HCI Group, Inc.
Form 10-K
February 22, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2016

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)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Shares, no par value	New York Stock Exchange
Preferred Share Purchase Rights	New York Stock Exchange
8.00% Senior Notes due 2020	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 market value of the common stock held by non-affiliates of the registrant as of June 30, 2016, computed by reference to the price at which the common stock was last sold on June 30, 2016, was $234,690,386.

The number of shares outstanding of the registrant s common stock, no par value, on February 14, 2017 was 10,282,438.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III of this Form 10-K is incorporated by reference from the registrant s definitive proxy statement which will be filed not later than 120 days after the end of the fiscal year covered by this Form 10-K.

HCI GROUP, INC. AND SUBSIDIARIES

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PART I

ITEM 1 *Business*

General

HCI Group, Inc. is a Florida-based company that, through its subsidiaries is engaged in a variety of business activities, including property and casualty insurance, reinsurance, real estate and information technology. Its principal business is property and casualty insurance. HCI was incorporated in 2006. References to we, our, us, the Company, or HC this Form 10-K generally refer to HCI Group, Inc. and its subsidiaries. Our principal executive offices are located at 5300 West Cypress Street, Suite 100, Tampa, Florida 33607, and our telephone number is (813) 849-9500.

Based on our organizational structure, revenue sources, and evaluation of financial and operating performances by management, we manage four operating divisions under one reporting segment, which includes the following operations:

a) Insurance Operations

Property and casualty insurance

Reinsurance

b) Other Operations

Real estate

Information technology

Insurance Operations

Property and Casualty Insurance

Our principal operating subsidiary, Homeowners Choice Property & Casualty Insurance Company, Inc. (HCPCI), was incorporated and began operations in 2007. Through HCPCI, we currently provide property and casualty insurance to homeowners, condominium owners and tenants on properties located in Florida. HCPCI s operations are supported by HCI and the following wholly owned subsidiaries of HCI:

Homeowners Choice Managers, Inc. acts as managing general agent and provides marketing, underwriting, claims settlement, accounting and financial services to HCPCI;

Southern Administration, Inc. provides policy administration services to HCPCI; and

Claddaugh Casualty Insurance Company Ltd. provides reinsurance to HCPCI. (See *Reinsurance* below)

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HCPCI began operations by participating in a take-out program through which we assumed insurance policies held by Citizens Property Insurance Corporation (Citizens), a Florida state-supported insurer. The take-out program is a legislatively mandated program designed to reduce the State s risk exposure by encouraging private companies to assume policies from Citizens. We have assumed policies in a series of separate transactions, which took place from July 2007 through November 2016. In addition, we acquired policies from one Florida carrier in November 2011. Substantially all of our premium revenue since inception has come from the policies acquired in these transactions and subsequent renewals. As of December 31, 2016, our premiums in force and policy count were approximately $375 million and 150,000, respectively.

Policyholders whose policies have been assumed by us or another insurance company have the option to opt out of the assumption and return to Citizens. With respect to our November 2013 through November 2016 assumptions, the opt-out provision was limited to the thirty-day period preceding and following the assumption date. Policyholders who stay with us may cancel their policies any time. Citizens has historically required us to offer renewals on the policies we acquire in the take-out program for a period of three years subsequent to their initial expiration. The policyholders have the option to renew with us or they may place their coverage with another insurance company. We strive to retain these policies by offering competitive rates and exceptional service to our policyholders. Opportunities to acquire large numbers of policies from Citizens meeting our strict underwriting criteria have diminished in recent years. We may, however, selectively pursue additional assumption transactions with Citizens as opportunities arise, provided the assumed policies meet our underwriting criteria. We also continually explore accretive opportunities to acquire business from other insurance companies.

HCPCI began writing flood coverage for Florida homeowners in January 2014 in response to the demand for an alternative to the Federal National Flood Insurance Program for Florida homeowners. The flood coverage is offered on a limited basis as a policy endorsement to eligible Florida customers who are most likely to be impacted by the significant rate increases that may result from the Biggert-Waters Flood Insurance Reform and Modernization Act of 2012. In October 2015, HCPCI was approved by the Florida Office of Insurance Regulation (FLOIR) to write standalone flood insurance policies for Florida homeowners. In addition, in 2016, we launched TypTap Insurance Company (TypTap), a Florida insurance subsidiary also approved by the FLOIR to write various insurance products for Florida homeowners. TypTap features an online platform for quoting and binding policies that is designed to be accessible by any Internet capable devices.

We plan to seek opportunities to enter the property and casualty insurance market and establish our presence in other states, especially with residential flood insurance. We previously had one Alabama domiciled insurance subsidiary, Homeowners Choice Assurance Company, Inc., which had not written any insurance policies and has been dissolved and its license surrendered as of December 31, 2016.

Our operating and growth strategies for our property and casualty insurance business are to continually optimize the existing book of business, manage our costs and expenses, diversify both geographically and with new product offerings, develop and deploy new technologies to streamline operations, including policy underwriting and production, and pursue accretive opportunities to acquire polices when they arise, whether from Citizens or other insurance companies.

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We face various challenges to implementing our operating and growth strategies. Since we currently write policies that cover Florida homeowners, condominium owners, and tenants, we cover losses that may arise from, among other things, catastrophes, which could have a significant adverse effect on our business, results of operations, and financial condition. To mitigate our risk of such catastrophic losses, we cede a portion of our exposure to reinsurers under contracts called catastrophe excess of loss reinsurance treaties. Reinsurance is by far the largest cost to our property and casualty insurance business. Even without catastrophic events, we may incur losses and loss adjustment expenses that deviate substantially from our estimates and that may exceed our reserves, in which case our net income and capital would decrease. Our operating and growth strategies may also be impacted by regulation of our business by the State of Florida and other states in which we may operate. Currently we are licensed to operate in only Florida. To operate in any other state we must first obtain a license from the insurance regulatory authorities in that state. Insurance regulators also must approve our policy forms and premium rates as well as monitor our compliance with financial and regulatory requirements. Additionally, we may compete with large, well-established insurance companies, possessing greater financial resources, larger agency networks, and greater name recognition. See Item 1A, Risk Factors, below.

Competition

We operate in highly competitive markets where we face competition from national, regional and residual market insurance companies and, in the case of flood insurance, the U.S. government. We believe that we have approximately 10 significant competitors writing homeowners property and casualty insurance in the state of Florida. Based on September 30, 2016 annualized premiums written data, from the FLOIR, excluding State Farm Florida Insurance Company, we are the fifth largest provider of homeowners property and casualty insurance in the state.

Our competitors may have larger financial capacities, greater resource availability, and more diversification in terms of insurance coverage. Our competitors include companies which market their products through agents, as well as companies which sell insurance directly to their customers. In addition, large national insurers that left the Florida market more than a decade ago after numerous hurricanes impacted the state, may reenter the Florida homeowners property and casualty insurance market and they may have certain competitive advantages such as increased name recognition, increased loyalty of their customer base, and reduced policy acquisition costs. We may also face competition from new or temporary entrants in our niche markets. In some cases, such entrants may, because of inexperience, desire for new business, or other reasons, price their insurance products below ours. This pricing pressure may lead to overall premium reductions across the Florida market. We did in fact implement a rate decrease in January 2016 for our new and renewal homeowners multi-peril business.

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Our competitive strategies focus on the following key areas:

Exceptional service We are committed to maintaining superior service to our policyholders and agents.

Claims settlement practices We focus on fair and timely settlement of policyholder claims.

Disciplined underwriting We analyze exposures and utilize available underwriting data to ensure policies meet our selective criteria.

New product offerings In addition to our flood-endorsed policies and wind-only program, we may cross-sell additional insurance products to our existing policyholders in order to broaden our lines of business and product mix or identify other lines of insurance to offer. Since the beginning of 2016, we have been offering flood-only policies to Florida customers.

Effective and efficient use of technology We strive to add or improve technology that can effectively and efficiently enhance service to our policyholders and agents. For instance, we currently use our internally developed application, *Exzeo*®, to increase the efficiency of our claims processing and settlement. In addition, our on-line platform for quoting and binding residential flood policies streamlines the underwriting and policy production processes.

Geographical expansion We continue to seek opportunities to expand our business within the state of Florida and perhaps into other states to increase overall geographic diversification.

Price In the case of flood insurance, our rates are typically below the rates of the National Flood Insurance Program administered by the Federal Emergency Management Agency, which is the dominant provider of flood insurance in the United States.

Seasonality of Our Business

Our insurance business is seasonal as hurricanes and tropical storms affecting Florida typically occur during the period from June 1 through November 30 each year. Moreover, with our reinsurance treaty years typically effective on June 1 each year, any variation in the cost of our reinsurance, whether due to changes in reinsurance rates or changes in the total insured value of our policy base, will occur and be reflected in our financial results beginning June 1 each year.

Government Regulation

We are subject to the laws and regulations in any state in which we conduct our insurance business. The regulations cover all aspects of our business and are generally designed to protect

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the interests of insurance policyholders as opposed to the interests of shareholders. Such regulations relate to a wide variety of financial and non-financial matters including:

- authorized lines of business;
- capital and surplus requirements;
- approval of allowable rates and forms;
- approval of reinsurance contracts;
- investment parameters;
- underwriting limitations;
- transactions with affiliates;
- dividend limitations;
- changes in control; and
- market conduct.

Our failure to comply with certain provisions of applicable insurance laws and regulations could have a material, adverse effect on our business, results of operations or financial condition.

Regulatory Uncertainty

Certain states including Florida have adopted laws or are considering proposed legislation which, among other things, limits the ability of insurance companies to effect rate increases or to cancel, reduce or non-renew insurance coverage with respect to existing policies. The Florida legislature continuously considers bills affecting the Florida residential property insurance market. Current law penalizes insurers for noncompliance with the insurance code, establishes a private cause of action relating to claims payment practices, extends the notice period applicable to non-renewals of certain residential policies, prevents non-renewals and cancellation except for material misrepresentation and non-payment of premium and establishes procedures governing rate filings. Any changes in such laws and regulations could have a material, adverse effect on our operations or our ability to expand.

State Licensure and Approval

Most states, including Florida, require licensure and regulatory approval prior to the marketing of insurance products. Typically, licensure review is comprehensive and includes a review of a company s business plan, solvency, reinsurance, rates, and forms, the character of its officers and directors and other of its financial and non-financial aspects. The regulatory authorities may prevent entry into a new market by not granting a license. In addition, regulatory authorities may preclude or delay our entry into markets by disapproving or withholding approval of our product filings.

Statutory Reporting and Examination

All insurance companies must file quarterly and annual statements with certain regulatory agencies and are subject to regular and special examinations by those agencies. The National Association of Insurance Commissioners mandates that all insurance companies be examined once every five years. However, the FLOIR has the authority to conduct an examination whenever it is deemed appropriate. HCPCI s latest financial examination completed by the FLOIR related to the year ended December 31, 2010. The FLOIR is currently conducting its financial examination related to the five years ended December 31, 2015.

Liability for Losses and Loss Adjustment Expenses

Our liability for losses and loss adjustment expenses represents our estimate of the total cost of (i) claims that have been incurred, but not yet paid (case reserves), (ii) claims that have been incurred but not yet reported to us (IBNR), and (iii) loss adjustment expenses (LAE) which are intended to cover the ultimate cost of settling claims, including investigation and defense of lawsuits resulting from such claims. We base our estimates on various assumptions and actuarial data we believe to be reasonable under the circumstances. The process of estimating the liability is inherently subjective and is influenced by many variables such as past loss experience, current claim trends and the prevailing social, economic and legal environments.

Significant time can elapse between the occurrence of an insured loss, the reporting of the loss to us and our payment of that loss. Our liability for losses and LAE, which we believe represents the best estimate at a given point in time based on facts, circumstances and historical trends then known, may necessarily be adjusted to reflect additional facts that become available during the loss settlement period.

For a discussion and summary of the activity in the liability for losses and LAE for the years ended December 31, 2016, 2015 and 2014, see Note 15 Losses and Loss Adjustment Expenses to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

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Loss Development

Our liability for losses and LAE represents estimated costs ultimately required to settle all claims for a given period. The following table illustrates development of the estimated liability for losses and LAE as of December 31 for the years 2007 (inception) through 2016 (amounts in thousands):

Schedule of Loss Development

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Original liability for losses and LAE[1]	$ 1,688	$ 14,763	$ 19,178	$ 22,146	$ 27,424	$ 41,168	$ 43,686	$ 48,908	$ 51,690	$ 70,492
Re-estimated losses and LAE[2] as of:										
1 year later	1,412	10,879	18,399	26,776	27,309	38,712	47,344	57,807	72,229	
2 years later	1,236	10,991	19,866	26,003	28,536	40,015	50,280	65,367		
3 years later	1,268	11,661	19,361	27,226	28,499	42,976	54,696			
4 years later	1,327	11,528	19,617	26,544	29,038	45,279				
5 years later	1,330	11,424	18,969	26,871	30,788					
6 years later	1,330	11,361	19,020	27,732						
7 years later	1,330	11,302	19,426							
8 years later	1,331	11,459								
9 years later	1,331									
Cumulative redundancy (deficiency)[3]	357	3,304	(248)	(5,586)	(3,364)	(4,111)	(11,010)	(16,459)	(20,539)	
Cumulative amount of liability paid as of:										
1 year later	760	7,725	10,481	16,833	15,652	22,365	26,595	33,347	41,053	
2 years later	1,108	9,229	15,336	20,708	21,707	31,824	38,695	49,122		
3 years later	1,108	10,339	17,065	23,732	25,350	37,041	45,655			
4 years later	1,327	10,947	17,992	25,063	26,772	40,152				
5 years later	1,330	11,121	18,375	25,681	28,052					
6 years later	1,330	11,167	18,465	26,238						
7 years later	1,330	11,302	18,506							
8 years later	1,331	11,305								
9 years later	1,331									
Gross premiums earned	$ 9,546	$ 61,925	$ 110,011	$ 119,757	$ 143,606	$ 233,607	$ 337,113	$ 365,488	$ 423,120	$ 378,678

1 Represents management s original estimated liability for (i) unpaid claims, (ii) IBNR, and (iii) loss adjustment expenses.

2 Represents the re-estimated liabilities in later years for unpaid claims, IBNR and loss adjustment expenses for each of the respective years.

3 Represents the difference between the latest re-estimate and the original estimate. A redundancy indicates the original estimate is higher than the current estimate whereas a deficiency indicates the original estimate is lower than the current estimate.

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For the years ended December 31, 2016, 2015 and 2014, revenues from insurance operations before intracompany elimination represented 95.5%, 97.5% and 97.2%, respectively, of total revenues of all operating segments. At December 31, 2016, 2015 and 2014, insurance operations total assets represented 87.9%, 91.8% and 94.1%, respectively, of the combined assets of all operating segments. There was no other operating division representing ten percent or more of our total revenues or combined assets. See Note 16 Segment Information to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Reinsurance

We have a Bermuda domiciled wholly owned reinsurance subsidiary, Claddaugh Casualty Insurance Company Ltd. We selectively retain risk in Claddaugh, displacing the need for HCPCI to pay premiums to third party reinsurers. Claddaugh fully collateralizes its exposure to HCPCI by depositing funds into a trust account. Claddaugh also from time to time mitigates a portion of its risk through retrocession contracts.

Other Operations

Real Estate

Our real estate operations consist of multiple properties we own and operate.

Properties Used in Operations

Our real estate used in operations consists of our headquarters building in Tampa, Florida, and our secondary insurance operations site in Ocala, Florida. At our headquarters, we lease available space to non-affiliates at various terms. The Ocala location, in addition to day-to-day operational use, serves as our alternative site in the event we experience any significant disruption at our headquarters building.

Operations at Investment Properties

Our investment properties consist of a combined 24 acres of waterfront property, land and land improvements that include one full-service restaurant and two marinas as well as two recently acquired retail shopping centers. The combined marina facilities offer to the general public: a) one dry-stack boat storage facility with capacity for approximately 314 boats; b) approximately 74 wet slips; c) two fuel facilities; and d) open areas for parking and storage. Dry-stack boat storage space is generally rented on a monthly or annual basis while the wet slips are rented on a daily or monthly basis. We acquired the restaurant and marina operations in connection with our purchase of those properties and we continue to operate them to enhance the property values. We also lease available space to non-affiliates at one of these locations.

One retail shopping center with 61,400 square feet of net rentable space is located in Sorrento, Florida and is anchored by a large, well-known grocery retailer. It was formerly the subject of a real estate development and construction project in which we were involved through an acquisition, development and construction loan arrangement (ADC Arrangement).

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Under the ADC Arrangement, Greenleaf Capital, one of our wholly owned subsidiaries, had an option to purchase the property when the construction project was completed contingent upon tenant rental commitments for at least 90% of rentable space being secured by the developer. On August 16, 2016, we exercised the purchase option and acquired the property for a purchase price of $12,250,000, which resulted in a bargain purchase gain as of the acquisition date of approximately $2,071,000. See Note 6 Business Acquisitions to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Another retail shopping center with 49,995 square feet of net rentable space is located in Melbourne, Florida and also anchored by a large, well-known grocery retailer. In December 2016, we acquired full ownership of the property in which we had a 90% non-controlling interest, resulting in a gain on remeasurement of approximately $4,005,000. Subsequent to the acquisition, we incurred an impairment loss of $388,000 due to the unexpected closure of one tenant s business. This property had been developed through a limited liability company described elsewhere in this report for U.S. GAAP purposes as a joint venture. See *Investment in Unconsolidated Joint Venture* in Note 4 Investments to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Ongoing Investment Project

We have one real estate development project described as a joint venture arrangement under U.S. GAAP, which we consolidate with our operations. We believe this type of cooperation with experienced real estate developers will enable us to grow our real estate portfolio and diversify our future sources of income. See Note 4 Investments to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K for additional information.

Information Technology

Our information technology operations include a team of experienced software developers with extensive knowledge in designing and creating web-based applications and products for mobile devices. The operations, which are located in Tampa, Florida and Noida, India, are focused on developing cloud-based, innovative products and services that support in-house operations as well as our third party relationships with our agency partners and claim vendors.

Proplet™

Proplet is an online platform for quoting homeowners policies for our subsidiary, HCPCI. This platform offers a map based solution for quoting.

TypTap™

TypTap is an online platform for quoting and binding residential flood policies for our subsidiary, TypTap Insurance Company. This platform focuses on simplifying the user experience, which is entirely online. It is designed to be accessible from a mobile phone or any other internet capable device.

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SAMS™

SAMS is an online platform for supporting back-office policy and claims management for both of our insurance subsidiaries, HCPCI and TypTap Insurance Company. *SAMS* processes the full life cycle of a policy from policy quoting and issuance to agency management, cash receipts/disbursements, claims reserving and claim payments.

Some of the technologies originally developed in-house for our own insurance operations have been launched for use by third parties. These technologies include the following:

Exzeo®

Exzeo is a cloud-based application available at Exzeo.com which provides a highly customizable environment to support automation and process management to high volume environments. Exzeo.com specifically supports property claim assignments, logistics, and accountability reporting with our third party partners. Exzeo.com has rich system integration through an application program interface (API), which allows hands-free data transfer from any API-capable applications such as *SAMS*.

Atlas Viewer™

Atlas Viewer is our interactive cloud-based data mapping and visualization application. An industry agnostic product, *Atlas Viewer* allows users to combine data from multiple sources and leverage location coordinates to make more informed business decisions. *Atlas Viewer* allows system to system integration through an API or allows users to upload documents to view and securely share data on a customized map. *Atlas Viewer* is offered as a subscription-based service.

CasaClue™

CasaClue is a large database containing residential property data points important to underwriting residential flood insurance. TypTap, described above, utilizes *CasaClue*.

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Financial Highlights

The following table summarizes our financial performance during the years ended December 31, 2016, 2015 and 2014:

(Amounts in millions except per share amounts)	2016	2015	2014
For the year ended December 31:			
Net premium earned	$ 243.6	$ 282.5	$ 252.1
Total revenue	$ 264.4	$ 286.0	$ 266.1
Losses and loss adjustment expenses	$ 124.7	$ 87.2	$ 79.5
Income before income taxes	$ 46.9	$ 106.2	$ 101.0
Net income	$ 29.0	$ 65.9	$ 62.7
Income available to common stockholders	$ 29.0	$ 65.9	$ 62.7
Earnings per share of common stock:			
Basic	$ 2.95	$ 6.51	$ 5.90
Diluted	$ 2.92	$ 5.90	$ 5.36
Dividends per common share	$ 1.20	$ 1.20	$ 1.10
Net cash provided by operating activities	$ 88.0	$ 45.2	$ 88.7
Cash dividends paid on common stock	$ 11.7	$ 11.7	$ 11.7
At December 31:			
Total investments	$ 298.7	$ 232.9	$ 168.8
Cash and cash equivalents	$ 280.5	$ 267.7	$ 314.4
Total assets	$ 670.1	$ 637.0	$ 598.6
Total stockholders equity	$ 243.7	$ 237.7	$ 182.6
Common shares outstanding (in millions)	9.7	10.3	10.2

Environmental Matters

Our subsidiaries that own waterfront property, including marina facilities, are subject to regulations under various federal, state, and local laws concerning the environment, including laws addressing the discharge of pollutants into the air and water and the management and disposal of hazardous substances and wastes and the cleanup of contaminated sites.

Employees

As of February 14, 2017, we employed 246 full-time individuals working primarily from our corporate offices in Florida and 76 employees located in India. In addition, our real estate operations have 77 employees leased through professional employer organizations.

Available Information

We file annual, quarterly, and current reports with the U.S. Securities and Exchange Commission (SEC). These filings are accessible free of charge on our website, www.hcigroup.com (click SEC filings at the Investor Information tab), as soon as reasonably practicable after they have been electronically filed with or furnished to the SEC.

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The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers, which can be accessed via the SEC s website at www.sec.gov. In addition, these filings are accessible at the SEC s Public Reference Room, which is located at 100 F Street, NE, Washington, DC 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330.

ITEM 1A *Risk Factors*

Our business is subject to a number of risks, including those described below, which could have a material effect on our results of operations, financial condition or liquidity and could cause our operating results to vary significantly from period to period.

Our historical revenue growth was derived primarily through policy assumptions and acquisitions. We cannot guarantee that future policy assumptions and acquisitions will be available to the extent they have in the past.

Substantially all of our historical revenue has been generated from policies assumed from Citizens, our acquisition of policies from one Florida insurance company and subsequent renewals of these policies. Our ability to grow our premium base may depend upon the availability of future policy assumptions and acquisitions upon acceptable terms. Opportunities to acquire large numbers of policies from Citizens meeting our strict underwriting criteria have diminished in recent years. We cannot ensure you that such opportunities will arise in the future.

Although we plan to enter the insurance market in other states, our insurance business is currently in Florida only. Thus, any catastrophic event or other condition affecting losses in Florida could adversely affect our financial condition and results of operations.

Any catastrophic event, a destructive weather pattern, a general economic trend, regulatory developments or other conditions specifically affecting the state of Florida could have a disproportionately adverse impact on our business, financial condition, and results of operations. While we actively manage our exposure to catastrophic events through our underwriting process and the purchase of reinsurance, the fact that our business is concentrated in the state of Florida subjects it to increased exposure to certain catastrophic events and destructive weather patterns such as hurricanes, tropical storms, and tornados. Changes in the prevailing regulatory, legal, economic, political, demographic and competitive environment, and other conditions in the state of Florida could also make it less attractive for us to do business in Florida and would have a more pronounced effect on our business than it would on other insurance companies that are geographically diversified. Since our business is concentrated in this manner, the occurrence of one or more catastrophic events or other conditions affecting losses in the state of Florida could have an adverse effect on our business, financial condition, and/or results of operations.

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Changing climate conditions could have an adverse impact on our business, results of operations or financial condition.

There is an emerging scientific consensus on global warming. Climate change, to the extent it produces rising temperatures and changes in weather patterns, may affect the frequency and severity of storms and other weather events, the affordability, availability and underwriting results of homeowners and property insurance, and, if frequency and severity patterns increase, could negatively affect our business, results of operations, and/or financial condition.

Our results may fluctuate based on many factors including cyclical changes in the insurance industry.

The insurance industry historically has been cyclical, characterized by periods of intense price competition due to excessive underwriting capacity, as well as periods when shortages of capacity permitted an increase in pricing and, thus, more favorable underwriting profits. As premium levels increase, there may be new entrants to the market, which could subsequently lead to a decrease in premium levels. Any of these factors could lead to a significant reduction in premium rates in future periods, less favorable policy terms and fewer opportunities to underwrite insurance risks, which could have a material, adverse effect on our results of operations and cash flows. In addition to these considerations, changes in the frequency and severity of losses suffered by insureds and insurers may affect the cycles of the insurance business significantly.

We cannot predict whether market conditions will improve, remain constant or deteriorate. Negative market conditions may impair our ability to write insurance at rates that we consider appropriate relative to the risk assumed. If we cannot write insurance at appropriate rates, our business would be materially and adversely affected.

Our business could be harmed if we lose the services of our key personnel.

Our operations are highly dependent on the efforts of our senior executive officers, particularly our chief executive officer, Paresh Patel, as well as our chief financial officer, Richard Allen. The loss of their leadership, industry knowledge and experience could negatively impact our operations. However, we have management succession plans to lessen any such negative impact. Apart from Mr. Patel, Mr. Allen, and Mark Harmsworth, our recently hired Senior Vice President of Finance, we have no employment agreements with any of our personnel nor do we offer any guarantee of any employee s ongoing service. We maintain key-man life insurance on Mr. Patel although such policy may be insufficient to cover us for the damage resulting to our company from the loss of Mr. Patel s services.

Our information technology systems may fail or be disrupted, which could adversely affect our business.

Our insurance business is highly dependent upon the successful and uninterrupted functioning of our computer and data processing systems. We rely on these systems to perform underwriting and other modeling functions necessary for writing business, as well as to handle our policy administration process (i.e., the printing and mailing of our policies, endorsements, renewal notices, etc.). The failure or disruption of these systems could interrupt our operations and result in a material, adverse effect on our business.

The growth of our insurance business is dependent upon the successful development and implementation of advanced computer and data processing systems as well as the development and deployment of new information technologies to streamline our operations, including policy underwriting, production and administration and claim handling. The failure of these systems to function as planned could slow our growth and adversely affect our future business volume and results of operations.

We conduct our business primarily from offices located in Tampa, Florida where tropical storms could damage our facilities or interrupt our power supply. The loss or significant impairment of functionality in these facilities for any reason could have a material, adverse effect on our business although we believe we have sufficient redundancies to replace our facilities if functionality is impaired. We contract with a third-party vendor to maintain complete daily backups of our systems, which are stored at the vendor s facility in Atlanta, Georgia. Access to these databases is strictly controlled and limited to authorized personnel. In the event of a disaster causing a complete loss of functionality at our Tampa location, we plan to temporarily use our secondary office in Ocala, Florida to continue our operations.

An unauthorized disclosure or loss of policyholder or employee information or other sensitive or confidential information, including by cyber-attack or other security breach, could cause a loss of data, give rise to remediation or other expenses, expose us to liability under federal and state laws, and subject us to litigation and investigations, which could have an adverse effect on our business, cash flows, financial condition and results of operations.

As part of our normal operations, we collect, process and retain certain sensitive and confidential information. We are subject to various federal and state privacy laws and rules regarding the use and disclosure of certain sensitive or confidential information, including the Gramm-Leach-Bliley Act and its state-law progeny. Despite the security measures we have implemented to help ensure data security and compliance with applicable laws and rules, which include firewalls, regular penetration testing and other measures, our facilities and systems, and those of our third-party service providers and vendors, may be vulnerable to cyber-attacks, security breaches, acts of vandalism, computer viruses, theft of data, misplaced or lost data, programming and human errors, physical break-ins, or other disruptions. In addition, we cannot ensure that we will be able to identify, prevent or contain the effects of possible cyber-attacks or other cybersecurity risks in the future that may bypass our security measures or disrupt our information technology systems or business.

Noncompliance with any privacy or security laws and regulations, or any security breach, cyber-attack or cybersecurity breach, and any incident involving the misappropriation, loss or other unauthorized disclosure or use of, or access to, sensitive or confidential member information, could require us to expend significant capital and other resources to continue to modify or enhance our protective measures and to remediate any damage caused by such breaches. In addition, this could result in interruptions to our operations and damage to our reputation, and misappropriation of confidential information could also result in regulatory enforcement actions, material fines and penalties, litigation or other liability or actions which could have a material adverse effect on our business, cash flows, financial condition and results of operations. As the regulatory environment related to information security, data collection and use, and privacy becomes increasingly rigorous, with new and constantly changing requirements applicable to our business, compliance with those requirements could also result in additional costs.

We rely on service providers and vendors to provide certain technology, systems and services that we use in connection with various functions of our business, including PCI DSS (Payment Card Industry Data Security Standard) compliant credit card processing, and we may entrust them with confidential information. The information systems of our third-party service providers and vendors are also vulnerable to an increasing threat of continually evolving cybersecurity risks. Unauthorized parties may attempt to gain access to these systems or our information through fraud or other means of deceiving our associates, third-party service providers or vendors. Hardware, software or applications we obtain from third parties may contain defects in design or manufacture or other problems that could unexpectedly compromise information security. The methods used to obtain unauthorized access, disable or degrade service or sabotage systems are also constantly changing and evolving and may be difficult to anticipate or detect for long periods of time. Ever-evolving threats mean our third-party service providers and vendors must continually evaluate and adapt their own respective systems and processes, and there is no assurance that they will be adequate to safeguard against all data security breaches or misuses of data. Any future significant compromise or breach of our data security via a third-party service provider or vendor could result in additional significant costs, lost revenues, fines, lawsuits, and damage to our reputation.

Because insurance rates are heavily regulated by state governments, inflation could adversely affect our financial condition and results of operations

The rates an insurer may charge to its policyholders are controlled by laws and state regulators. Because our ability to raise rates is subject to regulation, our exposure to the risks of price inflation and other economic forces may be more profound than the exposure to which other industries may be subject. Inflation and economic forces could increase our costs (such as the cost to repair a damaged home) and lower our profitability, while we would be unable to respond with higher rates, except with regulatory approval. While we attempt to use new technology to lower our overall costs, and invest in real estate to mitigate against negative economic forces, increased rates of price inflation could nonetheless have an adverse effect on our business, financial condition and/or results of operations.

Increased competition, competitive pressures, industry developments, and market conditions could affect the growth of our business and adversely impact our financial results.

The property and casualty insurance industry in Florida is cyclical and highly competitive. We compete not only with other stock companies but also with mutual companies, the U.S. government, other underwriting organizations and alternative risk sharing mechanisms. Our principal lines of business are written by numerous other insurance companies. Competition

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for any one account may come from very large, well-established national companies, smaller regional companies, other specialty insurers in our field, and new entrants to the Florida market. Many of these competitors have greater financial resources, larger agency networks and greater name recognition than our company. We compete for business not only on the basis of price, but also on the basis of financial strength, types of coverage offered, availability of coverage desired by customers, commission structure, and quality of service. We may have difficulty continuing to compete successfully on any of these bases in the future. Competitive pressures coupled with market conditions may affect our rate of premium growth and financial results.

Our ability to compete in the property and casualty insurance industry and our ability to expand our business may be negatively affected by the fact that we are not a long-established company. HCPCI and TypTap have each obtained a Demotech rating of A Exceptional, which is accepted by major mortgage companies operating in the state of Florida and many other states. Mortgage companies may require homeowners to obtain property insurance from an insurance company with an acceptable A.M. Best rating, which we do not currently have. Such a requirement could prevent us from expanding our business unless we obtain such rating, which may in turn limit our ability to compete with large, national insurance companies and certain regional insurance companies. A downgrade or loss of our Demotech rating could result in a substantial loss of business in the event insureds move their business to insurers with a sufficient financial strength rating.

There are inherent limitations and risks related to our projections and our estimates of claims and loss reserves. If our actual losses exceed our loss reserves, our financial results, our ability to expand our business, and our ability to compete in the property and casualty insurance industry may be negatively affected. In addition, industry developments could further increase competition in our industry. These developments could include

- an influx of new capital in the marketplace as existing companies attempt to expand their businesses and new companies attempt to enter the insurance business because of better pricing and/or terms;

- new programs or changes to existing programs in which federally or state-sponsored entities provide property insurance in catastrophe-prone areas or other alternative markets;

- changes in Florida s or any other states regulatory climate; and

- the enactment of federal proposals for an optional federal charter that would allow some competing insurers to operate under regulations different or less stringent than those applicable to our insurance subsidiaries.

These developments and others could make the property and casualty insurance marketplace more competitive by increasing the supply of insurance available.

If competition limits our ability to write new business at adequate rates, our future results of operations would be adversely affected.

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If our actual losses from claims exceed our loss reserves, our financial results would be adversely affected.

Our objective is to establish loss reserves that are adequate and represent management s best estimate of the ultimate cost to investigate and settle a specific claim. However, the process of establishing adequate reserves is complex and inherently uncertain, and the ultimate cost of a claim may vary materially from the amounts reserved. We regularly monitor and evaluate loss and loss adjustment expense reserve development to determine reserve adequacy.

Due to these uncertainties, the ultimate losses may vary materially from current loss reserves which could have a material, adverse effect on our future financial condition, results of operations and cash flows.

Our failure to pay claims accurately could adversely affect our insurance business, financial results and capital requirements.

We rely on our claims personnel to accurately evaluate and pay the claims made under our policies. Many factors could affect our ability to accurately evaluate and pay claims, including the accuracy of our external independent adjusters as they make their assessments and submit their estimates of damages; the training, background, and experience of our claims representatives; the ability of our claims personnel to ensure consistent claims handling given the input by our external independent adjusters; the ability of our claims department to translate the information provided by our external independent adjusters into acceptable claims settlements; and the ability of our claims personnel to maintain and update our claims handling procedures and systems as they evolve over time based on claims and geographical trends in claims reporting. Any failure to pay claims accurately could lead to material litigation, undermine our reputation in the marketplace, impair our corporate image and negatively affect our financial results.

The effects of emerging claim and coverage issues on our business are uncertain.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect our business by either extending coverage beyond our underwriting intent or by increasing the number or size of claims. In some instances, these changes may not become apparent until sometime after we have issued insurance contracts that are affected by the changes. As a result, the full extent of liability under our insurance contracts may not be known for many years after a contract is issued and renewed, and our financial position and results of operations may be adversely affected as a result of any such unforeseen changes.

If we are unable to expand our business because our capital must be used to pay greater than anticipated claims, our financial results may suffer.

Our future growth will depend on our ability to expand the number of insurance policies we write, to expand the kinds of insurance products we offer, and to expand the geographic markets in which we do business, all balanced by the insurance risks we choose to assume and cede. Our existing sources of funds include possible sales of our securities and our income from operations and investments. Unexpected catastrophic events in our market areas, such as hurricanes, may result in greater claims losses than anticipated, which could require us to limit or halt our growth while we redeploy our capital to pay these unanticipated claims unless we can raise additional capital.

HCI Group, Inc. depends on the ability of its subsidiaries to generate and transfer funds to meet its debt obligations.

HCI Group, Inc. does not have significant revenue generating operations of its own. Our ability to make scheduled payments on our debt obligations depends on the financial condition and operating performance of our subsidiaries. If the funds we receive from our subsidiaries, some of which are subject to regulatory restrictions on the payment of distributions, are insufficient to meet our debt obligations, we may be required to raise funds through the issuance of additional debt or equity securities, reduce or suspend dividend payments, or sell assets.

We may require additional capital in the future which may not be available or may only be available on unfavorable terms.

Our future capital requirements depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover losses. To the extent that our present capital is insufficient to meet future operating requirements or to cover losses, we may need to raise additional funds through financings or curtail our growth. Based on our current operating plan, we believe current capital together with our anticipated retained income will support our operations. However, we cannot provide any assurance in that regard, since many factors will affect our capital needs and their amount and timing, including our growth and profitability, and the availability of reinsurance, as well as possible acquisition opportunities, market disruptions and other unforeseeable developments. If we require additional capital, it is possible that equity or debt financing may not be available at all or may be available only on terms unfavorable to us. Equity financings could result in dilution to our shareholders, and in any case such securities may have rights, preferences and privileges that are senior to those of existing shareholders. If we cannot obtain adequate capital on favorable terms or at all, our business, financial condition or results of operations could be materially affected.

There may be limited markets for and restrictions on certain holdings in our investment portfolio.

Certain holdings in our investment portfolio include limited partnership interests and real estate joint ventures. We may increase our holdings in these types of investments. These investments may be illiquid in the near term as they are privately placed and are subject to certain restrictions or conditions that may limit our ability to immediately dispose of the investments. If it becomes necessary to sell any of these investments at a time when the fair market value is below our carrying value, we may incur significant losses which could have a material adverse effect on our net income and financial position.

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Our financial results may be negatively affected by the fact that a portion of our income is generated by the investment of our available cash.

A portion of our income is, and likely will continue to be, generated by the investment of our available cash. The amount of income so generated is a function of our investment policy, available investment opportunities, and the amount of available cash invested. We may alter our investment policy to accept higher levels of risk with the expectation of higher returns. Fluctuating interest rates and other economic factors make it difficult to estimate accurately the amount of investment income that will be realized. In fact, we have realized and may in the future realize losses on sales of our investments as well as other-than-temporary losses on our investment holdings.

Reinsurance coverage may not be available to us in the future at commercially reasonable rates or at all and we risk non-collectability of reinsurance amounts due us from reinsurers with which we have contracted.

Reinsurance is a method of transferring part of an insurance company s liability and premium under an insurance policy to another insurance company, or reinsurer. We use reinsurance arrangements to limit and manage the amount of risk we retain, to stabilize our underwriting results and to increase our underwriting capacity. The cost of such reinsurance is subject to prevailing market conditions beyond our control, such as the amount of capital in the reinsurance market and the occurrence of natural and man-made catastrophes. We cannot be assured that reinsurance will remain continuously available to us in the amounts we consider sufficient and at prices acceptable to us. As a result, we may determine to increase the amount of risk we retain or look for other alternatives to reinsurance, which could in turn have a material, adverse effect on our financial position, results of operations and cash flows.

With respect to the reinsurance treaties we currently have in effect, our ability to recover amounts due from reinsurers is subject to such reinsurers ability and willingness to pay and to meet their obligations to us. We attempt to select financially strong reinsurers with an A.M. Best rating of A- or better or we require the reinsurer to fully collateralize its exposure. While we monitor from time to time their financial condition, we rely principally on A.M. Best, our reinsurance broker, and other rating agencies in determining their ability to meet their obligations to us. Any failure on the part of any one reinsurance company to meet its obligations to us could have a material, adverse effect on our financial condition or results of operations.

We have exposure to unpredictable catastrophes, which can materially and adversely affect our financial results.

We write insurance policies that cover homeowners, condominium owners, and tenants for losses that result from, among other things, catastrophes. We are therefore subject to losses, including claims under policies we have written, arising out of catastrophes that may have a significant effect on our business, results of operations, and financial condition. A significant catastrophe could also have an adverse effect on our reinsurers. Catastrophes can be caused by various events, including hurricanes, tropical storms, tornadoes, windstorms, earthquakes, hailstorms, explosions, power outages, fires and man-made events. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Our policyholders are currently concentrated in Florida, which is especially subject to adverse weather conditions such as hurricanes and tropical storms. Therefore, although we attempt to manage our exposure to catastrophes through our underwriting process and the purchase of reinsurance protection, an especially severe catastrophe or series of catastrophes could exceed our reinsurance protection and may have a material, adverse impact on our results of operations and financial condition.

Industry trends, such as increased litigation against the insurance industry and individual insurers, the willingness of courts to expand covered causes of loss, rising jury awards, and the escalation of loss severity may contribute to increased costs and to the deterioration of the reserves of our insurance subsidiaries.

Loss severity in the property and casualty insurance industry may increase and may be driven by larger court judgments. In the event legal actions and proceedings are brought on behalf of classes of complainants, this may increase the size of judgments. The propensity of policyholders and third party claimants to litigate and the willingness of courts to expand causes of loss and the size of awards may render our loss reserves inadequate for current and future losses.

The failure of the risk mitigation strategies we utilize could have a material, adverse effect on our financial condition or results of operations.

We utilize a number of strategies to mitigate risk exposure within our insurance business, which include:

- engaging in vigorous underwriting;
- carefully evaluating terms and conditions of our policies;
- focusing on our risk aggregations by geographic zones and other bases; and
- ceding insurance risk to reinsurance companies.

However, there are inherent limitations in these tactics. We cannot provide assurance that an unanticipated event or series of events will not result in loss levels which could have a material, adverse effect on our financial condition or results of operations.

The failure of any of the loss limitation methods we employ could have a material, adverse effect on our financial condition or our results of operations.

Our insurance underwriting process is generally designed to limit our exposure to known and manageable risks. Various provisions of our policies, such as limitations or exclusions from coverage, which have been negotiated to limit our risks, may not be enforceable in the manner we intend.

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In addition, the policies we issue contain conditions requiring the prompt reporting of claims to us and our right to decline coverage in the event of a violation of that condition. While our insurance product exclusions and limitations reduce the loss exposure to us and help eliminate known exposures to certain risks, it is possible that a court or regulatory authority could nullify or void an exclusion or legislation could be enacted modifying or barring the use of such endorsements and limitations in a way that would adversely affect our loss experience, which changes could have a material, adverse effect on our financial condition or results of operations.

In the future, we may rely on independent agents to write our insurance policies, and if we are not able to contract with and retain independent agents, our revenues would be negatively affected.

Although voluntary policies comprise a small percentage of our business, we expect to increase the number of voluntary policies (policies not assumed or acquired from another company) we write as our business and product lines expand. An inability to sell our products through independent agents would negatively affect our revenues.

We must compete with other insurers for independent agents business. Our competitors may offer a greater variety of insurance products, lower premiums for insurance coverage, or higher commissions to their agents. If our products, pricing and commissions do not remain competitive, we may find it more difficult to attract business from independent agents to sell our products. A material reduction in the amount of our products that independent agents sell could negatively affect our revenues.

Our growth may depend on the success of our residential flood offering.

Our recently formed subsidiary, TypTap Insurance Company, is currently dedicated to providing residential flood insurance in Florida. TypTap plans to expand to other states and eventually establish itself as a leading alternative to the National Flood Insurance Program, administered by the Federal Emergency Management Agency, which has been the dominant provider of flood insurance in the United States for over 40 years.

The genesis of TypTap was the enactment in 2012 of The Biggert Waters Act which mandated that the National Flood Insurance Program establish actuarially sound premium rates. The national program s rates thereafter soared. Congress reacted in 2014 by enacting the Homeowner Flood Insurance Affordability Act which limits the national program s annual rate increases to between 15% and 25% depending on particular circumstances.

We entered the residential flood market in 2015 based upon our own analysis that in certain states and regions, with selective underwriting, we could profitably compete with the National Flood Insurance Program on the basis of lower rates. We are one of only a few private entrants into the flood insurance market. There is relatively little actuarial or historical data available relating to flood events. We have our own sophisticated underwriting algorithms for accepting flood insurance applications. Our algorithms, however, are untested.

There can be no assurance that future laws and regulations relating to flood insurance will not materially and adversely impact our ability to profitably compete in the residential flood market. Further there can be no assurance that our original analysis regarding residential flood insurance and its risks and costs will be proven correct over time or that our algorithms will deliver the anticipated underwriting results.

TypTap features an on-line platform for quoting and binding residential flood policies that is designed to be quick and easy to use and accessible by any Internet capable device, such as a mobile phone. We have only recently begun to explore and develop methods to market TypTap s flood insurance and its on-line platform. Since the federal flood program has dominated the flood insurance market for over 40 years, the market for private flood insurance is relatively new. There can be no assurance that our marketing efforts will be successful in producing substantial numbers of flood insurance policies for us or that prospective insureds will be receptive to our flood insurance or our on-line platform.

Our success depends on our ability to accurately price the risks we underwrite.

The results of our operations and our financial condition depend on our ability to underwrite and set premium rates accurately for a wide variety of risks, including risks associated with flood insurance and other new product offerings. Rate adequacy is necessary to generate sufficient premiums to pay losses, loss adjustment expenses, and underwriting expenses and to earn a profit. To price our products accurately, we must collect and properly analyze a substantial amount of data; develop, test and apply appropriate rating formulas; closely monitor and timely recognize changes in trends; and project both severity and frequency of losses with reasonable accuracy. Our ability to undertake these efforts successfully, and thus, price our products accurately, is subject to several risks and uncertainties, some of which are outside our control, including

- the availability of sufficient reliable data;
- the uncertainties that inherently characterize estimates and assumptions;
- our selection and application of appropriate rating and pricing techniques;
- changes in legal standards, claim settlement practices, and restoration costs; and
- legislatively imposed consumer initiatives.

In addition, we could underprice risks, which would negatively affect our profit margins. We could also overprice risks, which could reduce our retention, sales volume and competitiveness. The foregoing factors could materially and adversely affect our profitability.

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Use of current operating resources may be necessary to develop future new insurance products.

We may expand our product offerings by underwriting additional insurance products and programs. Claddaugh may offer reinsurance products to unaffiliated insurance companies. Expansion of our product offerings will result in increases in expenses due to additional costs incurred in actuarial rate justifications, software and personnel. Offering additional insurance products will also require regulatory approval, further increasing our costs and potentially affecting the speed with which we will be able to pursue new market opportunities. We cannot assure you that we will be successful bringing new insurance products to markets.

Use of current operating resources may be necessary to expand our insurance business geographically.

Although we currently conduct our homeowners insurance business in Florida, we plan to enter the homeowners insurance markets in other states. Geographic expansion of our insurance business will result in increases in expenses due to additional costs incurred in actuarial rate justifications, software, personnel and regulatory compliance. Although we plan to enter other states judiciously with attention to profitability, we cannot assure you that our entry into other states will be successful.

As an insurance holding company, we are currently subject to state regulation and in the future may become subject to federal regulation.

All states regulate insurance holding company systems. State statutes and administrative rules generally require each insurance company in the holding company group to register with the department of insurance in its state of domicile and to furnish information concerning the operations of the companies within the holding company system that may materially affect the operations, management or financial condition of the insurers within the group. As part of its registration, each insurance company must identify material agreements, relationships and transactions with affiliates, including without limitation, loans, investments, asset transfers, transactions outside of the ordinary course of business, certain management, service, and cost sharing agreements, reinsurance transactions, dividends, and consolidated tax allocation agreements.

Insurance holding company regulations generally provide that transactions between an insurance company and its affiliates must be fair and equitable, allocated between the parties in accordance with customary accounting practices, and fully disclosed in the records of the respective parties. Many types of transactions between an insurance company and its affiliates, such as transfers of assets among such affiliated companies, certain dividend payments from insurance subsidiaries and certain material transactions between companies within the system may be subject to prior approval by, or prior notice to, state regulatory authorities. If we are unable to obtain the requisite prior approval for a specific transaction, we would be precluded from taking the action, which could adversely affect our operations. In addition, state insurance regulations also frequently impose notice or approval requirements for the acquisition of specified levels of ownership in the insurance company or insurance holding company.

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Our Florida insurance subsidiaries are approved as admitted carriers in Florida and HCPCI is approved as a non-admitted carrier in Maryland, New Jersey, South Carolina and Virginia. We may in the future seek authorization to transact business in other states as well. We will therefore become subject to the laws and regulatory requirements of those states. These regulations may vary from state to state, and states occasionally may have conflicting regulations. Currently, the federal government s role in regulating or dictating the policies of insurance companies is limited. However, Congress, from time to time, considers proposals that would increase the role of the federal government in insurance regulation, either in addition to or in lieu of state regulation. The impact of any future federal insurance regulation on our insurance operations is unclear and may adversely impact our business or competitive position.

Our insurance subsidiaries are subject to extensive regulation, which may reduce our profitability or limit our growth. Moreover, if we fail to comply with these regulations, we may be subject to penalties, including fines and suspensions, which may adversely affect our financial condition and results of operations.

The insurance industry is highly regulated and supervised. Our insurance subsidiaries are subject to the supervision and regulation of the states in which they are domiciled and the states in which they transact insurance business. Such supervision and regulation is primarily designed to protect our policyholders rather than our shareholders. These regulations are generally administered by a department of insurance in each state and relate to, among other things

the content and timing of required notices and other policyholder information;

the amount of premiums the insurer may write in relation to its surplus;

the amount and nature of reinsurance a company is required to purchase;

participation in guaranty funds and other statutorily created markets or organizations;

business operations and claims practices;

approval of policy forms and premium rates;

standards of solvency, including risk-based capital measurements;

licensing of insurers and their products;

restrictions on the nature, quality and concentration of investments;

- restrictions on the ability of insurance company subsidiaries to pay dividends to insurance holding companies;
- restrictions on transactions between insurance companies and their affiliates;
- restrictions on the size of risks insurable under a single policy;
- requiring deposits for the benefit of policyholders;
- requiring certain methods of accounting;
- periodic examinations of our operations and finances;
- the form and content of records of financial condition required to be filed; and
- the level of reserves.

The FLOIR and regulators in other jurisdictions where we may become licensed and offer insurance products conduct periodic examinations of the affairs of insurance companies and require the filing of annual and other reports relating to financial condition, holding company issues and other matters. These regulatory requirements may adversely affect or inhibit our ability to achieve some or all of our business objectives. These regulatory authorities also conduct periodic examinations into insurers business practices. These reviews may reveal deficiencies in our insurance operations or non-compliance with regulatory requirements.

In certain states including Florida, insurance companies are subject to assessments levied by the states where they conduct their business. While we can recover these assessments from Florida policyholders through policy surcharges, our payment of the assessments and our recoveries may not offset each other in the same reporting period in our financial statements and may cause a material, adverse effect on our cash flows and results of operations in a particular reporting period.

In addition, regulatory authorities have relatively broad discretion to deny or revoke licenses for various reasons, including the violation of regulations. In some instances, we follow practices based on our interpretations of regulations or practices that we believe may be generally followed by the industry. These practices may turn out to be different from the interpretations of regulatory authorities. If we do not have the requisite licenses and approvals or do not comply with applicable regulatory requirements, insurance regulatory authorities could preclude or temporarily suspend us from carrying on some or all of our activities or otherwise penalize us. This could adversely affect our ability to operate our business.

Finally, changes in the level of regulation of the insurance industry or changes in laws or regulations themselves or interpretations by regulatory authorities could adversely affect our ability to operate our business, reduce our profitability and limit our growth.

Our revenue from real estate investments may be affected by the success and economic viability of our anchor retail tenants. Our reliance on a single or significant tenant at certain properties may impact our ability to lease vacated space and adversely affect returns on the specific property.

At certain retail centers, we may have tenants, commonly referred to as anchor tenants, occupying all or a large portion of the gross leasable space. In the event an anchor tenant becomes insolvent, suffers a downturn in business, ceases its operations at the retail center, or otherwise determines not to renew its lease, any reduction or cessation of rental payments to us could adversely affect the returns on our real estate investments. A lease termination or cessation of operations by an anchor tenant could also lead to the loss of other tenants at the specific retail location. We may then incur additional expenses to make improvements and prepare the vacated space to be leased to one or more new tenants.

Similarly, the leases of some anchor tenants may permit the anchor tenant to transfer its lease to another retailer. The transfer to a new anchor tenant could cause customer traffic in the retail center to decrease and thereby reduce the income generated by that retail center. A lease transfer to a new anchor tenant could also allow other tenants to make reduced rental payments or to terminate their leases.

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Our retail and other real estate properties may be subject to impairment charges which can adversely affect our financial results.

We periodically evaluate our long-lived assets and related intangible assets to determine if there has been any impairment in their carrying values. If we determine an impairment has occurred, we are required to record an impairment charge equal to the excess of the asset s carrying value over its estimated fair value. As our real estate operations grow, there is an increased potential that the impairment of an asset could have a material adverse effect on our financial results. In addition, our fair value estimates are based on several assumptions that are subject to economic and market uncertainties including, but not limited to, demand for space, competition for tenants, changes in market rental rates and costs to operate each property. As these factors are difficult to predict and are subject to future events that may alter our assumptions, the future cash flows estimated in our impairment analysis may not be achieved.

Our real estate operations include owning marina operations, which are subject to regulation under various federal, state, and local laws concerning the environment.

Our marina operations are subject to regulation under various federal, state, and local laws concerning the environment, including laws addressing the discharge of pollutants into the air and water and the management and disposal of hazardous substances and wastes and the cleanup of contaminated sites. We could incur substantial costs, including remediation costs, fines and civil or criminal sanctions and third-party damage or personal injury claims, if in the future we were to violate or become liable under environmental laws relating to our marina operations.

Our real estate operations include owning restaurant operations, which expose us to additional risks, which could negatively impact our operating results and financial condition.

Our restaurant operations expose us to unique business risks. For example, restaurant operations are dependent in large part on food, beverage, and supply costs that are not within our control. In addition, the restaurant industry is affected by changes in consumer preferences and discretionary spending patterns that could adversely affect revenues from restaurant operations. Moreover, the restaurant industry is affected by litigation and publicity concerning food quality, health, alcoholic beverages and other issues which can cause guests to avoid restaurants and that can result in liabilities. Any one of these risks, among others, could negatively impact our operating results and financial condition.

Our operations in India expose us to additional risks, which could negatively impact our business, operating results, and financial condition.

Our India operations expose us to additional risks including income tax risks, currency exchange rate fluctuations and risks related to other challenges caused by distance, language, and compliance with Indian labor laws and other complex foreign and U.S. laws and regulations that apply to our India operations. These numerous and sometimes conflicting laws and regulations include anti-corruption laws, such as the Foreign Corrupt Practices Act, and other local laws prohibiting corrupt payments to governmental officials, among others. Violations of these laws and regulations could result in fines and penalties, or criminal sanctions against us, our officers, or our employees. Although policies and procedures are designed to ensure compliance with these laws and regulations, there can be no assurance that our employees, contractors, or agents will not violate our policies.

Our ongoing investments in real estate and information technology businesses have inherent risks, and could burden our financial and human resources.

We have invested and expect to continue to invest in real estate and information technology businesses. Despite our due diligence prior to each venture, these investments may still involve significant risks and uncertainties, including distraction of management and employees from current operations, insufficient revenues to offset liabilities assumed and incurred expenses, inadequate return of capital, and failure to realize the anticipated benefits. There can be no assurance that such investments will be successful and will not adversely affect our financial condition and operating results.

There may be unintended consequences of the anti-takeover provisions of our shareholder rights agreement.

Our shareholder rights agreement is intended to deter coercive or unfair takeover tactics and to protect our shareholders interests by encouraging anyone seeking control of our company to negotiate with our board of directors. However, these rights may discourage, delay or prevent a tender offer or takeover attempt, including offers or attempts that could be beneficial to our shareholders. In addition, the rights agreement may deter investors from participating in any future equity offerings we propose.

ITEM 1B ***Unresolved Staff Comments***

Not applicable.

ITEM 2 ***Properties***

<u>*Real Estate Owned and Used in Operations*</u>

Tampa, Florida. The real estate consists of 3.5 acres of land, a three-story building with gross area of 122,000 square feet, and a four-level parking garage. This facility is used by us and our U.S. subsidiaries and serves as our headquarters. In addition, we lease an aggregate of approximately 38,200 square feet to non-affiliates.

Ocala, Florida. The real estate consists of 1.6 acres of land and an office building with gross area of approximately 16,000 square feet. The facility is designated for our insurance operations and will be used as an alternative location in the event a catastrophic event impacts our operations in Tampa, Florida.

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Investment Real Estate

Treasure Island, Florida. The real estate consists of approximately 10 acres of waterfront property and land improvements, a restaurant and a marina facility. The marina facility and the restaurant are currently owned and operated by us.

Tierra Verde, Florida. The real estate consists of 7.1 acres of waterfront property, a dry rack storage building with gross area of 57,500 square feet, and two buildings with retail space having an aggregate gross area of approximately 29,000 square feet. This marina facility is owned and operated by us. Approximately 5% of the available retail space is occupied by the Company, 52% of the retail space is leased to non-affiliates, and 43% of the retail space is available for lease.

Riverview, Florida. The real estate currently under development consists of 2.57 acres of land on which a retail center will be constructed for lease or for sale. This development project is operated and managed through a consolidated joint venture.

Sorrento, Florida. The real estate includes 5.42 acres of outparcel land intended for ground lease or resale and a retail shopping center with 61,400 square feet of net rentable area. This retail shopping center was acquired by us through the ADC Arrangement in August 2016. Approximately 74% of the rentable space is currently leased to a large, well-known grocery retailer.

Melbourne, Florida. The real estate includes 2.26 acres of outparcel land intended for ground lease, resale or future development and a retail shopping center with 49,995 square feet of rentable area. In December 2016, we acquired full ownership of this property from our co-developer. Approximately 42% of the rentable space is currently leased to a large well-known grocery retailer.

Leased Property

Noida, India. We lease 15,000 square feet of office space for our information technology operations. The lease commenced in 2013 and has an initial term of nine years.

Miami, Florida. We lease approximately 2,819 square feet of office space for our claims related administration. The lease commenced February 15, 2015 and has an initial term of three years.

Rental expense under all facility leases was $333,000, $304,000 and $222,000 during the years ended December 31, 2016, 2015 and 2014, respectively.

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ITEM 3 *Legal Proceedings*

We are a party to claims and legal actions arising routinely in the ordinary course of our business. Although we cannot predict with certainty the ultimate resolution of the claims asserted against us, we do not believe that any currently pending legal proceeding to which we are a party will have a material, adverse effect on our consolidated financial position, results of operations or cash flows.

In December 2014, we received two nearly identical letters from a single law firm representing two individual shareholders demanding we take action against our directors to remedy alleged damages to the Company. The Company, each of the directors and the two shareholders agreed to a settlement with respect to demands by the two shareholders. As a result, certain of the directors restricted shares were cancelled March 2, 2016. The cancelled shares were made up of 148,000 shares that would vest in the event our share price reached $50.00 and 12,000 shares that would vest in the event our share price reached $95.00. Our results of operations for the year ended December 31, 2015 included $936,000 of expense related to this settlement, primarily expense related to the reclassification from retained earnings of dividends paid through December 2015 and expense related to the acceleration and recognition of the unamortized portion of accounting expense determined at the grant date. Our board members and the Company have also implemented certain non-financial corporate governance changes. We are not aware of any other pending shareholder demands.

ITEM 4 *Mine Safety Disclosures*

Not applicable.

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PART II

ITEM 5 ***Market for the Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

Markets for Common Stock

Our common stock is trading on the New York Stock Exchange under the symbol HCI. The following table represents the high and low sales prices for our common stock as reported by the New York Stock Exchange for the periods indicated:

	Common Stock Price	
	High	**Low**
Calendar Quarter - 2016		
First Quarter	$ 35.75	29.30
Second Quarter	$ 33.95	26.82
Third Quarter	$ 33.04	26.43
Fourth Quarter	$ 40.45	24.35
Calendar Quarter - 2015		
First Quarter	$ 50.38	41.12
Second Quarter	$ 47.94	41.93
Third Quarter	$ 46.00	37.41
Fourth Quarter	$ 45.50	32.29

Holders

As of February 14, 2017, the market price for our common stock was $45.33 and there were 206 holders of record of our common stock.

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Dividends

The declaration and payment of dividends is at the discretion of our board of directors. Our ability to pay dividends depends on many factors, including the Company s operating results, financial condition, capital requirements, the availability of cash from our subsidiaries and legal and regulatory constraints and requirements on the payment of dividends and such other factors as our board of directors deems relevant. The following table represents the frequency and amount of all cash dividends declared on our common stock for the two most recent fiscal years:

Declaration Date	Payment Date	Date of Record	Per Share Amount
1/19/2015	3/20/2015	2/20/2015	$ 0.30
4/20/2015	6/19/2015	5/15/2015	$ 0.30
7/21/2015	9/18/2015	8/21/2015	$ 0.30
10/16/2015	12/18/2015	11/20/2015	$ 0.30
1/8/2016	3/18/2016	2/19/2016	$ 0.30
4/14/2016	6/17/2016	5/20/2016	$ 0.30
7/8/2016	9/16/2016	8/19/2016	$ 0.30
10/13/2016	12/16/2016	11/18/2016	$ 0.30

Under Florida law, a domestic insurer may not pay any dividend or distribute cash or other property to its stockholders unless certain requirements, which are discussed in Note 24 Regulatory Requirements and Restrictions to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K, are met. Hence Florida law may limit the availability of cash from our insurance subsidiaries for the payment of dividends to our shareholders.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table summarizes our equity compensation plans as of December 31, 2016. We currently have no equity compensation plans not approved by our stockholders.

Plan Category	**(a) Number of Securities To be Issued Upon Exercise of Outstanding Options**	**(b) Weighted-Average Exercise Price of Outstanding Options**	**(c) Number of Securities Remaining Available for Future Issuance under Equity Compensation Plans (Excluding Securities Reflected in Column (a))**
Equity Compensation Plans Approved by Stockholders	50,000	$ 4.02	4,236,825

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Performance Graph

The following graph compares the 5-year cumulative total dollar return to shareholders on our common stock relative to the cumulative total returns of the Russell 2000 Index and the NASDAQ Insurance Index. An investment of $100 (with reinvestment of all dividends) is assumed to have been made in our common stock and in each index on December 31, 2011 and its relative performance is tracked through December 31, 2016. The returns shown are based on historical results and are not intended to suggest future performance.

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Recent Sales of Unregistered Securities

All information related to sales of unregistered securities has been reported in a current report on Form 8-K.

Issuer Purchases of Equity Securities

The table below summarizes the number of shares of common stock repurchased during the three months ended December 31, 2016 under the repurchase plan approved by our Board of Directors in December 2015 (dollar amounts in thousands, except share and per share amounts):

For the Month Ended	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (a)	Approximate Dollar Value of Shares That May Yet Be Purchased Under The Plans or Programs
October 31, 2016	68,845	$ 29.05	68,845	$
November 30, 2016	7	$ 26.40	7	$
December 31, 2016		n/a		$
	68,852	$ 29.05	68,852	

(a) In December 2015, our Board of Directors approved a one-year plan to repurchase up to $20 million of common shares. In December 2016, our Board of Directors approved a one-year plan to repurchase up to $20 million of common shares during 2017. The approved amounts in each year exclude brokerage fees. See Note 19 Stockholders Equity to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

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ITEM 6 *Selected Financial Data*

The following selected consolidated financial data should be read in conjunction with Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes appearing in Item 8 Financial Statements and Supplementary Data of this Annual Report on Form 10-K. The consolidated statements of income data for the years ended December 31, 2016, 2015, and 2014 and the consolidated balance sheet data at December 31, 2016 and 2015 are derived from our audited consolidated financial statements appearing in Item 8 of this Annual Report on Form 10-K. The consolidated statements of income data for the years ended December 31, 2013 and 2012, and the consolidated balance sheet data at December 31, 2014, 2013, and 2012, are derived from our audited consolidated financial statements that are not included in this Annual Report on Form 10-K. The historical results are not necessarily indicative of the results to be expected in any future period.

	As of or for the Years Ended December 31,				
	2016	2015	2014	2013	2012
	(Dollar amounts in thousands, except per share amounts)				
Operating Revenue					
Gross premiums earned	$ 378,678	$ 423,120	$ 365,488	$ 337,113	$ 233,607
Premiums ceded	(135,051)	(140,614)	(113,423)	(102,865)	(75,939)
Net premiums earned	243,627	282,506	252,065	234,248	157,668
Net investment income	9,087	3,978	4,888	1,469	980
Net realized investment gains (losses)	2,601	(608)	4,735	80	276
Net other-than-temporary impairment losses recognized in income:					
Total other-than-temporary impairment losses	(2,252)	(5,275)	(107)		
Portion of loss recognized in other comprehensive income, before taxes	(230)	594			
Net other-than-temporary impairment losses	(2,482)	(4,681)	(107)		
Policy fee income	3,914	3,496	2,820	3,098	2,538
Gain on repurchases of convertible senior notes	153				
Gain on bargain purchase	2,071				179
Gain on remeasurement of previously held interest	4,005				
Other income	1,470	1,261	1,707	2,193	1,424
Total operating revenue	264,446	285,952	266,108	241,088	163,065
Operating Expenses					
Losses and loss adjustment expenses	124,667	87,224	79,468	65,123	66,310
Policy acquisition and other underwriting expenses	42,642	41,984	37,952	31,619	25,930
Salaries and wages	19,037	20,140	16,483	14,714	10,545
Interest expense	11,079	10,754	10,453	3,607	
Goodwill and other impairment losses	388				161

Other operating expenses	19,777	19,658	20,790	19,572	10,539
Total operating expenses	217,590	179,760	165,146	134,635	113,485
Income before income taxes	46,856	106,192	100,962	106,453	49,580
Income tax expense	17,835	40,331	38,298	40,891	19,423
Net income	$ 29,021	$ 65,861	$ 62,664	$ 65,562	$ 30,157
Preferred stock dividends			4	(104)	(322)
Income available to common stockholders	$ 29,021	$ 65,861	$ 62,668	$ 65,458	$ 29,835

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	As of or for the Years Ended December 31,				
	2016	2015	2014	2013	2012
	(Dollar amounts in thousands, except per share amounts)				
Per Share Data:					
Basic earnings per common share	$ 2.95	$ 6.51	$ 5.90	$ 5.82	$ 3.45
Diluted earnings per common share	$ 2.92	$ 5.90	$ 5.36	$ 5.63	$ 3.02
Dividends per common share	$ 1.20	$ 1.20	$ 1.10	$ 0.95	$ 0.88
Ratios to Net Premium Earned:					
Loss Ratio	51.17%	30.88%	31.53%	27.80%	42.06%
Expense Ratio	38.14%	32.76%	33.99%	29.67%	29.92%
Combined Ratio	89.31%	63.64%	65.52%	57.47%	71.98%
Ratios to Gross Premiums Earned:					
Loss Ratio	32.92%	20.61%	21.74%	19.32%	28.39%
Expense Ratio	24.54%	21.87%	23.45%	20.62%	20.19%
Combined Ratio	57.46%	42.48%	45.19%	39.94%	48.58%
Consolidated Balance Sheet Data:					
Total investments	$ 298,734	$ 232,917	$ 168,799	$ 146,028	$ 60,916
Total cash and cash equivalents	$ 280,531	$ 267,738	$ 314,416	$ 293,098	$ 229,914
Total assets	$ 670,064	$ 636,986	$ 598,557	$ 522,011	$ 338,288
Long-term debt	$ 138,863	$ 129,429	$ 125,886	$ 122,627	$
Total stockholders equity	$ 243,746	$ 237,722	$ 182,585	$ 160,521	$ 121,253

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ITEM 7 *Management s Discussion and Analysis of Financial Condition and Results of Operations*

The following discussion should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this annual report on Form 10-K.

Forward-Looking Statements

In addition to historical information, this annual report on Form 10-K contains forward-looking statements as defined under federal securities laws. Such statements, including statements about our plans, objectives, expectations, assumptions or future events, involve risks and uncertainties. These statements involve estimates, assumptions, known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from any future results, performances or achievements expressed or implied by the forward-looking statements. Typically, forward-looking statements can be identified by terminology such as anticipate, estimate, plan, project, continuing, ongoing, expect, believe, intend, may, will, should, could, and similar expressions. The important factors that could cause actual results to differ materially from those indicated by such forward-looking statements include but are not limited to the effect of governmental regulation; changes in insurance regulations; the frequency and extent of claims; uncertainties inherent in reserve estimates; catastrophic events; changes in the demand for, pricing of, availability of or collectability of reinsurance; restrictions on our ability to change premium rates; increased rate pressure on premiums; and other risks and uncertainties and other factors listed under Item 1A - Risk Factors and elsewhere in this annual report on Form 10-K and in our other Securities and Exchange Commission filings.

OVERVIEW

General

HCI Group, Inc. is a Florida-based company which through its subsidiaries is engaged in a variety of business activities, including property and casualty insurance, reinsurance, real estate and information technology. Its principal business is property and casualty insurance.

Based on our organizational structure, revenue sources, and evaluation of financial and operating performances by management, we manage four operating divisions under one reporting segment, which includes the following operations:

a) Insurance Operations

Property and casualty insurance

Reinsurance

b) Other Operations

Real estate

Information technology

We began insurance operations in 2007 by participating in a take-out program which is a legislatively mandated program designed to encourage private companies to assume policies from Citizens, a Florida state sponsored insurance carrier. Our growth since inception has resulted primarily from a series of policy assumptions from Citizens and policies assumed from one Florida insurance company. This growth track was beneficial to us in terms of reduced policy acquisition costs and, depending on the timing of the transaction, temporarily lower reinsurance costs.

Our general operating and growth strategies are to continually optimize our existing book of insurance business, manage our costs and expenses, diversify our business operations, develop and deploy new technologies to streamline operational processes, and maintain a strong balance sheet so we can quickly pursue accretive opportunities when they arise.

Recent Developments

On January 16, 2017, our Board of Directors declared a quarterly dividend of $0.35 per common share. The dividends will be paid March 17, 2017 to stockholders of record on February 17, 2017.

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RESULTS OF OPERATIONS

Comparison of the Year Ended December 31, 2016 with the Year Ended December 31, 2015

Our results of operations for the year ended December 31, 2016 reflect income available to common stockholders of $29,021,000, or $2.92 earnings per diluted common share, compared with income available to common stockholders of $65,861,000, or $5.90 earnings per diluted common share, for the year ended December 31, 2015. The year over year decline in our income available to stockholders was primarily attributable to a $44,442,000 decrease in gross premiums earned, and a $37,443,000 increase in losses and loss adjustment expenses. These factors contributed to a $59,336,000 decrease in pre-tax income and, as a result, our income tax expense decreased $22,496,000 year over year.

Revenue

Gross Premiums Earned for the years ended December 31, 2016 and 2015 were approximately $378,678,000 and $423,120,000, respectively. The decrease in 2016 was primarily attributable to policy attrition as well as a rate decrease effective on new and renewal policies beginning in January 2016.

Premiums Ceded for the years ended December 31, 2016 and 2015 were approximately $135,051,000 and $140,614,000, respectively, representing 35.7% and 33.2%, respectively, of gross premiums earned. The $5,563,000 decrease was primarily attributable to the lower costs of our 2016/17 reinsurance program, which began June 1, 2016, as compared with the costs of the 2015/16 program that began June 1, 2015. In addition, the reduction to our ceded premiums attributable to retrospective provisions under certain reinsurance contracts for calendar year 2016 was lower by approximately $5,645,000 as compared with calendar year 2015.

Our reinsurance program for 2016/17 provides coverage, which according to catastrophe models approved by the FLOIR, is sufficient to cover the probable maximum loss resulting from a 1 in 165 year event. Our reinsurance program for 2015/16 provided coverage for a probable maximum loss resulting from a 1 in 260 year event. As a result of our program and pricing changes, we expect our reinsurance costs for the 2016/17 program year to be approximately $48,000,000 below the cost for 2015/16.

Our premiums ceded represent amounts paid to reinsurers to cover losses from catastrophes that exceed the retention levels defined by our catastrophe excess of loss reinsurance treaties and to assume a proportional share of losses defined in one quota share arrangement, which was cancelled effective May 31, 2016. For the years ended December 31, 2016 and 2015, premiums ceded reflect net reductions of $12,677,000 and $18,322,000, respectively, related to provisions under certain multi-year catastrophe reinsurance contracts. See Economic Impact of Reinsurance Contracts with Retrospective Provisions under Critical Accounting Policies and Estimates. The rates we pay for reinsurance are based primarily on policy exposures reflected in gross premiums earned.

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Net Premiums Written for the years ended December 31, 2016 and 2015 totaled approximately $232,140,000 and $255,724,000, respectively. Net premiums written represent the premiums charged on policies issued during a fiscal period less any applicable reinsurance costs. We had approximately 150,000 policies in force at December 31, 2016 as compared with approximately 160,000 policies in force at December 31, 2015.

Net Premiums Earned for the years ended December 31, 2016 and 2015 were approximately $243,627,000 and $282,506,000, respectively, and reflect the gross premiums earned less reinsurance costs as described above.

The following is a reconciliation of our total Net Premiums Written to Net Premiums Earned for the years ended December 31, 2016 and 2015 (amounts in thousands):

	Years Ended December 31,	
	2016	**2015**
Net Premiums Written	$ 232,140	$ 255,724
Decrease in Unearned Premiums*	11,487	26,782
Net Premiums Earned	$ 243,627	$ 282,506

* Unearned premiums are impacted by the timing and size of any takeout completed during the year net of attrition.

Net Investment Income for the years ended December 31, 2016 and 2015 was approximately $9,087,000 and $3,978,000, respectively. The increase in 2016 was primarily due to $1,207,000 of income from limited partnership investments in 2016 versus losses of $3,244,000 in 2015. See Note 4 Investments under *Net Investment Income* to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Net Realized Investment Gains for the year ended December 31, 2016 were approximately $2,601,000 as compared with $608,000 of net realized investment losses for the year ended December 31, 2015. The losses in 2015 resulted primarily from sales intended to rebalance the mix of our investment portfolio to meet our long-term investment goals and strategies.

Net Other-Than-Temporary Impairment Losses for the years ended December 31, 2016 and 2015 were approximately $2,482,000 and $4,681,000, respectively. During 2016, we recognized impairment losses specific to four fixed-maturity securities, three of which were subject to credit loss impairment, and 17 equity securities. Three fixed-maturity securities were subject to credit related loss impairments resulting from our analysis of their expected cash flows. Seventeen equity securities were impaired because each of them had been in an unrealized loss position for a length of time with no near term prospect for recovery.

Policy Fee Income for the years ended December 31, 2016 and 2015 was approximately $3,914,000 and $3,496,000, respectively. Beginning in March 2015, we have used actual policy cancellations in our calculation of policy fee income whereas estimated attrition rates were used in this calculation prior to March 2015. In addition, the unearned portion of nonrefundable policy fee income was fully recognized for policies that were cancelled during 2016. As a result, our 2016 policy fee income was higher than in 2015 despite the decline in gross premiums earned.

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Expenses

Our *Losses and Loss Adjustment Expenses* amounted to approximately $124,667,000 and $87,224,000, respectively, for the years ended December 31, 2016 and 2015. Our 2016 losses and loss adjustment expenses were impacted by weather-related events in both years and two hurricanes, Hermine and Matthew, in 2016. Hurricane Matthew accounted for approximately $21,000,000 of our 2016 losses. In addition, trends involving assignment of insurance benefits and related litigation has caused us to continue strengthening our loss reserves. See Reserves for Losses and Loss Adjustment Expenses under Critical Accounting Policies and Estimates.

Policy Acquisition and Other Underwriting Expenses for the years ended December 31, 2016 and 2015 of approximately $42,642,000 and $41,984,000, respectively, primarily reflect commissions and premium taxes related to the policies that have renewed.

Salaries and Wages for the years ended December 31, 2016 and 2015 were approximately $19,037,000 and $20,140,000, respectively. The $1,103,000 decrease in 2016 was primarily attributable to a decrease in discretionary incentive pay in 2016. The level of discretionary incentive pay in 2016 was influenced in large part by our financial results for the year, which were negatively impacted by Hurricane Matthew in the fourth quarter. As of December 31, 2016, we had 243 employees located at our offices in Florida compared with 220 employees as of December 31, 2015. We also had 80 employees located in Noida, India at December 31, 2016 versus 84 at December 31, 2015.

Impairment loss for the year ended December 31, 2016 was approximately $388,000. The loss resulted from the write-down of lease intangibles and other assets associated with the unexpected closure of one tenant s business at one of our retail shopping centers.

Income Tax Expense for the years ended December 31, 2016 and 2015 was approximately $17,835,000 and $40,331,000, respectively, for state, federal and foreign income taxes resulting in an effective tax rate of 38.1% for 2016 and 38.0% for 2015.

Ratios:

The loss ratio applicable to the year ended December 31, 2016 (losses and loss adjustment expenses incurred related to net premiums earned) was 51.2% compared with 30.9% for the year ended December 31, 2015. The increase was primarily attributable to losses in October 2016 from Hurricane Matthew as well as reserve strengthening throughout 2016.

The expense ratio applicable to the year ended December 31, 2016 (defined as underwriting expenses, salaries and wages, interest and other operating expenses related to net premiums earned) was 38.1% compared with 32.7% for the year ended December 31, 2015. The increase in our expense ratio was primarily attributable to the decrease in 2016 net premiums earned.

The combined ratio (total of all expenses in relation to net premiums earned) is the measure of overall underwriting profitability before other income. Our combined ratio for the year ended December 31, 2016 was 89.3% compared with 63.6% for the year ended December 31, 2015. Our combined ratio was negatively impacted by increased expenses for losses and loss adjustment expenses and a reduction in 2016 net premiums earned.

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Due to the impact our reinsurance costs have on net premiums earned from period to period, our management believes the combined ratio measured to gross premiums earned is more relevant in assessing overall performance. The combined ratio to gross premiums earned for the year ended December 31, 2016 was 57.5% compared with 42.5% for the year ended December 31, 2015. The increase in 2016 was primarily attributable to the factors described above.

Comparison of the Year Ended December 31, 2015 with the Year Ended December 31, 2014

Our results of operations for the year ended December 31, 2015 reflect income available to common stockholders of $65,861,000, or $5.90 earnings per diluted common share, compared with income available to common stockholders of $62,668,000, or $5.36 earnings per diluted common share, for the year ended December 31, 2014. The year over year improvement in our income available to stockholders was primarily attributable to a $57,632,000 increase in gross premiums earned, resulting from assumptions of homeowners multi-peril policies and wind-only policies from Citizens in December 2014 and February 2015. The increase in 2015 was negatively impacted by increased reinsurance costs as a percentage of gross earned premium, $3,245,000 of net realized losses related to limited partnership investments, $4,681,000 of other-than-temporary impairment losses during 2015, $608,000 of net realized losses from investment sales, increased policy acquisition costs, and increased losses and loss adjustment expenses attributable to increased premiums and the settlement and further development of older claims which were recently reported to us.

Revenue

Gross Premiums Earned for the years ended December 31, 2015 and 2014 were approximately $423,120,000 and $365,488,000, respectively. The increase in 2015 was primarily attributable to the assumption from Citizens of approximately 6,000 homeowners multi-peril policies and approximately 30,000 wind-only policies in December 2014 and the assumption of 4,000 primarily homeowners multi-peril policies in February 2015. For the year ended December 31, 2015, gross premiums earned included approximately $93,296,000 and $8,411,000 from the December 2014 and February 2015 assumptions and the renewals of those assumed policies, respectively.

Premiums Ceded for the years ended December 31, 2015 and 2014 were approximately $140,614,000 and $113,423,000, respectively, representing 33.2% and 31.0%, respectively, of gross premiums earned. The $27,191,000 increase in net ceded premiums is attributable to higher rates implemented by the Florida Hurricane Catastrophe Fund and an overall increase in units of reinsurance purchased for the 2015/16 reinsurance program. Our reinsurance program for 2015/16 provides coverage, which according to catastrophe models approved by the FLOIR, is sufficient to cover the probable maximum loss resulting from a 1 in 260 year event. Our reinsurance program for 2014/15 provided coverage for a probable maximum loss resulting from a 1 in 182 year event. In addition, our reduction to ceded premiums attributable to retrospective provisions under certain reinsurance contracts was lower as compared with the corresponding period in 2014.

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Our premiums ceded represent amounts paid to reinsurers to cover losses from catastrophes that exceed the retention levels defined by our catastrophe excess of loss reinsurance treaties and to assume a proportional share of losses defined in one quota share arrangement. For the years ended December 31, 2015 and 2014, premiums ceded reflect net reductions of $18,322,000 and $23,543,000, respectively, related to provisions under certain reinsurance contracts. The rates we pay for reinsurance are based primarily on policy exposures reflected in gross premiums earned.

Net Premiums Written for the years ended December 31, 2015 and 2014 totaled approximately $255,724,000 and $294,230,000, respectively. The decrease in 2015 resulted from an increase of approximately $27,191,000 in premiums ceded during the year combined with a decrease of approximately $11,314,000 in gross premiums written. We had approximately 160,000 policies in force at December 31, 2015 compared to approximately 180,000 policies in force at December 31, 2014.

Net Premiums Earned for the years ended December 31, 2015 and 2014 were approximately $282,506,000 and $252,065,000, respectively, and reflect the gross premiums earned less reinsurance costs as described above.

The following is a reconciliation of our total Net Premiums Written to Net Premiums Earned for the years ended December 31, 2015 and 2014 (amounts in thousands):

	Years Ended December 31,	
	2015	**2014**
Net Premiums Written	$ 255,724	$ 294,230
Decrease (Increase) in Unearned Premiums*	26,782	(42,165)
Net Premiums Earned	$ 282,506	$ 252,065

* Unearned premiums are impacted by the timing and size of any takeout completed during the year net of attrition.

Net Investment Income for the years ended December 31, 2015 and 2014 was approximately $3,978,000 and $4,888,000, respectively. The decrease in 2015 is primarily due to $3,245,000 of net losses related to our limited partnership investments. See Note 4 Investments under *Net Investment Income* to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Net Realized Investment Losses for the year ended December 31, 2015 were approximately $608,000 as compared with $4,735,000 of net realized investment gains for the year ended December 31, 2014. The losses in 2015 primarily result from sales intended to rebalance the mix of our investment portfolio to meet our long-term investment goals and strategies.

Net Other-Than-Temporary Impairment Losses for the years ended December 31, 2015 and 2014 were approximately $4,681,000 and $107,000, respectively. During 2015, we recognized impairment losses specific to two fixed-maturity securities and 17 equity securities. Two fixed-maturity securities were subject to credit related loss impairments resulting from our analysis of their expected cash flows. Seventeen equity securities were impaired because each of them had been in an unrealized loss position for a length of time with no near term prospect for recovery.

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Policy Fee Income for the years ended December 31, 2015 and 2014 was approximately $3,496,000 and $2,820,000, respectively. The increase in 2015 is directly attributable to an increase in policy renewals.

Expenses

Our *Losses and Loss Adjustment Expenses* amounted to approximately $87,224,000 and $79,468,000, respectively, for the years ended December 31, 2015 and 2014. Our 2015 losses and loss adjustment expenses were impacted by an increase in the number of policies in force throughout 2015 as compared to 2014 as well as by significant weather-related events during 2015, which contributed to an increase in the volume of reported claims and losses incurred when compared to 2014. We also experienced unfavorable development during 2015 attributable to the settlement and further development of older claims, primarily those related to 2012 and 2014 loss dates. This development was considered in establishing our estimate for unpaid losses and loss adjustment expenses as of December 31, 2015. See Reserves for Losses and Loss Adjustment Expenses under Critical Accounting Policies and Estimates.

Policy Acquisition and Other Underwriting Expenses for the years ended December 31, 2015 and 2014 of approximately $41,984,000 and $37,952,000, respectively, primarily reflect brokerage fees and the amortization of deferred acquisition costs related to commissions payable to agents for production and renewal of policies and premium taxes. The increase in 2015 is primarily attributable to commissions and premium taxes related to the policies assumed from Citizens that have renewed and are included in 2015 premiums.

Salaries and Wages for the years ended December 31, 2015 and 2014 were approximately $20,140,000 and $16,483,000, respectively. The $3,657,000 increase in 2015 was primarily attributable to an increase in salaries due to an increase in employee headcount as well as merit increases during 2015. As of December 31, 2015, we had 220 employees located at our offices in Florida compared with 200 employees as of December 31, 2014. We also had 84 employees located in Noida, India at December 31, 2015 versus 79 at December 31, 2014.

Other Operating Expenses for the years ended December 31, 2015 and 2014 were approximately $19,658,000 and $20,790,000, respectively. The $1,132,000 decrease in 2015 was primarily attributable to a $2,411,000 decrease in stock-based compensation partially offset by an increase in other administrative expenses.

Income Tax Expense for the years ended December 31, 2015 and 2014 was approximately $40,331,000 and $38,298,000, respectively, for state, federal and foreign income taxes resulting in an effective tax rate of 38.0% for 2015 and 37.9% for 2014.

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Ratios:

The loss ratio applicable to the year ended December 31, 2015 was 30.9% compared with 31.5% for the year ended December 31, 2014. Losses on our wind-only policies, which we assumed from Citizens in December 2014, were minimal. This benefit, net of unfavorable development related to losses on our non-wind policies, contributed to this slight year over year improvement.

The expense ratio applicable to the year ended December 31, 2015 was 32.7% compared with 34.0% for the year ended December 31, 2014. The decrease in our expense ratio is primarily attributable to the increase in net premiums earned.

Our combined ratio for the year ended December 31, 2015 was 63.6% compared with 65.5% for the year ended December 31, 2014. Our combined ratio was positively impacted by an increase in net premiums earned.

The combined ratio to gross premiums earned for the year ended December 31, 2015 was 42.5% compared with 45.2% for the year ended December 31, 2014. The decrease in 2015 was primarily attributable to the factors described above.

Seasonality of Our Business

Our insurance business is seasonal as hurricanes and tropical storms affecting Florida typically occur during the period from June 1 through November 30 each year. Also, with our reinsurance treaty year typically effective on June 1 each year, any variation in the cost of our reinsurance, whether due to changes in reinsurance rates or changes in the total insured value of our policy base, will occur and be reflected in our financial results beginning June 1 each year.

LIQUIDITY AND CAPITAL RESOURCES

Throughout our history, our liquidity requirements have been met through issuances of our common and preferred stock, debt offerings and funds from operations. We expect our future liquidity requirements will be met by funds from operations, primarily the cash received by insurance subsidiaries from premiums written and investment income. We may consider raising additional capital through debt and equity offerings to support our growth and future investment opportunities.

Our insurance subsidiaries require liquidity and adequate capital to meet ongoing obligations to policyholders and claimants and to fund operating expenses. In addition, we attempt to maintain adequate levels of liquidity and surplus to manage any differences between the duration of our liabilities and invested assets. In the insurance industry, cash collected for premiums from policies written is invested, interest and dividends are earned thereon, and losses and loss adjustment expenses are paid out over a period of years. This period of time varies by the circumstances surrounding each claim. Substantially all of our losses and loss adjustment expenses, excluding litigated claims, are fully settled and paid within approximately 100 days of the claim receipt date. Additional cash outflow occurs through payments of underwriting costs such as commissions, taxes, payroll, and general overhead expenses.

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We believe that we maintain sufficient liquidity to pay claims and expenses, as well as to satisfy commitments in the event of unforeseen events such as reinsurer insolvencies, inadequate premium rates, or reserve deficiencies. We maintain a comprehensive reinsurance program at levels management considers adequate to diversify risk and safeguard our financial position.

In the future, we anticipate our primary use of funds will be to pay claims, reinsurance premiums, interest, and dividends and to fund operating expenses. In addition, we intend to continue investing in real estate to maximize returns and diversify our sources of income, pursue acquisition opportunities, or consider other strategic opportunities.

Senior Notes and Promissory Notes

The following table summarizes our principal and interest payment obligations for long-term debt at December 31, 2016:

	Maturity Date	**Interest Payment Due Date**
3.875% Convertible Senior Notes	March 2019	March 15 and September 15
8% Senior Notes	January 2020	January 30, April 30, July 30, and October 30
4% Promissory Note	Through February 2031	1st day of each month
3.75% Callable Promissory Note	Through September 2036	1st day of each month

See Note 13 Long-Term Debt to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Share Repurchase Plan

In December 2015, our Board of Directors approved a one-year plan to repurchase up to $20,000,000 of common shares under which we may purchase shares of common stock in open market purchases, block transactions and privately negotiated transactions in accordance with applicable federal securities laws. In December 2016, our Board of Directors approved a similar plan for 2017 to repurchase up to $20,000,000 of common shares. The approved amounts in each year exclude brokerage fees. See Note 19 Stockholders Equity to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Limited Partnership Investments

Our limited partnership investments consist of four private equity funds managed by their general partners. Three of these funds have unexpired capital commitments which are callable at the discretion of the fund s general partner for funding new investments or expenses of the fund. At December 31, 2016, there was an aggregate unfunded capital balance of $13,554,000. In December 2016, we provided notice of our intent to withdraw from one underperforming fund effective February 15, 2017. The withdrawal will have no significant impact on our results of operations. Our commitment with respect to that fund was fully funded prior to 2016. See *Limited Partnership Investments* under Note 4 Investment to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

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Real Estate Development in Progress

We currently have development projects through various limited liability companies. Although we have no outstanding commitment to fund any of the existing projects and we expect to finance existing and future development projects with cash from real estate operations and through property financings, we may be required to make additional capital contributions to maintain and complete these projects.

Revolving Credit Facility

At December 31, 2016, we had an outstanding loan balance of $9,463,000 with respect to one revolving credit facility. See Note 12 Revolving Credit Facility to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K.

Sources and Uses of Cash

Our cash flows from operating, investing and financing activities for the years ended December 31, 2016, 2015 and 2014 are summarized below.

Cash Flows for the Year ended December 31, 2016

Net cash provided by operating activities for the year ended December 31, 2016 was approximately $87,975,000, which consisted primarily of cash received from net premiums written less cash disbursed for operating expenses, losses and loss adjustment expenses and interest payments. Net cash used in investing activities of $49,028,000 was primarily due to the purchases of available-for-sale securities of $107,964,000, $12,056,000 of net cash used in acquiring one business, and the limited partnership investments of $4,670,000, offset by the proceeds from sales of available-for-sale securities of $63,581,000 and the $10,200,000 proceeds from the ADC Arrangement. Net cash used in financing activities totaled $26,157,000, which was primarily due to $11,347,000 used in the repurchases of our convertible senior notes, $20,026,000 used in our share repurchase plan and $11,691,000 of net cash dividend payments, offset by $18,200,000 in aggregate proceeds from the issuance of two promissory notes.

Cash Flows for the Year ended December 31, 2015

Net cash provided by operating activities for the year ended December 31, 2015 was approximately $45,270,000, which consisted primarily of cash received from net premiums written less cash disbursed for operating expenses, losses and loss adjustment expenses and interest payments. Net cash used in investing activities of $80,362,000 was primarily due to the funding of the limited partnership investments of $24,636,000, the purchases of available-for-sale securities of $131,379,000, the funding of the ADC Arrangement of $6,968,000, and $4,871,000 used to purchase real estate investments, decreased by redemptions and repayments of fixed-maturity securities of $9,344,000, and the proceeds from sales of available-for-sale securities of $79,406,000. Net cash used in financing activities totaled $11,525,000, which was primarily due to $1,610,000 used in our share repurchase plan and $11,681,000 of net cash dividend payments, offset by $2,295,000 of tax benefits on stock-based compensation.

Cash Flows for the Year ended December 31, 2014

Net cash provided by operating activities for the year ended December 31, 2014 totaled $88,729,000, which consisted primarily of cash received from net written premiums less cash disbursed for operating expenses, losses and loss adjustment expenses and interest payments. Net cash used in investing activities of $18,652,000 was primarily due to the purchases of available-for-sale securities of $127,622,000, the funding of the ADC Arrangement of $2,803,000 and the $4,500,000 cash contribution to a joint venture, offset by redemptions and repayments of fixed-maturity securities of $4,603,000, and the proceeds from sales of available-for-sale securities of $115,175,000. Net cash used in financing activities totaled $48,730,000, which was primarily due to $38,354,000 used in our share repurchase plan and $11,670,000 of net cash dividend payments.

Investments

The main objective of our investment policy is to maximize our after-tax investment income with a reasonable level of risk given the current financial market. Our excess cash is invested primarily in money market accounts and available-for-sale investments.

At December 31, 2016, we had $219,283,000 of available-for-sale investments, which are carried at fair value. Changes in the general interest rate environment affect the returns available on new fixed-maturity investments. While a rising interest rate environment enhances the returns available on new investments, it reduces the market value of existing fixed-maturity investments and thus the availability of gains on disposition. A decline in interest rates reduces the returns available on new fixed-maturity investments but increases the market value of existing fixed-maturity investments, creating the opportunity for realized investment gains on disposition.

With the exception of large national banks, it is our current policy not to maintain cash deposits of more than an aggregate of $10,000,000 in any one bank at any time. From time to time, we may have in excess of $10,000,000 of cash designated for investment and on deposit at a single national brokerage firm. In the future, we may alter our investment policy as to investments in federal, state and municipal obligations, preferred and common equity securities and real estate mortgages, as permitted by applicable law, including insurance regulations.

OFF-BALANCE SHEET ARRANGEMENTS

As of December 31, 2016, we had unexpired capital commitments for three of the four limited partnership in which we hold interests. Such commitments are not recognized in the financial statements but are required to be disclosed in the notes to the financial statements. See Note 22 Commitments and Contingencies to our consolidated financial statements under Item 8 of this Annual Report on Form 10-K and *Contractual Obligations and Commitments* below for additional information.

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CONTRACTUAL OBLIGATIONS AND COMMITMENTS

The following table summarizes our material contractual obligations and commitments as of December 31, 2016 (amounts in thousands):

		Payment Due by Period			
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Operating lease (1)	$ 734	191	258	285	
Service agreement (1)	119	22	46	51	
Reinsurance contracts (2)	38,800	19,400	19,400		
Variable rate debt (3)	9,463	9,463			
Unfunded capital commitment (4)	13,554	13,554			
Long-term debt obligations (5)	174,898	8,668	105,331	43,969	16,930
Total	$ 237,568	51,298	125,035	44,305	16,930

(1) Represents the lease for office space in Miami, Florida and the lease and maintenance service agreement for office space in Noida, India. Liabilities related to our India operations were converted from India Rupee to U.S. dollars using the January 3, 2017 exchange rate, the first available rate subsequent to December 31, 2016, which was a non-business day.
(2) Represents the minimum payment of reinsurance premiums under multi-year reinsurance contracts.
(3) Represents the outstanding balance drawn from our revolving credit facility.
(4) Represents the unfunded balance of capital commitments under the subscription agreements related to three limited partnerships in which we hold interests.
(5) Amounts represent principal and interest payments over the life of the convertible notes due March 15, 2019, the senior notes due January 30, 2020, one promissory note due through February 1, 2031 and one promissory note due through September 1, 2036.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

We have prepared our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). The preparation of these consolidated financial statements requires us to make estimates and judgments to develop amounts reflected and disclosed in our financial statements. Material estimates that are particularly susceptible to significant change in the near term are related to our losses and loss adjustment expenses, which include amounts estimated for claims incurred but not yet reported. We base our estimates on various assumptions and actuarial data we believe to be reasonable under the circumstances. Actual results may differ materially from these estimates.

We believe our accounting policies specific to losses and loss adjustment expenses, reinsurance with retrospective provisions, deferred income taxes, and stock-based compensation expense involve our most significant judgments and estimates material to our consolidated financial statements.

Reserves for Losses and Loss Adjustment Expenses. We establish reserves for the estimated total unpaid costs of losses including loss adjustment expenses (LAE). Loss and LAE reserves reflect management s best estimate of the total cost of (i) claims that have been incurred,

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but not yet paid in full, and (ii) claims that have been incurred but not yet reported to us (IBNR). Reserves established by us represent an estimate of the outcome of future events and, as such, cannot be considered an exact calculation of our liability. Rather, loss reserves represent, we believe, management s best estimate of our company s liability based on the application of actuarial techniques and other projection methodologies and taking into consideration other facts and circumstances known at the balance sheet date. The process of establishing loss reserves is complex and inherently imprecise, as it involves using judgment that is affected by many variables such as past loss experience, current claim trends and the prevailing social changes in our claims adjusting process, economic and legal environments. The impact of both internal and external variables on ultimate losses and LAE costs is difficult to estimate. Our exposure is impacted by both the risk characteristics of the physical locations where we write policies, such as hurricane and tropical storm-related risks, as well as risks associated with varying social, judicial and legislative characteristics in the locations in which we have exposure. In determining loss reserves, we give careful consideration to all available data and actuarial analyses.

Reserves represent estimates of the ultimate unpaid cost of all losses incurred, including losses for claims that have not yet been reported to our insurance companies. The amount of loss reserves for reported claims consist of case reserves established by our claims department (based on a case-by-case evaluation of the kind of risk involved, knowledge of the circumstances surrounding each claim and the insurance policy provisions relating to the type of loss) and bulk reserves for additional growth on carried case reserves on known claims established by senior management (based on historical patterns of development on aggregate claims grouped by loss date). The amounts of reserves for unreported claims and LAE (incurred but not reported claims, or IBNR) are determined using our historical information for each line of business adjusted to reflect current conditions. Inflation is ordinarily implicitly provided for in the reserving function through analysis of costs, trends and reviews of historical reserving results over multiple years.

Reserves are closely monitored and are recalculated periodically using the most recent information on reported claims and a variety of actuarial techniques. Specifically, claims management personnel complete weekly and ongoing reviews of existing case reserves, new claims, changes to existing case reserves, and paid losses with respect to the current and prior years. As we continue to expand historical data regarding paid and incurred losses, we use this data to develop expected ultimate loss and loss adjustment expense ratios. We then apply these expected loss and loss adjustment expense ratios to earned premium to derive a reserve level for each line of business. In connection with the determination of these reserves, we will also consider other specific factors such as recent weather-related losses, trends in historical reported and paid losses, and litigation and judicial trends regarding liability. Most of our business was gained through policy acquisitions and assumptions. Therefore, we use the loss ratio method, among other methods, to project an ultimate loss expectation, and then the related loss history must be regularly evaluated and loss expectations updated, with the possibility of variability from the initial estimate of ultimate losses.

When a claim is reported to us, our claims personnel establish a case reserve for the estimated amount of the ultimate amount payable to settle the claim. This estimate reflects an informed judgment based upon general insurance reserving practices and on the experience and knowledge of the claims adjuster. The individual estimating the reserve considers the nature and

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value of the specific claim, the severity of injury or damage, location, and the policy provisions relating to the type of loss. Case reserves are adjusted by us as more information becomes available. It is our policy to settle each claim as expeditiously as possible.

We maintain IBNR reserves to provide for claims that have been incurred but have not been reported and subsequent development on reported claims. The IBNR reserve is determined by estimating our insurance company s ultimate net liability for both reported and unreported claims and then subtracting the case reserves and payments made to date for reported claims.

Loss Reserve Estimation Methods. We apply the following general methods in projecting reserves for losses and LAE:

Reported loss development;

Paid loss development;

Reported Bornhuetter-Ferguson method;

Paid Bornhuetter-Ferguson method;

Loss ratio method; and

Frequency-Severity method.

Selected reserves are based on a review of the indications from these methods as well as other considerations such as emergence since the most recent evaluation and number of open claims for a given accident period.

Description of Ultimate Loss Estimation Methods. The reported loss development method relies on the assumption that, at any given state of maturity, ultimate losses can be reasonably predicted by multiplying cumulative reported losses (paid losses plus case reserves) by a cumulative development factor derived from development patterns observed in the historical reported data. The validity of the results of this method depends on the stability of claim reporting and settlement rates, as well as the consistency of case reserve levels. Case reserves do not have to be adequately stated for this method to be effective; they only need to have a fairly consistent level of adequacy for the historical experience that is considered. In order to derive loss development patterns that are predictive for our business, we compile and review loss development triangles of our experience on an accident quarter basis, and select loss development factors based on indications from this analysis of our data. We also consider industry data found in SNL Financial Property/Casualty Insurance as a reasonability measure for these selected development patterns.

The paid loss development method is mechanically identical to the reported loss development method described above, but applied to loss payments only. The paid method does not rely on case reserves or claim reporting patterns in making projections.

The validity of the results from using a loss development approach can be affected by many conditions, such as internal claim department processing changes, a shift between single and multiple claim payments, legal changes, or variations in our mix of business from year to year. Also, since the percentage of losses paid for immature accident quarters is often low, development factors for these maturities can be volatile. A small variation in the number of claims paid can

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have a leveraging effect that can lead to significant distortions in estimated ultimate losses for these highly leveraged accident quarters. Therefore, ultimate values for immature accident quarters are often based on alternative estimation techniques than more mature accident quarters.

The loss ratio method used by us relies on the assumption that remaining unreported losses are a function of the total expected losses rather than a function of currently reported losses. The expected loss ratio is multiplied by earned premium to produce ultimate losses. Reported incurred losses are then subtracted from this estimate to produce expected unreported losses.

The loss ratio method is most useful as an alternative to other models for immature loss years. For these immature years, the amounts reported or paid may be small and unstable, and therefore, not fully predictive of future development. Therefore, future development is assumed to follow an expected pattern that is supported by more stable historical data or by emerging trends. This method is also useful when variations in reporting or payment patterns distort the historical development of losses.

The paid and reported Bornhuetter-Ferguson methods are a weighting of the loss ratio method and the corresponding development method. Outstanding reserves or IBNR reserves are derived by applying the loss ratio estimate to the estimated unpaid or unreported percent of losses based on the development patterns from the development methods.

Finally, we employ the frequency/severity method for exposures that do not tend to follow historical payment and reported patterns, such as catastrophes. For such exposures, we estimate future development of reported claims and average severities on IBNR claims. We combine this estimate with our open claims in order to derive an estimate of expected unreported losses. Paid losses are added to this estimate in order to derive an estimate of ultimate losses. This method is based on the assumption that future unreported claims and the average severity of open claims and unreported claims can be reasonably estimated from the experience available.

While the property and casualty industry has incurred substantial aggregate losses from claims related to asbestos-related illnesses, environmental remediation, product and mold, and other uncertain or environmental exposures, we have not experienced significant losses from these types of claims. We have experienced material losses associated with sinkholes in past years, but the materiality of this hazard has decreased significantly since the passing of Florida Senate Bill 408 in 2011. We continue to segregate this data in our derivation of estimated required reserves. While the losses we have experienced from exposures to catastrophes have not historically been material, we have experienced significant losses related to recent catastrophes. These losses have followed materially different development patterns than the balance of our experience. To address this situation, we separate this exposure from the remainder of the business and derive reserves specific to each catastrophe event. Total reserves are determined by adding the reserves related to each line of business.

Currently, our estimated ultimate liability is calculated monthly using the principles and procedures described above, which are applied to the lines of business written. However, because the establishment of loss reserves is an inherently uncertain process, we cannot be certain that ultimate losses will not exceed the established loss reserves and have a material, adverse effect on

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our results of operations and financial condition. Changes in estimates, or differences between estimates and amounts ultimately paid, are reflected in the operating results of the period during which such adjustments are made.

Our reported results, financial position and liquidity would be affected by likely changes in key assumptions that determine our net loss reserves. Management does not believe that any reasonably likely changes in the frequency of claims would affect our loss reserves. However, management believes that a reasonably likely increase or decrease in the severity of claims could impact our net loss reserves. The table below summarizes the effect on net loss reserves and equity in the event of reasonably likely changes in the severity of claims considered in establishing loss and loss adjustment expense reserves. The range of reasonably likely changes in the severity of our claims was established based on a review of changes in loss year development and applied to loss reserves as a whole. The selected range of changes does not indicate what could be the potential best or worst case or likely scenarios:

Year Ended December 31, 2016		
Change in Reserves	Reserves	Percentage change in equity, net of tax
-20.0%	56,394	3.55%
-15.0%	59,918	2.66%
-10.0%	63,443	1.77%
-5.0%	66,967	0.89%
Base	**70,492**	
5.0%	74,017	- 0.89%
10.0%	77,541	- 1.77%
15.0%	81,066	- 2.66%
20.0%	84,590	- 3.55%

Economic Impact of Reinsurance Contracts with Retrospective Provisions. Certain of our reinsurance contracts include retrospective provisions that adjust premiums, increase the amount of future coverage, or result in profit commissions in the event losses are minimal or zero. In accordance with U.S. GAAP, we will recognize an asset in the period in which the absence of loss experience gives rise to an increase in future coverage or obligates the reinsurer to pay cash or other consideration under the contract. In the event that a loss arises, we will derecognize such asset in the period in which a loss arises. Such adjustments to the asset, which accrue throughout the contract term, will negatively impact our operating results when a catastrophic loss event occurs during the contract term. Effective June 1, 2016, retrospective provisions include premium adjustments only.

For the years ended December 31, 2016 and 2015, we accrued benefits of $13,610,000 and $21,692,000, respectively. For the year ended December 31, 2016, we recognized net ceded premiums of $933,000, representing amortization of $1,219,000 of previously deferred reinsurance costs for increased coverage offset by $2,152,000 of ceded premiums deferred for the period. For the year ended December 31, 2015, we recognized net ceded premiums of $3,370,000, representing amortization of previously deferred reinsurance costs for increased coverage decreased by an increase of ceded premiums deferred for the period. For the years ended December 31, 2016 and 2015, net reductions in ceded premiums totaled $12,677,000 and $18,322,000, respectively.

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In June 2016, we received cash totaling $37,800,000 in connection with the benefits accrued under two retrospective reinsurance contracts that were terminated effective May 31, 2016. In September 2016, we received the final cash payment of $5,716,000 under the terms of the remaining retrospective reinsurance contract which terminated May 31, 2016. As of December 31, 2016, we had $5,810,000 of accrued benefits and $2,152,000 of ceded premiums deferred, amounts that would be charged to earnings in the event we experience a catastrophic loss that exceeds the coverage limits provided under such agreements and in the period that the increased coverage is applicable. In July 2015, the Company received $14,100,000 under the terms of one of the retrospective reinsurance contracts, which terminated May 31, 2015. As of December 31, 2015, we had $35,716,000 of accrued benefits and $3,085,000 of ceded premiums deferred related to these agreements.

We believe the credit risk associated with the collectability of these accrued benefits is minimal based on available information about the individual reinsurer s financial position.

Income Taxes. We account for income taxes in accordance with U.S. GAAP, resulting in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. We determine deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur. Valuation allowances are provided against assets that are not likely to be realized, if any. We have elected to classify the related interest and penalties, if any, as income tax expense as permitted by current accounting standards.

Stock-Based Compensation. We account for stock based compensation awards under our shareholder approved incentive plans in accordance with the fair value recognition provisions of U.S. GAAP, which requires the measurement, and recognition of compensation for all stock-based awards made to employees and non-employee directors including stock options and restricted stock issuances based on estimated fair values. We recognize stock-based compensation in the consolidated statements of income on a straight-line basis over the vesting period. We use the Black-Scholes option-pricing model, which requires the following variables for input to calculate the fair value of each stock award on the option grant date: 1) expected volatility of our stock price, 2) the risk-free interest rate, 3) expected term of each award, 4) expected dividends, and 5) an expected forfeiture rate. For restricted stock awards with market-based conditions, we estimate their fair values by using a Monte Carlo simulation model, which requires the following variables for input: 1) expected dividends per share, 2) expected volatility, 3) risk-free interest rate, 4) estimated cost of capital, and 5) expected term of each award.

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ITEM 7A *Quantitative and Qualitative Disclosures About Market Risk*

Our investment portfolios at December 31, 2016 included fixed-maturity and equity securities, the purposes of which are not for trading or speculation. Our main objective is to maximize after-tax investment income and maintain sufficient liquidity to meet our obligations while minimizing market risk, which is the potential economic loss from adverse fluctuations in securities prices. We consider many factors including credit ratings, investment concentrations, regulatory requirements, anticipated fluctuation of interest rates, durations and market conditions in developing investment strategies. Our investment securities are managed primarily by outside investment companies and are overseen by the investment committee appointed by our board of directors.

Our investment portfolios are exposed to interest rate risk, credit risk and equity price risk. Fiscal and economic uncertainties caused by any government action or inaction may exacerbate these risks and potentially have adverse impacts on the value of our investment portfolios.

We classify our fixed-maturity and equity securities as available-for-sale and report any unrealized gains or losses, net of deferred income taxes, as a component of other comprehensive income within our stockholders equity. As such, any material temporary changes in their fair value can adversely impact the carrying value of our stockholders equity.

Interest Rate Risk

Our fixed-maturity securities are sensitive to potential losses resulting from unfavorable changes in interest rates. We manage the risk by analyzing anticipated movement in interest rates and considering our future capital needs.

The following table illustrates the impact of hypothetical changes in interest rates to the fair value of our fixed-maturity securities at December 31, 2016 (amounts in thousands):

Hypothetical Change in Interest Rates	Estimated Fair Value	Change in Estimated Fair Value	Percentage Increase (Decrease) in Estimated Fair Value
300 basis point increase	$ 145,268	$ (20,980)	(12.62)%
200 basis point increase	152,257	(13,991)	(8.42)%
100 basis point increase	159,250	(6,998)	(4.21)%
100 basis point decrease	173,250	7,002	4.21%
200 basis point decrease	180,193	13,945	8.39%
300 basis point decrease	185,912	19,664	11.83%

Credit Risk

Credit risk can expose us to potential losses arising principally from adverse changes in the financial condition of the issuers of our fixed-maturity securities. We mitigate the risk by investing in fixed-maturity securities that are generally investment grade, by diversifying our

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investment portfolio to avoid concentrations in any single issuer or business sector, and by continually monitoring each individual security for declines in credit quality. While we emphasize credit quality in our investment selection process, significant downturns in the markets or general economy may impact the credit quality of our portfolio.

The following table presents the composition of our fixed-maturity securities, by rating, at December 31, 2016 (amounts in thousands):

Comparable Rating	Amortized Cost	% of Total Amortized Cost	Estimated Fair Value	% of Total Estimated Fair Value
AAA	$ 1,514	1	$ 1,514	1
AA+, AA, AA-	29,249	17	29,092	17
A+, A, A-	59,966	36	59,264	36
BBB+, BBB, BBB-	53,333	32	53,548	32
BB+, BB, BB-	8,586	5	8,373	5
B+, B, B-	8,028	5	8,012	5
CCC+, CC and Not rated	6,555	4	6,445	4
Total	$ 167,231	100	$ 166,248	100

Equity Price Risk

Our equity investment portfolio at December 31, 2016 included common stocks, perpetual preferred stocks, mutual funds and exchange traded funds. We may incur potential losses due to declines in equity security prices. We manage the risk primarily through industry and issuer diversification and asset mix.

The following table illustrates the composition of our equity securities at December 31, 2016 (amounts in thousands):

	Estimated Fair Value	% of Total Estimated Fair Value
Stocks by sector:		
Financial	$ 24,326	46
Consumer	6,759	13
Energy	3,188	6
Industrial	3,156	6
Other (1)	5,110	9
	42,539	80
Mutual funds and Exchange traded funds by type:		
Debt	9,327	18
Equity	1,169	2

		10,496	20
Total	$	53,035	100

(1) Represents an aggregate of less than 5% sectors.

Foreign Currency Exchange Risk

At December 31, 2016, we did not have any material exposure to foreign currency related risk.

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ITEM 8 ***Financial Statements and Supplementary Data***

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of

HCI Group, Inc. and Subsidiaries:

We have audited the accompanying consolidated balance sheets of HCI Group, Inc. and Subsidiaries (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, stockholders equity, and cash flows for each of the years in the three year period ended December 31, 2016. The Company s management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of HCI Group, Inc. and Subsidiaries as of December 31, 2016 and 2015, and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company s internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 22, 2017 expressed an unqualified opinion.

/s/ Dixon Hughes Goodman LLP

Clearwater, Florida

February 22, 2017

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Report of Independent Registered Public Accounting Firm on Internal Control

To the Board of Directors and Stockholders of

HCI Group, Inc. and Subsidiaries

We have audited HCI Group, Inc. and Subsidiaries (the Company) internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, HCI Group, Inc. and Subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets and the related consolidated statements of income, comprehensive income, stockholders equity, and cash flows of HCI Group, Inc. and Subsidiaries as of and for the year ended December 31, 2016, and our report dated February 22, 2017, expressed an unqualified opinion on those consolidated financial statements.

/s/ Dixon Hughes Goodman LLP

Clearwater, Florida

February 22, 2017

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(Dollar amounts in thousands)

	December 31, 2016	December 31, 2015
Assets		
Fixed-maturity securities, available for sale, at fair value (amortized cost: $167,231 and $128,614, respectively)	$ 166,248	$ 125,009
Equity securities, available for sale, at fair value (cost: $47,750 and $47,548, respectively)	53,035	48,237
Limited partnership investments, at equity	29,263	23,930
Investment in unconsolidated joint venture, at equity	2,102	4,787
Real estate investments (Note 4 Consolidated Variable Interest Entity)	48,086	30,954
Total investments	298,734	232,917
Cash and cash equivalents (Note 4 Consolidated Variable Interest Entity)	280,531	267,738
Accrued interest and dividends receivable	1,654	1,390
Income taxes receivable	2,811	1,858
Premiums receivable	17,276	19,631
Prepaid reinsurance premiums	24,554	40,747
Deferred policy acquisition costs	16,639	18,602
Property and equipment, net	11,374	11,786
Intangible assets, net	4,899	
Deferred income taxes, net	250	3,189
Other assets	11,342	39,128
Total assets	$ 670,064	$ 636,986
Liabilities and Stockholders Equity		
Losses and loss adjustment expenses	$ 70,492	$ 51,690
Unearned premiums	175,803	187,290
Advance premiums	4,651	4,983
Assumed reinsurance balances payable	3,294	1,084
Accrued expenses (Note 4 Consolidated Variable Interest Entity)	6,513	6,316
Long-term debt	138,863	129,429
Other liabilities	26,702	18,472
Total liabilities	426,318	399,264
Commitments and contingencies (Note 22)		
Stockholders equity:		
7% Series A cumulative convertible preferred stock (no par value, 1,500,000 shares authorized, no shares issued and outstanding)		

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, 9,662,761 and 10,292,256 shares issued and outstanding in 2016 and 2015, respectively)		
Additional paid-in capital	8,139	23,879
Retained income	232,964	215,634
Accumulated other comprehensive income (loss), net of taxes	2,643	(1,791)
Total stockholders equity	243,746	237,722
Total liabilities and stockholders equity	$ 670,064	$ 636,986

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Income

(Dollar amounts in thousands, except per share amounts)

	Years Ended December 31, 2016	2015	2014
Revenue			
Gross premiums earned	$ 378,678	$ 423,120	$ 365,488
Premiums ceded	(135,051)	(140,614)	(113,423)
Net premiums earned	243,627	282,506	252,065
Net investment income	9,087	3,978	4,888
Net realized investment gains (losses)	2,601	(608)	4,735
Net other-than-temporary impairment losses recognized in income:			
Total other-than-temporary impairment losses	(2,252)	(5,275)	(107)
Portion of loss recognized in other comprehensive income, before taxes	(230)	594	
Net other-than-temporary impairment losses	(2,482)	(4,681)	(107)
Policy fee income	3,914	3,496	2,820
Gain on repurchases of convertible senior notes	153		
Gain on bargain purchase	2,071		
Gain on remeasurement of previously held interest	4,005		
Other	1,470	1,261	1,707
Total revenue	264,446	285,952	266,108
Expenses			
Losses and loss adjustment expenses	124,667	87,224	79,468
Policy acquisition and other underwriting expenses	42,642	41,984	37,952
Salaries and wages	19,037	20,140	16,483
Interest expense	11,079	10,754	10,453
Impairment loss	388		
Other operating expenses	19,777	19,658	20,790
Total expenses	217,590	179,760	165,146
Income before income taxes	46,856	106,192	100,962
Income tax expense	17,835	40,331	38,298
Net income	$ 29,021	$ 65,861	$ 62,664
Preferred stock dividends			4

Income available to common stockholders	$	29,021	$	65,861	$	62,668
Basic earnings per common share	$	2.95	$	6.51	$	5.90
Diluted earnings per common share	$	2.92	$	5.90	$	5.36
Dividends per common share	$	1.20	$	1.20	$	1.10

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

(Amounts in thousands)

	Years Ended December 31,		
	2016	**2015**	**2014**
Net income	$ 29,021	$ 65,861	$ 62,664
Other comprehensive income (loss):			
Change in unrealized gain (loss) on investments:			
Net unrealized gain (loss) arising during the period	7,317	(9,366)	3,870
Other-than-temporary impairment loss charged to investment income	2,482	4,681	107
Call and repayment losses charged to investment income	20	77	28
Reclassification adjustment for net realized (gain) loss	(2,601)	608	(4,735)
Net change in unrealized gain (loss)	7,218	(4,000)	(730)
Deferred income taxes on above change	(2,784)	1,543	282
Total other comprehensive income (loss), net of income taxes	4,434	(2,457)	(448)
Comprehensive income	$ 33,455	$ 63,404	$ 62,216

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Stockholders Equity

For the Year Ended December 31, 2016

(Dollar amounts in thousands)

	Series A Preferred Stock		Common Stock		Additional Paid-In	Retained	Accumulated Other Comprehensive (Loss) Income, Net of	Total Stockholders
	Shares	Amount	Shares	Amount	Capital	Income	Tax	Equity
Balance at December 31, 2015		$	10,292,256	$	$ 23,879	$ 215,634	$ (1,791)	$ 237,722
Net income						29,021		29,021
Total other comprehensive income, net of income taxes							4,434	4,434
Issuance of restricted stock			142,440					
Exercise of common stock options			60,000		150			150
Forfeiture of restricted stock			(13,298)					
Cancellation of restricted stock			(160,000)					
Repurchase and retirement of common stock			(14,934)		(464)			(464)
Repurchase and retirement of common stock under share repurchase plan			(643,703)		(20,026)			(20,026)
Common stock dividends						(11,691)		(11,691)
Tax benefits on stock-based compensation					641			641
Tax shortfalls on stock-based compensation					(239)			(239)
Stock-based compensation					4,198			4,198

Balance at December 31, 2016	$ 9,662,761	$	$ 8,139	$ 232,964	$ 2,643	$ 243,746

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Stockholders Equity – (Continued)

For the Year Ended December 31, 2015

(Dollar amounts in thousands)

	Series A Preferred Stock		Common Stock		Additional Paid-In	Retained	Accumulated Other Comprehensive Income (Loss), Net of	Total Stockholders
	Shares	Amount	Shares	Amount	Capital	Income	Tax	Equity
Balance at December 31, 2014		$	10,189,128	$	$ 20,465	$ 161,454	$ 666	$ 182,585
Net income						65,861		65,861
Total other comprehensive loss, net of income taxes							(2,457)	(2,457)
Issuance of restricted stock			83,260					
Exercise of common stock options			120,000		263			263
Shares surrendered upon exercising common stock options			(2,013)					
Forfeiture of restricted stock			(42,757)					
Repurchase and retirement of common stock			(17,493)		(792)			(792)
Repurchase and retirement of common stock under share repurchase plan			(37,869)		(1,610)			(1,610)
Common stock dividends						(11,681)		(11,681)
Tax benefits on stock-based compensation					2,295			2,295
Tax shortfalls on stock-based compensation					(1,954)			(1,954)
Stock-based compensation					5,212			5,212
Balance at December 31, 2015		$	10,292,256	$	$ 23,879	$ 215,634	$ (1,791)	$ 237,722

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Stockholders Equity – (Continued)

For the Year Ended December 31, 2014

(Dollar amounts in thousands)

	Series A Preferred Stock		Common Stock		Additional Paid-In	Retained	Accumulated Other Comprehensive Income (Loss), Net of	Total Stockholders
	Shares	Amount	Shares	Amount	Capital	Income	Tax	Equity
Balance at December 31, 2013	110,684	$	10,939,268	$	$ 48,966	$ 110,441	$ 1,114	$ 160,521
Net income						62,664		62,664
Total other comprehensive loss, net of income taxes							(448)	(448)
Conversion of preferred stock to common stock	(107,298)		107,298					
Issuance of restricted stock			108,720					
Exercise of common stock options			50,000		125			125
Forfeiture of restricted stock			(10,840)					
Repurchase and retirement of common stock			(14,617)		(643)			(643)
Repurchase and retirement of common stock under share repurchase plan			(990,701)		(38,354)			(38,354)
Redemption of Series A preferred stock	(3,386)				(34)			(34)
Deferred taxes on debt discount					215			215
Common stock dividends						(11,655)		(11,655)
Derecognition of preferred stock dividends						4		4

payable						
Tax benefits on stock-based compensation			2,080			2,080
Stock-based compensation			8,110			8,110
Balance at December 31, 2014	$ 10,189,128	$	$ 20,465	$ 161,454	$ 666	$ 182,585

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(Amounts in thousands)

	Years Ended December 31, 2016	2015	2014
Cash flows from operating activities:			
Net income	$ 29,021	$ 65,861	$ 62,664
Adjustments to reconcile net income to net cash provided by operating activities:			
Stock-based compensation	4,198	5,212	8,110
Net amortization of discounts and premiums on investments in fixed-maturity securities	726	855	782
Depreciation and amortization	5,408	5,251	4,958
Deferred income tax expense (benefit)	155	(1,101)	(4,742)
Net realized investment (gains) losses	(2,601)	608	(4,735)
Other-than-temporary impairment losses	2,482	4,681	107
Income from real estate investment under acquisition, development and construction arrangement		(344)	(85)
Gain on repurchases of convertible senior notes	(153)		
Gain on bargain purchase	(2,071)		
Gain on remeasurement of previously held investment	(4,005)		
Impairment loss	388		
Loss from unconsolidated joint venture		125	23
Net (income) loss from limited partnership interests	(1,207)	3,244	90
Distributions received from limited partnership interests	544	12	
Foreign currency remeasurement loss	29	66	29
Other	18	26	(1)
Changes in operating assets and liabilities:			
Accrued interest and dividends receivable	(300)	(331)	74
Income taxes	(1,192)	766	(3,167)
Premiums receivable	2,355	(3,807)	(1,150)
Prepaid reinsurance premiums	16,193	(6,651)	(6,030)
Deferred policy acquisition costs	1,963	(3,588)	(943)
Other assets	29,054	(7,230)	(20,086)
Losses and loss adjustment expenses	18,802	2,782	5,222
Unearned premiums	(11,487)	(26,781)	42,164
Advance premiums	(332)	603	(124)
Assumed reinsurance balances payable	2,210	866	(4,442)
Accrued expenses and other liabilities	(2,223)	4,157	10,011
Net cash provided by operating activities	87,975	45,282	88,729
Cash flows from investing activities:			
		(6,968)	(2,803)

Investment in real estate under acquisition, development, and construction arrangement			
Acquisition of real estate business, net of cash acquired	(11,651)		
Investments in limited partnership interests	(4,670)	(24,636)	(2,640)
Investment in unconsolidated joint venture	(90)	(435)	(4,500)
Purchase of property and equipment	(865)	(840)	(453)
Purchase of real estate investments	(2,261)	(4,871)	(413)
Purchase of fixed-maturity securities	(85,530)	(98,501)	(83,365)
Purchase of equity securities	(22,434)	(32,878)	(44,257)
Proceeds from investment in real estate under acquisition, development and construction arrangement	10,200		
Proceeds from sales of fixed-maturity securities	40,454	53,711	98,365
Proceeds from calls, repayments and maturities of fixed-maturity securities	4,692	9,344	4,603
Proceeds from sales of equity securities	23,127	25,695	16,810
Proceeds from sales of real estate investments		5	1
Net cash used in investing activities	(49,028)	(80,374)	(18,652)

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HCI GROUP, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows (Continued)

(Amounts in thousands)

	Years Ended December 31, 2016	2015	2014
Cash flows from financing activities:			
Net borrowing under revolving credit facility	1,238		
Proceeds from the exercise of common stock options	150	263	125
Cash dividends paid	(12,438)	(12,428)	(12,355)
Cash dividends received under share repurchase forward contract	747	747	685
Proceeds from the issuance of long-term debt	18,200		
Repurchases of convertible senior notes	(11,347)		
Repayment of debt	(455)		
Repurchases of common stock	(464)	(792)	(643)
Repurchases of common stock under share repurchase plan	(20,026)	(1,610)	(38,354)
Redemption of Series A preferred stock			(34)
Purchase of non-controlling interest	(2,064)		
Debt issuance costs	(339)		(234)
Tax benefits on stock-based compensation	641	2,295	2,080
Net cash used in financing activities	(26,157)	(11,525)	(48,730)
Effect of exchange rate changes on cash	3	(61)	(29)
Net increase (decrease) in cash and cash equivalents	12,793	(46,678)	21,318
Cash and cash equivalents at beginning of year	267,738	314,416	293,098
Cash and cash equivalents at end of year	$ 280,531	$ 267,738	$ 314,416
Supplemental disclosure of cash flow information:			
Cash paid for income taxes	$ 18,857	$ 38,371	$ 43,902
Cash paid for interest	$ 7,222	$ 7,211	$ 6,258
Non-cash investing and financing activities:			
Unrealized gain (loss) on investments in available-for-sale securities, net of tax	$ 4,434	$ (2,457)	$ (448)
Conversion of Series A preferred stock to common stock	$	$	$ 972
Details of business acquisition:			
Fair value of assets acquired	$ 32,569	$	$
Less: Purchase price	(14,514)		

Carrying value of previously held interest		(2,859)				
Gain on remeasurement of previously held interest		(4,005)				
Gain on bargain purchase		(2,071)				
Liabilities assumed	$	9,120	$		$	
Receivable from sales of available-for-sale securities	$	350	$		$	34
Payable on purchases of available-for-sale securities	$	50	$	1	$	1,908

See accompanying Notes to Consolidated Financial Statements.

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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

Note 1 Nature of Operations

HCI Group, Inc., together with its subsidiaries (HCI or the Company), is primarily engaged in the property and casualty insurance business through Homeowners Choice Property & Casualty Insurance Company, Inc. (HCPCI), its principal operating subsidiary. HCPCI is authorized to underwrite various homeowners property and casualty insurance products and allied lines business in the state of Florida. HCPCI also offers flood-endorsed and wind-only policies to new and pre-existing Florida customers. HCPCI s operations are supported by HCI Group, Inc. and the following HCI subsidiaries:

Homeowners Choice Managers, Inc. acts as managing general agent and provides marketing, underwriting, claims settlement, accounting and financial services to HCPCI;

Southern Administration, Inc. provides policy administration services to HCPCI; and

Claddaugh Casualty Insurance Company, Ltd. participates in the reinsurance program to HCPCI.

The Company s insurance subsidiaries also include TypTap Insurance Company (TypTap), a Florida insurance company approved by the Florida Office of Insurance Regulation (FLOIR) in January 2016. TypTap offers standalone flood policies to Florida homeowners. In 2016, the Company s Alabama insurance subsidiary, Homeowners Choice Assurance Company, Inc. (HCA) voluntarily surrendered its certificate of authority to the Alabama Department of Insurance and, as a result, formally terminated its plan to conduct business in the state of Alabama. Since its organization, HCA had no operations. The withdrawal was effective on June 30, 2016 and HCA was dissolved in December 2016.

In addition, HCI includes various subsidiaries predominantly engaged in the businesses of owning and leasing real estate, operating marina facilities and one restaurant, and developing software products.

The Company reports its operations under one business segment.

The Company obtained a majority of its policies through participation in a take-out program with Citizens Property Insurance Corporation (Citizens), a Florida state supported insurer. Policies were obtained in separate assumption transactions with Citizens that took place from July 2007 through November 2016. The Company is required to offer renewals on the policies acquired for a period of three years subsequent to the initial expiration of the assumed policies. During the first full year after assumption, such renewals are required to have rates that are equivalent to or less than the rates charged by Citizens. Substantially all of the Company s premium revenue since inception comes from these assumptions and one additional assumption through which the Company acquired the Florida policies of another Florida insurance carrier.

HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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

Note 2 Summary of Significant Accounting Policies

Basis of Presentation. The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP).

Adoption of New Accounting Standards.

In December 2016, the Company early adopted Accounting Standards Update No. 2016-15, Statement of Cash Flows (Topic 230), which provides guidance on how certain cash receipts and cash payments, specifically distributions received from equity method investees, are presented and classified. The Company elects to classify these distributions received using the cumulative earnings approach. Under this approach, distributions received are considered returns on investments and classified as cash inflows from operating activities, unless the Company s cumulative distributions received less distributions received in prior periods that were determined to be returns of investments exceed the cumulative equity in earnings recognized by the Company. When such an excess occurs, the current period distribution up to this excess is considered a return of investment and classified as cash inflows from investing activities. As a result of adopting this standard, the Company reclassified $544 and $12 of cash received from limited partnership interests during 2016 and 2015, respectively, from investing activities to operating activities. The change to the Company s net cash provided by (used in) operating activities and net cash used in investing activities at each reporting date has been applied retrospectively for the year ended December 31, 2015 and in all periods thereafter. The Company had no distributions from limited partnership interests during 2014. The adoption of this standard had no effect on the prior consolidated results of the Company s operations, comprehensive income, stockholders equity and financial position.

As of December 31, 2016, the Company adopted Accounting Standards Update No. 2015-09, Financial Services Insurance (Topic 944), which improves disclosure requirements for all insurance entities that issue short-duration contracts. The amendments in this update were applied retrospectively with supplementary information for each prior period presented, except for those requirements applying only to the current period which were applied prospectively. The adoption of this standard had no effect on the Company s consolidated results of operations and comprehensive income.

In addition, The Company adopted Accounting Standards Update No. 2014-15, Presentation of Financial Statements Going Concern (Subtopic 205-40), which provides guidance about management s responsibility to evaluate whether there is substantial doubt about an entity s ability to continue as a going concern and requirements for related footnote disclosures. The adoption of this standard in December 2016 had no effect on the Company s consolidated financial statements.

Principles of Consolidation. The accompanying consolidated financial statements include the accounts of HCI Group, Inc. and its majority-owned and controlled subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. In addition, the Company evaluates its relationships or investments for consolidation pursuant to authoritative accounting guidance related to the consolidation of variable interest entities under the

Variable Interest Model prescribed by the Financial Accounting Standards Board (FASB). A variable interest entity is consolidated when the Company has the power to direct activities that most

HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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

significantly impact the economic performance of the variable interest entity and has the obligation to absorb losses or the right to receive benefits from the variable interest entity that could potentially be significant to the variable interest entity. When a variable interest entity is not consolidated, the Company uses the equity method to account for the investment. Under this method, the carrying value is generally the Company s share of the net asset value of the unconsolidated entity, and changes in the Company s share of the net asset value are recorded in net investment income.

The Company has a 100% equity interest in one venture (treated as a joint venture under U.S. GAAP) that owns land in Riverview, Florida on which a retail center is being constructed for lease or for sale. The Company consolidates this joint venture as its primary beneficiary (see Note 4 Investments under *Consolidated Variable Interest Entity*).

Use of Estimates. The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as well as the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ materially from these estimates. Material estimates that are particularly susceptible to significant change in the near term are primarily related to losses and loss adjustment expenses, reinsurance with retrospective provisions, deferred income taxes, and stock-based compensation expense.

Business Acquisitions. The Company accounts for business acquisitions using the acquisition method, which requires it to measure and recognize the assets acquired, liabilities assumed, and any noncontrolling interest in the acquiree at their acquisition date fair values. In the event that the fair value of net assets acquired exceeds the purchase price, a bargain purchase gain is recorded. In a step acquisition in which there is a change in ownership interest and control is obtained when there is a previously held equity interest, a gain or loss from remeasurement of the previously held equity interest to fair value is recorded.

Acquisitions of income-producing real properties are typically considered business acquisitions. As such, the Company allocates the purchase price to land, land improvements, buildings, tenant improvements, intangibles such as the value of significant tenant (i.e. anchor tenant) relationships, in-place leases, and assumed liabilities, if any. Tangible assets are presented as real estate investments on the Company s consolidated balance sheet. Buildings subject to leases are valued as if vacant. The value attributable to in-place leases reflects the costs we would have incurred to lease the property to the occupancy level that existed at the acquisition date. These costs include leasing commissions, tenant improvement allowances, and other direct costs required to lease the property. In addition, the estimated fair value of in-place leases reflects the value of base rental revenues that would have been earned during the assumed periods of vacancy and the related carrying costs that would have been incurred to lease the vacant property to its existing occupancy. The Company also reviews terms of the assumed leases to evaluate whether the terms are favorable or unfavorable relative to the market at the acquisition date. In the event the assumed leases are not at market terms, the Company recognizes an intangible asset for a lease with favorable terms and a liability if the terms of the lease are unfavorable.

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HCI GROUP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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

Cash and Cash Equivalents. The Company considers all short-term highly liquid investments with original maturities of less than three months to be cash and cash equivalents. At December 31, 2016 and 2015, cash and cash equivalents consisted of cash on deposit with financial institutions and securities brokerage firms.

Investments in Available-for-Sale Securities. Investments consist of fixed-maturity and equity securities. Fixed-maturity securities include debt securities and redeemable preferred stock. Securities may be classified as either trading, held to maturity or available-for-sale. The Company s available-for-sale securities are carried at fair value. Temporary changes in the fair value of available-for-sale securities are excluded from net investment income and reported in stockholders equity as a component of accumulated other comprehensive income, net of deferred income taxes. Realized investment gains and losses from sales are recorded on the trade date and are determined using the first-in first-out (FIFO) method. Investment income is recognized as earned and discounts or premiums arising from the purchase of debt securities are recognized in investment income using the interest method over the estimated remaining term of the security. Gains and losses from call redemptions and repayments are charged to investment income.

The Company reviews all securities for other-than-temporary impairment on a monthly basis. When the fair value of any investment is lower than its cost, an assessment is made to determine whether the decline is temporary or other-than-temporary. If the decline is determined to be other-than-temporary, the investment is written down to fair value and an impairment loss is recognized in income in the period in which the Company makes such determination.

When reviewing impaired fixed-maturity securities, the Company considers its ability and intent to hold these securities and whether it is probable that the Company will be required to sell these securities prior to their anticipated recovery or maturity. For the fixed-maturity securities that the Company intends to sell or it is probable that the Company will have to sell the fixed-maturity securities before recovery or maturity, the unrealized losses are recognized as other-than-temporary losses in income. In instances where there are credit related losses associated with the impaired fixed-maturity securities for which the Company asserts that it does not have the intent to sell, and it is probable that the Company will not be required to sell until a market price recovery or maturity, the amount of the other-than-temporary impairment loss related to credit losses is recognized in income, and the amount of the other-than-temporary impairment loss related to other non-credit factors such as changes in interest rates or market conditions is recorded as a component of other comprehensive income.

When determining impairment due to a credit related loss, the Company carefully considers factors such as the issuer s financial ratios and condition, the security s current ratings and maturity date, and overall market conditions in estimating the cash flows expected to be collected. The expected cash flows discounted at the effective interest rate of the security implicit at the date of acquisition is then compared with the security s amortized cost at the measurement date. A credit loss is incurred when the present value of the expected cash flows is less than the security s amortized cost. The Company considers various factors in determining whether an individual security is other-than-temporarily impaired (see Note 4 Investments).

Limited Partnership Investments. The Company has interests in limited partnerships that are not registered under the United Stated Securities Act of 1933, as amended, the securities laws of

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any state or the securities laws of any other jurisdictions. The partnership interest cannot be resold in the public market and any withdrawal is subject to the terms and conditions of the partnership agreement. The Company has no influence over partnership operating and financial policies. The Company did not elect the fair value option and, therefore, uses the equity method to account for these investments (see Note 4 Investments). The Company will generally recognize its share of the limited partnership s earnings or losses on a three- to six-month lag.

Pursuant to U.S. GAAP, these limited partnerships which are private equity funds must measure their investments at fair value and reflect the unrealized gains or losses in the fair value of their investments on their statement of income. As a result, the carrying value of limited partnership investments at each reporting date approximates their estimated fair value.

Investment in Unconsolidated Joint Venture. The Company has a 90% equity interest in a limited liability company (treated as a joint venture under U.S. GAAP) that owns land for lease or for sale and, until December 2016, owned and operated a retail shopping center. The joint venture was determined to be a variable interest entity as it lacks sufficient equity to finance its activities without additional subordinated financial support. Despite having a majority equity interest, the Company does not have the power to direct the activities that most significantly impact the economic performance of the joint venture and, accordingly, is not required to consolidate the joint venture as its primary beneficiary. As a result, the Company uses the equity method to account for this investment.

Ownership of the retail shopping center was distributed to members of the limited liability company in December 2016. The operating agreement also contained an embedded purchase option which allowed the Company to purchase the entire interest of the other party to the venture after the expiration of a restricted period. The Company purchased the other member s interest in December 2016 (see Note 4 Investments).

When evidence indicates an impairment may occur, the Company evaluates whether a decline in value is other than temporary. Evidence may include continuing operating losses of the joint venture, a declining occupancy rate, a decrease in real estate value, and an oversupply of rental property in close vicinity to the investment property. Should available evidence indicate the recovery of the initial investment is less likely, the Company would compare the carrying value of the investment with its expected residual value and recognize an impairment loss in earnings.

Real Estate Investments. Real estate investments include real estate and the related assets purchased for investment purposes (see Note 4 Investments).

Prior to August 16, 2016, there was one Acquisition, Development and Construction loan agreement (ADC Arrangement). Under the ADC Arrangement, the Company provided financing to the property developer for the acquisition, development, and construction of a retail shopping center. The Company also expected 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 a joint venture was determined by the Company s evaluation of the characteristics and the risks and rewards of the ADC Arrangement. Because the Company expected to receive more than 50% of the residual profit from the ADC Arrangement which had characteristics similar to a real estate investment, the costs of the real estate project were capitalized and interest was recognized in net investment income.

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In addition, the Company considered any rights or features embedded in the ADC Arrangement that might require bifurcation and derivative accounting. Due to its participation in the expected residual profit, which was deemed a variable interest, the Company evaluated if the Company had the power to direct the activities that significantly impact the economic performance of the entity to which the Company provided financing for possible consolidation as the primary beneficiary under the Variable Interest Model as prescribed by FASB (see *ADC Arrangement* in Note 4 Investments).