

FEDERATED NATIONAL HOLDING CO
Form 10-Q
May 11, 2015

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 March 31, 2015
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 0-2500111

Federated National Holding Company
(Exact name of registrant as specified in its charter)

Florida	65-0248866
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

14050 N.W. 14th Street, Suite 180, Sunrise, Florida 33323
(Address of principal executive offices) (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.

Large accelerated filer Accelerated filer 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

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

Common Stock, \$.01 par value –14,172,923 outstanding as of May 3, 2015

FEDERATED NATIONAL HOLDING COMPANY

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PART I: FINANCIAL INFORMATION

Item 1. Financial Statements

FEDERATED NATIONAL HOLDING COMPANY
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

	Period Ending	
	March	December
	31, 2015	31, 2014
	(Dollars in Thousands)	
ASSETS		
Investments		
Debt maturities, available for sale, at fair value	\$288,193	\$284,099
Debt maturities, held to maturity, at amortized cost	7,462	7,417
Equity securities, available for sale, at fair value	40,726	39,247
 Total investments	 336,381	 330,763
 Cash and short term investments	 88,163	 40,157
Prepaid reinsurance premiums	46,039	54,502
Premiums receivable, net of allowance for credit losses of \$148 and \$148, respectively	29,809	27,275
Reinsurance recoverable, net	13,034	12,534
Deferred policy acquisition costs	15,765	13,610
Income taxes receivable	2,090	1,810
Property, plant and equipment, net	1,720	1,749
Other assets	8,265	7,231
Contingent quota-share profit sharing	14,000	14,000
 Total assets	 \$555,266	 \$503,631
 LIABILITIES AND SHAREHOLDERS' EQUITY		
Unpaid losses and LAE	\$84,475	\$78,330
Unearned premiums	203,433	192,424
Debt	5,000	-
Premiums deposits and customer credit balances	11,291	7,381
Deferred income taxes, net	1,897	1,341
Claims payments outstanding	9,653	10,152
Accounts payable and accrued expenses	8,967	10,924
Deferred quota-share profit sharing	8,750	10,500
 Total liabilities	 333,466	 311,052
 Shareholders' equity:		
Common stock, \$0.01 par value. Authorized 25,000,000 shares; issued and outstanding 13,701,122 and 13,632,414, respectively	137	136
Preferred stock, \$0.01 par value. Authorized 1,000,000 shares; none issued or outstanding	-	-
Additional paid-in capital	128,611	127,302
Accumulated other comprehensive income		
Unrealized net gains on investments, available for sale	8,925	7,718

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Total accumulated other comprehensive income	8,925	7,718
Retained earnings	66,140	57,423
Total Federated National Holding Company equity	203,813	192,579
Non-controlling interest	17,987	-
Total shareholders' equity	221,800	192,579
Total liabilities and shareholders' equity	\$555,266	\$503,631

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended March 31,	
	2015	2014
	(Dollars in Thousands)	
Revenue:		
Gross premiums written	\$ 106,702	\$ 81,102
Gross premiums ceded	(25,958)	(3,306)
Net premiums written	80,744	77,796
Decrease in prepaid reinsurance premiums	(24,949)	(16,795)
Increase in unearned premiums	(11,009)	(16,997)
Net change in prepaid reinsurance premiums and unearned premiums	(35,958)	(33,792)
Net premiums earned	44,786	44,004
Commission income	1,126	954
Finance revenue	427	311
Direct written policy fees	2,492	1,827
Net investment income	1,546	1,007
Net realized investment gains	1,704	1,331
Other income	1,378	281
Quota-share profit sharing, net	1,477	-
Total revenue	54,936	49,715
Expenses:		
Losses and LAE	23,949	20,828
Operating and underwriting expenses	6,322	3,667
Salaries and wages	5,137	3,050
Amortization of deferred policy acquisition costs	5,044	8,442
Total expenses	40,452	35,987
Income before provision for income tax expense	14,484	13,728
Provision for income tax expense	5,711	5,305
Income before non-controlling interest	8,773	8,423
Non-controlling interest	(511)	-
Net income attributable to Federated National Holding Company common stockholders	\$ 9,284	\$ 8,423
Net income per share - basic	\$ 0.68	\$ 0.77
Net income per share - diluted	\$ 0.66	\$ 0.74

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Weighted average number of common shares outstanding - basic	13,656,190	10,948,646
Weighted average number of common shares outstanding - diluted	13,976,131	11,317,458
Dividends paid per share	\$0.04	\$0.03

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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FEDERATED NATIONAL HOLDING COMPANY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

	Three Months Ended March 31, 2015 2014 (Dollars in Thousands)	
Net income	\$9,284	\$8,423
Change in net unrealized gains on investments available for sale	1,965	880
Comprehensive income before tax	11,249	9,303
Income tax expense related to items of other comprehensive income	(758)	(430)
Comprehensive income	\$10,491	\$8,873

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

IndexFEDERATED NATIONAL HOLDING COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended March 31, 2015 2014	
	(Dollars in Thousands)	
Cash flow from operating activities:		
Net income	\$9,284	\$8,423
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of investment premium or discount, net	1,253	844
Depreciation and amortization of property plant and equipment, net	152	76
Net realized investment gains	(1,704)	(1,331)
Non-cash compensation	999	134
Changes in operating assets and liabilities:		
Premiums receivable	(2,535)	(1,537)
Prepaid reinsurance premiums	8,463	6,755
Reinsurance recoverable, net	(500)	33
Income taxes recoverable	(280)	-
Deferred income tax expense, net of other comprehensive income	(202)	(574)
Policy acquisition costs, net of amortization	(2,156)	(1,757)
Other assets	(1,034)	(970)
Contingent quota-share profit sharing	(1,750)	-
Unpaid losses and LAE	6,145	1,538
Unearned premiums	11,009	16,997
Debt	5,000	-
Premium deposits and customer credit balances	3,911	3,383
Income taxes payable	-	1,978
Claims payments outstanding	(499)	(991)
Accounts payable and accrued expenses	(1,957)	(383)
Net cash provided by operating activities	33,599	32,618
Cash flow used by investing activities:		
Proceeds from sale of investment securities	56,264	20,946
Purchases of investment securities available for sale	(59,466)	(44,387)
Purchases of property and equipment	(122)	(218)
Net cash used by investing activities	(3,324)	(23,659)
Cash flow provided by financing activities:		
Exercised stock options	\$27	\$353
Dividends paid	(566)	(341)
Non-controlling interest	17,987	-
Tax benefit related to non-cash compensation	283	72
Net cash provided by financing activities	17,731	84
Net increase in cash and short term investments	48,006	9,043
Cash and short term investments at beginning of period	40,157	41,446
Cash and short term investments at end of period	\$88,163	\$50,489

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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FEDERATED NATIONAL HOLDING COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended March 31,	
(continued)	2015	2014
	(Dollars in Thousands)	
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes	\$5,662	\$3,885
Non-cash investing and finance activities:		
Accrued dividends payable	\$567	\$336

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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Federated National Holding Company
Notes to Condensed Consolidated Financial Statements

(1) Organization and Business

In this Quarterly Report on Form 10-Q, “FNHC” and the terms “Company”, “we”, “us” and “our” refer to Federated National Holding Company and its subsidiaries, unless the context indicates otherwise. We changed our name on September 11, 2012, pursuant to approval received at our annual shareholders’ meeting, from 21st Century Holding Company so that our parent company and other subsidiary companies’ names are consistent with our primary insurance subsidiary and the name under which we have been writing insurance for more than 23 years.

FNHC 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”), commercial general liability, federal flood, personal auto and various other lines of insurance in Florida and various other states. We market and distribute 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”). FNIC 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 their policyholders. Through contractual relationships with a network of approximately 3,800 independent agents, of which approximately 2,300 actively sell and service our products, FNIC is authorized to underwrite homeowners’, commercial general liability, fire, allied lines, and personal automobile insurance in Florida. FNIC is licensed as an admitted carrier in Alabama, Louisiana, Georgia, and Texas and underwrites commercial general liability insurance in those states. FNIC also underwrites homeowners’ insurance in Alabama and Louisiana and just became admitted in South Carolina to underwrite homeowners insurance. Additionally, we underwrite personal automobile insurance in Georgia and Texas.

FNIC is licensed as a non-admitted carrier in Missouri and Nevada and can underwrite commercial general liability insurance in these states. Currently, we do not have any operations in these states. A non-admitted carrier, sometimes referred to as an “excess and surplus lines” carrier, is permitted to do business in a state and, although it is strictly regulated to protect policyholders from a variety of illegal and unethical practices, including fraud, non-admitted carriers are subject to considerably less regulation with respect to policy rates and forms. Non-admitted carriers are not required to financially contribute to and benefit from the state guarantee fund, which is used to pay for losses if an insurance carrier becomes insolvent or unable to pay the losses due their policyholders.

The Company has entered into a joint venture to organize Monarch National Insurance Company, 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”) on March 19, 2015. The Company’s joint venture partners are a majority-owned limited partnership of Crosswinds Holdings Inc., f/k/a C.A. Bancorp Inc., a publicly traded Canadian private equity firm and asset manager; and Transatlantic Reinsurance Company. For more information regarding the organization of Monarch National Insurance Company, please see Note 11, Subsequent Events.

We previously entered into a Coexistence Agreement effective August 30, 2013 (the “Coexistence Agreement”) with Federated Mutual Insurance Company (“Federated Mutual”) pursuant to which, among other things, we may continue to use “Federated” until at least August 30, 2020, after which time we have agreed to either cease using “Federated” in commerce or otherwise adopt and use trade names that are not confusingly similar to Federated Mutual’s trademarks. We continue to develop our brand under the “FedNat” name, which is the name by which agents generally know us.

As of September 30, 2014, we had satisfied all applicable conditions of the Consent Order we entered into in January 2011 (the “Consent Order”) with the Florida Office of Insurance Regulation (“Florida OIR”). We entered into the Consent Order in connection with the merger of our one of our wholly owned insurance subsidiaries, American Vehicle Insurance Company (“American Vehicle”), into FNIC, with FNIC continuing the operations of both entities. As of the date of this Report, the only operational restriction that remains in effect is a requirement to obtain OIR approval prior to writing commercial multi-peril business or any new commercial property business, including condo associations, under any other line of business for which FNIC is authorized. FNIC currently has no commercial multi-peril policy premium in-force and the current commercial habitation book of business is fully earned. The Consent Order required us to, among other things, limit the number of policies that we write in the Tri-County area and imposed certain other operational requirements on us, all of which we have complied with.

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