Heritage Insurance Holdings, Inc.
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

Commission File Number

001-36462

Heritage Insurance Holdings, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	45-5338504
(State of Incorporation)	(IRS Employer Identification No.)

2600 McCormick Drive, Suite 300

Clearwater, Florida 33759

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

(727) 362-7200

(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 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 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

The aggregate number of shares of the Registrant's Common Stock, $0.0001 par value, outstanding on November 3, 2016 was 31,566,410.

HERITAGE INSURANCE HOLDINGS, INC.

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FORWARD-LOOKING STATEMENTS

Statements in this Quarterly Report on Form 10-Q ("Form 10-Q") or in documents incorporated by reference that are not historical facts are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements about anticipated growth in revenue, earnings per share, estimated unpaid losses on insurance policies, investment returns and expectations about our liquidity, and our ability to meet our investment objectives and to manage and mitigate market risk with respect to our investments. These statements are based on current expectations, estimates and projections about the industry and market in which we operate, and management's beliefs and assumptions. Without limiting the generality of the foregoing, words such as "may," "will," "expect," "believe," "anticipate," "intend," "could," "would," "estimate," or "continue" or the negative variatio comparable terminology are intended to identify forward-looking statements. Forward-looking statements are not guarantees of future performance and involve certain known and unknown risks and uncertainties that could cause actual results to differ materially from those expressed or implied by such statements. The risks and uncertainties include, without limitation:

- increased costs of reinsurance, non-availability of reinsurance, and non-collectability of reinsurance;
- the potential for discontinuation of the Citizens depopulation program and our inability to select favorable Citizens policies to assume;
- a lack of significant redundancy in our operations;
- our exposure to catastrophic events;
- our failure to attract and retain qualified employees and independent agents or our loss of key personnel;
- our inability to generate investment income;
- our inability to maintain our financial stability rating;
- effects of emerging claim and coverage issues relating to legal, judicial, environmental and social conditions;
- the failure of our risk mitigation strategies or loss limitation methods; and
- other risks and uncertainties described in the section entitled "Risk Factors" in Part I, Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2015.

Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or operating results.

These forward-looking statements are subject to numerous risks, uncertainties and assumptions about us described in our filings with the Securities and Exchange Commission (the "SEC"). The forward-looking statements we make in our Form 10-Q are valid only as of the date of our Form 10-Q and may not occur in light of the risks, uncertainties and assumptions that we describe from time to time in our filings with the SEC. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from our forward-looking statements is included in the section entitled "Risk Factors" in Part I, Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2015. Except as required by applicable law, we undertake no obligation and disclaim any obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

PART I – FINANCIAL INFORMATION

Item 1 – Financial Statements

HERITAGE INSURANCE HOLDINGS, INC.

Condensed Consolidated Balance Sheets

(Amounts in thousands, except per share and share amounts)

ASSETS	September 30, 2016 (unaudited)	December 31, 2015
Fixed maturity securities, available for sale, at fair value (amortized cost of $509,184 and $370,967 in 2016 and 2015, respectively)	$ 517,573	$ 371,783
Equity securities, available for sale, at fair value (cost of $33,935 and $32,439 in 2016 and 2015, respectively)	32,205	28,313
Total investments	549,778	400,096
Cash and cash equivalents	130,835	236,277
Restricted cash	19,261	13,085
Accrued investment income	4,624	3,409
Premiums receivable, net	35,161	30,565
Prepaid reinsurance premiums	168,650	78,517
Income taxes receivable	5,280	—
Deferred income taxes	—	7,964
Deferred policy acquisition costs, net	42,129	34,800
Property and equipment, net	17,600	17,111
Intangibles, net	26,402	2,120
Goodwill	48,267	8,028
Other assets	5,727	5,426
Total Assets	$ 1,053,714	$ 837,398
LIABILITIES AND STOCKHOLDERS' EQUITY		
Unpaid losses and loss adjustment expenses	$ 125,695	$ 83,722
Unearned premiums	323,354	302,493
Reinsurance payable	177,867	60,210
Deferred income taxes	6,966	—
Income tax payable	—	2,092
Advance premiums	20,382	12,138
Accrued compensation	5,500	2,305
Other liabilities	16,706	17,885

Total Liabilities	676,470	480,845
Commitments and contingencies (Note 15)		
Stockholders’ Equity:		
Common stock, $0.0001 par value, 50,000,000 shares authorized, 30,141,744 shares issued and 29,016,744 outstanding at September 30, 2016 and 30,441,410 outstanding at December 31, 2015	3	3
Additional paid-in capital	206,240	202,628
Accumulated other comprehensive income (loss)	4,116	(2,033)
Treasury stock, at cost, 1,424,666 shares at September 30, 2016	(20,562)	—
Retained earnings	187,447	155,955
Total Stockholders' Equity	377,244	356,553
Total Liabilities and Stockholders' Equity	$ 1,053,714	$ 837,398

See accompanying notes to unaudited condensed consolidated financial statements.

HERITAGE INSURANCE HOLDINGS, INC.

Condensed Consolidated Statements of Income and Other Comprehensive Income

(Unaudited)

(Amounts in thousands, except per share and share amounts)

	Three Months Ended September 30, 2016	2015	Nine Months Ended September 30, 2016	2015
REVENUE:				
Gross premiums written	$147,232	$148,993	$471,793	$418,558
Change in gross unearned premiums	17,464	(20,759)	8,483	(37,222)
Gross premiums earned	164,696	128,234	480,276	381,336
Ceded premiums	(63,141)	(45,873)	(163,461)	(102,640)
Net premiums earned	101,555	82,361	316,815	278,696
Net investment income	2,326	1,973	6,586	5,696
Net realized gains	1,119	1,946	1,762	1,827
Other revenue	4,306	2,964	10,988	7,241
Total revenue	109,306	89,244	336,151	293,460
EXPENSES:				
Losses and loss adjustment expenses	53,906	35,791	169,663	102,239
Policy acquisition costs	22,597	15,512	61,478	40,858
General and administrative expenses	14,191	10,226	44,602	33,366
Total expenses	90,694	61,529	275,743	176,463
Income before income taxes	18,612	27,715	60,408	116,997
Provision for income taxes	7,682	10,902	23,688	44,728
Net income	$10,930	$16,813	$36,720	$72,269
OTHER COMPREHENSIVE INCOME:				
Change in net unrealized gains (losses) on investments	(1,237)	(1,168)	11,773	(6,638)
Reclassification adjustment for net realized investment (gains) losses	(1,119)	(1,946)	(1,762)	(1,827)
Income tax benefit (expense) related to items of other comprehensive income (loss)	908	1,201	(3,862)	3,265
Total comprehensive income	$9,482	$14,900	$42,869	$67,069
Weighted average shares outstanding				
Basic	29,213,222	30,177,633	29,742,984	29,952,668
Diluted	29,213,222	30,483,553	29,786,156	30,289,328
Earnings per share				
Basic	$0.37	$0.56	$1.23	$2.41
Diluted	$0.37	$0.55	$1.23	$2.39

See accompanying notes to unaudited condensed consolidated financial statements.

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HERITAGE INSURANCE HOLDINGS, INC.

Condensed Consolidated Statements of Stockholders’ Equity

Nine Months Ended September 30, 2016 and 2015

(Unaudited)

(Amounts in thousands, except share amounts)

	Common Shares	Par Value	Additional Paid-In Capital	Retained Earnings	Treasury Shares	Accumulated Other Comprehensive (Loss) Income	Total Stockholders' Equity
Balance at December 31, 2015	30,441,410	$ 3	$ 202,628	$ 155,955	$ —	$ (2,033)	$ 356,553
Buy-back common shares of Company stock	(1,424,666)	—	—	—	(20,562)	—	(20,562)
Stock-based compensation	—	—	3,612	—	—	—	3,612
Dividends declared on common stock	—	—	—	(5,228)	—	—	(5,228)
Net unrealized change in investments, net of tax	—	—	—	—	—	6,149	6,149
Net income	—	—	—	36,720	—	—	36,720
Balance at September 30, 2016	29,016,744	$ 3	$ 206,240	$ 187,447	$ (20,562)	$ 4,116	$ 377,244

	Common Shares	Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance at December 31, 2014	29,794,960	$ 3	$ 188,342	$ 65,021	$ 1,723	$ 255,089
Stock-based compensation	—	—	1,873	—	—	1,873
Issuance of restricted common stock in connection with the acquisition of BRC Restoration	79,850	—	2,000	—	—	2,000
Exercise of stock options and warrants	410,600	—	6,369	—	—	6,369
Net unrealized change in investments, net of tax	—	—	—	—	(5,200)	(5,200)

Net income	—	—	—	72,269	—	72,269
Balance at September 30, 2015	30,285,410	$ 3	$ 198,584	$ 137,290	$ (3,477)	$ 332,400

See accompanying notes to unaudited condensed consolidated financial statements.

HERITAGE INSURANCE HOLDINGS, INC.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(Amounts in thousands)

	Nine Months Ended September 30, 2016	2015
OPERATING ACTIVITIES		
Net income	$36,720	$72,269
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock-based compensation	3,612	1,873
Amortization of bond discount	5,924	4,688
Depreciation and amortization	6,075	926
Net realized gains	(1,762)	(1,827)
Deferred income taxes, net of acquired	11,069	3,445
Changes in operating assets and liabilities:		
Accrued investment income	(1,215)	(665)
Premiums receivable, net	(3,194)	(6,561)
Restricted cash	(6,176)	(8,447)
Prepaid reinsurance premiums	(85,341)	(80,393)
Reinsurance premium payable	—	(14,398)
Income taxes receivable	(5,280)	(6,666)
Deferred policy acquisition costs, net	(7,329)	(8,124)
Other assets	225	(1,284)
Unpaid losses and loss adjustment expenses	41,973	22,976
Unearned premiums	(8,484)	37,222
Reinsurance payable	117,657	118,476
Income taxes payable	(2,092)	(12,808)
Accrued compensation	1,977	11,224
Advance premiums	6,153	7,923
Other liabilities	(10,917)	(22,311)
Net cash provided by operating activities	99,595	117,538
INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments available for sale	135,802	119,181
Purchases of investments available for sale	(203,091)	(201,885)
Acquisition of a business, net of cash acquired	(110,319)	(6,000)
Proceeds from sale of investment in mortgage loan	—	6,849
Cost of property and equipment acquired	(1,639)	(1,263)
Net cash used in investing activities	(179,247)	(83,118)
FINANCING ACTIVITIES		

Proceeds from exercise of stock options	—	6,369
Dividends	(5,228)	—
Purchase of treasury stock	(20,562)	—
Net cash (used in) provided by financing activities	(25,790)	6,369
(Decrease) Increase in cash and cash equivalents	(105,442)	40,789
Cash and cash equivalents at beginning of period	236,277	160,481
Cash and cash equivalents at end of period	$130,835	$201,270
Supplemental Cash Flows Information:		
Income taxes paid, net	$27,912	$61,200
Issuance of shares for consideration in the acquisition of a business	$—	$2,000

See accompanying notes to unaudited condensed consolidated financial statements.

HERITAGE INSURANCE HOLDINGS, INC.

Notes to Unaudited Condensed Consolidated Financial Statements

(Amounts in thousands, except per share and share amounts, unless otherwise indicated)

NOTE 1. BASIS OF PRESENTATION

Basis of Presentation

The condensed consolidated financial statements as of and for the three and nine months ended September 30, 2016 and 2015 include Heritage Insurance Holdings, Inc. (“Parent Company”) and its wholly owned subsidiaries: Heritage Property & Casualty Insurance Company (“Heritage P&C”), which provides personal and commercial residential insurance; Heritage MGA, LLC, the managing general agent that manages substantially all aspects of our insurance subsidiary’s business; Contractors’ Alliance Network, LLC (“CAN”), our vendor network manager which includes BRC Restoration Specialists, Inc. (“BRC”), our provider of restoration, emergency and recovery services; Zephyr Acquisition Company (“ZAC”) and its wholly-owned subsidiary, Zephyr Insurance Company, Inc. (“Zephyr”), our provider for writing insurance policies for residential wind insurance within the State of Hawaii; Skye Lane Properties, LLC, our property management subsidiary; First Access Insurance Group, LLC, our retail agency; Osprey Re Ltd. (“Osprey”), our reinsurance subsidiary that provides a portion of the reinsurance protection purchased by our insurance subsidiary; and Heritage Insurance Claims, LLC, an inactive subsidiary reserved for future development. The assets of BRC, a building restoration company, were acquired and merged into CAN in 2015. The assets of SVM Restoration Services Inc. (“SVM”), a water mitigation company, were acquired and merged into CAN in 2014.

Our primary products are personal and commercial residential insurance, which we currently offer in Florida, under authorization from the Florida Office of Insurance Regulation (“FLOIR”). We also began offering personal residential insurance in the states of North Carolina, South Carolina and through the Zephyr acquisition, Hawaii. We are also licensed to do business in Georgia, Alabama and Mississippi. We conduct our operations under one business segment.

The condensed consolidated financial information included herein as of and for the three and nine months ended September 30, 2016 and 2015 does not include all of the information and footnotes required by U.S. generally accepted accounting principles (“GAAP”) for complete financial statements. However, such information reflects all adjustments consisting of normal recurring accruals which are, in the opinion of management, necessary for a fair statement of the financial condition and results of operations for the interim periods. The results for the three and nine months ended September 30, 2016 and 2015 are not indicative of annual results. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. The December 31, 2015 consolidated balance sheet was derived from the Company’s audited consolidated financial statements as of and for the year ended December 31, 2015.

For further information, refer to the consolidated financial statements and footnotes thereto included in Heritage Insurance Holdings, Inc.’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015. References to “we,” “us,” “our,” or the “Company” refer to Heritage Insurance Holdings, Inc. and its consolidated subsidiaries.

The Company qualifies as an “emerging growth company” as defined in Section 2(a)(19) of the Securities Act, of 1933, as amended, as modified by the Jumpstart Our Business Startups Act of 2012 (the “JOBS Act”). As a result, the Company is eligible to take advantage of certain temporary exemptions from various reporting requirements applicable to other public companies that are not emerging growth companies. The Company intends to continue to take advantage of some, but not all, of the exemptions available to emerging growth companies until such time that it is no longer an emerging growth company. The Company has, however, irrevocably elected not to take advantage of the extended transition period afforded by the JOBS Act for the implementation of new or revised accounting standards. As a result, the Company will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

Changes to significant accounting policies

We have made no material changes to our significant accounting policies as reported in our Annual Report on Form 10-K for the year ended December 31, 2015.

Reclassifications

Certain prior year amounts have been reclassified to conform to current year presentation. Such classifications include reclassifying goodwill and intangibles from other assets in the accompanying condensed consolidated balance sheets.

Recent Accounting Pronouncements

The Company describes below recent pronouncements that may have a significant effect on its financial statements or on its disclosures upon future adoption. The Company does not discuss recent pronouncements that are not anticipated to have an impact on, or are unrelated to, its financial condition, results of operations, or related disclosures.

In August 2016, the Financial Accounting Standards Board issued ("FASB") ASC 2016-15, Classification of Certain Cash Receipts and Cash Payments. ASC 2016-15 is a new accounting standard that will make eight targeted changes to how cash receipts and cash payments are presented and classified in the statement of cash flows. This updated is effective on January 1, 2018, and will require adoption on a retrospective basis. The Company is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures.

In June 2016, the FASB issued Accounting Standards Update ("ASU"), ASU 2016-13, Financial Instruments – Credit Losses (Topic 326) (ASU 2016-13), Measurement of Credit Losses on Financial Instruments. ASU 2016-13 requires credit losses on most financial assets measured at amortized cost and certain other instruments to be measured using an expected credit loss model (referred to as the current expected credit loss (CECL) model). ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those years, with early adoption permitted for fiscal years and interim periods beginning after December 15, 2018. The Company is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting (ASU 2016-09), which requires an entity to record all excess tax benefits and tax deficiencies as an income tax benefit or expense in the income statement. ASU 2016-09 will also require an entity to elect an accounting policy to either estimate the number of forfeitures or account for forfeitures when they occur. ASU 2016-09 becomes effective for the Company during the first quarter of 2017. The Company is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, Leases (ASU 2016-02), which provides guidance on the recognition, measurement, presentation and disclosure of leases. The new standard supersedes present U.S. GAAP guidance on leases and requires substantially all leases to be reported on the balance sheet as right-of-use assets and lease liabilities, as well as additional disclosures. The new standard is effective as of January 1, 2019, and early adoption is permitted. The Company is evaluating the impact of the new guidance on its consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (ASU 2016-01), which will significantly change the income statement impact of equity investments held by an entity, and the recognition of changes in fair value of financial liabilities when the fair value option is elected. ASU 2016-01 becomes effective for the Company during the first quarter 2018. The Company is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures.

In May 2014, the FASB issued ASU Topic 2014-09, Revenue from Contracts with Customers (Topic 606). The ASU creates a new topic, Topic 606, to provide guidance on revenue recognition for entities that enter into contracts with customers to transfer goods or services or enter into contracts for the transfer of nonfinancial assets. 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. Additional disclosures are required to provide quantitative and qualitative information regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after December 15, 2017. Early adoption is not permitted. The Company is evaluating the impact of the new guidance on its consolidated financial statements.

There are no other recently issued accounting standards that apply to the Company or that are expected to have a material impact on the Company’s results of operations, financial condition or cash flows.

NOTE 3. ACQUISITION

On March 21, 2016, the Company acquired 100% of the outstanding stock of ZAC and its wholly-owned subsidiary, Zephyr, in exchange for approximately $110,319, net of cash acquired. Zephyr is a specialty property insurance provider that offers policies for residential customers in Hawaii that only cover the peril of the windstorm-hurricane insurance policies. This acquisition furthers the Company’s strategic push to diversify business operations and achieve potential reinsurance synergies while expanding growth opportunities outside of Florida.

The transaction was accounted for using the acquisition method of accounting. The valuations of assets acquired and liabilities assumed are based on preliminary estimates of fair value and are subject to revision as the Company finalizes its analysis. The results of operations of ZAC have been included in the Company's condensed consolidated financial statements since the date of acquisition. The acquisition method requires significant use of estimates and is based on the information available to management at the time these condensed consolidated financial statements were prepared. As the acquisition was recently completed, the Company has not yet completed its assessment of the fair value of the intangible assets acquired, nor the related amortization expense applicable to definite-lived intangible assets during the period between the acquisition date and period end. As such, the total estimated purchase price in excess of net assets acquired and liabilities assumed has initially been recorded as goodwill and identified intangible assets. Goodwill is not deductible for tax purposes and will not be amortized, but is subject to annual impairment tests using a fair-value based approach. The Company is entitled to a holdback provision, for purposes of securing the indemnification obligation of the sellers for any damages arising out of or relating to a previous dispute should one arise. The following table summarizes the preliminary unaudited, estimated fair value of the assets acquired and liabilities assumed. The Company is in the process of finalizing the purchase price allocation and, accordingly, the following allocation of the purchase price, before income taxes, is subject to adjustments during the measurement period:

Purchase Consideration	
Cash, net of cash acquired	$110,319
Assets acquired	
Investments	$76,543
Premiums and agent's receivable	1,403
Other assets	526
Prepaid reinsurance premiums	4,792
Intangible assets – value of business acquired	5,004
Intangible assets	24,203
Total assets acquired	$112,471
Total liabilities assumed	$(42,391)
Net assets acquired	$70,080
Goodwill	40,239
Total purchase price	$110,319

Pro Forma Information

The following table presents selected unaudited pro forma information, assuming the acquisition of ZAC had occurred on January 1, 2015. The unaudited pro forma information is not necessarily indicative of the results that the Company would have achieved had the transaction taken place on January 1, 2015, and the unaudited pro forma information does not purport to be indicative of future financial results.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenue	$109,306	$100,709	$344,972	$320,905
Net income	$10,930	$20,982	$38,673	$80,886
Basic, earnings per share	$0.37	$0.70	$1.33	$2.70
Diluted, earnings per share	$0.37	$0.69	$1.33	$2.67

Our consolidated results of operations include the results of ZAC since the acquisition date. ZAC's revenues and pre-tax net income included in our results of operations since the acquisition for the three months ended September 30, 2016 were $8,985 and $4,566, respectively, and for the nine months ended September 30, 2016, $19,347 and $11,073, respectively. For the three and nine months ended September 30, 2016, income before taxes included $2,016 and $4,780, respectively, of amortization expense related to the identified intangible assets recorded as a result of the acquisition.

NOTE 4. INVESTMENTS

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

	Cost or Adjusted / Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
September 30, 2016				
U.S. government and agency securities	$27,473	$ 316	$ 7	27,782
States, municipalities and political subdivisions	284,949	4,815	124	289,640
Special revenue	56,957	438	185	57,210
Industrial and miscellaneous	136,392	3,053	30	139,415
Redeemable preferred stocks	3,413	124	11	3,526
Total fixed maturities	509,184	8,746	357	517,573
Nonredeemable preferred stocks	14,439	661	57	15,043
Equity securities	19,496	1,209	3,543	17,162
Total equity securities	33,935	1,870	3,600	32,205
Total investments	$543,119	$ 10,616	$ 3,957	$549,778

	Cost or Adjusted / Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
December 31, 2015				
U.S. government and agency securities	$25,474	$ 16	$ 387	$25,103
States, municipalities and political subdivisions	184,145	2,107	137	186,115
Special revenue	42,593	19	204	42,408
Industrial and miscellaneous	115,313	294	932	114,675
Redeemable preferred stocks	3,442	61	21	3,482
Total fixed maturities	370,967	2,497	1,681	371,783
Nonredeemable preferred stocks	12,443	338	43	12,738
Equity securities	19,996	398	4,819	15,575
Total equity securities	32,439	736	4,862	28,313
Total investments	$403,406	$ 3,233	$ 6,543	$400,096

The Company calculates the gain or loss realized on the sale of investments by comparing the sales price (fair value) to the cost or adjusted/amortized cost of the security sold. The Company determines the cost or adjusted/amortized cost of the security sold using 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.

	2016 Gains (Losses)	2016 Fair Value at Sale	2015 Gains (Losses)	2015 Fair Value at Sale
	(In thousands)			
Three Months Ended September 30,				
Fixed maturities	$1,091	$ 17,301	$1,200	$ 62,412
Equity securities	289	1,739	826	15,949
Total realized gains	1,380	19,040	2,026	78,361
Fixed maturities	(232)	575	(75)	5,948
Equity securities	(29)	445	(5)	328
Total realized losses	(261)	1,020	(80)	6,276
Net realized gains	$1,119	$ 20,060	$1,946	$ 84,637

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	2016 Gains (Losses)	Fair Value at Sale	2015 Gains (Losses)	Fair Value at Sale
	(In thousands)			
Nine Months Ended September 30,				
Fixed maturities	$2,668	$ 166,350	$1,237	$ 66,513
Equity securities	46	7,855	716	20,581
Total realized gains	2,714	174,205	1,953	87,094
Fixed maturities	(66)	12,973	(116)	11,219
Equity securities	(886)	2,948	(10)	2,196
Total realized losses	(952)	15,921	(126)	13,415
Net realized gains	$1,762	$ 190,126	$1,827	$ 100,509

The table below summarizes the Company’s fixed maturities at September 30, 2016 by contractual maturity periods. Actual results may differ as issuers may have the right to call or prepay obligations, with or without penalties, prior to the contractual maturity of those obligations.

	September 30, 2016					
	Cost or Amortized Cost	Percent of Total		Fair Value	Percent of Total	
	(In thousands)			(In thousands)		
Due in one year or less	$70,683	14	%	$ 70,696	14	%
Due after one year through five years	177,559	35	%	178,915	34	%
Due after five years through ten years	165,557	32	%	169,966	33	%
Due after ten years	95,385	19	%	97,996	19	%
Total	$509,184	100	%	$ 517,573	100	%

The following table summarizes the Company’s net investment income 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)	
Fixed maturities	$2,338	$1,936	$6,368	$5,254
Equity securities	495	439	1,465	1,292
Cash, cash equivalents and short-term investments	79	150	215	361
Other investments	14	67	(96)	128
Net investment income	2,926	2,592	7,952	7,035
Investment expenses	600	619	1,366	1,339

Net investment income, less investment expenses	$2,326	$1,973	$6,586	$5,696

The Company does not intend to sell investments that are in an unrealized loss position and it is not likely that the Company will be required to sell any investments before recovery of their amortized cost basis. As such, the Company does not consider those investments with an unrealized loss to be other-than-temporarily impaired at September 30, 2016 or December 31, 2015. There were no material other-than-temporary impairments or credit losses related to available-for-sale securities in the nine months ended September 30, 2016 and 2015. In addition, there were no material gross realized gains or losses in the nine months ended September 30, 2016 and 2015.

The following tables present an aging of our unrealized investment losses by investment class as of September 30, 2016 and December 31, 2015:

	Less Than Twelve Months			Twelve Months or More		
	Number of Securities	Gross Unrealized Losses	Fair Value	Number of Securities	Gross Unrealized Losses	Fair Value
	(In thousands)					
September 30, 2016						
U.S. government and agency securities	13	$ 7	$7,815	1	$ —	$38
States, municipalities and political subdivisions	111	116	62,818	2	8	1,492
Special revenue	30	23	6,623	4	7	1,972
Industrial and miscellaneous	82	157	12,402	13	27	2,215
Redeemable preferred stocks	8	5	384	1	6	212
Total fixed maturities	244	308	90,042	21	48	5,929
Nonredeemable preferred stocks	138	35	2,165	5	22	324
Equity securities	52	304	2,848	126	3,240	8,066
Total equity securities	190	339	5,013	131	3,262	8,390
Total investments	434	$ 647	$95,055	152	$ 3,310	$14,319

	Less Than Twelve Months			Twelve Months or More		
	Number of Securities	Gross Unrealized Losses	Fair Value	Number of Securities	Gross Unrealized Losses	Fair Value
	(In thousands)					
December 31, 2015						
U.S. government and agency securities	19	$ 385	$ 19,849	2	$ 3	$ 397
States, municipalities and political subdivisions	14	50	10,979	1	3	164
Special revenue	141	870	73,312	5	61	1,318
Industrial and miscellaneous	134	279	60,203	10	9	1,646
Redeemable preferred stocks	9	21	950	—	—	—
Total fixed maturities	317	1,605	165,293	18	76	3,525
Nonredeemable preferred stocks	19	29	1,560	5	14	250
Equity securities	48	2,975	8,416	20	1,844	2,680
Total equity securities	67	3,004	9,976	25	1,858	2,930
Total investments	384	$ 4,609	$ 175,269	43	$ 1,934	$ 6,455

NOTE 5. FAIR VALUE OF FINANCIAL INSTRUMENTS

For the Company's investments in U.S government securities that do not have prices in active markets, agency securities, state and municipal governments, and corporate bonds, the Company obtains the fair value from its third-party valuation service and evaluates the relevant inputs, assumptions, methodologies and conclusions associated with such valuations. The valuation service calculates prices for the Company's investments in the aforementioned security types on a month-end basis by using several matrix-pricing methodologies that incorporate inputs from various sources. The model the valuation service uses to price U.S. government securities and securities of states and municipalities incorporates inputs from active market makers and inter-dealer brokers. To price corporate bonds and agency securities, the valuation service calculates non-call yield spreads on all issuers, uses option-adjusted yield spreads to account for any early redemption features, then adds final spreads to the U.S. Treasury curve as of quarter end. The inputs the valuation service uses in its calculations are not quoted prices in active markets, but are observable inputs, and therefore represent Level 2 inputs.

The following tables present information about the Company's assets measured at fair value on a recurring basis. The Company assesses the levels for the investments at each measurement date, and transfers between levels are recognized on the actual date of the event or change in circumstances that caused the transfer in accordance with the Company's accounting policy regarding the recognitions of transfers between levels of the fair value hierarchy. For the nine months ended September 30, 2016 and the year ended December 31, 2015, there were no transfers in or out of Levels 1, 2 and 3.

September 30, 2016	Total	Level 1	Level 2	Level 3
	(in thousands)			
Fixed maturities investments:				
U.S. government and agency securities	$27,782	$766	$27,016	$ —
States, municipalities and political subdivisions	289,640	—	289,640	—
Special revenue	57,210	23,947	33,263	—
Industrial and miscellaneous	139,415	—	139,415	—
Redeemable preferred stocks	3,526	3,526	—	—
Total fixed maturities investments	517,573	28,239	489,334	—
Nonredeemable preferred stocks	15,043	15,043	—	—
Equity securities	17,162	17,162	—	—
Total equity securities	32,205	32,205	—	—
Total investments	$549,778	$60,444	$489,334	$ —

December 31, 2015	Total	Level 1	Level 2	Level 3
	(in thousands)			
Assets:				
Certificates of deposit (1)	$3,300	$3,300	$—	$ —
Fixed maturities investments:				
U.S. government and agency securities	25,103	22,361	2,742	—
States, municipalities and political subdivisions	186,115	—	186,115	—
Special revenue	42,408	—	42,408	—
Industrial and miscellaneous	114,675	—	114,675	—
Redeemable preferred stocks	3,482	3,482	—	—
Total fixed maturities investments	375,083	29,143	345,940	—
Nonredeemable preferred stocks	12,738	12,738	—	—
Equity securities	15,575	15,575	—	—
Total equity securities	28,313	28,313	—	—
Total investments	$403,396	$57,456	$345,940	$ —

(1) Includes commercial paper with maturities of three months or less at time of purchase of $3,300 classified in cash and cash equivalents.

NOTE 6. PROPERTY AND EQUIPMENT, NET

Property and equipment, net consisted of the following at September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015
	(In thousands)	
Land	$2,582	$ 2,582
Building	10,301	9,599
Computer hardware and software	3,132	2,502
Office furniture and equipment	759	634
Tenant and leasehold improvements	3,330	3,300
Vehicle fleet	845	693
Total, at cost	20,949	19,310
Less: accumulated depreciation and amortization	3,349	2,199
Property and equipment, net	$17,600	$ 17,111

Depreciation expense for property and equipment was $797 and $1,150 for the three and nine months ended September 30, 2016, respectively. The Company's real estate consists of 14 acres of land and four buildings with a gross area of approximately 191 square feet.

NOTE 7. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and Intangible Assets

As of September 30, 2016 and December 31, 2015 goodwill was $48,267 and $8,028, respectively, and intangible assets were $26,402 and $2,120, respectively. The increase in goodwill and intangible assets reflects the goodwill and intangible assets recorded in connection with the Zephyr acquisition. The preliminary purchase price allocation to goodwill and intangible assets has not been finalized and is subject to change. As of September 30, 2016, the amount of goodwill that we expect to be deductible for income tax purposes is $8,028. The Company has estimated the useful life of the value of business acquired (see Note 3) to be one year and is amortizing the balance based on the remaining percentage of acquired unearned premium from Zephyr. The Company has estimated the useful life of the other intangible assets to range between 10-15 years and is currently amortizing at an average of 12.5 years until the finalization of the purchase price allocation is completed and the useful lives have been finalized.

	Goodwill (in thousands)
Balance as of December 31, 2015	$ 8,028
Goodwill acquired	40,239
Impairment	—
Balance as of September 30, 2016	$ 48,267

Estimated annual pretax amortization of intangible assets for the remainder of 2016 and each of the next five years and thereafter is as follows (in thousands):

Remainder of 2016	$931
2017	2,435
2018	2,128
2019	2,128
2020	2,116
2021	2,104
Thereafter	14,560

$26,402

Amortization expense of intangible assets was $2,061 and $4,924 for the three and nine months ended September 30, 2016, respectively. The Company recorded no amortization expense for the three and nine months ended September 30, 2015.

NOTE 8. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share (“EPS”) for the periods indicated.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Basic earnings per share:				
Net income attributable to common stockholders (000's)	$10,930	$16,813	$36,720	$72,269
Weighted average shares outstanding	29,213,222	30,177,633	29,742,984	29,952,668
Basic earnings per share:	$0.37	$0.56	$1.23	$2.41
Diluted earnings per share:				
Net income attributable to common stockholders (000's)	$10,930	$16,813	$36,720	$72,269
Weighted average shares outstanding	29,213,222	30,177,633	29,742,984	29,952,668
Weighted average dilutive shares	-	305,920	43,172	336,660
Total weighted average dilutive shares	29,213,222	30,483,553	29,786,156	30,289,328
Diluted earnings per share:	$0.37	$0.55	$1.23	$2.39

As of September 30, 2016, the Company has repurchased 1,424,666 shares of the Company’s stock in open market transactions for $20,562. As of September 30, 2016, the Company had $49,438 remaining to purchase shares under its authorized $70,000 share repurchase plan.

NOTE 9. DEFERRED POLICY ACQUISITION COSTS

The Company defers certain costs in connection with written policies, called Deferred Policy Acquisition Costs (“DPAC”), net of corresponding amounts of ceded reinsurance commissions, called Deferred Reinsurance Ceding Commissions (“DRCC”). Net DPAC is amortized over the effective period of the related insurance policies.

The Company anticipates that its DPAC costs will be fully recoverable in the near term. The table below depicts the activity with regard to DPAC during 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)			
Beginning Balance	$42,568	$31,948	$34,800	$24,370
Policy acquisition costs deferred	22,158	16,058	68,807	48,982
Amortization	(22,597)	(15,512)	(61,478)	(40,858)
Ending Balance	$42,129	$32,494	$42,129	$32,494

NOTE 10. INCOME TAXES

During the nine months ended September 30, 2016 and 2015, the Company recorded $23,688 and $44,728, respectively, of income tax expense which corresponds to an estimated annual effective tax rate of 39.2% and 38.2%, respectively.

The table below summarizes the significant components of our net deferred tax assets (liabilities):

	September 30, 2016 (in thousands)	December 31, 2015
Deferred tax assets:		
Unearned premiums	$ 17,772	$ 17,979
Tax-related discount on loss reserve	1,766	1,140
Unrealized loss	—	1,617
Stock-based compensation	2,828	1,277
Other	1,705	256
Total deferred tax assets	$ 24,071	$ 22,269
Deferred tax liabilities:		
Deferred acquisition costs	$ 15,664	$ 13,424
Unrealized gain	2,542	—
Investment basis difference on purchase	840	—
Intangibles	10,224	—
Property and equipment	477	473
Other	1,290	408
Total deferred tax liabilities	31,037	14,305
Net deferred tax (liabilities) assets	$ (6,966)	$ 7,964

In assessing the net realizable value of deferred tax assets, the Company considered whether it is more likely than not that it will not realize some portion or all of the deferred tax assets. The ultimate realization of deferred tax assets depends upon the generation of future taxable income during the periods in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment.

As of September 30, 2016 and December 31, 2015, we had no significant uncertain tax positions.

NOTE 11. REINSURANCE

The Company's reinsurance program is designed, utilizing the Company's risk management methodology, to address its exposure to catastrophes or large non-catastrophic losses. The Company's program provides reinsurance protection for catastrophes including hurricanes, tropical storms and tornadoes. The Company's reinsurance agreements are part of its catastrophe management strategy, which is intended to provide its stockholders an acceptable return on the risks assumed in its property business, and to reduce variability of earnings, while providing protection to the Company's policyholders.

2016 - 2017 Reinsurance Program

The Company placed its reinsurance program for the period from June 1, 2016 through May 31, 2017 during the second quarter of 2016. This reinsurance program incorporates the catastrophe risk of our two insurance subsidiaries, Heritage P&C, a Florida based insurer and Zephyr, a Hawaii based insurer, into one reinsurance structure. The programs are incorporated into one reinsurance structure and are allocated amongst traditional reinsurers, catastrophe bonds issued by Citrus Re Ltd., a Bermuda special purpose insurer formed in 2014 ("Citrus Re"), and the Florida Hurricane Catastrophe Fund ("FHCF").Coverage is shared by both insurers unless otherwise noted. The 2016-2017 reinsurance program provides, including retention, first event coverage up to $1.9 billion in Florida, first event coverage up to $1.1 billion in Hawaii, and multiple event coverage up to $3.0 billion.

The reinsurance program, which is segmented into layers of coverage, protects the Company for excess property catastrophe losses and loss adjustment expenses. The Company's 2016-2017 reinsurance program incorporates the mandatory coverage required by law to be placed with FHCF, which is available only for Florida catastrophe risk. For the 2016 hurricane season, the Company reduced its selected participation percentage in the FHCF from 75% to 45%. The Company also purchased private reinsurance below, alongside and above the FHCF layer, as well as aggregate reinsurance coverage. The following describes the various layers of the Company's June 1, 2016 to May 31, 2017 reinsurance program.

- The Company's Retention. If a first catastrophic event strikes Florida, the Company has a primary retention of the first $40 million of losses and loss adjustment expenses, of which Osprey is responsible for $20 million. If a first catastrophic event strikes Hawaii, the Company has a primary retention of the first $30 million of losses and loss adjustment expenses, of which Osprey is responsible for $15 million. If a second event strikes Florida, Heritage P&C's primary retention decreases to $15 million and the remainder of the losses are ceded to third parties. If a second event strikes Hawaii, Zephyr's primary retention decreases to $5 million. In the second event only for a loss exceeding $190 million, there is an additional Company co-participation of 5.4% subject to a maximum co-participation of $11.6 million. Heritage P&C and Zephyr each have a $5 million primary retention for events beyond the second catastrophic event. Osprey has no primary retention beyond the first catastrophic event in Florida or Hawaii. Additionally, Osprey is responsible for payment of up to $5.3 million of reinstatement premium, depending on the amount of losses incurred.

- Shared Layers above retention and below FHCF. Immediately above the retention, the Company has purchased $374 million of reinsurance from third party reinsurers. Through the payment of a reinstatement premium, the Company is able to reinstate the full amount of this reinsurance one time. To the extent that $374 million or a portion thereof is exhausted in a first catastrophic event, the Company has purchased reinstatement premium protection insurance to pay the required premium necessary for the reinstatement of this coverage.

- FHCF Layer. The Company's FHCF program provides coverage for Florida events only and includes an estimated maximum provisional limit of 45% of $1.3 billion, in excess of its retention of $399 million. The limit and retention of the FHCF coverage is subject to upward or downward adjustment based on, among other things, submitted exposures to FHCF by all participants. The Company has purchased coverage alongside from third party reinsurers and through reinsurance agreements with Citrus Re. To the extent the FHCF coverage is adjusted, this private reinsurance with third party reinsurers and Citrus Re will adjust to fill in any gaps in coverage up to the reinsurers' aggregate limits for this layer. The FHCF coverage cannot be reinstated once exhausted, but it does provide coverage for multiple events.

- Layers alongside the FHCF. The Florida reinsurance program includes third party layers alongside the FHCF. These include 2015 C and 2015 B series catastrophe bonds, which cover Florida only for the 2016 season, and 2016 D and 2016 E catastrophe bond series issued by Citrus Re, which total $377.5 million of coverage, as discussed below, as well as a traditional reinsurance layer providing $200 million of coverage. Through a reinstatement, the Company is able to reinstate the full amount of the $200 million of reinsurance one time. These 2016 catastrophe bonds and the traditional reinsurance layer provide coverage for both Florida and Hawaii catastrophe losses.
- 2016 Class D and E Notes: During February 2016, Heritage P&C and Zephyr entered into two catastrophe reinsurance agreements with Citrus Re. The agreements provide for three years of coverage from catastrophic losses caused by named storms, including hurricanes, beginning on June 1, 2016. Heritage P&C and Zephyr pay a periodic premium to Citrus Re during this three-year risk period. Citrus Re issued an aggregate of $250 million of principal-at-risk variable notes due February 2019 to fund the reinsurance trust account and its obligations to Heritage P&C and Zephyr under the reinsurance agreements. The Class D notes provide $150 million of coverage and the Class E notes provide $100 million of coverage. The Class D and Class E notes provide reinsurance coverage for a sliver of the catastrophe coverage that had previously been provided by the FHCF. The limit of coverage is fully collateralized by a reinsurance trust account for the benefit of Heritage P&C and Zephyr. The maturity date of the notes may be extended up to two additional years to satisfy claims for catastrophic events occurring during the three-year term of the reinsurance agreements.

- 2015 Class B and C Notes: During April 2015, Heritage P&C entered into catastrophe reinsurance agreements with Citrus Re. The 2015 notes do not provide coverage for Zephyr for the 2016 hurricane season. The agreements provide for three years of coverage from catastrophic losses caused by named storms, including hurricanes, beginning on June 1, 2015. Heritage P&C pays a periodic premium to Citrus Re during this three-year risk period. Citrus Re issued principal-at-risk variable notes due April 2018 to fund the reinsurance trust account and its obligations to Heritage P&C under the reinsurance agreements. The Class B notes provide $97.5 million of coverage, and the Class C notes provide $30 million of coverage. The Class B and Class C notes provide reinsurance coverage for a sliver of the catastrophe coverage that had previously been provided by the FHCF. The limit of coverage is fully collateralized by a reinsurance trust account for the benefit of Heritage P&C. The maturity date of the notes may be extended up to two additional years to satisfy claims for catastrophic events occurring during the three-year term of the reinsurance agreements.

Layers above the FHCF - Florida program

- 2015 Class A Notes: During April 2015, Heritage P&C entered into catastrophe reinsurance agreements with Citrus Re. The 2015 notes do not provide coverage for Zephyr for the 2016 hurricane season. The agreements provide for three years of coverage from catastrophic losses caused by named storms, including hurricanes, beginning on June 1, 2015. Heritage P&C pays a periodic premium to Citrus Re during this three-year risk period. Citrus Re issued principal-at-risk variable notes due April 2018 to fund the reinsurance trust account and its obligations to Heritage P&C under the reinsurance agreements. The Class A notes provide $150 million of coverage for a layer above the FHCF. The limit of coverage is fully collateralized by a reinsurance trust account for the benefit of Heritage P&C. The maturity date of the notes may be extended up to two additional years to satisfy claims for catastrophic events occurring during the three-year term of the reinsurance agreements.

- 2014 Class A Notes: Coverage immediately below and above the 2015 Class A notes is provided by the 2014 reinsurance agreements entered into with Citrus Re. The first contract with Citrus Re provides $150 million of coverage immediately below 2015 Class A, and the second contract provides an additional $50 million of coverage which sits immediately above 2015 Class A. During April 2014, Heritage P&C entered into two catastrophe reinsurance agreements with Citrus Re. The 2014 notes do not provide coverage for Zephyr for the 2016 hurricane season. The agreements provide for three years of coverage from catastrophe losses caused by certain named storms, including hurricanes, beginning on June 1, 2014. The limit of coverage of $200 million is fully collateralized by a reinsurance trust account for the benefit of Heritage P&C. Heritage P&C pays a periodic premium to Citrus Re during this three-year risk period. Citrus Re issued $200 million of principal-at-risk variable notes due April 2017 to fund the reinsurance trust account and its obligations to Heritage P&C under the reinsurance agreements. The maturity date of the notes may be extended up to two additional years to satisfy claims for catastrophic events occurring during the three-year term of the reinsurance agreements.

- Multi-Zonal Layers – The Company purchased additional layers which provide coverage for Florida for a second event and both first and second event coverage for Hawaii. The first event coverage for Hawaii is a counterpart to the Florida-only catastrophe bond layers and FHCF layer. There is a total of $282 million of reinsurance coverage purchased on this basis, with $260 million having a prepaid reinstatement. The multi-zonal occurrence layer provides first and second event coverage of $260 million for Hawaii and second event coverage of $260 million for Florida. A top and drop multi-zonal layer provides first and subsequent event coverage of $22 million for Hawaii and second or subsequent event coverage of $22 million for Florida.

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Aggregate Coverage. In addition to what is described above, much of the reinsurance is structured in a way to provide aggregate coverage. $682 million of limit is structured on this basis. To the extent that this coverage is not fully exhausted in the first catastrophic event, it provides coverage commencing at its reduced retention for second and subsequent events where underlying coverage has been previously exhausted. $460 million has a reinstatement, which is prepaid.

For a first catastrophic event striking Florida, our reinsurance program provides coverage for $1.9 billion of losses and loss adjustment expenses, including our retention, and we are responsible for all losses and loss adjustment expenses in excess of such amount. For a first catastrophic event striking Hawaii, our reinsurance program provides coverage for $1.1 billion of losses and loss adjustment expenses, including our retention, and we are responsible for all losses and loss adjustment expenses in excess of such amount. For subsequent catastrophic events, our total available coverage depends on the magnitude of the first event, as we may have coverage remaining from layers that were not previously fully exhausted. $860 million of limit purchased in 2016 includes a reinstatement, with $825 million being prepaid. In total, we have purchased $3.0 billion of potential reinsurance coverage, including our retention, for multiple catastrophic events. Our ability to access this coverage, however, will be subject to the severity and frequency of such events.

2015 – 2016 Reinsurance Program

During the second quarter of 2015, the Company placed its reinsurance program for the period from June 1, 2015 through May 31, 2016. The Company's 2015-2016 reinsurance program incorporated the mandatory coverage required by law to be placed with FHCF. For the 2015 hurricane season, the Company selected 75% participation in the FHCF. The Company also purchased private reinsurance below, alongside and above the FHCF layer, as well as aggregate reinsurance coverage. The following describes the various layers of the Company's June 1, 2015 to May 31, 2016 reinsurance program.

- The Company's Retention. For the first catastrophic event, the Company had a primary retention of the first $35 million of losses and loss adjustment expenses, of which Osprey was responsible for $20 million. For a second event, Heritage P&C's primary retention decreased to $5 million and Osprey is responsible for $10 million. To the extent that there is reinsurance coverage remaining, Heritage P&C has a $5 million primary retention for events beyond the second catastrophic event. Osprey had no primary retention beyond the second catastrophic event.

- Layers Below FHCF. Immediately above the Company's retention, the Company purchased $440 million of reinsurance from third party reinsurers. Through the payment of a reinstatement premium, the Company was able to reinstate the full amount of this reinsurance one time. To the extent that $440 million or a portion thereof was exhausted in a first catastrophic event, the Company had purchased reinstatement premium protection insurance to pay the required premium necessary for the reinstatement of this coverage. A portion of this coverage wrapped around the FHCF and provided coverage alongside and above the FHCF.

- FHCF Layer. The Company's FHCF coverage included an estimated maximum provisional limit of 75% of $920 million, or $690 million, in excess of its retention and private reinsurance of $336 million. The limit and retention of the FHCF coverage was subject to upward or downward adjustment based on, among other things, submitted exposures to FHCF by all participants. The Company had purchased coverage alongside from third party reinsurers and through reinsurance agreements with Citrus Re. To the extent the FHCF coverage was adjusted, this private reinsurance with third party reinsurers and Citrus Re would adjust to fill in any gaps in coverage up to the reinsurers' aggregate limits for this layer. The FHCF coverage could not be reinstated once exhausted, but it did provide coverage for multiple events.

- CAT Bond Layer alongside the FHCF. During April 2015 Heritage P&C entered into three catastrophe reinsurance agreements with Citrus Re. The agreements provided for three years of coverage from catastrophic losses caused by named storms, including hurricanes, beginning on June 1, 2015. Heritage P&C paid periodic premiums to Citrus Re during the three-year risk period. Citrus Re issued an aggregate of $277.5 million of principal-at-risk variable notes due April 2017 to fund the reinsurance trust account and its obligations to Heritage P&C under the reinsurance agreements. These notes were issued in three classes. The Class A notes provide $150 million of coverage for the layer immediately above the FHCF. The Class B notes provided $97.5 million of coverage, and the Class C notes provided $30 million of coverage. The Class B and Class C notes provided reinsurance coverage for a sliver of the catastrophe coverage that had previously been provided by the FHCF. The limit of coverage was fully collateralized by a reinsurance trust account for the benefit of Heritage P&C. The maturity date of the notes may be extended up to two additional years to satisfy claims for catastrophic events occurring during the three-year term of the reinsurance agreements.

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CAT Bond Layer above the FHCF. Immediately above the FHCF layer had the coverage provided by the 2015 reinsurance agreement entered into with Citrus Re. The Citrus Re 2015 Class A notes provided up to $150 million of coverage immediately above the FHCF layer. Coverage immediately above the 2015 Class A notes was provided by the 2014 reinsurance agreements entered into with Citrus Re. The first contract with Citrus Re provided $150 million of coverage and the second contract provided an additional $50 million of coverage.

- Aggregate Coverage. In addition to the layers described above, the Company also purchased $125 million of aggregate reinsurance coverage for losses and loss adjustment expenses in excess of $1.648 billion for a first catastrophic event. To the extent that this coverage was not fully exhausted in the first catastrophic event, it provided coverage commencing at its reduced retention for second and subsequent events and where underlying coverage had been previously exhausted. There was no reinstatement of the aggregate reinsurance coverage once exhausted, but it did provide coverage for multiple events.

For a first catastrophic event, our 2015-2016 reinsurance program provided coverage for $1.8 billion of losses and loss adjustment expenses, including our retention, and were responsible for all losses and loss adjustment expenses in excess of such amount. For subsequent catastrophic events, our total available coverage depended on the magnitude of the first event, as we may have had coverage remaining from layers that were not previously fully exhausted. We also purchased reinstatement premium protection insurance to provide an additional $440.0 million of coverage. Our aggregate reinsurance layer also provided coverage for second and subsequent events to the extent not exhausted in prior events. In total, we purchased $2.3 billion of reinsurance coverage, including our retention, for multiple catastrophic events for the 2015-2016 hurricane season.

Property Per Risk Coverage

The Company also purchased property per risk coverage for losses and loss adjustment expenses in excess of $1 million per claim. The limit recovered for an individual loss is $9 million and total limit for all losses is $27 million. There are two reinstatements available with additional premium due based on the amount of the layer exhausted. In addition, the Company purchased facultative reinsurance in excess of $10 million for any commercial properties it insured for which the total insured value exceeded $10 million.

2014 – 2015 Reinsurance Program

During the second quarter of 2014, the Company placed its reinsurance program for the period from June 1, 2014 through May 31, 2015. The Company's 2014-2015 reinsurance program incorporated the mandatory coverage required by law to be placed with FHCF. The Company also purchased private reinsurance below, alongside and above the FHCF layer, as well as aggregate reinsurance coverage. The following describes the various layers of the Company's June 1, 2014 to May 31, 2015 reinsurance program.

- The Company's Retention. For the first catastrophic event, the Company had a primary retention of the first $15 million of losses and loss adjustment expenses, of which Osprey was responsible for $6 million. For a second event, Heritage P&C's primary retention decreased to $2 million and Osprey was responsible for $4 million. To the extent that there was reinsurance coverage remaining, Heritage P&C had a $2 million primary retention for events beyond the third catastrophic event. Osprey had no primary retention beyond the second catastrophic event.

- Layers Below FHCF. Immediately above the Company's retention, the Company purchased $185 million of reinsurance from third party reinsurers. Through the payment of a reinstatement premium, the Company was able to reinstate the full amount of this reinsurance one time. To the extent that $185 million or a portion thereof was exhausted in a first catastrophic event, the Company purchased reinstatement premium protection insurance to pay the required premium necessary for the reinstatement of this coverage. A portion of this coverage wrapped around the FHCF and provided coverage alongside the FHCF.

- FHCF Layer. The Company's FHCF coverage included an estimated maximum provisional limit of 90% of $484 million, or $436 million, in excess of its retention and private reinsurance of $181 million. The limit and retention of the FHCF coverage was subject to upward or downward adjustment based on, among other things, submitted exposures to FHCF by all participants. The Company purchased coverage alongside from third party reinsurers. The layer alongside was in the amount of $48 million. To the extent the FHCF coverage was adjusted, this private reinsurance would adjust to fill in any gaps in coverage up to the reinsurers' aggregate limits for this layer. The FHCF coverage could not be reinstated once exhausted, but it did provide coverage for multiple events.

- CAT Bond Layer. Immediately above the FHCF layer was the coverage provided by the reinsurance agreements entered into with Citrus Re. The first contract with Citrus Re provided $150 million of coverage and the second contract provided an additional $50 million of coverage. Osprey provided $25 million of coverage alongside the second contract.

- Aggregate Coverage. In addition to the layers described above, the Company purchased $105 million of aggregate reinsurance coverage for losses and loss adjustment expenses in excess of $825.0 million for a first catastrophic event. To the extent that this coverage was not fully exhausted in the first catastrophic event, it provided coverage commencing at its reduced retention levels for second and subsequent events and where underlying coverage had been previously exhausted. There was no reinstatement of the aggregate reinsurance coverage once exhausted, but it did provide coverage for multiple events. Osprey provided $20 million of protection in the layer above $940 million.

For a first catastrophic event, the Company’s 2014-2015 reinsurance program provided coverage for $990 million of losses and loss adjustment expenses, including its retention, and the Company was responsible for all losses and loss adjustment expenses in excess of such amount. For subsequent catastrophic events, the Company’s total available coverage depended on the magnitude of the first event, as the Company may have had coverage remaining from layers that were not previously fully exhausted. The Company purchased reinstatement premium protection insurance to provide an additional $185 million of coverage. The Company’s aggregate reinsurance layer also provided coverage for second and subsequent events to the extent not exhausted in prior events.

Assumption Transactions and Assumed Premiums Written

The following table depicts written premiums, earned premiums and losses, showing the effects that the Company's assumption transactions have on these components of the Company's consolidated statements of operations and comprehensive income:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(In thousands)			
Premium written:				
Direct	$147,691	$115,876	$463,778	$352,162
Assumed	(459)	33,117	8,015	66,396
Ceded	(5,164)	(611)	(248,823)	(183,033)
Net premium written	$142,068	$148,382	$222,970	$235,525
Change in unearned premiums:				
Direct	$8,538	$(11,996)	$(32,143)	$(82,979)
Assumed	8,926	(8,763)	40,626	45,757
Ceded	(57,977)	(45,262)	85,362	80,393
Net change	$(40,513)	$(66,021)	$93,845	$43,171
Premiums earned:				
Direct	$156,229	$103,880	$431,635	$269,183
Assumed	8,467	24,354	48,641	112,153
Ceded	(63,141)	(45,873)	(163,461)	(102,640)
Net premiums earned	$101,555	$82,361	$316,815	$278,696
Losses and LAE incurred:				
Direct	$59,381	$25,266	$141,181	$68,269
Assumed	(3,753)	10,525	30,208	33,970
Ceded	(1,722)	—	(1,726)	—
Net losses and LAE incurred	$53,906	$35,791	$169,663	$102,239

The following table highlights the effects that the Company's assumption transactions have on unpaid losses and loss adjustment expenses and unearned premiums:

	September 30, 2016	December 31, 2015
	(In thousands)	
Unpaid losses and loss adjustment expenses:		
Direct	$96,604	$ 60,223
Assumed	30,155	23,499
Gross unpaid losses and LAE	126,759	83,722
Ceded	(1,064)	—
Net unpaid losses and LAE	$125,695	$ 83,722
Unearned premiums:		

Direct	$320,241	$ 258,754
Assumed	3,113	43,739
Gross unearned premiums	323,354	302,493
Ceded	(168,650)	(78,517)
Net unearned premiums	$154,704	$ 223,976

NOTE 12. RESERVE FOR UNPAID LOSSES

The Company determines the reserve for unpaid losses on an individual-case basis for all incidents reported. The liability also includes amounts which are commonly referred to as incurred but not reported, or “IBNR”, claims as of the balance sheet date.

The table below summarizes the activity related to the Company's reserve for unpaid losses:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Balance, beginning of period	$117,485	$61,846	$83,722	$51,469
Less: reinsurance recoverable on paid losses	—			