million, which was in excess of the point estimate recommended by the independent actuary. The range of reserve estimates for unpaid claims established by our independent appointed actuary was from $76.7 million to $87.4 million. Adverse development related to Florida non-standard auto business was $19.2 million for the year ended December 31, 2003 compared to $9.5 million for 2002. Average unpaid claims reserves were increased by 28% in 2003, whereas average settlements increased by only 17%.

Florida Non-Standard Automobile
(in U.S. dollars)

		Number of Claims		Average Dollars	
	Total Pending as of 12/31	Total Reported In	Total Settled In	Unpaid Claim Reserve	Settled Claim
2003	12,569	32,792	32,558	$2,846	$2,302
2002	12,335	32,098	29,695	$2,217	$1,969
2001	9,932	21,031	11,099	$1,979	$1,657

Long-Haul Trucking

At December 31, 2003 and 2002 the provision for unpaid claims for our U.S. long-haul trucking business was $453.5 million, and $267.4 million, respectively. Adverse development related to long-haul trucking business in the U.S. was $18.4 million for the year ended December 31, 2003 compared to $14.2 million in 2002. Development was experienced at Lincoln General Insurance Company on the trucking liability line of business for accident years 2001 and 2002. This development was the result of reserve strengthening in the current year for prior years due to the availability of more recent trends in loss settlement patterns that was not available at year end 2002.

Commercial Automobile

At December 31, 2003 and 2002 the provision for unpaid claims for our U.S. commercial automobile business was $143.0 million, and $168.4 million, respectively. Adverse development related to commercial automobile in the U.S. was $15.3 million for the year ended December 31, 2003 compared to $1.7 million in 2002. During 2003 we carried out a more extensive analysis of both internal and external data to determine appropriate levels of indemnity and allocated loss adjustment expenses for our taxi business at American Country. American Country now incorporates a more extensive analysis of both internal and external data as well as redefining the internal costs to be allocated to loss adjustment expenses. Additional development was experienced at Lincoln General Insurance Company on the commercial automobile liability line of business for accident years 2001 and 2002, similar to the long-haul trucking line of business. This development was the result of reserve strengthening in the current year for prior years due to the availability of more recent trends in loss settlement patterns that was not available at year end 2002.

Southern United Non-Standard Automobile

Although average settlements have remained consistent from 2001 to 2003, average reserves have increased 85% over the same period. The justification for this case reserve increase is that claims activities in newer territories such as South Carolina are developing with greater than expected frequency and severity requiring additions to the reserves. At December 31, 2003, the provision for unpaid claims for non-standard automobile at Southern United was $37.1 million, which was in excess of the point estimated recommended by the independent actuary. The range of reserve estimates for unpaid claims established by our independent appointed actuary was from $34.6 million to $41.8 million. Adverse development related to Southern United non-standard auto business improved to $4.9 million for the year ended December 31, 2003 compared to $6.3 million for 2002.

At Southern United we have put new management in place and have increased the quality and number of our claims staff to ensure that claims are investigated and adjudicated promptly and to avoid delays in establishing reserves for the ultimate cost of personal injury claims.

Southern United Non-Standard Automobile (in U.S. dollars)

	Number of Claims			Average Dollars	
	Total Pending as of 12/31	Total Reported In	Total Settled In	Unpaid Claim Reserve	Settled Claim
2003	5,399	27,844	30,199	$5,801	$1,790
2002	7,754	36,632	38,239	$4,383	$1,707
2001	9,361	35,720	32,125	$3,129	$1,792

Canadian Operations

Alberta Non-Standard Automobile

Alberta non-standard automobile business contributed $34.5 million of the prior years claims development in 2003, compared to $16.3 million in 2002. An increase in average reserves due to the continued escalation in bodily injury claim settlements as well as the standardization of our reserving methodology was the reason for the adverse claims development in 2002 and 2003 in Alberta, where we increased existing case reserves based on actual settlement patterns.

Ontario Private Passenger Automobile

Adverse development of our Ontario automobile business claims liabilities was driven by several factors. The following chart identifies the number of reported claims and the increase in reserves and settled claims from 2001 through 2003. The increase in fraudulent claims, the erosion of the tort threshold and accelerating health cost inflation contributed to the required increase in claims liabilities related to prior years. During that period we continued to revise our reserve methodology to react to the changing claims settlement environment. Although our average claims reserves at December 31, 2003 exceeded our average settlements in 2003, we expect claim settlements to approximate our current reserving position in the future.

Ontario Private Passenger Automobile

	Number of Claims			Average Dollars	
	Total Pending as of 12/31	Total Reported In	Total Settled In	Unpaid Claim Reserve	Settled Claim
2003	4,859	9,376	9,609	$30,865	$9,792
2002	5,092	11,711	11,700	$19,774	$8,619
2001	5,081	12,529	12,473	$14,366	$6,866

Evolving case law and the erosion of the tort threshold in Ontario has led to an extension of the reporting period during which a plaintiff may bring suit. The adverse development experienced by us was part of an industry wide adverse development situation that began to materialize in 2000 and continued through 2003. The escalation in health cost inflation and the higher incidence of fraud in Ontario significantly exceeded industry expectations.

Also, beginning in 2000, we identified significantly increased frequency and severity trends in health care costs in Ontario where we are required to offer unlimited coverages and much higher liability limits than our other markets. As changes to Ontario automobile policies have occurred, the changes have been reflected in our assessment of unpaid claims for current and prior years as well as our assessment of claims that occur in future periods. As a result, we increased our estimate for unpaid claims relating to automobile third party liability claims incurred prior to 2003. The estimated provisions related to automobile accident benefit claims were also increased as the assumed inflation rate and severity factors previously utilized were found to be inadequate based on the actual development experienced in 2003. We increased our reserves related to tort liability and revised our expected loss estimates for automobile accident benefit claims in our 2003 unpaid claims liabilities to account for the upward changes in both health care cost inflation and severity. Actuarial assumptions were also changed in 2003 to account for the shift in loss development trends. The numerous changes to Ontario automobile legislation and court decisions throughout the 1990 s has inhibited the Canadian insurance industry s ability to accurately predict the ultimate claims liabilities associated with Ontario automobile policies, which includes automobile, trucking and motorcycle risks. Bill 198 was enacted in late 2002 and in addition favourable regulations were implemented during 2003. We have also been able to obtain significant rate increases in 2002 and 2003 for our Ontario automobile products. In addition to the enactment of more favorable automobile insurance legislation in Ontario to combat fraud and control the tort claims in the no-fault system, we believe we have taken the necessary steps to reflect the ultimate cost of claims from these years.

Trucking and Commercial Automobile

At December 31, 2003 and 2002 the provision for unpaid claims for our Canadian trucking and commercial automobile business was $158.2 million and $81.8 million, respectively. Increases in reserves were due to larger than anticipated settlements, particularly in the U.S., which required upward adjustments to open claim files. Average claim file reserves were increased to reflect this pattern of settlement. Case reserves were increased to reflect the increased cost on injury claims similar to the development experienced on the Ontario automobile business.

Reinsurance

We purchase reinsurance from third parties in order to reduce our liability on individual risks and our exposure to catastrophic events. Reinsurance is insurance purchased by one insurance company from another for part of the risk originally underwritten by the purchasing insurance company. The practice of ceding insurance to reinsurers allows an insurance company to reduce its exposure to loss by size, geographic area, 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.

We generally purchase reinsurance to limit our net exposure to a maximum amount on any one loss of $500,000 in Canada and US$500,000 in the United States with respect to property claims and $1.0 million in Canada and US$1.0 million in the United States with respect to liability claims. In addition, we purchase catastrophe reinsurance which provides coverage in the event of a series of claims arising out of a single occurrence, which limits this exposure in Canada to $5.0 million per occurrence to a maximum coverage of $50.0 million, and in the United States to US$5.0 million per occurrence to a maximum coverage of US$50.0 million. On January 1, 2003, our net exposure for Ontario automobile business claims was increased to $2.5 million. For most of the non-standard automobile business that we write in the United States, the liability is limited to the minimum statutory liability limits, which are typically not greater than US$40,000 per occurrence, depending on the state. The cost of our external reinsurance represented 4.7% of gross premiums written for the year ended December 31, 2001, 5.4% for the year ended December 31, 2002, and 4.5% for the year ended December 31, 2003.

Reinsurance ceded does not relieve us of our ultimate liability to our insureds in the event that any reinsurer is unable to meet its obligations under its reinsurance contracts. We therefore enter 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 our reinsurers or us on the anniversary date and are subject to renegotiation annually. We regularly evaluate the financial condition of our reinsurers and monitor the concentrations of credit risk to minimize our exposure to significant losses as a result of insolvency of a reinsurer. We believe that the amounts we have recorded as reinsurance recoverables are appropriately established. However, estimating amounts of reinsurance recoverables is subject to various uncertainties and the amounts ultimately recoverable may vary from amounts currently recorded. As of December 31, 2003, we had $176.3 million recoverable from third party reinsurers and other insurers, which are generally unsecured. At December 31, 2003, 93% of the receivables were due from reinsurers that were rated A- or higher.

Estimating amounts of reinsurance recoverables is also impacted by the uncertainties involved in the establishment of provisions for unpaid claims. As our underlying reserves continue to develop, the amount ultimately recoverable may vary from amounts currently recorded. Our reinsurance recoverables are generally unsecured. We regularly evaluate our reinsurers, and the respective amounts recoverable, and a provision for uncollectable reinsurance is recorded, if needed. The following table summarizes the composition of the amounts due from reinsurers at December 31, 2003, by the rating as assigned by A.M. Best to the applicable reinsurers.

A.M. Best Rating	**December 31, 2003**
A++	17.9%
A+	23.9%
A	42.6%
A-	8.6%
B++/B+/B/B-	5.4%
C++u/C	0.1%
Not Rated	1.5%
Total	100.%

Results of Operations

For the years ended December 31, 2003 and 2002

Gross Premiums Written

During the year ended December 31, 2003, premiums written increased by 24% to $2.6 billion compared to $2.1 billion in 2002. For the year ended December 31, 2003, gross premiums written for our U.S. operations were $2.0 billion, an increase of 21% over 2002, and for our Canadian operations were $654.9 million, an increase of 33% over 2002. The effect of currency translation reduced reported levels of gross premiums written for the U.S. operations by $234.8 million or 11% for the year ended December 31, 2003 compared to 2002.

For the year ended December 31, 2003, gross premiums written from trucking and commercial automobile increased 31% to $1.1 billion compared to $844.4 million in 2002. Gross premiums written from non-standard automobile increased 17% to $966.1 million in 2003 compared to 2002. Increased premium rates and firming market conditions continue to be prevalent in all of our geographic locations. We continue to experience both volume growth and rate increases for both trucking lines and non-standard automobile in most of our markets, with the exception of Ontario and metropolitan Chicago where rate increases have led to a reduction in volume.

Net Premiums Written

Net premiums written increased 25% to $2.5 billion compared with $2.0 billion for the year ended December 31, 2002 as a result of higher levels of gross premiums written and a reduction in the percentage ceded to reinsurers. Net premiums written from our U.S. operations increased 23% to $1.9 billion compared with $1.5 billion in the year ended December 31, 2002. Net premiums written from our Canadian operations increased 33% to $616 million compared with $463 million for the year ended December 31, 2002.

Net Premiums Earned

Net premiums earned increased 37% to a record $2.4 billion for the year ended December 31, 2003, compared with $1.7 billion for 2002. For our U.S. operations, net premiums earned increased 38% to $1.8 billion in the year ended December 31, 2003 compared with $1.3 billion in 2002, and for our Canadian operations increased by 33% to $554 million compared with $415 million in 2002. Net premiums earned have increased due to the growth in written premiums in 2002 and 2003 and the strategy of shortening the policy duration of most of our non-standard automobile business to six month policy terms. In a rising rate environment, shorter policy terms lead to an acceleration of the benefit of rate increases.

Investment Income

Investment income increased to $78.4 million compared with $64.9 million for the year ended December 31, 2002. The investment portfolio has grown by 28% since the beginning of 2003 due to positive cash flow from operations and capital raised. This growth has been accomplished in a declining interest rate environment with new funds being invested primarily in short-term fixed income products. Our annualized investment yield for December 31, 2003 declined to 3.3% compared to 3.9% in 2002 reflecting the trend in short-term interest rates.

Net Realized Gains

Net realized gains amounted to $55.0 million in the year ended December 31, 2003 compared with net realized gains of $16.3 million in 2002. The majority of these gains were realized from the disposal of equity investments, including the disposal of an investment in USA Insurance Group which amounted to $18.8 million. As a result of our increased investment in common shares during 2003 and improved market performance, unrealized gains increased to $52.5 million at December 31, 2003 compared to $32.6 million at December 31, 2002. In deciding whether to reduce the carrying value of common shares, we take into account a number of factors, including whether the decline in market value is more than 20% and has persisted for a period exceeding six months. In the case of fixed income securities, we also take into account whether the issuer is in financial distress (unable to pay interest or some other situation that would question the issuer s ability to satisfy their debt obligations).

Claims Incurred

Our claims ratio for 2003 was 74.3%, compared to 71.4% for 2002. The claims ratio for our U.S. operation was 71.5%, compared with 69.2% for 2002. The claims ratio for our Canadian operation was 83.7% compared to 78.3% for 2002. The results for 2003 and 2002 reflect increases in provisions for unpaid claims occurring prior to December 31, 2002 and December 31, 2001, respectively. These increases amounted to approximately $196.8 million, which increased the claims ratio by 8.3% for 2003, compared to $101.1 million and 5.8%, respectively, for 2002.

For our U.S. operations, prior years claims development increased the claims incurred by $92.8 million, a 5.1% increase to the claims ratio, in 2003 compared to $35.3 million, a 2.7% increase to the claims ratio in 2002. In 2003, the source of the prior years development in the U.S. operation was primarily split between long haul trucking ($18.4 million), and non-standard auto ($45.2 million). Our MGA non-standard automobile business represented $21.1 million of the total U.S. operations prior years claims development in 2003 compared to $1.3 million in 2002. We adjusted our initial loss development factors on a number of our MGA programs to reflect actual loss trends experienced in 2003 and these new loss development factors will be used in the prospective reserving process. Florida non-standard auto contributed $19.2 million of the adverse development in 2003, compared to $9.5 million in 2002. Continued cost escalation of loss adjusting expenses and an increase in the number of files litigated in Florida non-standard auto required upward adjustments to open claims reserves for both the current and prior years.

For our Canadian operations, prior years claims development increased the claims incurred by $104.0 million, a 18.8% increase to the claims ratio, in 2003 compared to $65.8 million, a 15.9% increase to the claims ratio, in 2002. Kingsway General s Alberta non-standard automobile business contributed $34.5 million of the prior years claims development in 2003, compared to $16.3 million in 2002. An increase in average reserves due to the continued escalation in bodily injury claim settlements was the reason for the adverse claims development in 2003 for Alberta non-standard automobile, where we increased existing case reserves based on actual settlement patterns. Our Ontario private passenger automobile business contributed $32.8 million of the prior years claims development in 2003, compared to $26.4 million in 2002. Continued health care cost inflation and bodily injury award increases beyond expected levels required reserve levels to be increased on open files for Ontario non-standard automobile on average by approximately 56% in 2003. Our Canadian trucking business contributed $14.0 million to the 2003 prior years claims development, compared to $6.4 million in 2002. Increases in reserves were due to larger than anticipated settlements, particularly in the U.S., which required upward adjustments to open claim files. Average claim file reserves were increased in 2003 to reflect this pattern of settlement. Our commercial automobile business in Canada contributed $18.6 million of the prior years claims development in 2003 compared to $8.7 million in 2002. Case reserves were increased to reflect the increased cost on injury claims similar to the development experienced on the Ontario automobile business. We conducted a detailed claim file review of our Canadian operations during 2003 to determine the adequacy of case reserving. As a result, revised guidelines have been established for setting reserves for new bodily injury and accident benefit claims in all provinces and for all lines of business. In addition, new Ontario automobile regulations curtailing health care costs and increasing tort award deductibles should reduce the cost escalation trends experienced over the last several years.

Underwriting Expenses

Our expense ratio for 2003 improved to 27.1% compared to 28.4% in 2002. The expense ratio for our Canadian operations for 2003 was 28.1%, compared to 30.1% in 2002 and the expense ratio for our U.S. operations was 26.8% and 28.0%, respectively, in 2003 and 2002. In order to be more consistent with industry practice and the treatment of expenses on MGA business, effective October 1, 2002, we initiated the deferral of underwriting and marketing costs relating to the acquisition of premiums on all of our business, where previously such deferral was applied only to our MGA business. The impact of this change was an increase in net income of $7.4 million for 2003 compared to $4.2 million in 2002.

Combined Ratio

The combined ratio deteriorated to 101.4% compared with 99.8% in 2002, which produced an underwriting loss of $33.9 million compared with an underwriting profit of $2.6 million in 2002. For 2003, our U.S. operations combined ratio was 98.3% (97.2% in 2002) and for our Canadian operations combined ratio increased to 111.8% (108.4% in 2002). The combined ratio increased by 8.3% and 5.8% for the year ended December 31, 2003 and 2002, respectively, due to prior year claims development. For our U.S. operations prior year claims development increased the combined ratio by 5.1% in 2003 and 2.7% in 2002, and for the Canadian operations by 18.8% in 2003 and 15.9% in 2002. Assessments from the residual market (Facility Association) in Ontario were $6.3 million in 2003 and $1.4 million in 2002 which also increased the Canadian operations combined ratio by 1.1% in 2003 and 0.3% in 2002.

Interest Expense

Interest expense for 2003 was $21.0 million, compared to $12.3 million in 2002, reflecting the issuance of $78 million in senior unsecured debentures in December 2002 and several private placements of 30-year floating rate subordinated debentures in the U.S. totaling $116.0 million.

Net Income and Earnings Per Share

Income before income taxes for 2003 increased by 10% to $77.6 million, compared to $70.7 million in 2002. Income taxes were affected by income generated in lower tax jurisdictions coupled with losses from our Canadian operations in both 2002 and 2003. Net income for 2003 was $85.3 million, a 7% increase over the $79.5 million reported for 2002. Diluted earnings per share were $1.62 for 2003, compared to $1.61 for 2002.

Currency Translation

We report our results in Canadian dollars whereas we have a significant part of our operations denominated in U.S. dollars. During 2003 the Canadian dollar appreciated significantly against the U.S. dollar which impacted our reported results in 2003 compared to 2002. Currency translation reduced gross premiums written by $234.8 million, net premiums earned by $226.1 million, investment income by $10.8 million, net income by $10.5 million and earnings per share by $0.20 compared to the same translation rates prevailing in 2002.

Book Value Per Share and Return on Equity

For 2003, shareholders equity was reduced by $105.4 million and book value per share by $1.88 or 18% as a result of the unrealized currency translation adjustment on the conversion of the investment in the U.S. operations into Canadian dollars. Despite this adjustment, book value per share increased to $12.63 from $12.56 at December 31, 2002.

Our annualized return on equity was 12.9% for 2003 compared to 13.8% in 2002.

Balance Sheet

Total assets as at December 31, 2003 grew to $3.6 billion, compared to $3.0 billion as at December 31, 2002. The investment portfolio, including cash and accrued investment income, increased to $2,674.1 million (market value $2,726.7 million), compared to $2,094.9 million (market value $2,127.5 million) as at December 31, 2002. Investment portfolio per share increased 12% to $47.90 compared to $42.93 as at December 31, 2002. Unrealized gains on the investment portfolio were $52.5 million (94 cents per share outstanding) at December 31, 2003 compared to $32.6 million (67 cents per share) at December 31, 2002.

Results of Operations

For the years ended December 31, 2002 and 2001

Gross Premiums Written

Our gross premiums written in 2002 increased 99% to $2.1 billion, compared with $1.1 billion in 2001. Gross premiums written for our U.S. operations in 2002 increased 130% to $1.6 billion, compared with $709.2 million in 2001. For 2002, U.S. operations represented 77% of gross premiums written compared with 67% in 2001. Gross premiums written from Canadian operations in 2002 increased 38% to $490.8 million compared with $356.0 million in 2001.

Gross premiums written from non-standard automobile increased 52% to $828.1 million over 2001. Non-standard automobile insurance covers drivers 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. In 2002, we continued to experience both volume growth and rate increases in most of our non-standard automobile markets. In Canada, we implemented rate increases in early 2002 and again in the third quarter of 2002 to improve the profitability of our Ontario automobile business. During the third quarter, we obtained approval for a rate increase as well as permission to eliminate certain classes of risk in Ontario. The impact of these initiatives was to increase rates by an average of 22.3% and for many of our policyholders in the metropolitan Toronto area by over 40%. We currently do not offer policy terms of longer than six months duration for non-standard automobile in Ontario. Our Canadian operations experienced a 41% increase in non-standard automobile premiums and our U.S. operations experienced a 55% increase from existing markets compared to 2001. In 2002, gross premiums written from trucking and commercial automobile increased 175% to $844.4 million compared to $307.2 million in 2001. As a result of the market conditions, we experienced growth through additional new business as well as through the ability to charge higher premiums for the business. Trucking and commercial automobile represented 40% of gross premiums written in 2002 compared with 29% in 2001.

The programs that we started to implement with MGAs in the United States during the last half of 2001 for non-standard automobile, trucking and commercial automobile expanded in 2002. In 2002 these programs generated $961.4 million or 45% of our gross premiums written compared with $206.0 million or 19% in 2001. We were able to grow this aspect of our business due to limited competition, and as a result, we were able to implement more favorable pricing than the companies we replaced. In each of these arrangements, the MGAs compensation is dependent on the underwriting profit they generate.

American Country was acquired on April 5, 2002 and its results have been consolidated with our U.S. operations since March 31, 2002. American Country contributed $36.0 million or 3% of the increase in our gross premiums written during 2002.

Net Premiums Written

Net premiums written in 2002 increased 98% to $2.0 billion compared with $1.0 billion for 2001. Net premiums written from our U.S. operations in 2002 increased 128% to $1.5 billion compared with $679.1 million for 2001. Net premiums written from our Canadian operations increased 38% to $463.0 million from $335.9 million for 2001. The increase in net premiums written is attributable to the aforementioned increases in gross premiums written. In 2002, reinsurance premiums ceded represented 5.4% of gross premiums written compared to 4.7% in 2001 as a result of the increased cost of reinsurance coverages.

Net Premiums Earned

Net premiums earned for 2002 increased 99% to $1.7 billion, compared with $872.8 million for 2001. For U.S. operations, net premiums earned for 2002 increased 140% to $1,322.5 million compared with $550.9 million in 2001. Net premiums earned from our Canadian operations for 2002 increased by 29% to $415.2 million compared with $321.9 million for 2001. Earned premiums grew due to the increase in written premiums.

Investment Income

Investment income for 2002 increased to $64.9 million compared with $52.6 million for 2001. The growth in our premiums written generated positive cash flow from operations which increased the investment portfolio by $600.4 million during 2002, which was offset by the impact of lower interest rates.

Net Realized Gains

Net realized gains amounted to $16.3 million in 2002 compared with $12.1 million in 2001. Included in net realized gains were adjustments to the carrying value of investments for declines in market value considered other than temporary of $6.6 million in 2002 compared to $1.2 million in 2001.

Claims Incurred

Our claims ratio for 2002 was 71.4%, compared to 70.6% for 2001. The claims ratio for the U.S. operations for 2002 was 69.2% compared with 68.9% for 2001. The slight deterioration in the U.S. operations claims ratio was a reflection of adverse claims development amounting to $35.2 million. The claims ratio for our Canadian operations in 2002 was 78.3% compared to 73.5% for 2001. The claims ratio for our Canadian operations was adversely influenced by results from our Ontario automobile business, which experienced $63.9 million of adverse prior year claims development. The claims ratio for the Canadian operation for 2002 was 64.6% excluding our Ontario automobile business. For 2002, net premiums earned from our Ontario automobile business amounted to $137.0 million, which produced claims incurred of $145.3 million.

Underwriting Expenses

Our expense ratio for 2002 was 28.4%, compared to 28.5% for 2001. The expense ratio for Canada for 2002 was 30.1%, compared to 29.6% for 2001, and the expense ratio for the U.S. for 2002 was 28.0%, compared to 27.9% for 2001. In order to be more consistent with industry practice and the treatment of expenses on our MGA business, effective October 1, 2002 we initiated the deferral of underwriting and marketing costs relating to the acquisition of premiums on all of our business, where previously such deferral was applied only to our MGA business. The impact of this change was to defer an additional $6.6 million of underwriting expenses, which reduced the expense ratio by 0.3% for the year.

Combined Ratio

The combined ratio of 99.8% for 2002 produced an underwriting profit of $2.6 million, compared with $7.6 million profit reported in 2001. For 2002, the U.S. operations combined ratio was 97.2% (96.8% in 2001) and for the Canadian operations the combined ratio was 108.4% (103.1% in 2001). The results of our Canadian operations were adversely affected by results from our Ontario automobile business due to increases in accident benefit loss costs. In 2002, the U.S. operations produced an underwriting profit of $37.5 million compared to an underwriting profit of $17.5 million in 2001. The Canadian operations produced an underwriting loss of $34.9 million compared to a underwriting loss of $9.8 million for 2001. For 2002, our Ontario automobile business generated $137.0 million, or 8%, of net premiums earned at a combined ratio of 131.4%, and produced an underwriting loss of $43.1 million. The combined ratio for 2002 and 2001 was influenced by adverse development on prior year claims. In 2002, adverse development of prior year claims amounted to $101.1 million, which increased the combined ratio by 5.8% for the year. Adverse development for prior year claims during the year ended December 31, 2001 amounted to $33.9 million, which increased the combined ratio by 3.9% in 2001.

Interest Expense

Interest expense in 2002 was $12.3 million, compared to $11.4 million for 2001. The increase was primarily the result of an increase in our bank debt during the year.

Net Income and Earnings Per Share

Our net income for 2002 increased 77% to $79.5 million, compared to $44.9 million in 2001. As a result of a higher proportion of income before tax being generated in lower tax jurisdictions, and net losses incurred in higher tax jurisdictions, in 2002, we reported a consolidated income tax credit of $8.8 million compared to an income tax expense of $10.1 million in 2001. Prior to January 1, 2002, we amortized goodwill arising from acquisitions over the applicable useful life of the asset acquired, which in 2001 resulted in expense of $5.8 million after tax. Diluted earnings per share for 2002 were $1.61, compared to $1.19 in 2001 on 31% more shares outstanding in 2002.

Book Value Per Share and Return on Equity

Book value per share was $12.56 at December 31, 2002 compared to $11.03 at December 31, 2001. Our return on equity was 13.8% in 2002 compared to 13.3% for 2001. Our investment portfolio increased to $2,094.9 million (market value $2,127.5 million) as at December 31, 2002, compared to $1,235.4 million (market value $1,247.0 million) as at December 31, 2001.

Financial Condition

Liquidity and Capital Resources

The purpose of liquidity management is to ensure that there is sufficient cash to meet all financial commitments and obligations as they fall due. We believe that we have the flexibility to obtain, from internal sources, the funds needed to fulfill our cash requirements during the current financial year and also to satisfy regulatory capital requirements. However, such funds may not provide sufficient capital to enable us to pursue additional market opportunities.

Our insurance operations create liquidity by collecting and investing premiums from new and renewal business in advance of earning those premiums and paying claims. This creates a liquid float of money that we hold on behalf of our policyholders. We earn investment income on this float until we pay the claim. As long as we continue to grow and remain profitable, the float grows and continues to be available for investment. Net cash provided from the growth in operations in 2001 was $207.3 million, in 2002 was $600.4 million, and in 2003 was $617.2 million which significantly increased our investment portfolio. Net cash provided by financing activities in 2001 was $200.7 million, in 2002 was $129.5 million, and in 2003 was $229.4 million. The following is a description of our various financing arrangements.

Bank Indebtedness

In February 1999, we entered into a US$100 million five-year fixed term unsecured credit facility at a fixed rate of LIBOR plus a spread which varied with our credit rating. We drew down the facility in full and entered into an interest rate swap transaction whereby we fixed our rate at 5.91% plus a spread based on our credit rating or the ratio of funded debt to total capitalization, whichever is higher, for the term of the facility. As of December 31, 2003, we were in compliance with all of the covenants of this credit facility and we had a principal balance of $101.9 million (US$80 million). A principal repayment of US$2.5 million was paid before December 31, 2003. This facility matured in March 2004.

In May 2002, we entered into a $66.5 million 364 day revolving credit facility at a floating interest rate determined based on the type of loan and our senior unsecured debt rating. The facility was renewed in May 2003. As of December 31, 2003, the effective interest rate was approximately 3%, we were in compliance with all of the covenants of this credit facility and we had approximately $53.0 million outstanding.

In March 2004 we entered into a $150 million revolving credit facility with Canadian Imperial Bank of Commerce, LaSalle Bank National Association and The Bank of Nova Scotia which replaced the US$100 million and $66.5 million facilities. The debt is guaranteed by Kingsway America and has a maturity date of March 4, 2005. The credit facility contains numerous covenants that limit our ability, among other things, to borrow money, make particular types of investments or other restricted payments, sell assets, merge or consolidate, pay dividends or redeem capital stock, and incur liens to secure indebtedness. The facility also requires us to maintain specified financial ratios.

Canadian Senior Debenture Offering

On December 6, 2002, Kingsway Financial sold $78 million aggregate principal amount of 8.25% senior unsecured debentures due December 31, 2007. The net proceeds of the offering amounted to approximately $77.1 million, after the application of the underwriters discount and commission. The yield on the debentures to maturity is 8.298%. The debentures are unconditionally guaranteed by Kingsway America. Kingsway Financial s obligations under, and Kingsway America s guarantee of, the debentures will rank equally with the senior notes described below. We used a portion of the net proceeds of the senior unsecured debentures to provide approximately $50 million to Kingsway America to support the growth of our U.S. operations, approximately $16.4 million to pay a portion of the amount outstanding under our $66.5 million unsecured revolving credit facility and the balance for general corporate purposes.

U.S. Senior Note Offering

In January 2004 Kingsway America Inc. issued US$100 million 7.50% senior notes due 2014 in a private offering. The notes are fully and unconditionally guaranteed by Kingsway Financial. The notes will be redeemable at Kingsway America s option on or after February 1, 2009. Approximately US$60 million was used to repay existing bank indebtedness and the remainder will be used for general corporate purposes. In March 2004 the senior notes offering was reopened and an additional US$25 million of these senior note were issued. The proceeds from this reopening were used to repay existing bank indebtedness.

Subordinated Debt

Since December 2002, Kingsway America issued US$90.5 million in 30-year subordinated deferrable interest debentures in six private placement transactions. This subordinated debt is described in more detail in the Contractual Obligations table and note thereto set forth below.

Contractual Obligations

	Payments Due by Period					
(in thousands of Canadian dollars)	**2004**	**2005**	**2006**	**2007**	**Thereafter**	**Total**
Contractual Obligations						
Bank indebtedness	$153,895	$ --	$ --	$ --	$ --	$153,895
Senior unsecured debentures (1)	--	--	--	78,000	--	78,000
Subordinated indebtedness	--	--	--	--	115,981	115,981
Other liabilities	2,695	--	--	--	--	2,695
Total	$156,590	$ --	$ --	$78,000	$115,981	$350,571

1. Between December 4, 2002 and December 16, 2003, six subsidiary trusts of the Company issued U.S.$90.5 million of 30 year capital securities to third parties in separate private transactions. In each instance, a corresponding floating rate junior subordinated deferrable interest debenture was then issued by Kingsway America Inc. to the trust in exchange for the proceeds from the private sale. The floating rate debentures bear interest at the rate of the London interbank offered interest rate for three-month U.S. dollar deposits, plus spreads ranging from 3.85% to 4.20%, but until dates ranging from December 4, 2007 to January 8, 2009, the interest rates will not exceed 12.45% to 12.75%. The Company has the right to call each of these securities at par anytime after five years from their issuance until their maturity. These debentures are unconditionally guaranteed by Kingsway Financial. The floating rate debenture issued by Kingsway America and Kingsway Financial s guarantee of all debentures will rank junior to the senior notes issued by Kingsway America and the guarantee thereof by Kingsway Financial. The net proceeds to the Company were $95,613,000 in 2003 and $22,198,000 in 2002 after deducting expenses of $6,273,000 and $1,438,000, respectively. The proceeds were used to increase the capital of our U.S. insurance subsidiaries.

As a result of our capital raising activities, our debt service requirements are significantly higher than in prior years. As of December 31, 2003, on a pro forma basis, giving effect to Kingsway America s issuance of US$125 million 7.50% senior notes due 2014, we would have had approximately $398.8 million of total indebtedness. The total amount of our debt service obligations in 2004 is expected to be approximately $26 million. For the year 2003, under the various insurance regulatory restrictions, based on our December 2003 financial statements, our insurance and reinsurance subsidiaries would have aggregate dividend capacity of $212.9 million. Kingsway America s payments under its debt obligations are funded through dividends from its U.S. subsidiaries and capital infusions by Kingsway Financial.

Off-Balance Sheet Financing

We do not engage in any off-balance sheet financing arrangements.

Common Share Offering

In July 2003, Kingsway Financial sold 6.71 million common shares. The shares were sold only in Canada at a price of $16.70 per share resulting in total gross proceeds of $112.1 million. Approximately $102.4 million of the proceeds of the offering were used to increase the capital of certain of our insurance subsidiaries, and the remainder used for general corporate purposes.

Standard & Poor s Rating of Kingsway Financial s Counterparty Credit and Senior Unsecured Debt

On September 30, 2003, Standard & Poor s Ratings Services placed the counterparty credit and senior unsecured debt ratings of Kingsway Financial on CreditWatch with negative implications. The credit watch placement followed the announcement by Kingsway that it had identified a shortfall in its prior years claims reserving for Kingsway General.

On October 31, 2003, Standard & Poor s announced that it had removed Kingsway Financial from CreditWatch and lowered its counterparty and senior unsecured debt credit ratings on Kingsway Financial to BBB- from BBB with a stable outlook. According to Standard & Poor s, a BBB- rating (fourth out of nine rating levels) indicates that the obligor has adequate capacity to meet its financial obligations; however, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitments. A plus or minus designation within a ratings category indicates relative standing within the category.

On January 29, 2004, Standard & Poor s issued its rating of BBB- on the US$100 million of our senior notes due 2014 issued in the private offering completed in January 2004. On March 8, 2004, Standard & Poor s issued its rating of BBB- on an additional US$25 million of our senior notes due 2014 issued in the private offering completed in March 2004. According to Standard & Poor s, a BBB- rating (fourth out of nine rating levels) indicates that the obligation has adequate protection parameters; however, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitments under the obligation. A plus or minus designation within a ratings category indicates relative standing within the category.

DBRS s Rating of our Senior Debentures and Senior Notes

On October 3, 2003, Dominion Bond Rating Service Limited (DBRS) confirmed its previous rating of BBB with a stable outlook on the Senior Debentures. According to DBRS, a BBB rating (fourth out of nine rating levels) indicates that protection of interest and principal is considered adequate, but that the entity is more susceptible to adverse changes in financial and economic conditions, or there may be other adversities present which reduce the strength of the entity and its rated securities. DBRS also assigned a rating trend of stable to our Senior Debentures. According to DBRS, a rating trend gives an indication of what direction the rating in question is headed should the given conditions and tendencies continue.

On February 3, 2004, DBRS issued its rating of BBB with a stable outlook on US$100 million of our senior notes issued in the private offering completed in January 2004. On March 9, 2004, DBRS issued its rating of BBB with a stable outlook on an additional US$25 million of our senior notes issued in the private offering completed in March 2004.

Impact of Ratings Changes

We would expect that a downgrade in our rating by either Standard & Poor s or DBRS would have a negative impact on our business, such as causing an increase in the interest rate on our bank credit facility.

Shareholders Equity

As a result of the common share offering and our profitability, shareholders equity increased to $705.0 million at December 31, 2003 compared to $612.9 million at December 31, 2002. During 2003, shareholders equity was negatively impacted by the unrealized currency translation adjustment of our U.S. dollar denominated net assets into Canadian dollars amounting to $105.4 million. Book value per share outstanding was $12.63 per share at December 31, 2003, an increase compared to $12.56 per share at December 31, 2002. Book value per share at December 31, 2003 was reduced by $1.88 or 13% due to the unrealized currency translation adjustment of our U.S. dollar denominated net assets into Canadian dollars. Book value per share outstanding increased 17% in 1998, 2% in 1999, 13% in 2000, 38% in 2001 and 14% in 2002.

Legal Proceedings

In the ordinary course of business, we are, from time to time, involved in various claims and legal proceedings, including class actions. While it is not possible to estimate the final outcome of these various proceedings at this time, we do not believe the outcome of such proceedings will have a material impact on our results.

On July 25, 2003, Kingsway commenced an action against PricewaterhouseCoopers, LLP, Miller, Herbers, Lehman & Associates, Inc. and the former Directors of American Country relating to the understatement of the reserves of American Country s insurance subsidiary for the years 1998 through 2001 and associated costs and damages thereon. These reserve deficiencies occurred prior to our acquisition of American Country in April 2002. As a result of the deficiencies, we restated American Country s financial results for the years ended December 31, 2001 and 2000 and the three months ended March 31, 2002.

Systems and Technology

We believe that efficient information systems are important to processing policies and claims and retrieving information quickly to interface with our agents, MGAs and brokers and insureds. Although we believe our current information systems are sufficient to support the expected growth in our business, we are reviewing our systems with the intent of significantly upgrading and improving their capabilities. We are also in the process of implementing and expanding an electronic imaging system in our insurance subsidiaries to provide immediate access to all data and files and reduce the cost of storage and filing. We also have a point-of-sale system to make our products readily available through our agents, MGAs and brokers network, providing our agents, MGAs and brokers with a direct interface and allowing them to quote and issue policies electronically. We expect the enhancements and additions to our systems to increase our operating efficiencies and reduce our operating costs, and to help us strengthen our important relationships with our independent agents, MGAs and brokers.

Employees

As of December 31, 2003, we employed approximately 2,027 personnel, of whom approximately 709 are located in Canada and approximately 1,318 are located in the United States. None of our employees are represented by a labor union and we have never experienced a work stoppage. We believe our relationship with our employees is good.

Risk Factors

Our insurance subsidiaries provision for unpaid claims may be inadequate, which would result in a reduction in our net income.

Our insurance subsidiaries provisions for unpaid claims do not represent an exact calculation of our actual liability, but are estimates involving actuarial and statistical projections at a given point in time of what we expect to be the cost of the ultimate settlement and administration of known and unknown claims. 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 and as such, the process is inherently complex and imprecise. Actual losses from claims may deviate, perhaps substantially, from the provisions for unpaid claims reflected in our financial statements. As of December 31, 2003, our provisions for unpaid claims were $1,669.7 million, which we believe are adequate.

We base our provisions for unpaid claims on facts and circumstances then known, estimates of future trends in claims severity and other variable factors such as inflation. Furthermore, factors such as inflation, claims settlement patterns, legislative activity and litigation trends, all of which are difficult to predict, may have a substantial impact on our actual claims experience. As time passes and more information about the claims becomes known, the estimates are appropriately adjusted upward or downward to reflect this additional information. Because of the elements of uncertainty encompassed in this estimation process, and the extended time it can take to settle many of the more substantial claims, several years of experience are usually required before a meaningful comparison can be made between actual losses and the original provisions for unpaid claims.

The development of the provisions for unpaid claims is shown by the difference between estimates of claims as of the initial year-end and the re-estimated liability at each subsequent year end. Favorable development (reserve redundancy) means that the original claims estimates were higher than subsequently determined. Unfavorable development (reserve deficiency) means that the original claims estimates were lower than subsequently determined. During 2003, we experienced reserve deficiencies of $196.8 million on prior periods. Of this deficiency, 17% was related to non-standard automobile, standard automobile and motorcycle business in Ontario, 9% was related to our commercial automobile business in Canada, 10% was related to our non-standard automobile business in Florida, 18% was related to our non-standard automobile business in Alberta, 11% to our MGA non-standard automobile programs in the United States, 9% was related to trucking in the United States, and 7% was related to our trucking business in Canada. Although we have made adjustments in our reserving practices to reflect this claims experience, we cannot assure you that these unfavorable trends will not require additional reserves in the future. In addition, we have in the past, and may in the future, acquire other insurance companies. We cannot assure you that the provisions for unpaid claims of the companies that we acquire are or will be adequate.

To the extent our insurance subsidiaries actual claims experience is less favorable than our current claims estimates reflected in our provisions for unpaid claims, we will be required to increase our provisions for unpaid claims which will reduce our profitability in future periods. Moreover, insufficiencies in our insurance subsidiaries provisions for unpaid claims could have a material adverse effect on our results of operations and financial condition.

We may experience difficulty in managing our growth, which could adversely affect our results of operations and financial condition.

We have grown rapidly over the last several years. As a result, our gross premiums increased 66% in 2001, 99% in 2002 and 24% in 2003. This growth may place a strain on our management systems and operational and financial resources. Rapid growth in gross premiums may also place a strain on the surplus of our subsidiaries. We plan to continue to expand our specialty focus into selected regional markets in the United States and Canada and to increase the distribution of our core products in our existing markets. Our future growth and the successful integration and management of new Managing General Agent (MGA) relationships, acquired businesses and other new business involves numerous risks that could adversely affect our growth and profitability, and are contingent on various factors, including:

- expanding our financial, operational and management information systems;
- managing our relationships with independent agents, MGAs and brokers, including maintaining adequate controls;
- expanding our executive management and the infrastructure required to effectively control our growth;
- maintaining ratings for certain of our insurance subsidiaries;
- increasing the statutory capital of our insurance subsidiaries to support additional underwriting;
- accurately setting provisions for claims for new business where we lack historical underwriting experience;
- obtaining regulatory approval for appropriate premium rates; and
- obtaining the required regulatory approvals to offer additional insurance products or expand into additional states and provinces.

We cannot assure you that we will be able to manage our growth effectively or that we will be successful in expanding our business, that our existing infrastructure will be able to support additional expansion or that any new business will be profitable. If we are unable to manage our growth, our results of operations and financial condition may be adversely affected.

We rely on independent agents, MGAs and brokers and are exposed to risks.

We market and distribute our automobile insurance products through a network of over 2,900 independent agents and approximately 20 MGAs in the United States and over 3,000 independent brokers across Canada. In 2003, approximately 56% of our gross written premiums in the United States were sourced through MGAs and approximately 44% were sourced through independent agents. Our insurance products are marketed through a large number of independent agents, MGAs and brokers and we rely heavily on their ability to attract new business. These independent agencies and MGAs typically represent more than one insurance company, which may expose us to competition within the agencies and, therefore, we cannot rely on their commitment to our insurance products. In some markets, we operate pursuant to open market arrangements in which we have no formal relationships with the brokers who place our risk in these markets. Loss of all or a substantial portion of the business provided by these intermediaries could have a material adverse effect on our business, results of operations and financial condition.

Our independent agents, MGAs and brokers generally have the ability to bind insurance policies and a few MGAs may settle claims on our behalf, and we have only limited ability to exercise control over them. In the event that an independent agent, MGA or broker exceeds its authority by binding us on a risk that does not comply with our underwriting guidelines, we may be at risk for that policy until we effect a cancellation. Although to date we have not experienced a material loss from improper use of binding authority by our agents, MGAs or brokers, any improper use of such authority may result in losses that could have a material adverse effect on our business, results of operations and financial condition.

In accordance with industry practice, our customers often pay the premiums for their policies to agents, MGAs or brokers for payment over to us. These premiums are considered paid when received by the agent, MGA or broker and thereafter the customer is no longer liable to us for those amounts, whether or not we have actually received the premiums from the agent, MGA or broker. Consequently, we assume a degree of risk associated with our reliance on independent agents, MGAs and brokers in connection with the settlement of insurance balances.

In addition, MGAs are subject to regulation as insurance producers, including licensing requirements, and, to the extent that the MGA has the ability to bind insurance policies and to settle claims, the MGA is subject to regulation of these functions. Noncompliance by any of our MGAs with applicable regulatory requirements could have adverse regulatory implications on us.

Engaging in acquisitions involves risks and, if we are unable to effectively manage these risks, our business may be materially harmed.

From time to time we engage in discussions concerning acquisition opportunities, although we cannot assure you that any such discussions will result in a transaction. As a result of such discussions, we may enter into acquisition transactions. Acquisitions entail numerous risks, including the following:

- difficulties in the integration of the acquired business;
- assumption of unknown material liabilities, including deficient provisions for unpaid claims;
- diversion of management s attention from other business concerns;
- failure to achieve financial or operating objectives; and
- potential loss of policyholders or key employees of acquired companies.

We may not be able to integrate successfully any business, operations, personnel, services or products that we may acquire in the future.

The highly competitive environment in which we operate could have an adverse effect on our business, results of operations and financial condition.

The property and casualty markets in which we operate are highly competitive. We compete, and will continue to compete, with major North American and other insurers, many of which have greater financial, marketing and management resources than we do. There may also be other companies that may be planning to enter the insurance industry of which we are not aware. Insurers in our markets generally compete on the basis of price, consumer recognition, coverages offered, claims handling, financial stability, customer service and geographic coverage. Although our pricing is influenced to some degree by that of our competitors, we generally believe that it is not in our best interest to compete solely on price, and may from time to time experience a loss of market share during periods of intense price competition. Our business could be adversely impacted by the loss of business to competitors offering competitive insurance products at lower prices. This competition could affect our ability to attract and retain profitable business.

In our non-standard automobile business, we compete with both large national underwriters and smaller regional companies. Our competitors include other companies that, like us, serve the independent agency market, as well as companies that sell insurance directly to customers. Direct underwriters may have certain competitive advantages over agency underwriters, including increased name recognition, loyalty of the customer base to the insurer rather than to an independent agency and reduced costs to acquire policies. Any new, proposed or potential legislative or industry developments could further increase competition in our markets. New competition from these developments could cause the demand for our products to decrease, which would adversely affect our profitability. In addition, in certain provinces or states, government-operated risk plans may provide non-standard automobile insurance products at a lower price than those we provide.

Additionally, our markets may attract competition from time to time from new or temporary entrants. In some cases, such entrants may, because of inexperience, the desire for new business or for other reasons, price their insurance below the rates that we believe offer an acceptable premium for the related risk. Further, a number of our competitors, including new entrants to our markets, are developing e-business capabilities which may impact the level of business transacted through our more traditional distribution channels or which may affect pricing in the market as a whole.

Our operating results may fluctuate as a result of many factors, including cyclical patterns in the property and casualty insurance industry and in the automobile insurance market.

The results of companies in the property and casualty insurance industry have been subject to significant fluctuations and uncertainties. The industry s profitability can be affected significantly by many factors, including:

- rising costs that are not known by companies at the time they price their products, such as unforeseen case law developments;
- and unpredictable developments, including weather-related and other natural catastrophes;
- changes in insurance and tax laws and regulation, as well as new legislative initiatives; and
- general economic conditions, such as fluctuations in interest rates, inflationary pressures and other changes in the investment environment, which affect returns on invested capital and may impact the ultimate payout of loss amounts.

In addition, the profitability of automobile insurers can be affected significantly by many factors, including:

- regulatory regimes which limit their ability to detect and defend against fraudulent claims and fraud rings;
- developing trends in tort and class action litigation which may encourage frivolous litigation or expose automobile insurers to allegations of bad faith;
- changes in consumer protection laws which could limit the use of used or like kind and quality after-market parts or to compel compensation for alleged diminution in value notwithstanding repair of the vehicle; and
- changes in laws or regulations, including the adoption of consumer initiatives regarding rates charged for automobile or other insurance coverage or claims handling procedures.

The financial performance of the property and casualty insurance industry has historically tended to fluctuate in cyclical patterns of soft markets characterized generally by increased competition resulting in lower premium rates followed by hard markets characterized generally by lessening competition and increasing premiums rates. Although an individual insurance company s financial performance depends on its own specific business characteristics, the profitability of most property and casualty insurance companies tends to follow this cyclical market pattern with profitability generally increasing in hard markets and decreasing in soft markets.

Our operations are restricted by the terms of our credit agreements and debt indentures, which could limit our ability to plan for or to react to market conditions or meet our capital needs.

Our credit agreements and debt indentures contain numerous covenants that limit our ability, among other things, to borrow money, make particular types of investments or other restricted payments, sell assets, merge or consolidate, pay dividends or redeem capital stock, and incur liens to secure indebtedness. These agreements also require us to maintain specified financial ratios, including a requirement that we maintain on a consolidated basis a specified ratio of net premiums written to statutory capital and surplus, or capital surplus ratio. The covenants under our debt agreements could limit our ability to plan for or react to market conditions or to meet our capital needs. Our ability to comply with the capital surplus ratios and other financial covenants in these agreements may be affected by events beyond our control and we may have to curtail some of our operations and growth plans to maintain compliance.

If we are not able to comply with the covenants and other requirements contained in our credit agreements and debt indentures, an event of default under the relevant debt instrument could occur. If an event of default does occur, it could trigger a default under our other debt instruments, we could be prohibited from accessing additional borrowings, and the holders of the defaulted debt instrument could declare amounts outstanding with respect to such debt to become immediately due and payable. Upon such an event, our assets and cash flow may not be sufficient to fully repay borrowings under our outstanding debt instruments. In addition, such a repayment under an event of default could adversely affect our liquidity and force us to cease or substantially slow our growth.

If we are unable to maintain our current claims-paying ratings, our ability to write insurance and compete with other insurance companies may be adversely impacted.

Third party rating agencies assess and rate the claims-paying ability of insurers and reinsurers based upon criteria established by the rating agencies. Periodically these rating agencies evaluate us to confirm that we continue to meet the criteria of the ratings previously assigned to us. Financial strength ratings are an important factor in establishing the competitive position of insurance companies and may be expected to have an effect on an insurance company s premiums.

Our insurance subsidiaries are rated by A.M. Best, which issues independent opinions of an insurer s financial strength and ability to meet policyholder obligations. Our Canadian subsidiaries, Kingsway General Insurance Company and York Fire & Casualty Insurance Company possess a B++ (very good) rating from A.M. Best (5th highest of 15 rating levels) and Jevco Insurance Company, possesses an A- (Excellent) rating from A.M. Best (fourth highest of 15 rating levels).

Of our U.S. subsidiaries, Lincoln General Insurance Company and Universal Casualty Company have an A- (Excellent) rating (fourth highest of 15 rating levels), American Service Insurance Company, Inc. has a B++ (Very Good) rating (fifth highest of 15 rating levels), American Country Insurance Company and Southern United Fire Insurance Company have a B+ (Very Good) rating (sixth highest of 15 rating levels), and U.S. Security Insurance Company has a B (Fair) rating (seventh highest of 15 rating levels). According to A.M. Best, companies rated as A and A- (Excellent) are deemed secure and are assigned to insurers which have, on balance, excellent balance sheet strength and operating performance and business profile when compared to the standards established by A.M. Best and, in A.M. Best s opinion, have a strong ability to meet their ongoing obligations to policyholders. According to A.M. Best, companies rated as B++ and B+ (Very Good) are deemed secure and are assigned to insurers which have, on balance, very good balance sheet strength and operating performance and business profile when compared to the standards established by A.M. Best and, in A.M. Best s opinion, have a good ability to meet their ongoing obligations to policyholders. According to A.M. Best, companies rated as B (Fair) are deemed vulnerable and are assigned to insurers which have, on balance, fair balance sheet strength and operating performance and business profile when compared to the standards established by A.M. Best and, in A.M. Best s opinion, have an ability to meet their ongoing obligations to policyholders.

On March 5, 2004, A.M. Best lowered the financial strength rating of Kingsway General and York Fire to B++ (Very Good) from A- (Excellent) and assigned a negative outlook. A.M. Best stated that the lowered ratings of Kingsway General and York Fire were based on their operating and underwriting performance and weak capitalization, partially offset by significant rate increases in 2002 and 2003, the strengthening of loss reserves, the progress made to reduce claim costs, as well as the explicit financial support of Kingsway Financial. In addition, A.M. Best has concerns regarding the impact of regulatory changes to automobile insurance products occurring in Ontario and Alberta on the profitability of Kingsway General and York Fire. A.M. Best also stated that the financial strength ratings of all of our insurance subsidiaries in both the United States and Canada will remain under pressure pending our ability to lower underwriting leverage by raising capital, meeting our 2004 profit targets, controlling premium growth and eliminating adverse loss reserve development.

We cannot assure you that A.M. Best will not downgrade our ratings or place them under review with negative implications, in the future. If we are unable to maintain our current ratings, our ability to write insurance business and compete with other insurance companies may be adversely affected. Rating agencies evaluate insurance companies based on financial strength and the ability to pay claims, factors which are more relevant to policyholders than investors. Financial strength ratings by rating agencies are not ratings of securities or recommendations to buy, hold or sell any security.

The majority of our gross premiums written are derived from the non-standard automobile and trucking insurance markets. If the demand for insurance in these markets declines, our results of operations could significantly decline.

For the year ended December 31, 2003, approximately 36.6% of our gross premiums written were attributable to non-standard automobile and 30.7% were attributable to trucking insurance. The size of both the non-standard automobile and trucking insurance markets can be affected significantly by many factors outside of our control, such as the underwriting capacity and underwriting criteria of standard automobile insurance carriers and trucking insurers, and we may specifically be affected by these factors. Additionally, an economic downturn in one or more of our principal markets could result in fewer automobile sales and a lower volume of goods shipped by truck resulting in less demand for these insurance products. To the extent that these insurance markets are affected adversely for any reason, our gross premiums written will be disproportionately affected due to our substantial reliance on these insurance markets.

If we fail to comply with applicable insurance laws or regulatory requirements, our business, results of operations and financial condition could be adversely affected.

As an insurance company, we are subject to numerous laws and regulations. These laws and regulations delegate regulatory, supervisory and administrative powers to federal, provincial or state insurance commissioners and agencies. Such regulation generally is designed to protect policyholders rather than shareholders, and is related to matters including:

- rate setting;
- risk-based capital and solvency standards;
- restrictions on the amount, type, nature, quality and quantity of investments;
- the maintenance of adequate reserves for unearned premiums and unpaid claims;
- restrictions on the types of terms that can be included in insurance policies;
- standards for accounting;
- marketing practices;
- claims settlement practices;
- the examination of insurance companies by regulatory authorities, including periodic financial and market conduct examinations;
- the licensing of insurers and their agents;
- limitations on dividends and transactions with affiliates;
- approval of certain reinsurance transactions; and
- insolvency proceedings.

In addition, these statutes typically require us periodically to file financial statements and annual reports, prepared on a statutory accounting basis, and other information with insurance regulatory authorities, including information concerning our capital structure, ownership, financial condition and general business operations. We allocate considerable time and resources to comply with these requirements.

Any failure to comply with applicable laws or regulations could result in the imposition of fines or significant restrictions on our ability to do business, which could adversely affect our results of operations or financial condition. In addition, any changes in laws or regulations, including the adoption of consumer initiatives regarding rates charged for automobile or other insurance coverage or claims handling procedures, could materially adversely affect our business, results of operations and financial condition.

In the past, various state insurance departments have levied fines on some of our subsidiaries in connection with regulatory examinations. During the most recently completed insurance regulatory examinations of certain of our U.S. insurance subsidiaries, the insurance departments conducting the examinations raised certain regulatory compliance issues, and we expect that some amount of fines will be imposed in connection with one or more of these examinations. The subsidiaries involved are working with the regulators to resolve these issues, and we do not expect that any of these matters will have a material adverse effect on our business.

In order to enhance the regulation of insurer solvency, a risk based capital, or RBC, formula was adopted by the U.S. National Association of Insurance Commissioners, or NAIC, for U.S. insurance companies. State insurance regulators monitor the financial status of an insurer by reviewing the insurer s compliance with RBC requirements. The provinces in Canada in which we operate have similar solvency requirements. If our insurance subsidiaries do not comply with these minimum capital requirements, they may be restricted or prohibited from operating. If our insurance subsidiaries are required to increase their reserves in the future, as a result of unexpectedly poor claims experience or otherwise, they may violate these minimum capital requirements unless we are able to take actions to improve the solvency of those subsidiaries. As a result, our business, results of operations, and financial condition may be materially adversely affected.

It is not possible to predict the future impact of changing federal, state and provincial regulation on our operations, and there can be no assurance that laws and regulations enacted in the future will not be more restrictive than existing laws.

Our business could be adversely affected as a result of changing political, regulatory, economic or other influences.

The insurance industry is subject to changing political, economic and regulatory influences. These factors affect the practices and operation of insurance and reinsurance organizations. Legislatures in Canada, the United States, Barbados, Bermuda and local jurisdictions in which we operate have periodically considered programs to reform or amend their respective insurance and reinsurance systems. Recently, the insurance and reinsurance regulatory framework has been subject to increased scrutiny in many jurisdictions. For example, in the United States, current and proposed federal measures that may affect our business include proposals regarding insurance coverage for terrorism, natural disaster protection and tort reform. In Canada, we experienced an extension of the reporting period during which a plaintiff may bring suit against us under the tort provisions of the current Ontario automobile legislation which negatively impacted our results of operations in 2002 and 2003.

Changes in current insurance regulation may include increased governmental involvement in the insurance industry, initiatives aimed at premium controls, or may otherwise change the business and economic environment in which insurance industry participants operate. In some states, the automobile insurance industry has been under pressure in past years from regulators, legislators or special interest groups to reduce, freeze or set rates at levels that are not necessarily related to underlying costs or risks, including initiatives to roll back automobile and other personal line rates. These changes, if adopted, may limit our ability to price automobile insurance adequately and could require us to discontinue unprofitable product lines, make unplanned modifications of our products and services, or may result in delays or cancellations of sales of our products and services. We cannot predict the future impact of changing laws or regulations on our operations and any changes could have a material adverse effect on our results of operations or financial condition.

Rate freezes on automobile insurance premiums in Ontario and Alberta were effected in October and November of 2003, respectively. The government of Ontario has indicated that the rate freeze is in anticipation of an insurance reform program that would produce sufficient cost reductions to allow insurance companies to reduce premium rates by 10 percent on average. In December 2003 the Ontario legislature passed the Automobile Insurance Rate Stabilization Act of 2003 (the Rate Stabilization Act), which requires insurers to submit their risk classification system and rates for automobile insurance to the Financial Services Commission of Ontario (FSCO) for review and approval. Under this act, FSCO is authorized to require insurers to vary their rate classification system and reduce their rates according to specified criteria. The Alberta government has indicated that its rate freezes are in anticipation of a rate reform program that will reward safe drivers while allowing rate increases to be imposed on drivers with at-fault claims and poor driving records. There is no certainty as to how any legislation adopted in connection with these reforms will impact our Ontario and Alberta automobile business.

Our business may be materially adversely affected if the tax laws of the United States or Canada change or relevant tax authorities successfully challenge our interpretations of these laws.

We operate wholly owned subsidiary reinsurance companies in Barbados and Bermuda for the sole purpose of reinsuring risks from our own subsidiaries. Legislation was proposed in 2002 which would have disallowed a deduction for U.S. income tax purposes for premiums paid to certain specified related reinsurers. If this or similar legislation were to be enacted, this could have the effect of increasing the taxes payable by us or certain of our subsidiaries. We cannot assure you that any such legislation or similar legislation will not be enacted.

Due to our corporate structure and to differences in the tax laws of the United States and Canada, we deduct interest paid on certain of our debt in the United States as well as in Canada. Such deductions are based on our interpretation of applicable tax laws. There is no guarantee that the Internal Revenue Service or any other tax authority will not challenge our interpretation, and if such a challenge were made and were successful, the taxes payable by us or certain of our subsidiaries could be increased. In addition, amendments or changes in applicable income tax laws or regulations, including those arising from judicial decisions or administrative pronouncements, could deny a deduction for interest to taxpayers with a structure similar to ours.

We may not be able to realize our investment objectives, which could significantly reduce our net income.

We depend on income from our investment portfolio for a substantial portion of our earnings. In 2001, 2002, and 2003, net investment income and net realized capital gains accounted for approximately 6.9%, 4.5% and 5.3%, respectively, of our consolidated revenue. A significant decline in investment yields in our investment portfolio or an impairment of securities that we own could have a material adverse effect on our business, results of operations and financial condition. We currently maintain and intend to continue to maintain an investment portfolio comprising primarily fixed income securities. As of December 31, 2003, the fair value of our investment portfolio included $2.2 billion of fixed income securities. For 2001, 2002 and 2003, the change in net unrealized gains in our portfolio reflected an increases of $12.0 million, an increase of $21.0 million, and an increase of $20.0 million, respectively. Due to fluctuations in the yields on fixed income securities, we face reinvestment risk as these securities mature because the funds may be reinvested at rates lower than the maturing security.

Our ability to achieve our investment objectives is affected by general economic conditions that are beyond our control. General economic conditions can adversely affect the markets for interest-rate-sensitive securities, including the extent and timing of investor participation in such markets, the level and volatility of interest rates and, consequently, the value of fixed income securities. In addition, changing economic conditions can result in increased defaults by the issuers of securities that we own. Interest rates are highly sensitive to many factors, including monetary policies, domestic and international economic and political conditions and other factors beyond our control.

General economic conditions, stock market conditions and many other factors can also adversely affect the securities markets and, consequently, the value of the securities we own. We may not be able to realize our investment objectives, which could reduce our net income significantly.

We derive the majority of our premiums from a few geographic areas, which may cause our business to be affected by catastrophic losses or business conditions in these areas.

We derive most of our premiums from a relatively small number of jurisdictions, including Illinois, Florida, Ontario and California. Our results of operations may, therefore, be adversely affected by any catastrophic losses in these areas. Catastrophic losses can be caused by a wide variety of events, including earthquakes, hurricanes, tropical storms, tornadoes, wind, ice storms, hail, fires, terrorism, riots and explosions, and their incidence and severity are inherently unpredictable. Catastrophic losses are characterized by low frequency but high severity due to aggregation of losses, and could result in adverse effects on our results of operations or financial condition. Our results of operations may also be adversely affected by general economic conditions, competition, regulatory actions or other business conditions that affect losses or business conditions in the areas in which we do business.

If reinsurance rates rise significantly or reinsurance becomes unavailable or reinsurers are unable to pay our claims, we may be adversely affected.

We purchase reinsurance from third parties in order to reduce our liability on individual risks. Reinsurance does not relieve us of our primary liability to our insureds. A third party reinsurer s insolvency or inability or unwillingness to make payments under the terms of a reinsurance treaty could have a material adverse effect on our financial condition or results of operations. As of December 31, 2003, we had $176.3 million recoverable from third party reinsurers and other insurers. The majority of these recoverables are unsecured. The losses reported by the reinsurance industry since 2001 have adversely affect the financial resources of some reinsurers and their ability to pay claims. Also, the material decline in the worldwide equity markets and the defaults and credit downgrades on bonds of many companies have contributed to a significant decline in the net equity of some reinsurers.

The amount and cost of reinsurance available to our insurance companies are subject, in large part, to prevailing market conditions beyond our control. Our ability to provide insurance at competitive premium rates and coverage limits on a continuing basis depends in part upon the extent to which we can obtain adequate reinsurance in amounts and at rates that will not adversely affect our competitive position. We cannot assure you that we will be able to maintain our current reinsurance facilities, which generally are subject to annual renewal. If we are unable to renew any of these facilities upon their expiration or obtain other reinsurance facilities in adequate amounts and at favorable rates, we may need to modify our underwriting practices or reduce our underwriting commitments.

Kingsway Financial is a holding company and its operating subsidiaries are subject to dividend restrictions.

Kingsway Financial is an insurance holding company with assets consisting primarily of the capital stock of its subsidiaries. Our operations are and will continue to be limited by the earnings of our subsidiaries and the distribution or other payment of such earnings to us in the form of dividends, loans, advances or the reimbursement of expenses. The payment of dividends, the making of loans and advances or the reimbursement of expenses to us by our subsidiaries is contingent upon the earning of those subsidiaries and is subject to various business considerations. In addition, payments of dividends to us by our insurance and reinsurance subsidiaries are subject to various statutory and regulatory restrictions imposed by the insurance laws of the domiciliary jurisdiction of such subsidiaries, including Barbados and Bermuda. For the year 2004, under these insurance regulatory restrictions, based on our December 31, 2003 financial statements, our insurance and reinsurance subsidiaries would have aggregate dividend capacity of $212.9 million. The inability of our subsidiaries to pay dividends to us could have a material adverse effect on our business and financial condition.

Our business depends upon key employees, and if we are unable to retain the services of these key employees or to attract and retain additional qualified personnel, our business may suffer.

We are substantially dependent on a number of key employees. Our success has been, and will continue to be, dependent on our ability to retain the services of our existing key employees and to attract and retain additional qualified personnel in the future. The loss of the services of any of our key employees, or the inability to identify, hire and retain other highly qualified personnel in the future, could adversely affect the quality and profitability of our business operations. There are no employment contracts in place for any of our executives.

Various factors may inhibit potential acquisition bids that could be beneficial to our shareholder.

Regulatory provisions may delay, defer or prevent a takeover attempt that shareholders may consider in their best interest. For example, under the terms of applicable U.S. state statutes, any person or entity desiring to purchase more than a specified percentage (commonly 10%) of our outstanding voting securities is required to obtain regulatory approval prior to its purchase of our shares. These requirements would generally require a potential bidder to obtain the prior approval by the insurance departments of the states in which our U.S. subsidiaries are domiciled and may require pre-acquisition notification in applicable states that have adopted pre-acquisition notification provisions. Obtaining these approvals could result in material delays or deter any such transaction.

Regulatory requirements could make a potential acquisition of our Company more difficult and may prevent shareholders from receiving the benefit from any premium over the market price of our common shares offered by a bidder in a takeover context. Even in the absence of a takeover attempt, the existence of these provisions may adversely affect the prevailing market price of our common shares if they are viewed as discouraging takeover attempts in the future.

In addition, the Shareholder Rights Plan adopted by our board of directors may also have anti-takeover effects. Our Shareholders Rights Plan is designed to protect our shareholders in the event of unsolicited offers to acquire us, and other coercive takeover tactics which, in the opinion of our board of directors, could impair its ability to represent shareholder interests. The provisions of our Shareholder Rights Plan may render an unsolicited takeover more difficult or less likely to occur or might prevent such a takeover, even though such takeover may offer our shareholders the opportunity to sell their shares at a price above the prevailing market price.

Fluctuations in currency exchange rates could negatively affect our results.

We publish our consolidated financial statements in Canadian dollars. In 2003, 75% of our premiums were from our U.S. operations and are currently denominated in U.S. dollars. Therefore, fluctuations in the U.S.-Canadian dollar exchange rate will impact our results of operations and financial condition from period to period. Our Canadian insurance operations generally write policies denominated in Canadian dollars and invest in Canadian dollars. Our U.S. operations generally write policies denominated in U.S. dollars and invest in U.S. dollars. Although investing in local currencies limits the effect of currency exchange rate fluctuations on local operating results, fluctuations in such rates could affect our operations or results, and do affect the translation of these results into Canadian dollars in our consolidated financial statements. During 2003, shareholders equity was reduced by $105.4 million as a result of the currency translation adjustment of our U.S. dollar denominated assets into Canadian dollars.

DISCLOSURE CONTROLS AND PROCEDURES

A. Evaluation of Disclosure Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, as of the end of the period covered by this annual report have conducted an evaluation of the effectiveness of disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e)) pursuant to Rule 13a-15 promulgated under the Securities Exchange Act of 1934. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective and designed to ensure that all material information required to be filed in this annual report has been made known to them in a timely fashion.

B. Changes in Internal Controls

There have been no significant changes in internal controls, or in factors that could significantly affect internal controls, subsequent to the date our Chief Executive Officer and Chief Financial Officer completed their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

AUDIT COMMITTEE AND AUDIT COMMITTEE FINANCIAL EXPERT

The Registrant s Audit Committee is composed of the following directors: Mr. David H. Atkins (Chair), Mr. Thomas A. Di Giacomo and Mr. F. Michael Walsh. The Registrant s board of directors has determined that Mr. David H. Atkins is an audit committee financial expert and independent, as that term is defined by the New York Stock Exchange s listing standards applicable to the Registrant. The Commission has indicated that the designation of Mr. Atkins as the audit committee financial expert does not deem him an expert for any purpose, impose any duties, obligations or liability on Mr. Atkins that are greater than those imposed on members of the audit committee and board of directors who do not carry this designation or identification, or affect the duties, obligations or liability of any other member of the audit committee or board of directors.

CODE OF ETHICS

The Registrant has adopted a code of ethics and business conduct for all employees and officers. The Registrant has also adopted a code of ethics that applies to Kingsway's principal executive officer, principal financial officer, principal accounting officer and other senior financial personnel. These codes of ethics are available at the Registrant s website, www.kingsway-financial.com/investor.htm.

PRINCIPAL ACCOUNTANT FEES AND SERVICES

KPMG LLP has served as the Registrant s auditors since 1989. In 2003 and 2002, fees for audit, audit-related, tax and other services provided to the Registrant by KPMG LLP were as follows:

Year Ended December 31,	2003	2002
Audit fees	$2,775,000	$2,002,000
Audit-related fees	$ 586,000	$ 460,000
Tax fees	$ 124,000	$ 50,000
Other fees	$ 58,000	$ 122,000
Total	$3,543,000	$2,634,000

Pursuant to the terms of its charter, the Audit Committee establishes the auditors fees. Such fees are based upon the complexity of the matters in question and the time incurred by the auditors. The Audit Committee reviews and considers whether the provision of services other than audit services is compatible with maintaining the auditors independence. In 2003, the Audit Committee considered and pre-approved expenditure limits for the Registrant s auditors and established a system to review and pre-approve the provision of non-audit services by the Registrant s auditors to ensure they are consistent with maintaining the auditors independence. The Audit Committee pre-approved 100% of the services performed by the Registrant s auditors for audit-related and non-audit related services for the year ended December 31, 2003.

A discussion of the nature of the services provided under each category is provided below.

Audit Fees

These are services rendered for the audit of the financial statements or services that are provided for statutory and regulatory filings or engagements and include reporting in connection with the various securities offerings of the Registrant.

Audit-Related Fees

These are fees for assurance and related services that are reasonable related to the performance of the audit or review of financial statements and are not reported in the Audit Fee category. This work included appointed actuary services.

Tax Fees

These services included analyses of various tax matters affecting the Registrant and its subsidiaries.

All Other Fees

These services were mainly actuarial services relating to specific actuarial analyses required by the Registrant.

OFF-BALANCE SHEET ARRANGEMENTS

See page 100 of Item 3 of this report.

CONTRACTUAL OBLIGATIONS

See page 99 of Item 3 of this report.

UNDERTAKING AND CONSENT TO SERVICE OF PROCESS

A. Undertaking

Registrant undertakes to make available, in person or by telephone, representatives to respond to inquiries made by the Commission staff, and to furnish promptly, when requested to do so by the Commission staff, information relating to: the securities registered pursuant to Form 40-F; the securities in relation to which the obligation to file an annual report on Form 40-F; or transactions in said securities.

B. Consent to Service of Process

Registrant has previously filed with the Commission a Form F-X in connection with the registration of Common Shares.

EXHIBITS

The following exhibits are filed as part of this report:

Exhibit Number	Title
1.	Consent of KPMG LLP
99.1	Certification of William G. Star, Chief Executive Officer, pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act

Exhibit Number	Title
99.2	Certification of W. Shaun Jackson, Chief Financial Officer, pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act
99.3	Certification of William G. Star, Chief Executive Officer, pursuant to Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350)
99.4	Certification of W. Shaun Jackson, Chief Financial Officer, pursuant to Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350)
99.5	Page 74 of the 2003 Annual Report of Kingsway Financial Services Inc.
99.6	Page 75 of the 2003 Annual Report of Kingsway Financial Services Inc.

SIGNATURES

Pursuant to the requirements of the Exchange Act, the Registrant certifies that it meets all of the requirements for filing on Form 40-F and has duly caused this annual report to be signed on its behalf by the undersigned, thereto duly authorized.

KINGSWAY FINANCIAL SERVICES INC.

May 11, 2004

By: /s/ W. Shaun Jackson

W. Shaun Jackson
Executive Vice President and
Chief Financial Officer

EXHIBIT INDEX