NATIONAL SECURITY GROUP INC
Form 10-Q
May 13, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For Quarterly Period Ended March 31, 2016

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to .

Commission File Number 0-18649

The National Security Group, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	63-1020300 (IRS Employer Identification No.)
661 East Davis Street Elba, Alabama (Address of principal executive offices)	36323 (Zip-Code)

Registrant's Telephone Number including Area Code (334) 897-2273

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 þ No o

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). þ Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in rule 12b-2 of the Act). (Check One) : Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller reporting company þ

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

As of May 13, 2016, there were 2,512,425 shares, $1.00 par value, of the registrant’s common stock outstanding.

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Cautionary Statement Regarding Forward-Looking Statements

Any statement contained in this report which is not a historical fact, or which might otherwise be considered an opinion or projection concerning the Company or its business, whether expressed or implied, is meant as and should be considered a forward-looking statement as that term is defined in the Private Securities Litigation Reform Act of 1995. The following report contains forward-looking statements that are not strictly historical and that involve risks and uncertainties. Such statements include any statements containing the words “expect,” “plan,” “estimate,” “anticipate” or other words of a similar nature. Management cautions investors about forward-looking statements. Forward-looking statements involve certain evaluation criteria, such as risks, uncertainties, estimates, and/or assumptions made by individuals informed of the Company and industries in which we operate. Any variation in the preceding evaluation criteria could cause actual results to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include, without limitation, the following:

The insurance industry is highly competitive and the Company encounters significant competition in all lines of business from other insurance companies. Many of the competing companies have more abundant financial resources than the Company.

Insurance is a highly regulated industry. It is possible that legislation may be enacted which would have an adverse effect on the Company's business.

The Company is subject to regulation by state governments for each of the states in which it conducts business. The Company cannot predict the subject of any future regulatory initiative(s) or its (their) impact on the Company's business.

The Company is rated by various insurance rating agencies. If a rating is downgraded from its current level by one of these agencies, sales of the Company's products and stock price could be adversely impacted.

The Company's financial results are adversely affected by increases in policy claims received by the Company. While a manageable risk, this fluctuation is often unpredictable.

The Company's investments are subject to a variety of risks. Investments are subject to defaults and changes in market value. Market value can be affected by changes in interest rates, market performance and the economy.

The Company mitigates risk associated with life policies through implementing effective underwriting and reinsurance strategies. These factors mitigate, not eliminate, risk related to mortality and morbidity exposure. The Company has established reserves for claims and future policy benefits based on amounts determined by independent actuaries. There is no assurance that these estimated reserves will prove to be sufficient or that the Company will not incur claims exceeding reserves, which could result in operating losses and loss of capital.

The Company mitigates risk associated with property and casualty policies through implementing effective underwriting and reinsurance strategies. The Company obtains reinsurance which increases underwriting capacity and limits the risk associated with policy claims. The Company is subject to credit risk with regard to reinsurers as reinsurance does not alleviate the Company's liability to its insured's for the ceded risks. The Company utilizes a third-party to develop a reinsurance treaty with reinsurers who are reliable and financially stable. However, there is no guarantee that booked reinsurance recoverable will actually be recovered. A reinsurer's insolvency or inability to make payments due could have a material adverse impact on the financial condition of the Company.

The Company's ability to continue to pay dividends to shareholders is contingent upon profitability and capital adequacy of the insurance subsidiaries. The insurance subsidiaries operate under regulatory restrictions that could limit the ability to fund future dividend payments of the Company. An adverse event or series of events could materially impact the ability of the insurance subsidiaries to fund future dividends, and consequently, the Board of Directors would have to suspend the declaration of dividends to shareholders.

The Company is subject to the risk of adverse settlements or judgments resulting from litigation of contested claims. It is difficult to predict or quantify the expected results of litigation because the outcome depends on decisions of the court and jury that are based on facts and legal arguments presented at the trial.

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PART I. Financial Information

Item 1. Financial Statements

THE NATIONAL SECURITY GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS (In thousands)

	March 31, 2016 (UNAUDITED)	December 31, 2015
ASSETS		
Investments		
Fixed maturities held-to-maturity, at amortized cost (estimated fair value: 2016 - $2,475; 2015 - $2,504)	$ 2,370	$ 2,439
Fixed maturities available-for-sale, at estimated fair value (cost: 2016 - $93,990; 2015 - $92,077)	95,319	91,812
Equity securities available-for-sale, at estimated fair value (cost: 2016 - $2,420; 2015 - $2,420)	5,057	4,897
Trading securities	107	107
Mortgage loans on real estate, at cost	190	202
Investment real estate, at book value	3,291	3,291
Policy loans	1,676	1,655
Company owned life insurance	4,932	4,898
Other invested assets	3,185	3,256
Total Investments	116,127	112,557
Cash	4,163	6,763
Accrued investment income	848	797
Policy receivables and agents' balances, net	11,776	11,296
Reinsurance recoverable	1,446	1,660
Deferred policy acquisition costs	8,542	8,485
Property and equipment, net	2,004	1,946
Deferred income tax asset, net	3,141	3,824
Other assets	565	513
Total Assets	$ 148,612	$ 147,841
LIABILITIES AND SHAREHOLDERS' EQUITY		
Property and casualty benefit and loss reserves	$ 8,244	$ 9,645
Accident and health benefit and loss reserves	3,173	3,197
Life and annuity benefit and loss reserves	32,016	31,962
Unearned premiums	30,543	29,852
Policy and contract claims	856	826
Other policyholder funds	1,584	1,561
Short-term notes payable and current portion of long-term debt	857	857
Long-term debt	17,102	17,100
Accrued income taxes	172	101
Other liabilities	7,298	7,857
Total Liabilities	101,845	102,958
Contingencies		
Shareholders' equity		
Common stock	2,512	2,512

Additional paid-in capital	5,341	5,341
Accumulated other comprehensive income	1,581	525
Retained earnings	37,333	36,505
Total Shareholders' Equity	46,767	44,883
Total Liabilities and Shareholders' Equity	$ 148,612	$ 147,841

The Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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THE NATIONAL SECURITY GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
(In thousands, except per share amounts)

	Three months ended March 31,	
	2016	2015
REVENUES		
Net premiums earned	$15,165	$14,706
Net investment income	991	1,002
Net realized investment gains	7	142
Other income	154	158
Total Revenues	16,317	16,008
BENEFITS, LOSSES AND EXPENSES		
Policyholder benefits and settlement expenses	9,047	8,262
Amortization of deferred policy acquisition costs	787	899
Commissions	2,108	2,055
General and administrative expenses	2,129	2,031
Taxes, licenses and fees	600	655
Interest expense	345	320
Total Benefits, Losses and Expenses	15,016	14,222
Income Before Income Taxes	1,301	1,786
INCOME TAX EXPENSE		
Current	221	471
Deferred	139	7
	360	478
Net Income	$941	$1,308
INCOME PER COMMON SHARE BASIC AND DILUTED	$0.37	$0.52
DIVIDENDS DECLARED PER SHARE	$0.045	$0.04

The Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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THE NATIONAL SECURITY GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)
(In thousands)

	Three months ended March 31,	
	2016	2015
Net income	$941	$1,308
Other comprehensive income (loss), net of tax		
Changes in:		
Unrealized gains on securities, net of reclassification adjustment of $12 and $94 for 2016 and 2015, respectively	1,158	365
Unrealized loss on interest rate swap	(102)	(117)
Other comprehensive income, net of tax	1,056	248
Comprehensive income	$1,997	$1,556

The Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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THE NATIONAL SECURITY GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED)
(In thousands)

	Total	Retained Earnings	Accumulated Other Comprehensive Income	Common Stock	Additional Paid-in Capital
Balance at December 31, 2015 (AUDITED)	$44,883	$36,505	$ 525	$ 2,512	$ 5,341
Net income for March 31, 2016	941	941			
Other comprehensive income (net of tax)	1,056		1,056		
Cash dividends	(113)	(113)			
Balance at March 31, 2016	$46,767	$37,333	$ 1,581	$ 2,512	$ 5,341

The Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

THE NATIONAL SECURITY GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) (In thousands)

	Three months ended March 31, 2016	2015
Cash Flows from Operating Activities		
Net income	$941	$1,308
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation expense and amortization/accretion, net	85	79
Increase in cash surrender value of company owned life insurance	(34)	(44)
Net realized gains on investments	(7)	(142)
Deferred income taxes	139	7
Amortization of deferred policy acquisition costs	787	899
Changes in assets and liabilities:		
Change in accrued investment income	(51)	(45)
Change in reinsurance recoverable	214	(571)
Policy acquisition costs deferred	(844)	(893)
Change in accrued income taxes	71	5
Change in net policy liabilities and claims	(1,137)	1,075
Change in other assets/liabilities, net	(695)	1,247
Other, net	8	8
Net cash provided by (used in) operating activities	(523)	2,933
Cash Flows from Investing Activities		
Purchase of:		
Available-for-sale securities	(4,613)	(7,582)
Property and equipment	(97)	(69)
Proceeds from sale or maturities of:		
Held-to-maturity securities	74	346
Available-for-sale securities	2,666	5,256
Other invested assets, net	(17)	383
Net cash used in investing activities	(1,987)	(1,666)
Cash Flows from Financing Activities		
Change in other policyholder funds	23	15
Repayments of long-term debt	—	(500)
Dividends paid	(113)	(100)
Net cash used in financing activities	(90)	(585)
Net change in cash and cash equivalents	(2,600)	682
Cash and cash equivalents, beginning of year	6,763	6,426
Cash and cash equivalents, end of period	$4,163	$7,108

The Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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THE NATIONAL SECURITY GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED AMOUNTS EXCEPT FOR DECEMBER 31, 2015 AMOUNTS)

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Basis of Presentation
The accompanying condensed consolidated financial statements include the accounts of The National Security Group, Inc. (the Company) and its wholly-owned subsidiaries: National Security Insurance Company (NSIC), National Security Fire and Casualty Company (NSFC) and NATSCO, Inc. (NATSCO). NSFC includes a wholly-owned subsidiary, Omega One Insurance Company (Omega). The accompanying condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). In the opinion of management, all adjustments, consisting of normal and recurring items, necessary for the fair presentation of the condensed consolidated financial statements have been included. All significant intercompany transactions and accounts have been eliminated. The financial information presented herein should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2015, which includes information and disclosures not presented herein.

Use of Estimates
The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Among the more significant estimates included in these condensed consolidated financial statements are reserves for future life insurance policy benefits, liabilities for losses and loss adjustment expenses, reinsurance recoverable associated with loss and loss adjustment expense liabilities, deferred policy acquisition costs, deferred income tax assets and liabilities, assessments of other-than-temporary impairments on investments and accruals for contingencies. Actual results could differ from these estimates.

Earnings Per Share
Earnings per share of common stock is based on the weighted average number of shares outstanding during each year. The adjusted weighted average shares outstanding were 2,512,425 at March 31, 2016 and 2,507,452 at March 31, 2015. The Company did not have any dilutive securities as of March 31, 2016 and 2015.

Reclassifications
Certain 2015 amounts have been reclassified from the prior year condensed consolidated financial statements to conform to the 2016 presentation.

Concentration of Credit Risk
The Company maintains cash balances which are generally held in non-interest bearing demand deposit accounts subject to FDIC insured limits of $250,000 per entity. At March 31, 2016, the net amount exceeding FDIC insured limits was $2,099,000 at one financial institution. The Company has not experienced any losses in such accounts. Management of the Company reviews financial information of financial institutions on a quarterly basis and believes the Company is not exposed to any significant credit risk on cash and cash equivalents.

Policy receivables are reported at unpaid balances. Policy receivables are generally offset by associated unearned premium liabilities and are not subject to significant credit risk. Receivables from agents, less provision for credit losses, are composed of balances due from independent agents. At March 31, 2016, the single largest balance due from one agent totaled $902,000.

Reinsurance contracts do not relieve the Company of its obligations to policyholders. A failure of a reinsurer to meet their obligation could result in losses to the insurance subsidiaries. Allowances for losses are established if amounts are believed to be uncollectible. At March 31, 2016 and December 31, 2015, no amounts were deemed uncollectible. The Company, at least annually, evaluates the financial condition of all reinsurers and evaluates any potential concentrations of credit risk. At March 31, 2016, management does not believe the Company is exposed to any significant credit risk related to its reinsurance program.

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Change in Accounting Principle:

Effective January 1, 2016, the Company elected to change its method of presentation relating to placement fees associated with the issuance of trust preferred securities in accordance with FASB ASU 2015-03. Prior to 2016, the Company’s policy was to present these fees in Other Assets on the balance sheet, net of accumulated amortization. Beginning in 2016, the Company has presented these fees as a direct reduction in the related note payable.

Accounting Changes Not Yet Adopted

Revenue from Contracts with Customers
In May 2014, the Financial Accounting Standards Board (FASB) issued guidance on a comprehensive new revenue recognition standard. This standard will not impact accounting for insurance contracts, leases, financial instruments and guarantees. For those contracts that are impacted by the new guidance, the guidance will require an entity to recognize revenue upon the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to, in exchange for those goods or services. The guidance requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In August 2015, the FASB issued a deferral of the effective date by one year. This guidance is effective retrospectively for fiscal years beginning after December 15, 2017 and interim periods within those years. Early adoption of this standard is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Although insurance contracts are specifically scoped out of this new guidance, the Company has minor services that may be subject to the new revenue recognition guidance and are still in the process of evaluating the impact, if any, the guidance may have on its condensed consolidated financial statements.

Presentation of Financial Statements - Going Concern
In August 2014, the FASB issued guidance on determining when and how to disclose going concern uncertainties in the financial statements, and requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year of the date the financial statements are issued. The updated guidance is effective for annual periods ending after December 15, 2016 and interim periods thereafter. Early adoption is permitted. The Company does not expect the adoption to have a material impact on its financial position, results of operations or disclosures.

Recognition and Measurement of Financial Assets and Financial Liabilities
In January 2016, the FASB issued guidance that requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. The guidance requires entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes and requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset. The guidance eliminates the requirement for public companies to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. This guidance is effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. The Company does not expect the adoption to have a material impact on its financial position or results of operations.

Leases

In February 2016, the FASB issued guidance that requires lessees (for capital and operating leases) to recognize the lease liability and right-of-use asset at the commencement date of the lease. This guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. The Company does not expect the adoption to have a material impact on its financial position or results of operations.

Contingent Put and Call Options in Debt Instruments

In March 2016, the FASB issued guidance that clarifies the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts. This guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within

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those years. The Company does not expect the adoption to have a material impact on its financial position or results of operations.

Recently Adopted Accounting Standards

Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items
In January 2015, the FASB issued guidance that eliminates from GAAP the concept of extraordinary items. The Company adopted this standard on January 1, 2016. This guidance did not have a material effect on results of operations or financial position.

Amendments to the Consolidation Analysis
In February 2015, the FASB issued additional guidance regarding the consolidation of certain legal entities. The guidance modifies the evaluation of whether or not limited partnerships and similar legal entities are variable interest entities (VIEs) and the consolidation analysis of entities involved with VIEs, particularly those that have fee arrangements and related party relationships. The Company adopted this standard on January 1, 2016. This guidance did not have a material effect on results of operations or financial position.

Interest - Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs.
In April 2015, the FASB issued guidance to simplify the presentation of debt issuance costs. This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability. The Company adopted this standard retrospectively on January 1, 2016, which resulted in the reclassification of $258,000 of unamortized debt issuance costs related to Company borrowings from other assets to long-term debt within our condensed consolidated balance sheet as of December 31, 2015. The adoption also resulted in the reclassification of $3,000 from general expenses to interest expense for the three months ended March 31, 2015.

Disclosure about Short-Duration Contracts
In May 2015, the FASB issued guidance that enhances disclosure about short-duration insurance liabilities to help users understand the nature, amount, timing and uncertainty of future cash flows related to insurance liabilities and the effect of those cash flows on the statement of comprehensive income. The Company adopted this standard on January 1, 2016. Required disclosures will be included in the notes to consolidated financial statements included in the Company's 2016 Annual Report on Form 10-K and in interim reports beginning in 2017.

Simplifying the Accounting for Measurement-Period Adjustments
In September 2015, the FASB issued guidance that requires an acquirer to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The acquirer must record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The guidance requires an entity to present on the face of the income statement or to disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. The Company adopted this standard on January 1, 2016. This guidance did not have a material effect on results of operations or financial position.

NOTE 2 – VARIABLE INTEREST ENTITIES

The Company holds a passive interest in a limited partnership that is considered to be a Variable Interest Entity (VIE) under the provisions of ASC 810 Consolidation. The Company is not the primary beneficiary of the entity and is not required to consolidate under ASC 810. The entity is a private placement investment fund formed for the purpose of investing in private equity investments. The Company owns less than 1% of the limited partnership. The carrying value of the investment totals $228,000 and is included as a component of Other Invested Assets in the accompanying condensed consolidated balance sheets.

In December 2005, the Company formed National Security Capital Trust I, a statutory trust created under the Delaware Statutory Trust Act, for the sole purpose of issuing, in private placement transactions, $9,000,000 of trust preferred

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securities (TPS) and using the proceeds thereof, together with the equity proceeds received from the Company in the initial formation of the Trust, to purchase $9,279,000 of variable rate subordinated debentures issued by the Company. The Company owns all voting securities of the Trust and the subordinated debentures are the sole assets of the Trust. The Trust will meet the obligations of the TPS with the interest and principal paid on the subordinated debentures. The Company received net proceeds from the TPS transactions, after commissions and other costs of issuance, of $9,005,000. The Company also holds all the voting securities issued by the Trust and such trusts are considered to be VIE's. The Trust is not consolidated because the Company is not the primary beneficiary of the trust. The Subordinated Debentures, disclosed in Note 7, are reported in the accompanying condensed consolidated balance sheets as a component of long-term debt. The Company's equity investments in the Trust total $279,000 and are included in Other Assets in the accompanying condensed consolidated balance sheets.

In June 2007, the Company formed National Security Capital Trust II for the sole purpose of issuing, in private placement transactions, $3,000,000 of trust preferred securities (TPS) and using the proceeds thereof, together with the equity proceeds received from the Company in the initial formation of the Trust, to purchase $3,093,000 unsecured junior subordinated deferrable interest debentures. The Company owns all voting securities of the Trust and the subordinated debentures are the sole assets of the Trust. The Trust will meet the obligations of the TPS with the interest and principal paid on the subordinated debentures. The Company received net proceeds from the TPS transactions, after commissions and other costs of issuance, of $2,995,000. The Company also holds all the voting securities issued by the Trust and such trusts are considered to be VIE's. The Trust is not consolidated because the Company is not the primary beneficiary of the Trust. The Subordinated Debentures, disclosed in Note 7, are reported in the accompanying consolidated balance sheets as a component of long-term debt. The Company's equity investments in the Trust total $93,000 and are included in Other Assets in the accompanying condensed consolidated balance sheets.

NOTE 3 – INVESTMENTS

The amortized cost and aggregate fair values of investments in available-for-sale securities as of March 31, 2016 are as follows (dollars in thousands):

Available-for-sale securities:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Corporate debt securities	$ 38,378	$ 1,157	$ 1,173	$ 38,362
Mortgage backed securities	14,212	370	103	14,479
Private label asset backed securities	8,866	40	631	8,275
Obligations of states and political subdivisions	13,933	938	3	14,868
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	18,601	744	10	19,335
Total fixed maturities	93,990	3,249	1,920	95,319
Equity securities	2,420	2,747	110	5,057
Total	$ 96,410	$ 5,996	$ 2,030	$ 100,376

The amortized cost and aggregate fair values of investments in held-to-maturity securities as of March 31, 2016 are as follows (dollars in thousands):

Held-to-maturity securities:	Amortized Cost	Gross Unrealized	Gross Unrealized	Fair Value

		Gains	Losses	
Mortgage backed securities	$ 2,332	$ 102	$ —	$2,434
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	38	3	—	41
Total	$ 2,370	$ 105	$ —	$2,475

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(UNAUDITED AMOUNTS EXCEPT FOR DECEMBER 31, 2015 AMOUNTS)

The amortized cost and aggregate fair values of investments in available-for-sale securities as of December 31, 2015 are as follows (dollars in thousands):

Available-for-sale securities:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Corporate debt securities	$ 38,245	$ 747	$ 1,728	$37,264
Mortgage backed securities	15,324	157	224	15,257
Private label asset backed securities	6,029	24	380	5,673
Obligations of states and political subdivisions	14,654	869	47	15,476
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	17,825	413	96	18,142
Total fixed maturities	92,077	2,210	2,475	91,812
Equity securities	2,420	2,590	113	4,897
Total	$ 94,497	$ 4,800	$ 2,588	$96,709

The amortized cost and aggregate fair values of investments in held-to-maturity securities as of December 31, 2015 are as follows (dollars in thousands):

Held-to-maturity securities:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Mortgage backed securities	$ 2,395	$ 62	$ —	$2,457
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	44	3	—	47
Total	$ 2,439	$ 65	$ —	$2,504

The amortized cost and aggregate fair value of debt securities at March 31, 2016, by contractual maturity, are presented in the following table (dollars in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Dollars in Thousands)	Amortized Cost	Fair Value
Available-for-sale securities:		
Due in one year or less	$ 2,038	$2,069
Due after one year through five years	15,799	16,127
Due after five years through ten years	34,131	33,956
Due after ten years	42,022	43,167
Total	$ 93,990	$95,319
Held-to-maturity securities:		
Due in one year or less	$ —	$—
Due after one year through five years	66	69
Due after five years through ten years	99	108
Due after ten years	2,205	2,298
Total	$ 2,370	$2,475

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED AMOUNTS EXCEPT FOR DECEMBER 31, 2015 AMOUNTS)

A summary of securities available-for-sale with unrealized losses as of March 31, 2016, along with the related fair value, aggregated by the length of time that investments have been in a continuous unrealized loss position, is as follows (dollars in thousands):

	Less than 12 months		12 months or longer		Total		
March 31, 2016	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Total Securities in a Loss Position
Fixed maturities							
Corporate debt securities	$8,769	$ 284	$4,349	$ 889	$13,118	$ 1,173	25
Mortgage backed securities	2,393	79	710	24	3,103	103	11
Private label asset backed securities	4,985	414	1,790	217	6,775	631	10
Obligations of state and political subdivisions	—	—	339	3	339	3	1
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	995	3	352	7	1,347	10	3
Equity securities	—	—	1,176	110	1,176	110	1
	$17,142	$ 780	$8,716	$ 1,250	$25,858	$ 2,030	51

There were no securities held-to-maturity with unrealized losses as of March 31, 2016.

A summary of securities available-for-sale with unrealized losses as of December 31, 2015, along with the related fair value, aggregated by the length of time that investments have been in a continuous unrealized loss position, is as follows (dollars in thousands):

	Less than 12 months		12 months or longer		Total		
December 31, 2015	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Total Securities in a Loss Position
Fixed maturities							
Corporate debt securities	$18,205	$ 821	$3,783	$ 907	$21,988	$ 1,728	44
Mortgage backed securities	9,069	161	675	63	9,744	224	20
Private label asset backed securities	4,962	379	84	1	5,046	380	10
Obligations of state and political subdivisions	1,920	36	331	11	2,251	47	5
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	6,131	70	1,452	26	7,583	96	12
Equity securities	—	—	1,173	113	1,173	113	1
	$40,287	$ 1,467	$7,498	$ 1,121	$47,785	$ 2,588	92

There were no securities held-to-maturity with unrealized losses as of December 31, 2015.

The Company conducts periodic reviews to identify and evaluate securities in an unrealized loss position in order to identify other-than-temporary impairments. For securities in an unrealized loss position, the Company assesses whether the Company has the intent to sell the security or more-likely-than-not will be required to sell the security before the anticipated recovery. If either of these conditions is met, the Company is required to recognize an other-than-temporary impairment with the entire unrealized loss reported in earnings. For securities in an unrealized loss position that do not meet these conditions, the Company assesses whether the impairment of a security is other-than-temporary. If the impairment is determined to be other-than-temporary, the Company is required to separate the other-than-temporary impairments into two components: the amount representing the credit loss and the amount related to all other factors. The credit loss is the portion of the amortized book value in excess of the net present value of the projected future cash flows discounted at the effective interest rate implicit in the debt security prior to impairment. The credit loss component of other-than-temporary impairments is reported in earnings, whereas the amount relating to factors other than credit losses are recorded in other comprehensive income, net of taxes.

Management has evaluated each security in a significant unrealized loss position. The Company has no material exposure to sub-prime mortgage loans and less than 5.14% of the fixed income investment portfolio is rated below investment grade. In evaluating whether or not the equity loss positions were other-than-temporary impairments, Management evaluated financial information on each company and where available, reviewed analyst reports from at least two independent sources. Based on a review of the available financial information, the prospect for future earnings of each company and consideration of the Company's intent and ability to hold the securities until market values recovered, it was determined that the securities in an accumulated loss position in the portfolio were temporary impairments.

For the three months ended March 31, 2016 and year ended December 31, 2015, the Company realized no other-than-temporary impairments. At March 31, 2016, the single largest loss not realized as an impairment was in the bond portfolio and totaled $247,000. The second largest loss position was in the bond portfolio and totaled $245,000. The third largest loss position was in the bond portfolio and totaled $196,000. At December 31, 2015, the single largest loss not realized as an impairment was in the bond portfolio and totaled $252,000. The second largest loss position was in the bond portfolio and totaled $211,000. The third largest loss position was in the bond portfolio and totaled $186,000.

Major categories of investment income are summarized as follows (dollars in thousands):

	Three months ended March 31,	
	2016	2015
Fixed maturities	$901	$894
Equity securities	28	30
Mortgage loans on real estate	1	4
Investment real estate	2	2
Policy loans	32	29
Company owned life insurance change in surrender value	34	44
Other	49	42
	1,047	1,045
Less: Investment expenses	56	43
Net investment income	$991	$1,002

Major categories of realized investment gains and losses are summarized as follows (dollars in thousands):

	Three months ended March 31,	
	2016	2015
Fixed maturities	$17	$142
Other, principally real estate	(10)	—
Net realized investment gains	$7	$142

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An analysis of the net change in unrealized appreciation on available-for-sale securities follows (dollars in thousands):

	March 31, 2016	December 31, 2015
Net change in unrealized appreciation on available-for-sale securities before deferred tax	$1,754	$ (3,225)
Deferred income tax	(596)	1,097
Net change in unrealized appreciation on available-for-sale securities	$1,158	$ (2,128)

NOTE 4 – FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Our available-for-sale securities consists of fixed maturity and equity securities which are recorded at fair value in the accompanying consolidated balance sheets. The change in the fair value of these investments, unless deemed to be other-than-temporarily impaired, is recorded as a component of other comprehensive income.

We are permitted to elect to measure financial instruments and certain other items at fair value, with the change in fair value recorded in earnings. We elected not to measure any eligible items using the fair value option.

Accounting standards define fair value as the price that would be received to sell an asset or would be paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establishes a framework to make the measurement of fair value more consistent and comparable. In determining fair value, we primarily use prices and other relevant information generated by market transactions involving identical or comparable assets.

The Company categorizes assets and liabilities carried at their fair value based upon a fair value hierarchy:
Level 1 – Quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 1 assets and liabilities consist of money market fund deposits and certain of our marketable debt and equity instruments, including equity instruments offsetting deferred compensation, that are traded in an active market with sufficient volume and frequency of transactions.

Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 2 assets include certain of our marketable debt and equity instruments with quoted market prices that are traded in less active markets or priced using a quoted market price for similar instruments. Level 2 assets also include marketable equity instruments with security-specific restrictions that would transfer to the buyer, marketable debt instruments priced using indicator prices which represent non-binding market consensus prices that can be corroborated by observable market quotes, as well as derivative contracts and debt instruments priced using inputs that are observable in the market or can be derived principally from or corroborated by observable market data. Marketable debt instruments in this category generally include commercial paper, bank time deposits, repurchase agreements for fixed-income instruments, and a majority of floating-rate notes, corporate bonds, and municipal bonds.

Level 3 - Unobservable inputs to the valuation methodology that are significant to the measurement of fair value of assets or liabilities.

Level 3 assets and liabilities include marketable debt instruments, non-marketable equity investments, derivative contracts, and company issued debt whose values are determined using inputs that are both unobservable and significant to the values of the instruments being measured. Level 3 assets also include marketable debt instruments that are priced using indicator prices that we were unable to corroborate with observable market quotes.

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Marketable debt instruments in this category generally include asset-backed securities and certain floating-rate notes, corporate bonds, and municipal bonds.

Assets/Liabilities Measured at Fair Value on a Recurring Basis

Financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2016 are summarized in the following table by the type of inputs applicable to the fair value measurements (in thousands):

	Fair Value Measurements at Reporting Date Using			
Description	Total	Level 1	Level 2	Level 3
Financial Assets				
Fixed maturities available-for-sale				
Corporate debt securities	$38,362	$—	$38,362	$—
Mortgage backed securities	14,479	—	14,479	—
Private label asset backed securities	8,275	—	8,275	—
Obligations of states and political subdivisions	14,868	—	14,868	—
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	19,335	19,335	—	—
Trading securities	107	107	—	—
Equity securities available-for-sale	5,057	3,881	—	1,176
Total Financial Assets	$100,483	$23,323	$75,984	$1,176
Financial Liabilities				
Interest rate swap	$(1,574)	$—	$—	$(1,574)
Total Financial Liabilities	$(1,574)	$—	$—	$(1,574)

The methods and assumptions the Company uses to estimate the fair value of assets and liabilities measured at fair value on a recurring basis are summarized below.

Fixed maturities available-for-sale — The fair values of the Company’s public fixed maturity securities are generally based on prices obtained from independent pricing services. Consistent with the fair value hierarchy described above, securities with validated quotes from pricing services are generally reflected within Level 2, as they are primarily based on observable pricing for similar assets and/or other market observable inputs.

Trading securities — Trading securities consist primarily of mutual funds whose fair values are determined consistent with similar instruments described above under “Fixed Maturities” and below under “Equity Securities.”

Equity securities — Equity securities consist principally of investments in common and preferred stock of publicly traded companies and privately traded securities. The fair values of our publicly traded equity securities are based on quoted market prices in active markets for identical assets and are classified within Level 1 in the fair value hierarchy.

Estimated fair values for our privately traded equity securities require a substantial level of judgment. Privately traded equity securities are classified within Level 3.

Interest rate swaps — Interest rate swaps are recorded at fair value either as assets, within other assets or as liabilities, within other liabilities. The fair values of our interest rate swaps are provided by a third-party broker and are classified within Level 3.

As of March 31, 2016, Level 3 fair value measurements of assets include $1,176,000 of equity securities in a local community bank whose value is based on an evaluation of the financial statements of the entity. The Company does not develop the unobservable inputs used in measuring fair value.

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As of March 31, 2016, Level 3 fair value measurements of liabilities include $1,574,000 net fair value of various interest rate swap agreements whose value is based on analysis provided by a third party broker who utilizes financial modeling tools and assumptions on interest and other factors. The Company does not develop the unobservable inputs used in measuring fair value. Additional information regarding the interest rate swap agreements is provided in Note 7.

The table below presents a reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended March 31, 2016 (in thousands):

For the three months ended March 31, 2016	Equity Securities Available-for-Sale	Interest Rate Swap
Beginning balance	$ 1,173	$(1,419)
Total gains or losses (realized and unrealized):		
Included in earnings	—	—
Included in other comprehensive income	3	(155)
Purchases:	—	—
Sales:	—	—
Issuances:	—	—
Settlements:	—	—
Transfers in/(out) of Level 3	—	—
Ending balance	$ 1,176	$(1,574)
The amount of total gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets and liabilities still held as of March 31, 2016:	$ —	$—

For the three months ended March 31, 2016, there were no assets or liabilities measured at fair values on a nonrecurring basis.

Financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2015 are summarized in the following table by the type of inputs applicable to the fair value measurements (in thousands):

	Fair Value Measurements at Reporting Date Using			
Description	Total	Level 1	Level 2	Level 3
Financial Assets				
Fixed maturities available-for-sale				
Corporate debt securities	$37,264	$—	$37,264	$—
Mortgage backed securities	15,257	—	15,257	—
Private label asset backed securities	5,673	—	5,673	—
Obligations of states and political subdivisions	15,476	—	15,476	—
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	18,142	18,142	—	—
Trading securities	107	107	—	—
Equity securities available-for-sale	4,897	3,724	—	1,173

Total Financial Assets	$96,816	$21,973	$73,670	$1,173
Financial Liabilities				
Interest rate swap	$(1,419)	$—	$—	$(1,419)
Total Financial Liabilities	$(1,419)	$—	$—	$(1,419)

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The table below presents a reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2015 (in thousands):

For the year ended December 31, 2015	Equity Securities Available-for-Sale	Interest Rate Swap
Beginning balance	$ 1,116	$(1,238)
Total gains or losses (realized and unrealized):		
Included in earnings	—	—
Included in other comprehensive income	57	(181)
Purchases:	—	—
Sales:	—	—
Issuances:	—	—
Settlements:	—	—
Transfers in/(out) of Level 3	—	—
Ending balance	$ 1,173	$(1,419)
The amount of total gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets and liabilities still held as of December 31, 2015:	$ —	$—

For the year ended December 31, 2015, there were no assets or liabilities measured at fair values on a nonrecurring basis.

The Company is exposed to certain risks in the normal course of its business operations. The primary risk that is managed through the use of derivatives is interest rate risk on floating rate borrowings. This risk is managed through the use of interest rate swap agreements which are designated as cash flow hedges. For cash flow hedges, the effective portion of the gain or loss on the interest rate swap is included as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged transaction is recognized in earnings. The Company does not hold or issue derivatives that are not designated as hedging instruments. See Note 7 for additional information about the interest rate swap agreements.

The following methods and assumptions were used to estimate fair value of each class of financial instrument for which it is practical to estimate that value:

Cash and cash equivalents — the carrying amount is a reasonable estimate of fair value.

Fixed maturities held-to-maturity — the carrying amount is amortized cost; the fair values of the Company's public fixed maturity securities that are classified as held-to-maturity are generally based on prices obtained from independent pricing services.

Mortgage loans — the carrying amount is a reasonable estimate of fair value due to the restrictive nature and limited marketability of the mortgage notes.

Policy loans — the carrying amount is a reasonable estimate of fair value.

Company owned life insurance — the carrying amount is a reasonable estimate of fair value.

Other invested assets — the carrying amount is a reasonable estimate of fair value.

Other policyholder funds — the carrying amount is a reasonable estimate of fair value.

Debt — the carrying amount is a reasonable estimate of fair value.

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The carrying amount and estimated fair value of the Company's financial instruments as of March 31, 2016 and December 31, 2015 are as follows (in thousands):

	March 31, 2016		December 31, 2015	
Assets and related instruments	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Held-to-maturity securities	$2,370	$ 2,475	$2,439	$ 2,504
Mortgage loans	190	190	202	202
Policy loans	1,676	1,676	1,655	1,655
Company owned life insurance	4,932	4,932	4,898	4,898
Other invested assets	3,185	3,185	3,256	3,256
Liabilities and related instruments				
Other policyholder funds	1,584	1,584	1,561	1,561
Short-term notes payable and current portion of long-term debt	857	857	857	857
Long-term debt	17,102	17,102	17,100	17,100

NOTE 5 – PROPERTY AND EQUIPMENT

Major categories of property and equipment are summarized as follows (dollars in thousands):

	March 31, 2016	December 31, 2015
Building and improvements	$ 3,348	$ 3,350
Electronic data processing equipment	1,726	1,631
Furniture and fixtures	533	529
	5,607	5,510
Less accumulated depreciation	3,603	3,564
Property and equipment, net	$ 2,004	$ 1,946

Depreciation expense for the three months ended March 31, 2016 was $39,000 ($168,000 for the year ended December 31, 2015).

NOTE 6 – INCOME TAXES

The Company recognizes tax-related interest and penalties as a component of tax expense. The Company files income tax returns in the U.S. federal jurisdiction and various states. The Company is not subject to examinations by authorities related to its U.S. federal or state income tax filings for years prior to 2010. Tax returns have been filed through the year 2014.

Net deferred tax liabilities are determined based on the estimated future tax effects of differences between the financial statement and tax basis of assets and liabilities given the provisions of the enacted tax laws. Management believes that, based on its historical pattern of taxable income, the Company will produce sufficient income in the future to realize its deferred tax assets. The Company recognized net deferred tax asset positions of $3,141,000 at March 31, 2016 and $3,824,000 at December 31, 2015.

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The tax effect of significant differences representing deferred tax assets and liabilities are as follows (dollars in thousands):

	As of March 31, 2016	As of December 31, 2015
General expenses	$1,487	$ 1,569
Unearned premiums	2,082	2,039
Claims liabilities	724	730
Litigation settlement	1,748	1,748
AMT credit	742	816
Impairment on real estate owned	187	187
Unrealized loss on interest rate swaps	535	483
Deferred tax assets	7,505	7,572
Depreciation	(112)	(111)
Deferred policy acquisition costs	(2,904)	(2,885)
Unrealized gains on securities available-for-sale	(1,348)	(752)
Deferred tax liabilities	(4,364)	(3,748)
Net deferred tax asset		