FEDERATED NATIONAL HOLDING CO
Form 10-Q
November 08, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED September 30, 2016

OR

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

FOR THE TRANSITION PERIOD FROM ___________________TO _______________________

Commission File number 000-25001

Federated National Holding Company

(Exact name of registrant as specified in its charter)

Florida (State or Other Jurisdiction of Incorporation or Organization)	65-0248866 (IRS Employer Identification Number)
14050 N.W. 14th Street, Suite 180, Sunrise, FL (Address of principal executive offices)	33323 (Zip Code)

800-293-2532

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has electronically submitted and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of November 4, 2016, the registrant had 13,801,757 shares of common stock outstanding.

Table of Contents

FEDERATED NATIONAL HOLDING COMPANY

TABLE OF CONTENTS

Table of Contents

PART I: FINANCIAL INFORMATION

Item 1. Financial Statements

FEDERATED NATIONAL HOLDING COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

(Unaudited)

	September 30, 2016	December 31, 2015
ASSETS		
Investments:		
Debt securities, available-for-sale, at fair value (amortized cost of $370,881 and $338,021, respectively)	$ 378,879	$ 339,178
Debt securities, held-to-maturity, at amortized cost	5,880	6,619
Equity securities, available-for-sale, at fair value (cost of $34,905 and $33,581, respectively)	41,334	38,534
Total investments (including $28,290 and $22,670 related to the VIE, respectively)	426,093	384,331
Cash and cash equivalents (including $14,753 and $14,616 related to the VIE, respectively)	106,200	53,038
Prepaid reinsurance premiums	58,763	120,771
Premiums receivable, net of allowance of $57 and $302, respectively (including $1,589 and $355 related to the VIE, respectively)	63,605	38,594
Reinsurance recoverable, net	25,151	12,714
Deferred acquisition costs	41,247	15,547
Income taxes receivable	16,706	2,691
Property and equipment, net	3,863	2,894
Other assets (including $1,269 and $1,037 related to the VIE, respectively)	7,829	7,605
TOTAL ASSETS	$ 749,457	$ 638,185
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Loss and loss adjustment expense reserves	$ 127,485	$ 97,340

Unearned premiums	309,283	253,960
Debt from consolidated variable interest entity	4,903	4,887
Deferred income taxes, net	12,912	5,627
Other liabilities	31,521	25,612
Total liabilities	486,104	387,426
SHAREHOLDERS’ EQUITY:		
Preferred stock, $0.01 par value: 1,000,000 shares authorized	—	—
Common stock, $0.01 par value: 25,000,000 shares authorized; 13,801,607 and 13,798,773 shares issued and outstanding, respectively	138	138
Additional paid-in capital	136,359	131,998
Accumulated other comprehensive income	8,800	3,985
Retained earnings	99,336	96,461
Total Federated National Holding Company shareholders’ equity	244,633	232,582
Noncontrolling interest	18,720	18,177
Total shareholders’ equity	263,353	250,759
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$ 749,457	$ 638,185

See accompanying notes to unaudited consolidated financial statements.

Table of Contents

FEDERATED NATIONAL HOLDING COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Revenue:				
Net premiums earned	$ 69,405	$ 62,286	$ 184,447	$ 156,298
Net investment income	2,164	1,907	6,398	5,154
Net realized investment gains	1,126	1,126	2,060	3,743
Other income	11,095	7,280	34,909	21,130
Total revenue	83,790	72,599	227,814	186,325
Costs and expenses:				
Losses and loss adjustment expenses	43,613	28,412	120,183	75,510
Commissions and other underwriting expenses	34,512	21,610	75,408	47,934
General and administrative expenses	4,044	4,887	13,211	11,973
Interest expense	81	65	259	161
Total costs and expenses	82,250	54,974	209,061	135,578
Income before income taxes	1,540	17,625	18,753	50,747
Income taxes	102	7,054	6,594	19,519
Net income	1,438	10,571	12,159	31,228
Net income (loss) attributable to noncontrolling interest	44	(22)	239	(383)
Net income attributable to Federated National Holding Company shareholders	$ 1,394	$ 10,593	$ 11,920	$ 31,611
Net income per share attributable to Federated National Holding Company shareholders:				
Basic	$ 0.10	$ 0.77	$ 0.86	$ 2.31
Diluted	$ 0.10	$ 0.76	$ 0.85	$ 2.26
Weighted average number of shares of common stock outstanding:				
Basic	13,780	13,749	13,807	13,710
Diluted	13,943	13,977	13,999	13,978

Dividends declared per share of common stock	$ 0.08	$ 0.04	$ 0.17	$ 0.13

See accompanying notes to unaudited consolidated financial statements.

Table of Contents

FEDERATED NATIONAL HOLDING COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income	$ 1,438	$ 10,571	$ 12,159	$ 31,228
Change in net unrealized (losses) gains on investments, available-for-sale	(774)	(2,671)	8,316	(4,681)
Comprehensive income before income taxes	664	7,900	20,475	26,547
Income tax benefit (expense) related to items of other comprehensive income	152	1,083	(3,197)	1,734
Comprehensive income	816	8,983	17,278	28,281
Less: comprehensive income (loss) attributable to noncontrolling interest	44	(17)	543	(494)
Comprehensive income attributable to Federated National Holding Company shareholders	$ 772	$ 9,000	$ 16,735	$ 28,775

See accompanying notes to unaudited consolidated financial statements.

Table of Contents

FEDERATED NATIONAL HOLDING COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(In thousands, except share data)

(Unaudited)

		Common Stock		Additional	Accumulated Other		Total Shareholders' Equity Attributable to Federated National Holding		Total
	Preferred Stock	Issued Shares	Amount	Paid-in Capital	Comprehensive Income	Retained Earnings	Company Shareholders	Noncontrolling Interest	Shareholders' Equity
Balance as of December 31, 2015	$ —	13,798,773	$ 138	$ 131,998	$ 3,985	$ 96,461	$ 232,582	$ 18,177	$ 250,759
Net income	—	—	—	—	—	11,920	11,920	239	12,159
Other comprehensive income	—	—	—	—	4,815	—	4,815	304	5,119
Dividends	—	—	—	—	—	(3,563)	(3,563)	—	(3,563)
Shares issued under share-based compensation plans	—	288,815	—	360	—	—	360	—	360
Tax benefits from share-based	—	—	—	—	—	—	—	—	—
awards	—	—	—	843	—	—	843	—	843
Repurchases of common stock	—	(285,981)	—	—	—	(5,482)	(5,482)	—	(5,482)
Share-based compensation	—	—	—	3,158	—	—	3,158	—	3,158
Balance as of September 30,	$ —	13,801,607	$ 138	$ 136,359	$ 8,800	$ 99,336	$ 244,633	$ 18,720	$ 263,353

2016

See accompanying notes to unaudited consolidated financial statements.

Table of Contents

FEDERATED NATIONAL HOLDING COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
	(in thousands)	
Cash flow from operating activities:		
Net income	$ 12,159	$ 31,228
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Net realized investment gains	(2,060)	(3,743)
Amortization of investment premium or discount, net	3,910	3,795
Depreciation and amortization	620	495
Share-based compensation	4,001	3,175
Changes in operating assets and liabilities:		
Prepaid reinsurance premiums	62,008	(40,967)
Premiums receivable, net	(25,011)	(7,653)
Reinsurance recoverable, net	(12,437)	4,186
Deferred acquisition costs	(25,699)	88
Income taxes receivable, net	(14,858)	(3,953)
Loss and loss adjustment expense reserves	30,146	13,343
Unearned premiums	55,323	57,973
Deferred income taxes, net of other comprehensive income	5,491	5,277
Other, net	5,676	16,970
Net cash provided by operating activities	99,269	80,214
Cash flow from investing activities:		
Sales, maturities and redemptions of investment securities	151,884	134,918
Purchases of investment securities	(188,576)	(195,278)
Purchases of property and equipment	(1,573)	(1,500)
Net cash used in investing activities	(38,265)	(61,860)
Cash flow from financing activities:		
Noncontrolling interest equity investment	—	18,498
Tax benefit related to share-based compensation	843	869
Purchases of FNHC common stock	(5,482)	—
Issuance of common stock for share-based awards	360	130
Dividends paid	(3,563)	(1,847)
Net cash (used in) provided by financing activities	(7,842)	17,650
Net increase in cash and cash equivalents	53,162	36,004

Cash and cash equivalents at beginning of period	53,038	40,157
Cash and cash equivalents at end of period	$ 106,200	$ 76,161

See accompanying notes to unaudited consolidated financial statements.

Table of Contents

FEDERATED NATIONAL HOLDING COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Continued)

	Nine Months Ended September 30,	
	2016	2015
	(in thousands)	
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes	$ 14,360	$ 15,662
Non-cash investing and finance activities:		
Accrued dividends payable	$ 1,134	$ 712

See accompanying notes to unaudited consolidated financial statements.

Table of Contents

1. ORGANIZATION, CONSOLIDATION AND BASIS OF PRESENTATION

Organization

Federated National Holding Company, (“FNHC,” the “Company,” “we,” or “us”), is an insurance holding company that controls substantially all steps in the insurance underwriting, distribution and claims processes through our subsidiaries and our contractual relationships with our independent agents and general agents. We are authorized to underwrite, and/or place through our wholly owned subsidiaries, homeowners’ multi-peril (“homeowners’”), personal automobile, commercial general liability, federal flood, and other lines of insurance in Florida and other states. We market, distribute and service our own and third-party insurers’ products and our other services through a network of independent agents.

Our wholly owned insurance subsidiary is Federated National Insurance Company (“FNIC”), which is licensed as an admitted carrier in Florida, Texas, Georgia, Alabama, Louisiana and South Carolina. We also serve as managing general agent for Monarch National Insurance Company (“MNIC”), which was founded in 2015 through the joint venture, described below, and is licensed as an admitted carrier in Florida. An admitted carrier is an insurance company that has received a license from the state department of insurance giving the Company the authority to write specific lines of insurance in that state. These companies are also bound by rate and form regulations, and are strictly regulated to protect policyholders from a variety of illegal and unethical practices, including fraud. Admitted carriers are also required to financially contribute to the state guarantee fund, which is used to pay for losses if an insurance carrier becomes insolvent or unable to pay the losses due to their policyholders.

On March 19, 2015, the Company entered into a joint venture to organize MNIC, which received its certificate of authority to write homeowners’ property and casualty insurance in Florida from the Florida Office of Insurance Regulation (the “Florida OIR”). The Company’s joint venture partners are a majority-owned limited partnership of Crosswinds Holdings Inc., a publicly traded Canadian private equity firm and asset manager (“Crosswinds”); and Transatlantic Reinsurance Company (“TransRe”).

The Company and Crosswinds each invested $14.0 million in Monarch Delaware Holdings LLC (“Monarch Delaware”), the indirect parent company of MNIC, for a 42.4% interest in Monarch Delaware (each holding 50% of the voting interests in Monarch Delaware). TransRe invested $5.0 million for a 15.2% non-voting interest in Monarch Delaware and advanced an additional $5.0 million in debt evidenced by a six-year promissory note bearing 6% annual interest payable by Monarch National Holding Company (“MNHC”), a wholly owned subsidiary of Monarch Delaware and the direct parent company of MNIC.

Significant Customer

We entered into an Insurance Agency Master Agreement with Ivantage Select Agency, Inc., ("ISA"), an affiliate of Allstate Insurance Company ("Allstate"), pursuant to which we are authorized by ISA to appoint Allstate agents to offer our homeowners' and commercial general liability insurance products to consumers in Florida. As a percentage of the total homeowners' premiums we underwrote in the three months ended September 30, 2016 and 2015, 24.7% and 25.4%, respectively, were from Allstate's network of Florida agents. For the nine months ended September 30, 2016 and 2015 23.9% and 23.3%, respectively, of the homeowners' premiums we underwrote were from Allstate's network of Florida agents.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of FNHC and all other entities in which we have a controlling financial interest and any variable interest entities ("VIE") in which we are the primary beneficiary. All material inter-company accounts and transactions have been eliminated in consolidation. A VIE is an entity that does not have sufficient equity to finance its own activities without additional financial support or where investors lack certain characteristics of a controlling financial interest. We assess our contractual, ownership or other interests in a VIE to determine if our interest participates in the variability the VIE was designed to absorb and pass onto variable interest holders. We perform an ongoing qualitative assessment of our variable interests in VIEs to determine whether we have a controlling financial interest and would therefore be considered the primary beneficiary of the VIE. If we determine we are the primary beneficiary of a VIE, we consolidate the assets and liabilities of the VIE in our consolidated financial statements.

In connection with the investment in Monarch Delaware, we have determined that we are the primary beneficiary of this VIE, as we possess the power to direct the activities of the VIE that most significantly impact its economic performance. Accordingly, we consolidate the VIE in our consolidated financial statements. Refer to Note 12 for additional information on the VIE.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the rules and regulations of the Securities and Exchange Commission ("SEC"). Accordingly, these financial statements do not include all of the information and notes required by GAAP for

Table of Contents

complete financial statements. Additionally, operating results for interim periods are not necessarily indicative of the results that can be expected for a full year. These unaudited consolidated financial statements reflect, in the opinion of management, all material adjustments (which include only normal recurring adjustments) necessary to fairly state, in all material respects, our financial position and results of operations for the periods presented. Certain GAAP policies, which significantly affect the determination of financial condition, results of operations and cash flows, are summarized below.

This report should be read in conjunction with the Company's 2015 Annual Report on Form 10-K, as amended (the "2015 Form 10-K").

2. SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES

Our significant accounting policies were described in Note 2 to our Consolidated Financial Statements set forth in Part II, Item 8, "Financial Statements and Supplementary Data" of the 2015 Form 10-K. There have been no significant changes in our significant accounting policies for the nine months ended September 30, 2016.

Accounting Estimates and Assumptions

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Future events and their effects cannot be determined with absolute certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates.

Similar to other property and casualty insurers, our liability for losses and loss adjustment expense reserves, although supported by actuarial projections and other data, is ultimately based on management's reasoned expectations of future events. Although considerable variability is inherent in these estimates, we believe that this liability is adequate. Estimates are reviewed regularly and adjusted as necessary. Such adjustments are reflected in current operations. Refer to Note 6 accompanying our consolidated financial statements for a discussion of our liability for losses and loss adjustment expense reserves.

Reclassifications

Certain amounts in prior year's consolidated financial statements have been reclassified to conform to the 2016 presentation. These reclassifications had no effect on the reported consolidated statements of operations, balance sheets, and cash flows. In the current period, the Company concluded it was appropriate to reclassify certain revenue accounts that do not have material balances and include them within other income in the consolidated statements of operations. In addition, during the current period, the Company reclassified certain costs and expenses, principally, operating and underwriting expenses, salaries and wages and amortization of deferred policy acquisition costs. These respective account balances are now included in commissions and other underwriting expenses and general and administrative expenses in the consolidated statements of operations. The Company believes these reclassifications provide greater clarity and insight into the consolidated financial statements for the periods presented.

Adjustments

During our third quarter 2015 analysis of actual experience to date under the July 1, 2014 quota share reinsurance contract, we re-evaluated the accounting treatment for quota share reinsurance contracts with retrospective rating provisions. As a result of this re-evaluation, we concluded reinsurance contracts, which have retrospective rating provisions, should be accounted for under Accounting Standards Codification 944, Financial Services — Insurance ("ASC 944"), where amounts due to (from) the assuming companies are accrued based on estimated contract experience to date as though the contracts were terminated. Refer to Note 2 in our Form 10-Q for the period ended September 30, 2015 for additional information.

The adjustments to our accounting for the July 1, 2014 quota share reinsurance treaty, inclusive of other adjustments, are not material in any prior quarter or annual period based on an analysis of quantitative and qualitative factors in accordance with SEC guidance.

As a result, we recorded these adjustments during the year ended December 31, 2015. The prior period adjustments increased net income by $2.2 million for the three and nine months ended September 30, 2015, respectively.

Adopted Accounting Pronouncements

In February 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis ("ASU 2015-02"). ASU 2015-02 amended the consolidation guidance by modifying the evaluation criteria for whether limited partnerships and similar legal entities are variable interest entities or voting interest entities, eliminating the presumption that a general partner should consolidate a limited partnership, and affecting the consolidation analysis of reporting entities that are involved with variable interest entities. We adopted the provisions of ASU 2015-02 effective January 1, 2016 and re-evaluated all legal entity investments under the revised consolidation model. The adoption of ASU 2015-02 did not have any impact on our consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Interest-Imputation of Interest. ASU 2015-03 reduces the complexity of disclosing debt issuance costs and debt discount and premium on the balance sheet by requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability, consistent with debt discounts. The Company adopted this ASU retrospectively as of January 1, 2016. Other assets and debt from consolidated variable interest entity have been reclassified to be consistent with the adoption of this standard, which resulted in a reduction of $0.1 million each. There were no changes to shareholders' equity as a result of this adoption. There were no other impacts on the Company's consolidated financial statements.

In May 2015, the FASB issued ASU 2015-09, Financial Services – Insurance (Topic 944): Disclosures about Short-Duration-Contracts. The amendments in this ASU apply to all insurance entities that issue short-duration contracts as defined in Topic 944, Financial Services—Insurance. The amendments require insurance entities to disclose for annual reporting periods information on the liability for unpaid claims and claim adjustment expenses. The amendments in this ASU are effective for annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016. This new guidance affects disclosures only and will have no impact on the Company's consolidated financial statements.

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"). ASU 2014-09 requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. ASU 2014-09 will replace most existing revenue recognition guidance in United States Generally Accepted Accounting Principles when it becomes effective. In July 2015, the FASB voted to delay the effective date of ASU 2014-09 by one year, making it effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, with early adoption permitted as of the original effective date. ASU 2014-09 permits the use of either the retrospective or cumulative effect transition method. In addition, during 2016 the FASB issued ASU 2016-08, ASU 2016-10, and ASU 2016-12, all of which clarify certain implementation guidance within ASU 2014-09. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures.

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Most notably, this new guidance requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. This new guidance is effective for annual reporting periods beginning after December 15, 2017. We are currently evaluating the impact the adoption of this standard would have on the Company’s consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) (“ASU 2016-02”). Upon the effective date, ASU 2016-02 will supersede the current lease guidance in Topic 840, Leases. Under the new guidance, lessees will be required to recognize for all leases, with the exception of short-term leases, a lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis. Concurrently, lessees will be required to recognize a right-of-use asset, which is an asset that represents the lessee’s right to use, or control the use of, a specified asset for the lease term. ASU 2016-02 is effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted. The guidance is required to be applied using a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative periods presented in the financial statements. We are currently evaluating the effects the adoption of ASU 2016-02 will have on the Company’s consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU 2016-09”), which is intended to simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods therein. Early application is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments- Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (“ASU 2016-13”) which significantly changes the measurement of credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. ASU 2016-13 will require entities to record allowances for available-for-sale debt securities rather than reduce the carrying amount, as currently performed under the other-than-temporary impairment model. Additionally, the standard will require enhanced disclosures for financial assets measured at amortized cost and available-for-sale debt securities to help the financial statement users better understand significant judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an entity’s portfolio. ASU 2016-13 is effective for interim and annual

Table of Contents

reporting periods beginning after December 15, 2019, with early adoption permitted. We are currently evaluating the effects the adoption of ASU 2016-13 will have on the Company’s consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). ASU 2016-15 provides guidance on the following eight specific cash flow classification issues: (1) debt prepayment or debt extinguishment costs; (2) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; (3) contingent consideration payments made after a business combination; (4) proceeds from the settlement of insurance claims; (5) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; (6) distributions received from equity method investees; (7) beneficial interests in securitization transactions; and (8) separately identifiable cash flows and application of the predominance principle. Current GAAP does not include specific guidance on these eight cash flow classification issues. The amendments of this ASU are effective for reporting periods beginning after December 15, 2017, with early adoption permitted. The Company is evaluating the effect that ASU 2015-16 will have on its consolidated financial statements and related disclosures.

3. FAIR VALUE

Fair value measurements are generally based upon observable and unobservable inputs. Observable inputs are based on market data from independent sources, while unobservable inputs reflect the Company’s view of market assumptions in the absence of observable market information. All assets and liabilities that are carried at fair value are classified and disclosed in one of the following categories:

Level 1 — Quoted prices (unadjusted) in active markets for identical assets or liabilities. An active market is defined as a market where transactions for the financial statement occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 — Quoted market prices for similar assets or liabilities and valuations, using models or other valuation techniques that use observable market data. All significant inputs are observable, or derived from observable information in the marketplace, or are supported by observable levels at which transactions are executed in the market place.

Level 3 — Instruments that use non-binding broker quotes or model driven valuations that do not have observable market data or those that are estimated based on an ownership interest to which a proportionate share of net assets is attributed. Currently, the Company has no level 3 investments.

The Company's financial instruments measured at fair value and the level of the fair value hierarchy of inputs used were as follows:

	September 30, 2016			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
Debt securities:				
United States government obligations and authorities	$ 38,933	$ 26,877	$ —	$ 65,810
Obligations of states and political subdivisions	—	150,873	—	150,873
Corporate	—	149,210	—	149,210
International	—	12,986	—	12,986
	38,933	339,946	—	378,879
Equity securities	40,458	876	—	41,334
Total investments	$ 79,391	$ 340,822	$ —	$ 420,213

Table of Contents

	December 31, 2015			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
Debt securities:				
United States government obligations and authorities	$ 34,733	$ 26,820	$ —	$ 61,553
Obligations of states and political subdivisions	—	110,702	—	110,702
Corporate	—	154,620	—	154,620
International	—	12,303	—	12,303
	34,733	304,445	—	339,178
Equity securities	38,012	522	—	38,534
Total investments	$ 72,745	$ 304,967	$ —	$ 377,712

4. INVESTMENTS

Unrealized Gains and Losses

The following table details the difference between amortized cost or cost and estimated fair value, by major investment category, at September 30, 2016 and at December 31, 2015:

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)			
September 30, 2016				
Debt securities - available-for-sale:				
United States government obligations and authorities	$ 64,810	$ 1,039	$ 39	$ 65,810
Obligations of states and political subdivisions	148,366	2,556	49	150,873
Corporate	144,990	4,305	85	149,210
International	12,715	273	2	12,986

	370,881	8,173	175	378,879
Debt securities - held-to-maturity:				
United States government obligations and authorities	4,173	70	59	4,184
Corporate	1,636	47	—	1,683
International	71	2	—	73
	5,880	119	59	5,940
Equity securities	34,905	7,278	849	41,334
Total investments	$ 411,666	$ 15,570	$ 1,083	$ 426,153

Table of Contents

	Amortized Cost or Cost (in thousands)	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2015				
Debt securities - available-for-sale:				
United States government obligations and authorities	$ 61,384	$ 489	$ 320	$ 61,553
Obligations of states and political subdivisions	109,152	1,590	40	110,702
Corporate	154,957	1,153	1,490	154,620
International	12,528	18	243	12,303
	338,021	3,250	2,093	339,178
Debt securities - held-to-maturity:				
United States government obligations and authorities	4,275	30	204	4,101
Corporate	2,253	14	20	2,247
International	91	—	—	91
	6,619	44	224	6,439
Equity securities	33,581	6,809	1,856	38,534
Total investments	$ 378,221	$ 10,103	$ 4,173	$ 384,151

Net Realized Gains and Losses

The Company calculates the gain or loss realized on the sale of investments by comparing the sales price (fair value) to the cost or amortized cost of the security sold. Net realized gains and losses on investments are determined in accordance with the specific identification method. The following tables detail the Company's net realized gains (losses) by major investment category for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(in thousands)		(in thousands)	
Gross realized gains:				
Debt securities	$ 897	$ 226	$ 2,822	$ 973
Equity securities	597	1,847	1,752	4,188
Total gross realized gains	1,494	2,073	4,574	5,161

Gross realized losses:				
Debt securities	(20)	(178)	(614)	(504)
Equity securities	(348)	(769)	(1,900)	(914)
Total gross realized losses	(368)	(947)	(2,514)	(1,418)
Net realized gains on investments	$ 1,126	$ 1,126	$ 2,060	$ 3,743

During the three months ended September 30, 2016 and 2015, the proceeds from sales of available-for-sale investment securities were $30.1 million and $42.5 million, respectively. During the nine months ended September 30, 2016 and 2015, the proceeds from sales of available-for-sale investment securities were $129.5 million and $134.9 million, respectively.

Table of Contents

Contractual Maturity

The amortized cost and estimated fair value of debt securities as of September 30, 2016 and December 31, 2015 by contractual maturity are shown below. Expected maturities may differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2016		December 31, 2015	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Securities with maturity dates:	(in thousands)			
Debt securities, available-for-sale:				
One year or less	$ 41,507	$ 41,565	$ 24,470	$ 24,488
Over one through five years	182,129	185,001	170,797	171,113
Over five through ten years	145,639	150,694	142,728	143,545
Over ten years	1,606	1,619	26	32
	370,881	378,879	338,021	339,178
Debt securities, held-to-maturity:				
One year or less	413	413	486	487
Over one through five years	1,887	1,949	1,899	1,915
Over five through ten years	3,580	3,578	4,234	4,037
	5,880	5,940	6,619	6,439
Total	$ 376,761	$ 384,819	$ 344,640	$ 345,617

Net Investment Income

The following table summarizes the Company’s net investment income for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended	Nine Months Ended

	September 30,		September 30,	
	2016	2015	2016	2015
	(in thousands)			
Interest income	$ 1,963	$ 1,760	$ 5,801	$ 4,773
Dividends income	201	147	597	381
Net investment income	$ 2,164	$ 1,907	$ 6,398	$ 5,154

Table of Contents

Aging of Gross Unrealized Losses

As of September 30, 2016 and December 31, 2015, gross unrealized losses and related fair values for available-for-sale debt securities and equity securities, grouped by duration of time in a continuous unrealized loss position, were as follows:

	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
September 30, 2016			(in thousands)			
Debt securities - available-for-sale:						
United States government obligations and authorities	$ 8,995	$ 38	$ 121	$ 1	$ 9,116	$ 39
Obligations of states and political subdivisions	28,481	47	1,015	2	29,496	49
Corporate	11,405	33	3,345	52	14,750	85
International	1,170	1	302	1	1,472	2
	50,051	119	4,783	56	54,834	175
Equity securities	5,590	679	2,179	170	7,769	849
Total investments	$ 55,641	$ 798	$ 6,962	$ 226	$ 62,603	$ 1,024

	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2015			(in thousands)			
Debt securities - available-for-sale:						
United States government obligations and authorities	$ 30,464	$ 303	$ 659	$ 17	$ 31,123	$ 320
Obligations of states and political subdivisions	16,652	40	—	—	16,652	40
Corporate	87,176	1,420	3,590	70	90,766	1,490

International	8,660	191	281	52	8,941	243
	142,952	1,954	4,530	139	147,482	2,093
Equity securities	11,790	1,850	84	6	11,874	1,856
Total investments	$ 154,742	$ 3,804	$ 4,614	$ 145	$ 159,356	$ 3,949

The Company holds its equity securities and some of its debt securities as available-for-sale and as such, these securities are recorded at fair value. The Company continually monitors the difference between cost and the estimated fair value of its investments, which involves uncertainty as to whether declines in value are temporary in nature. If the decline of a particular investment is deemed temporary, the Company records the decline as an unrealized loss in shareholders' equity. If the decline is deemed to be other than temporary, the Company will write the security's cost-basis or amortized cost-basis down to the fair value of the investment and recognizes an other than temporary impairment ("OTTI") loss in our consolidated statement of operations. Additionally, any portion of such decline related to debt securities that is believed to arise from factors other than credit will be recorded as a component of other comprehensive income rather than charged against income.

The Company's assessment of equity securities initially involves an evaluation of all securities that are in an unrealized loss position, regardless of the duration or severity of the loss, as of the applicable balance sheet date. Such initial review consists primarily of assessing whether: (i) there has been a negative credit or news event with respect to the issuer that could indicate the existence of an OTTI; and (ii) the Company has the ability and intent to hold an equity security for a period of time sufficient to allow for an anticipated recovery (generally considered to be one year from the balance sheet date).

To the extent that an equity security in an unrealized loss position is not impaired based on the initial review described above, the Company then evaluates such equity security by considering qualitative and quantitative factors. These factors include but are not limited to facts and circumstances specific to individual securities, asset classes, the financial condition of the issuer, changes in dividend payment, the length of time fair value had been less than cost, the severity of the decline in fair value below cost, industry outlook and our ability and intent to hold each position until its forecasted recovery.

If the Company intends to sell, or it is more likely than not that, the Company will sell, a debt security before recovery of its amortized cost basis, the total amount of the unrealized loss position is recognized as an OTTI loss in our consolidated statement of operations. To the extent a debt security in an unrealized loss position is not impaired based on the preceding; the Company will consider that security to be impaired when it believes collection of the amortized cost is not probable.

During the Company's quarterly evaluation of its securities for impairment, there were no identified OTTI losses in our investments in debt and equity securities during the three months ended September 30, 2016 and $0.3 million OTTI losses in our investments in debt and equity securities during the nine months ended September 30, 2016. We did not have any OTTI losses in our investments in debt and equity securities that were in an unrealized loss position during the three and nine months ended September 30, 2015.

Collateral Deposits

As of September 30, 2016, investments with fair values of approximately $10.7 million, the majority of which were debt securities, were deposited with governmental authorities and into custodial bank accounts as required by law or contractual obligations.

5. REINSURANCE

Reinsurance is used to mitigate the exposure to losses, manage capacity and protect capital resources. The Company reinsures (cedes) a portion of written premiums on an excess of loss or a quota share basis in order to limit our loss exposure. To the extent that reinsuring companies are unable to meet their obligations assumed under these reinsurance agreements, we remain primarily liable to our policyholders.

We are selective in choosing reinsurers and consider numerous factors, the most important of which are the financial stability of the reinsurer or capital specifically pledged to uphold the contract, its history of responding to claims and its overall reputation. In an effort to minimize our exposure to the insolvency of a reinsurer, we evaluate the acceptability and review the financial condition of the reinsurer at least annually with the assistance of our reinsurance broker.

Significant Reinsurance Contracts

FNIC and MNIC operate primarily by underwriting and accepting risks for their direct account on a gross basis and reinsuring a portion of the exposure on either an individual risk or an aggregate basis to the extent those exceed the desired retention level. We continually evaluate the relative attractiveness of different forms of reinsurance contracts and different markets that may be used to achieve our risk and profitability objectives. All of our reinsurance contracts do not relieve FNIC or MNIC from their direct obligations to the insured.

FNIC's 2015-2016 catastrophe reinsurance program, which ran either from June 1 to May 31 or from July 1 to June 30, consists of the Florida Hurricane Catastrophe Fund ("FHCF"), excess of loss treaties placed with the private market and a 40% property quota-share program. The property quota-share reinsurance is a form of proportional reinsurance that provides coverage for the homeowners' property lines for wind related catastrophes in Florida. The FHCF treaty affords coverage for losses sustained in Florida and represents only a portion of the reinsurance coverage in Florida.

The excess of loss and FHCF treaties, which became effective on July 1, 2015 and June 1, 2015, respectively, insure for approximately $1.82 billion of aggregate catastrophic losses and loss adjustment expenses ("LAE") with a maximum single event coverage totaling approximately $1.26 billion, with the Company retaining the first $12.9 million in Florida and $5.0 million in Louisiana, Alabama and South Carolina for losses and LAE from each event. Ceded premiums in connection with this program totaled approximately $149.7 million.

Additionally, the Company's private market excess of loss treaties became effective July 1, 2016 and all private layers have prepaid automatic reinstatement protection, which affords us additional coverage against multiple catastrophic events in the same hurricane season. The Company obtained multiple year protection for a portion of its program; as a result, some of the coverage will expire on June 30, 2017, and a portion of the coverage will remain in-force one additional treaty year until June 30, 2018. These private market excess of loss treaties structure coverage into layers, with a cascading feature such that substantially all private layers attach after $18.45 million in losses for FNIC's Florida exposure. If the aggregate limit of the preceding layer is exhausted, the next layer drops down (cascades) in its place. Additionally, any unused layer protection drops down for subsequent events until exhausted.

FNIC's 2016-2017 reinsurance programs, costing approximately $179.5 million, include approximately $125.7 million for the private reinsurance for Federated National's Florida exposure, including prepaid automatic premium reinstatement protection on all layers, along with approximately $53.8 million payable to the FHCF. The combination of private and FHCF reinsurance treaties will afford Federated National with approximately $2.22 billion of aggregate coverage with a maximum single event coverage totaling approximately $1.58 billion, exclusive of retentions. FNIC maintained its FHCF participation at 75% for the 2016 hurricane season. FNIC’s single event pre-tax retention for a catastrophic event in Florida is $18.45 million. In addition, FNIC purchases separate underlying reinsurance layers in Louisiana, Alabama, and South Carolina to cover losses and LAE outside of Florida for each catastrophic event from $8.0 million to $18.45 million. Depending on the characteristics of the catastrophic event, and the states involved, FNIC’s single event pre-tax retention could be as low as $8.0 million. The maximum pre-tax retention of $18.45 million for Florida represents 7.01% of the Company’s shareholders’ equity as of September 30, 2016.

MNIC’s 2016-2017 catastrophe reinsurance program, which runs from either June 1 to May 31 or June 1 to June 30 (13 month period), consists of the FHCF and private market excess of loss treaties. All private layers have prepaid automatic reinstatement protection, which affords MNIC additional coverage, and have a cascading feature such that substantially all layers attach at $3.4 million for MNIC's Florida exposure.

The Company’s property quota share treaties, which are included in the reinsurance program, run for a two-year period from July 1 to July 1 of the following year. The property quota-share treaties consist of two different treaties, one for 30% which became effective July 1, 2014, and the other for 10% which became effective July 1, 2015. The combined treaties provided a 40% quota-share reinsurance on the first $100 million of covered losses for the homeowners’ property insurance program in Florida. The treaties are accounted for as retrospectively rated contracts whereby the estimated ultimate premium or commission is recognized over the period of the contracts.

On July 1, 2016, the 30% property quota-share treaty expired on a cut-off basis, which means as of that date the Company will retain 30% of its unearned premiums and losses. The reinsurers will remain liable for 30% of the paid losses occurring during the term of the treaty, until the treaty is commuted.

The Company’s private passenger automobile quota share treaties are typically one-year programs which become effective at different points in the year and cover auto policies across several states. These automobile quota share treaties cede 75% to 90% of all written premiums entered into by the Company.

Certain reinsurance agreements require FNIC to secure the credit, regulatory and business risk. Fully funded trust agreements securing these risks totaled $2.6 million as of September 30, 2016 and $3.5 million as of December 31, 2015.

Reinsurance Recoverables

Amounts recoverable from reinsurers are recognized in a manner consistent with the claims liabilities associated with the reinsurance placement and presented on the consolidated balance sheet as reinsurance recoverables. The following table presents reinsurance recoverables as reflected in the consolidated balance sheets as of September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015
	(in thousands)	
Reinsurance recoverable on paid losses	$ 8,094	$ 5,218
Reinsurance recoverable on unpaid losses	17,057	7,496
Reinsurance recoverable, net	$ 25,151	$ 12,714

Table of Contents

Premiums Written and Earned

The following table presents premiums written and earned for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(in thousands)		(in thousands)	
Net premiums written:				
Direct	$ 161,137	$ 129,840	$ 468,379	$ 368,560
Ceded	(96,327)	(119,985)	(259,307)	(231,046)
	$ 64,810	$ 9,855	$ 209,072	$ 137,514
Net premiums earned:				
Direct	$ 147,624	$ 112,253	$ 413,056	$ 310,587
Ceded	(78,219)	(49,967)	(228,609)	(154,289)
	$ 69,405	$ 62,286	$ 184,447	$ 156,298

6. LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

The liability for loss and LAE reserves is determined on an individual-case basis for all claims reported. The liability also includes amounts for unallocated expenses, anticipated future claim development and incurred but not yet reported (“IBNR”).

Activity in the liability for loss and LAE reserves is summarized as follows:

	Nine Months Ended September 30, 2016	Year Ended December 31, 2015
	(in thousands)	
Gross reserves, beginning of period	$ 97,340	$ 78,330
Less: reinsurance recoverable (1)	(7,496)	(10,394)
Net reserves, beginning of period	89,844	67,936
Incurred loss, net of reinsurance, related to:		
Current year	109,237	113,819
Prior years	10,946	(9,466)
Total incurred loss and LAE, net of reinsurance	120,183	104,353
Paid loss, net of reinsurance, related to:		
Current year	46,073	49,531
Prior years	53,526	32,914
Total paid loss and LAE, net of reinsurance	99,599	82,445
Net reserves, end of period	110,428	89,844
Plus: reinsurance recoverable (1)	17,057	7,496
Gross reserves, end of period	$ 127,485	$ 97,340

(1) Reinsurance recoverable in this table includes only ceded loss and LAE reserves.

The establishment of loss reserves is an inherently uncertain process and changes in loss reserve estimates are expected as such estimates are subject to the outcome of future events. The factors influencing changes in claim costs are often difficult to isolate or quantify and developments in paid and incurred losses from historical trends are frequently subject to multiple interpretations. Changes in estimates, or differences between estimates and amounts ultimately paid, are reflected in the operating results of the period during which such adjustments are made.

Table of Contents

During the nine months ended September 30, 2016, the Company experienced unfavorable loss and LAE reserve development on prior year accident years primarily in its all other peril homeowners' coverage in Florida. The deficiency primarily relates to higher severity above the expected development factor anticipated at December 31, 2015 which was driven by the impact from assignment of benefits and other related adjusting expenses.

During the year ended December 31, 2015, the Company experienced a redundancy on prior year accident years primarily a result of continued favorable loss experience (mostly caused by decreased severity in reported claims) in the Company's all other peril homeowners' coverage caused in part by the absence of severe weather in Florida. Specifically, we have experienced better severity than expected on the 2014 and 2013 accident years.

7. LONG-TERM DEBT

On March 17, 2015, MNHC, a wholly owned subsidiary of Monarch Delaware, and MNIC's direct parent, our consolidated VIE, issued a promissory note with a principal amount of $5.0 million bearing 6% annual interest, due March 17, 2021 with interest payable on an annual basis due March 17 each year. The debt was issued to TransRe, a related party, in connection with its investment in Monarch Delaware, and is being carried at the unpaid principal balance, net of debt issuance costs, and any accrued and unpaid interest is recognized in other liabilities in the consolidated balance sheet. The Company recorded $0.1 million of debt issuance costs related to the 6% promissory note.

8. INCOME TAXES

The provision for income tax expense for the three and nine months ended September 30, 2016 and 2015 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(in thousands)		(in thousands)	
Federal:				

Current	$ (10,433)	$ 5,040	$ (2,275)	$ 11,016
Deferred	10,709	1,194	8,222	5,982
Federal income tax expense	276	6,234	5,947	16,998
State:				
Current	(1,960)	665	(613)	1,760
Deferred	1,786	155	1,260	761
State income tax expense	(174)	820	647	2,521
Total income tax expense	$ 102	$ 7,054	$ 6,594	$ 19,519

The actual income tax expense differs from the “expected” income tax expense (computed by applying the combined applicable effective federal and state tax rates to income before income tax expense) as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(in thousands)		(in thousands)	
Computed expected tax expense provision, at federal rate	$ 552	$ 6,374	$ 6,604	$ 17,761
State tax, net of federal tax benefit	(148)	578	396	1,685
Other	(302)	102	(406)	73
Total income tax expense	$ 102	$ 7,054	$ 6,594	$ 19,519

The Company files income tax returns in the U.S. federal jurisdiction and various states and local jurisdictions. As a matter of course, various taxing authorities, including the Internal Revenue Service (“IRS”), regularly audit us. As of September 30, 2016, no open tax years are under examination by the IRS or any material state and local jurisdictions.

As of September 30, 2016 and December 31, 2015, we have determined that there are no uncertain tax positions.

Table of Contents

9. COMMITMENTS AND CONTINGENCIES

Legal Proceedings

In the ordinary course of business, the Company is involved in various legal proceedings, specifically claims litigation. The Company's insurance subsidiaries participate in most of these proceedings by either defending third-party claims brought against insureds or litigating first-party coverage claims. The Company accounts for such activity through the establishment of loss and LAE reserves. We believe that the ultimate liability, if any, with respect to such ordinary-course claims litigation, after consideration of provisions made for potential losses and costs of defense, is immaterial to our consolidated financial statements. The Company is also occasionally involved in other legal and regulatory proceedings, some of which may assert claims for substantial amounts. These other legal proceedings may occasionally make us party to individual actions in which extra-contractual damages, punitive damages or penalties are sought, such as claims alleging bad faith in the handling of insurance claims.

On a quarterly basis, the Company reviews these outstanding matters, if any. Consistent with GAAP, the Company establishes reserves for specific legal matters when it determines that the likelihood of an unfavorable outcome is probable and the loss is reasonably estimable. The Company does not establish reserves for identified legal matters when we believe that the likelihood of an unfavorable outcome is not probable. Based on our quarterly review, the Company believes that our accruals for probable and estimable losses are reasonable and that the amounts accrued do not have a material effect on our consolidated financial statements.

The Company is a party to a Co-Existence Agreement effective as of August 30, 2013 (the "Co-Existence Agreement") with Federated Mutual Insurance Company ("Mutual") pursuant to which the Company has agreed to certain restrictions on its use of the word "FEDERATED" without the word "NATIONAL" when referring to FNHC and FNIC. In response to Mutual's allegations that the Company's use of the word "FED" as part of the Company's federally registered "FEDNAT" trademark infringes on Mutual's federal and common law trademark rights, which the Company disputes, on July 21, 2016, the Company filed a declaratory judgment action for non-infringement of trademark in the U.S. District Court for the Southern District of Florida. Specifically, the Company seeks a declaration that its federally registered trademark "FEDNAT" does not infringe any alleged trademark rights of Mutual and that Mutual does not own any trademark rights to the name or mark "FED" in connection with insurance services outside of Owatonna, Minnesota. On July 26, 2016, Mutual filed a demand for arbitration against the Company before the American Arbitration Association alleging a breach of the Co-Existence Agreement. Both matters are in their preliminary stages and FNHC intends to vigorously defend against all of Mutual's allegations, although there can be no assurances as to the outcome of either matter.

Assessment Related Activity

We operate in a regulatory environment where certain entities and organizations have the authority to require us to participate in assessments. Currently these entities and organizations include: Florida Insurance Guaranty Association (“FIGA”), Citizens Property Insurance Corporation (“Citizens”), FHCF, Florida Joint Underwriters Insurance Association (“JUA”), Georgia Insurers Insolvency Pool (“GIIP”), Special Insurance Fraud Fund (“SIIF”), Fair Access to Insurance Requirements Plan (“FAIRP”), Georgia Automobile Insurance Plan (“GAIP”), Property Insurance Association of Louisiana (“PIAL”), Louisiana Automobile Insurance Plan (“LAIP”), South Carolina Property & Casualty Insurance Guaranty Association (“SCPCIGA”), Texas Property and Casualty Insurance Guaranty Association (“TPCIGA”), Texas Windstorm Insurance Association (“TWIA”), Texas Automobile Insurance Plan Association (“TAIPA”), Alabama Insurance Guaranty Association (“AIGA”), and Alabama Insurance Underwriters Association (“AIUA”).. As a direct premium writer in Florida, we are required to participate in certain insurer solvency associations under Florida law, administered by FIGA. Future assessments are likely, although the impact of these assessments on our balance sheet, results of operations or cash flow are undeterminable at this time.

FNIC is also required to participate in an insurance apportionment plan under Florida law, which is referred to as a JUA Plan. The JUA Plan provides for the equitable apportionment of any profits realized, or losses and expenses incurred, among participating automobile insurers. In the event of an underwriting deficit incurred by the JUA Plan which is not recovered through the policyholders in the JUA Plan, such deficit shall be recovered from the companies participating in the JUA Plan in the proportion that the net direct written premiums of each such member during the preceding calendar year bear to the aggregate net direct premiums written in this state by all members of the JUA Plan. FNIC was not assessed by the JUA Plan. Future assessments by this association are undeterminable at this time.

Leases

FNHC and its subsidiaries lease certain facilities, furniture and equipment under long-term lease agreements. Additional information about leases can be found in Note 8 to our Consolidated Financial Statements set forth in Part II, Item 8, “Financial Statements and Supplementary Data,” of the 2015 Form 10-K.

Table of Contents

10. SHAREHOLDERS’ EQUITY

Common Stock Repurchases

In March 2016, our Board of Directors authorized a program to repurchase shares of common stock of FNHC, at such times and at prices as management determines advisable, up to an aggregate of $10.0 million through March 31, 2017. Common stock repurchases are conducted in the open market. The amount and timing of all repurchase transactions are contingent upon market conditions, applicable legal requirements and other factors. This program may be modified, suspended or terminated by us at any time without notice.

Pursuant to our Board of Directors’ authorizations, the Company repurchased 285,981 shares of its common stock at a total cost of approximately $5.5 million, which is an average price per share of $19.22, during the nine months ended September 30, 2016. As of September 30, 2016, the remaining availability for future repurchases of our common stock was $4.5 million.

Share-Based Compensation Expense

The following table provides certain information in connection with the Company’s share-based compensation arrangements for the three and nine months ended September 30, 2016 and 2015, respectively:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(in thousands)		(in thousands)	
Restricted stock	$ 525	$ 936	$ 3,158	$ 2,277
Stock options	—	5	—	29
Total share-based compensation expense	$ 525	$ 941	$ 3,158	$ 2,306
Intrinsic value of options exercised	$ 12,464	$ 396	$ 13,681	$ 8,551
Fair value of restricted stock vested	$ 10,685			