HCI Group, Inc.
Form 10-Q
August 06, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2014

OR

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

Commission File Number

001-34126

HCI Group, Inc.

(Exact name of Registrant as specified in its charter)

Florida	**20-5961396**
(State of Incorporation)	**(IRS Employer Identification No.)**

5300 West Cypress Street, Suite 100

Tampa, FL 33607

(Address, including zip code, of principal executive offices)

(813) 849-9500

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 x No ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer x
Non-accelerated filer ¨	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 x

The aggregate number of shares of the Registrant s Common Stock, no par value, outstanding on July 24, 2014 was 11,202,338.

HCI GROUP, INC. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION

Item 1 *Financial Statements*

HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(Dollar amounts in thousands, except share amounts)

	June 30, 2014 (Unaudited)	December 31, 2013
Assets		
Fixed-maturity securities, available for sale, at fair value (amortized cost: $117,944 and $110,738, respectively)	$ 122,430	$ 112,151
Equity securities, available for sale, at fair value (cost: $35,791 and $17,248, respectively)	37,812	17,649
Real estate investments	18,938	16,228
Total investments	179,180	146,028
Cash and cash equivalents	302,048	293,398
Accrued interest and dividends receivable	1,263	1,133
Premiums receivable	28,762	14,674
Prepaid reinsurance premiums	33,277	28,066
Deferred policy acquisition costs	20,083	14,071
Property and equipment, net	12,643	13,132
Other assets	22,399	15,814
Total assets	$ 599,655	$ 526,316
Liabilities and Stockholders Equity		
Losses and loss adjustment expenses	$ 43,044	$ 43,686
Unearned premiums	206,657	171,907
Advance premiums	14,873	4,504
Assumed reinsurance balances payable	316	4,660
Accrued expenses	10,162	4,032
Dividends payable	3,111	19
Income taxes payable	103	543
Deferred income taxes, net	2,951	2,740
Long-term debt	128,205	126,932
Other liabilities	14,140	6,772
Total liabilities	423,562	365,795

Commitments and contingencies (Note 13)

Stockholders equity:		
7% Series A cumulative convertible preferred stock (liquidation preference $10.00 per share), no par value, 1,500,000 shares authorized, 0 and 110,684 shares issued and outstanding at June 30, 2014 and December 31, 2013, respectively		
Series B junior participating preferred stock (no par value, 400,000 shares authorized, no shares issued or outstanding)		
Preferred stock (no par value, 18,100,000 shares authorized, no shares issued or outstanding)		
Common stock, (no par value, 40,000,000 shares authorized, 10,690,069 and 10,939,268 shares issued and outstanding at June 30, 2014 and December 31, 2013, respectively)		
Additional paid-in capital	36,511	48,966
Retained income	135,585	110,441
Accumulated other comprehensive income, net of taxes	3,997	1,114
Total stockholders equity	176,093	160,521
Total liabilities and stockholders equity	$ 599,655	$ 526,316

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Income

(Unaudited)

(Dollar amounts in thousands, except per share amounts)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Revenue				
Gross premiums earned	$ 91,221	$ 81,952	$ 185,109	$ 164,499
Premiums ceded	(28,572)	(24,617)	(56,080)	(46,613)
Net premiums earned	62,649	57,335	129,029	117,886
Net investment income	1,481	295	2,540	434
Policy fee income	638	1,426	895	2,198
Net realized investment gains (losses)	1,167	(8)	1,171	12
Other	349	285	766	614
Total revenue	66,284	59,333	134,401	121,144
Expenses				
Losses and loss adjustment expenses	18,383	17,414	36,948	33,286
Policy acquisition and other underwriting expenses	9,559	7,308	18,688	13,276
Interest expense	2,609	846	5,183	1,532
Other operating expenses	9,350	7,358	18,889	13,473
Total expenses	39,901	32,926	79,708	61,567
Income before income taxes	26,383	26,407	54,693	59,577
Income tax expense	9,953	10,172	20,643	22,955
Net income	$ 16,430	$ 16,235	$ 34,050	$ 36,622
Preferred stock dividends	1	(32)	4	(66)
Income available to common stockholders	$ 16,431	$ 16,203	$ 34,054	$ 36,556
Basic earnings per common share	$ 1.53	$ 1.44	$ 3.14	$ 3.31

Diluted earnings per common share	$	1.39	$	1.40	$	2.84	$	3.20
Dividends per common share	$	0.27	$	0.23	$	0.55	$	0.45

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

(Unaudited)

(Amounts in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
Net income	$ 16,430	$ 16,235	$ 34,050	$ 36,622
Other comprehensive income (loss):				
Change in unrealized gain on investments:				
Unrealized gain (loss) arising during the period	3,541	(1,458)	5,847	(1,183)
Call and repayment losses charged to investment income	2	3	17	18
Reclassification adjustment for realized (gains) losses	(1,167)	8	(1,171)	(12)
Net change in unrealized gain (loss)	2,376	(1,447)	4,693	(1,177)
Deferred income taxes on above change	(917)	559	(1,810)	454
Total other comprehensive income (loss)	1,459	(888)	2,883	(723)
Comprehensive income	$ 17,889	$ 15,347	$ 36,933	$ 35,899

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(Unaudited)

(Amounts in thousands)

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Cash flows from operating activities:		
Net income	$ 34,050	$ 36,622
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock-based compensation	4,333	1,474
Net amortization of premiums on investments in fixed-maturity securities	440	134
Depreciation and amortization	2,436	1,045
Deferred income taxes (benefits)	(1,384)	5,831
Net realized investment gains	(1,171)	(12)
Income from real estate investments	(5)	
Gain on sale of real estate investment	(1)	
Foreign currency remeasurement (gain) loss	(12)	44
Changes in operating assets and liabilities:		
Premiums and reinsurance receivable	(14,088)	(17,663)
Advance premiums	10,369	7,244
Prepaid reinsurance premiums	(5,211)	(22,124)
Accrued interest and dividends receivable	(130)	(35)
Other assets	(6,457)	(3,431)
Assumed reinsurance balances payable	(4,344)	89
Deferred policy acquisition costs	(6,012)	(8,576)
Losses and loss adjustment expenses	(642)	3,581
Unearned premiums	34,750	37,197
Income taxes payable	(440)	(8,689)
Accrued expenses and other liabilities	13,449	9,810
Net cash provided by operating activities	59,930	42,541
Cash flows from investing activities:		
Investment in real estate under acquisition, development, and construction arrangement	(2,591)	
Purchase of property and equipment, net	(166)	(2,692)
Purchase of real estate investments	(312)	(115)
Purchase of fixed-maturity securities	(28,382)	(8,601)
Purchase of equity securities	(24,141)	(2,582)
Proceeds from sales of fixed-maturity securities	19,962	1,359
Proceeds from calls, repayments and maturities of fixed-maturity securities	1,630	1,736
Proceeds from sales of equity securities	5,930	1,313

Proceeds from sales of real estate investments	1	
Net cash used in investing activities	(28,069)	(9,582)
Cash flows from financing activities:		
Proceeds from the issuance of long-term debt		40,250
Proceeds from the exercise of common stock options	125	
Cash dividends paid	(6,319)	(5,094)
Cash dividends received under share repurchase forward contract	342	
Repurchases of common stock	(597)	(235)
Repurchases of common stock under share repurchase plan	(17,810)	
Redemption of Series A preferred stock	(34)	
Debt issuance costs	(234)	(1,525)
Tax benefits on stock-based compensation	1,304	280
Net cash (used in) provided by financing activities	(23,223)	33,676

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows, continued

(Unaudited)

(Amounts in thousands)

	Six Months Ended June 30, 2014	2013
Effect of exchange rate changes on cash	12	(37)
Net increase in cash and cash equivalents	8,650	66,598
Cash and cash equivalents at beginning of period	293,398	230,214
Cash and cash equivalents at end of period	$ 302,048	$ 296,812
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	$ 21,050	$ 25,535
Cash paid for interest	$ 2,652	$ 921
Non-cash investing and financing activities:		
Unrealized gain (loss) on investments in available-for-sale securities, net of tax	$ 2,883	$ (723)
Conversion of Series A Preferred Stock to common stock	$ 991	$ 435

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statement of Stockholders Equity

Six Months Ended June 30, 2014

(Unaudited)

(Dollar amounts in thousands, except per share amounts)

	Series A Preferred Stock Shares	Series A Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Income	Accumulated Other Comprehensive Income, Net of Tax	Total Stockholders Equity
Balance at December 31, 2013	110,684	$	10,939,268	$	$ 48,966	$ 110,441	$ 1,114	$ 160,521
Net income						34,050		34,050
Total other comprehensive income, net of income taxes							2,883	2,883
Conversion of preferred stock to common stock	(107,298)		107,298					
Issuance of restricted stock			98,720					
Exercise of common stock options			50,000		125			125
Forfeiture of restricted stock			(3,330)					
Repurchase and retirement of common stock			(13,541)		(597)			(597)
Repurchase and retirement of common stock under share repurchase plan			(488,346)		(17,810)			(17,810)
Redemption of Series A preferred stock	(3,386)				(25)	(9)		(34)
Deferred taxes on debt discount					215			215
Common stock dividends						(8,901)		(8,901)
Preferred stock dividends						4		4
Tax benefits on stock-based compensation					1,304			1,304

Stock-based compensation			4,333			4,333
Balance at June 30, 2014	$ 10,690,069	$	$ 36,511	$ 135,585	$ 3,997	$ 176,093

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statement of Stockholders Equity - continued

Six Months Ended June 30, 2013

(Unaudited)

(Dollar amounts in thousands, except per share amounts)

	Series A Preferred Stock		Common Stock		Additional Paid-In Capital	Retained Income	Accumulated Other Comprehensive Income, Net of Tax	Total Stockholders Equity
	Shares	Amount	Shares	Amount				
Balance at December 31, 2012	241,182	$	10,877,537	$	$ 63,875	$ 55,758	$ 1,620	$ 121,253
Net income						36,622		36,622
Total other comprehensive income, net of income taxes							(723)	(723)
Conversion of preferred stock to common stock	(49,432)		49,432					
Issuance of restricted stock			544,000					
Forfeiture of restricted stock			(29,080)					
Repurchase and retirement of common stock			(7,673)		(235)			(235)
Common stock dividends						(5,020)		(5,020)
Preferred stock dividends						(66)		(66)
Tax benefits on stock-based compensation					280			280
Stock-based compensation					1,474			1,474
Balance at June 30, 2013	191,750	$	11,434,216	$	$ 65,394	$ 87,294	$ 897	$ 153,585

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (unaudited)

(Dollar amounts in thousands, except per share amounts, unless otherwise stated)

Note 1 Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited, consolidated financial statements for HCI Group, Inc. and its subsidiaries (collectively, the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information, and the Securities and Exchange Commission (SEC) rules for interim financial reporting. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been omitted pursuant to such rules and regulations. However, in the opinion of management, the accompanying financial statements reflect all normal recurring adjustments necessary to present fairly the Company s financial position as of June 30, 2014 and the results of operations and cash flows for the periods presented. The results of operations for the interim periods presented are not necessarily indicative of the results of operations to be expected for any subsequent interim period or for the fiscal year ending December 31, 2014. The accompanying unaudited consolidated financial statements and notes thereto should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2013 included in the Company s Form 10-K, which was filed with the SEC on March 12, 2014.

In preparing the interim unaudited consolidated financial statements, management was required to make certain judgments, assumptions, and estimates that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the financial reporting date and throughout the periods being reported upon. Certain of the estimates result from judgments that can be subjective and complex and consequently actual results may differ from these estimates.

Material estimates that are particularly susceptible to significant change in the near term are related to the Company s losses and loss adjustment expenses, which include amounts estimated for claims incurred but not yet reported. The Company uses various assumptions and actuarial data it believes to be reasonable under the circumstances to make these estimates. In addition, accounting policies specific to reinsurance with retrospective provisions, deferred income taxes, and stock-based compensation expense involve significant judgments and estimates material to the Company s consolidated financial statements.

All significant intercompany balances and transactions have been eliminated.

Acquisition, Development and Construction Loan Arrangement

The Company has an acquisition, development and construction loan arrangement (ADC Arrangement) under which it provides financing to a property developer for the acquisition, development, and construction of a retail shopping center. The Company also expects to participate in the residual profit resulting from the ultimate sale or other use of the property. Classification and accounting for the ADC Arrangement as a loan, an investment in real estate, or joint venture is determined by the Company s evaluation of the characteristics and the risks and rewards of the ADC Arrangement. If the Company expects to receive more than 50% of the residual profit from the ADC arrangement and it has characteristics similar to a real estate investment, the costs of the real estate project will be capitalized and interest will be recognized in net investment income (see Note 3 Investments).

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (unaudited)

(Dollar amounts in thousands, except per share amounts, unless otherwise stated)

In addition, the Company considers any rights or features embedded in the ADC Arrangement that may require bifurcation and derivative accounting. Due to its participation in the expected residual profit, which is deemed a variable interest, the Company evaluates its involvements in the design and essential activities of the entity to which the Company provides financing for possible consolidation as the primary beneficiary under the Variable Interest Model prescribed by the Financial Accounting Standards Board (FASB).

Any subsequent changes in terms, rights or the developer s equity interest that may result in a reclassification or a change in the accounting treatment of the ADC Arrangement will be evaluated. The Company will continually assess the collectability of principal, accrued interest and fees.

Note 2 Recent Accounting Pronouncements

Accounting Standards Update No. 2014-12. In June 2014, the FASB issued Accounting Standards Update No. 2014-12 (ASU 2014-12), Compensation Stock Compensation (Topic 718). ASU 2014-12 applies to all reporting entities that grant their employees share-based payments in which the terms of the award provide that a performance target that affects vesting could be achieved after the requisite service period. ASU 2014-12 is effective for all entities for reporting periods beginning after December 15, 2015. Early adoption is permitted. Entities may apply the amendments in this Update either (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. Although the Company has share-based awards with performance targets, none of the awards permit vesting when a performance target is achieved after termination of an employee s service. Adoption of this guidance had no effect on the Company s consolidated financial statements.

Accounting Standards Update No. 2014-09. In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (ASU 2014-09), Revenue from Contracts with Customers (Topic 606). The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance throughout the Industry Topics of the Codification. ASU 2014-09 also amends the existing requirements for the recognition of a gain or loss on the transfer of nonfinancial assets that are not in a contract with a customer to be consistent with the guidance on recognition and measurement in this Update. ASU 2014-09 is effective for public entities for reporting periods beginning after December 15, 2016. Early adoption is not permitted. While the guidance specifically excludes revenues from insurance contracts, investments and financial instruments from the scope of the new guidance, the guidance will be applicable to the Company s other forms of revenue not specifically exempted from the guidance. The adoption of this guidance is not expected to have a material effect on the Company s consolidated financial statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (unaudited)

(Dollar amounts in thousands, except per share amounts, unless otherwise stated)

Note 3 Investments

The Company holds investments in fixed-maturity securities and equity securities that are classified as available-for-sale. At June 30, 2014 and December 31, 2013, the cost or amortized cost, gross unrealized gains and losses, and estimated fair value of the Company s available-for-sale securities by security type were as follows:

	Cost or Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
As of June 30, 2014				
Fixed-maturity securities				
U.S. Treasury and U.S. government agencies	$ 1,460	$ 49	$	$ 1,509
Corporate bonds	27,954	928	(9)	28,873
Commercial mortgage-backed securities	11,295	501	(37)	11,759
State, municipalities, and political subdivisions	70,601	2,964	(28)	73,537
Redeemable preferred stock	6,634	120	(2)	6,752
Total	117,944	4,562	(76)	122,430
Equity securities	35,791	2,387	(366)	37,812
Total available-for-sale securities	$ 153,735	$ 6,949	$ (442)	$ 160,242
As of December 31, 2013				
Fixed-maturity securities				
U.S. Treasury and U.S. government agencies	$ 4,549	$ 37	$ (22)	$ 4,564
Corporate bonds	25,139	484	(219)	25,404
Commercial mortgage-backed securities	10,929	499	(96)	11,332
State, municipalities, and political subdivisions	69,715	917	(181)	70,451
Redeemable preferred stock	406	5	(11)	400
Total	110,738	1,942	(529)	112,151
Equity securities	17,248	920	(519)	17,649
Total available-for-sale securities	$ 127,986	$ 2,862	$ (1,048)	$ 129,800

As of June 30, 2014 and December 31, 2013, $111 and $105, respectively, of U.S. Treasury securities relate to a statutory deposit held in trust for the Treasurer of Alabama.

Expected maturities will differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without penalties. The scheduled contractual maturities of fixed-maturity securities as of June 30, 2014 and December 31, 2013 are as follows:

	Amortized Cost	Estimated Fair Value
As of June 30, 2014		
Available-for-sale		
Due in one year or less	$ 2,218	$ 2,230
Due after one year through five years	31,124	31,764
Due after five years through ten years	58,468	60,968
Due after ten years	14,839	15,709
Commercial mortgage-backed securities	11,295	11,759
	$ 117,944	$ 122,430

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (unaudited)

(Dollar amounts in thousands, except per share amounts, unless otherwise stated)

	Amortized Cost	Estimated Fair Value
As of December 31, 2013		
Available-for-sale		
Due in one year or less	$ 2,366	$ 2,381
Due after one year through five years	24,829	25,145
Due after five years through ten years	59,083	59,582
Due after ten years	13,531	13,711
Commercial mortgage-backed securities	10,929	11,332
	$ 110,738	$ 112,151

Investment Sales

Proceeds received, and the gross realized gains and losses from sales of available-for-sale securities, for the three and six months ended June 30, 2014 and 2013 were as follows:

	Proceeds	Gross Realized Gains	Gross Realized Losses
Three months ended June 30, 2014			
Fixed-maturity securities	$ 18,271	$ 799	$
Equity securities	$ 3,166	$ 433	$ (65)
Three months ended June 30, 2013			
Fixed-maturity securities	$ 322	$ 2	$ (3)
Equity securities	$ 952	$ 44	$ (51)
Six months ended June 30, 2014			
Fixed-maturity securities	$ 19,962	$ 864	$ (9)
Equity securities	$ 5,930	$ 508	$ (192)

Six months ended June 30, 2013			
Fixed-maturity securities	$ 1,359	$ 34	$ (3)
Equity securities	$ 1,313	$ 64	$ (83)

Other-than-temporary Impairment (OTTI)

The Company regularly reviews its individual investment securities for OTTI. The Company considers various factors in determining whether each individual security is other-than-temporarily impaired, including:

- the financial condition and near-term prospects of the issuer, including any specific events that may affect its operations or earnings;

- the length of time and the extent to which the market value of the security has been below its cost or amortized cost;

- general market conditions and industry or sector specific factors;

- nonpayment by the issuer of its contractually obligated interest and principal payments; and

- the Company s intent and ability to hold the investment for a period of time sufficient to allow for the recovery of costs.

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (unaudited)

(Dollar amounts in thousands, except per share amounts, unless otherwise stated)

Securities with gross unrealized loss positions at June 30, 2014 and December 31, 2013, aggregated by investment category and length of time the individual securities have been in a continuous loss position, are as follows:

As of June 30, 2014	Less Than Twelve Months		Twelve Months or Greater		Total	
	Gross Unrealized Loss	Estimated Fair Value	Gross Unrealized Loss	Estimated Fair Value	Gross Unrealized Loss	Estimated Fair Value
Fixed-maturity securities						
Corporate bonds	$ (4)	$ 999	$ (5)	$ 1,227	$ (9)	$ 2,226
Commercial mortgage-backed securities	(3)	640	(34)	1,396	(37)	2,036
State, municipalities, and political subdivisions	(8)	2,220	(20)	203	(28)	2,423
Redeemable preferred stock	(2)	759		49	(2)	808
Total fixed-maturity securities	(17)	4,618	(59)	2,875	(76)	7,493
Equity securities	(184)	10,099	(182)	2,035	(366)	12,134
Total available-for-sale securities	$ (201)	$ 14,717	$ (241)	$ 4,910	$ (442)	$ 19,627

As of December 31, 2013	Less Than Twelve Months		Twelve Months or Greater		Total	
	Gross Unrealized Loss	Estimated Fair Value	Gross Unrealized Loss	Estimated Fair Value	Gross Unrealized Loss	Estimated Fair Value
Fixed-maturity securities						
U.S. Treasury and U.S. government agencies	$ (22)	$ 3,291	$	$	$ (22)	$ 3,291
Corporate bonds	(212)	9,502	(7)	230	(219)	9,732
Commercial mortgage-backed securities	(96)	2,179			(96)	2,179
State, municipalities, and political subdivisions	(181)	20,233			(181)	20,233
Redeemable preferred stock	(11)	239			(11)	239
Total fixed-maturity securities	(522)	35,444	(7)	230	(529)	35,674
Equity securities	(273)	10,742	(246)	1,069	(519)	11,811

Total available-for-sale securities	$	(795)	$	46,186	$	(253)	$	1,299	$	(1,048)	$	47,485

The Company believes there are no fundamental issues such as credit losses or other factors with respect to any of its available-for-sale securities. The unrealized losses on investments in fixed-maturity securities were caused primarily by interest-rate changes. It is expected that the securities will not be settled at a price less than the par value of the investments. In determining whether equity securities are other-than-temporarily impaired, the Company considers its intent and ability to hold a security for a period of time sufficient to allow for the recovery of cost. Because the declines in fair value are attributable to changes in interest rates or market conditions and not credit quality, and because the Company has the ability and intent to hold its available-for-sale investments until a market price recovery or maturity, the Company does not consider any of its investments to be other-than-temporarily impaired at June 30, 2014.

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Real Estate Investments

Real estate investments consist of the following as of June 30, 2014 and December 31, 2013:

	June 30, 2014	December 31, 2013
Land	$ 11,476	$ 11,299
Land improvements	1,399	1,351
Buildings	3,097	3,022
Other	1,273	1,262
Total, at cost	17,245	16,934
Less: accumulated depreciation and amortization	(903)	(706)
Real estate, net	16,342	16,228
ADC Arrangement classified as real estate investment	2,596	
Real estate investments	$ 18,938	$ 16,228

Depreciation and amortization expense related to real estate investments was $100 and $96, respectively, for the three months ended June 30, 2014 and 2013 and $198 and $191, respectively, for the six months ended June 30, 2014 and 2013.

Acquisition, Development and Construction Loan Arrangement (ADC Arrangement)

In June 2014, the Company s wholly owned subsidiary, Greenleaf Capital, LLC, entered into an ADC Arrangement under which it agreed to provide financing up to a maximum of $9,785 for the acquisition, development and construction of a retail shopping center and appurtenant facilities. Greenleaf Capital has an option to purchase the property when the construction project is completed contingent upon tenant rental commitments for at least 90% of rentable space being secured by the developer. The purchase price is calculated at maturity of the loan using a predetermined capitalization rate and the projected net operating income of the developed property. The loan has an initial term of 24 months and can be extended for an additional 12 months if the purchase option is not exercised by Greenleaf Capital. Prepayment is not permitted while the ADC Arrangement is in effect. The loan bears a fixed annual interest rate of 6% due monthly in arrears. The loan agreement is secured by a) a first mortgage on the land and improvements, b) assignment of all leases, rents, issues, and profits from the land and improvements, and c) personal guarantees.

Under this ADC Arrangement, Greenleaf Capital will provide substantially all necessary funds to complete the development and Greenleaf Capital will receive the entire residual profit of the developed property if it exercises the purchase option. The developer may make multiple draws on the credit facility as the construction progresses. Based on the characteristics of this ADC Arrangement which are similar to those of an investment, combined with the expected residual profit being greater than 50%, the arrangement is accounted for and reported in the balance sheet as a real estate investment. All project costs associated with the ADC Arrangement are capitalized. The loan commitment fee received by Greenleaf Capital is deferred and recognized in investment income on a straight-line basis over the term of the loan agreement.

Because of the purchase option and the substantial financial support provided by Greenleaf Capital, the developer who has no equity interest in the property is a variable interest entity (VIE). However, Greenleaf Capital s involvement is solely as the lender on the mortgage loan with

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protective rights as the lender. Greenleaf Capital does not have power to direct the activities that most significantly impact economic performance of the VIE. As a result, Greenleaf Capital is not the primary beneficiary and is not required to consolidate the VIE. At June 30, 2014, the Company s maximum exposure to loss relating to the VIE was $2,596 representing the carrying value of the ADC Arrangement.

In addition, Greenleaf Capital determined that the option to purchase the entire developed property is not a derivative financial instrument pursuant to U.S. GAAP. As such, the embedded feature is not required to be bifurcated and the fair value accounting for the embedded feature at each reporting date is not applicable.

Note 4 Fair Value Measurements

The Company records and discloses certain financial assets at their estimated fair value but does not elect the fair value option for the ADC Arrangement and its long-term debt. The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows:

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities.
Level 2 - Other inputs that are observable for the asset and liability, either directly or indirectly.
Level 3 - Inputs that are unobservable.

The following table presents information about the Company s financial assets measured at estimated fair value on a recurring basis, the estimated fair values of the real estate investment under the ADC Arrangement, and long-term debt that are reflected in the financial statements at carrying value. The table indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value as of June 30, 2014 and December 31, 2013:

	Fair Value Measurements Using			
	(Level 1)	**(Level 2)**	**(Level 3)**	**Total**
As of June 30, 2014				
Financial Assets:				
Cash and cash equivalents	$ 302,048	$	$	$ 302,048
Fixed-maturity securities:				
U.S. Treasury and U.S. government agencies	668	841		1,509
Corporate bonds	27,875	998		28,873
Commercial mortgage-backed securities		11,759		11,759
State, municipalities, and political subdivisions		73,537		73,537

Redeemable preferred stock	6,752			6,752
Total fixed-maturity securities	35,295	87,135		122,430
Equity securities	37,812			37,812
Total available-for-sale securities	73,107	87,135		160,242
ADC Arrangement classified as real estate investment			2,522	2,522
Total	$ 375,155	$ 87,135	$ 2,522	$ 464,812
Financial Liabilities:				
Long-term debt:				
8% Senior notes	$	$ 43,422	$	$ 43,422
3.875% Convertible senior notes			99,642	99,642
Total long-term debt	$	$ 43,422	$ 99,642	$ 143,064

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	Fair Value Measurements Using			
	(Level 1)	(Level 2)	(Level 3)	Total
As of December 31, 2013				
Financial Assets:				
Cash and cash equivalents	$ 293,398	$	$	$ 293,398
Fixed-maturity securities:				
U.S. Treasury and U.S. government agencies	3,520	1,044		4,564
Corporate bonds	24,476	928		25,404
Commercial mortgage-backed securities		11,332		11,332
State, municipalities, and political subdivisions		70,451		70,451
Redeemable preferred stock	400			400
Total fixed-maturity securities	28,396	83,755		112,151
Equity securities	17,649			17,649
Total available-for-sale securities	46,045	83,755		129,800
Total	$ 339,443	$ 83,755	$	$ 423,198
Financial Liabilities:				
Long-term debt:				
8% Senior notes	$	$ 43,390	$	$ 43,390
3.875% Convertible senior notes			86,630	86,630
Total long-term debt	$	$ 43,390	$ 86,630	$ 130,020