Heritage Insurance Holdings, Inc.
Form 10-K
March 08, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Year Ended December 31, 2015

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 001-36462

Heritage Insurance Holdings, Inc.

Delaware	45-5338504
(STATE OF INCORPORATION)	(I.R.S. ID)

2600 McCormick Drive, Suite 300, Clearwater, Florida 33759

(727) 362-7200

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.0001 per share	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 o No x

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) 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. o

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	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 o No x

The aggregate market value of the Registrant's common stock held by non-affiliates was $593,101,859 on June 30, 2015, computed on the basis on the closing sale price of the Registrant's common stock on the New York Stock Exchange on that date.

As of March 1, 2016, the number of shares outstanding of the Registrant's common stock was 30,441,410.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement for its Annual Meeting of Stockholders are incorporated by reference into Part III of this Annual Report on Form 10-K, provided that if such Proxy Statement is not filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year covered by this Form 10-K, an amendment to this Form 10-K shall be filed no later than the end of such 120-day period.

HERITAGE INSURANCE HOLDINGS, INC.

FORM 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2015

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This Annual Report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws. These forward-looking statements include, but are not limited to, statements regarding: our core strategy; our growth, results of operations or liquidity; statements concerning projections, predictions, expectations, estimates or forecasts as to our business, financial and operational results and future economic performance; statements of management’s goals and objectives; projections of revenue, earnings, capital structure and other financial items; assumptions underlying statements regarding us and our business; and other similar expressions concerning matters that are not historical facts. These forward-looking statements are subject to risks and uncertainties that could cause actual results and events to differ. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included throughout this filing and particularly in Item 1A: "Risk Factors" and Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” set forth in this Annual Report on Form 10-K. All forward-looking statements included in this document are based on information available to us on the date hereof, and we assume no obligation to revise or publicly release any revision to any such forward-looking statement, except as may otherwise be required by law.

These statements are based on current expectations, estimates and projections about the industry and market in which we operate, and management’s beliefs and assumptions. Without limiting the generality of the foregoing, words such as “may,” “will,” “expect,” “believe,” “anticipate,” “intend,” “could,” “would,” “estimate,” or “continue” or the negative variat or comparable terminology are intended to identify forward-looking statements. Forward-looking statements are not guarantees of future performance and involve certain known and unknown risks and uncertainties that could cause actual results to differ materially from those expressed or implied by such statements. The risks and uncertainties include, without limitation:

- our limited operating history;
- the possibility that actual losses may exceed reserves;
- the concentration of our business in Florida;
- our exposure to catastrophic events;
- the fluctuation in our results of operations;
- the discontinuation of the Citizens depopulation program and our inability to select favorable Citizens policies to assume;
- increased costs of reinsurance, non-availability of reinsurance, and non-collectability of reinsurance;
- increased competition, competitive pressures, and market conditions;
- our failure to accurately price the risks we underwrite;
- inherent uncertainty of our models and our reliance on such model as a tool to evaluate risk;
- the failure of our claims department to effectively manage or remediate claims;
- low renewal rates and failure of such renewals to meet our expectations;
- our failure to execute our growth strategy;
- failure of our information technology systems and unsuccessful development and implementation of new technologies;
- we do not have significant redundancy in our operations;
- our failure to attract and retain qualified employees and independent agents or our loss of key personnel;
- our inability to generate investment income;
- our inability to maintain our financial stability rating;
- effects of emerging claim and coverage issues relating to legal, judicial, environmental and social conditions;
- the failure of our risk mitigation strategies or loss limitation methods; and
- changes in regulations and our failure to meet increased regulatory requirements.

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

The forward-looking statements speak only as of the date on which they are made, and, except as required by law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrences of anticipated events. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in the forward-looking statements. Consequently, you should not place undue reliance on forward-looking statements.

PART I

Item 1. Business

Our Business

Heritage Insurance Holdings, Inc., ("we", "our", "us" and "Heritage Insurance") is a property and casualty insurance holding company that provides personal and commercial residential insurance. We are headquartered in Clearwater, Florida and, through our subsidiary, Heritage Property & Casualty Insurance Company ("Heritage P&C"), we provide personal residential insurance for single-family homeowners and condominium owners, rental property insurance and commercial residential insurance in the state of Florida and North Carolina. We are vertically integrated and control or manage substantially all aspects of insurance underwriting, customer service, actuarial analysis, distribution and claims processing and adjusting. We are led by an experienced senior management team with an average of 31 years of insurance industry experience. We began operations in August 2012, and in December 2012 we began selectively assuming policies from Citizens Property Insurance Corporation ("Citizens"), a Florida state-supported insurer, through participation in a legislatively established "depopulation program" designed to reduce the state's risk exposure by encouraging private companies to assume insurance policies from Citizens. We also write policies outside the Citizens depopulation program, which we refer to as voluntary policies. Heritage P&C is currently rated "A" ("Exceptional") by Demotech, Inc. ("Demotech"), a rating agency specializing in evaluating the financial stability of insurers.

In addition to Heritage P&C, our other subsidiaries include: Heritage MGA, LLC, the managing general agent that manages substantially all aspects of our insurance subsidiary's business; Contractors' Alliance Network, LLC, ("CAN") our vendor network manager that also houses with BRC Restoration Specialists Inc. ("BRC"), our provider of restoration, emergency and recovery services; Skye Lane Properties, LLC, our property management subsidiary; First Access Insurance Group, LLC, our retail agency; Osprey Re Ltd ("Osprey"); our reinsurance subsidiary that provides a portion of the reinsurance protection purchased by our insurance subsidiary; and Heritage Insurance Claims, LLC an inactive subsidiary reserved for future development. The assets of BRC, a building restoration company, were acquired and merged into CAN in 2015. The assets of SVM Restoration Services Inc., ("SVM"), a water mitigation company, were acquired and merged into CAN in 2014.

Our Company

Our company was initially formed as a Florida limited liability company in 2012. On January 1, 2014, we formed a Delaware limited liability company, also named Heritage Insurance Holdings, LLC, and merged with it in order to domicile the Company in Delaware. Effective May 22, 2014, Heritage Insurance Holdings, LLC converted into a Delaware corporation named Heritage Insurance Holdings, Inc.

Our primary products are personal and commercial residential insurance, which at December 31, 2015 were offered only in Florida under authorization from the Florida Office of Insurance Regulation ("FLOIR"). We conduct our operations under one business segment.

As of December 31, 2015, we had 253,726 personal residential policies in force, representing $478.0 million of annualized premium and 3,405 commercial residential policies in force, representing $113.5 million of annualized premium. Approximately 75% of our personal policies and 72% of our commercial policies as of December 31, 2015 were assumed from Citizens. For the years ended December 31, 2015 and 2014, we had gross premiums written of $586.1 million and $436.4 million, respectively, and net income of $92.5 million and $47.1 million, respectively. At December 31, 2015, we had total assets of $837.4 million and total stockholders' equity of $356.6 million.

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As of December 31, 2015, Citizens had approximately 504,000 insurance policies, of which approximately 480,000 were personal residential policies and approximately 8,300 were commercial residential policies. We have selectively assumed personal residential policies from Citizens in 22 separate assumption transactions between December 2012 and December 2015, including 10 in 2015. In October 2014 we completed our first commercial residential assumption transaction. A substantial portion of our revenue since our inception has come from these assumed policies. We intend to continue assuming policies from Citizens that meet our assumption strategy and underwriting criteria. However, given the reduced policy count at Citizens resulting from the depopulation program, we do not anticipate future assumptions to yield as many policies as historical assumption transactions.

In order to assume a policy from Citizens, we must obtain the prior approval of the insurance agent that wrote the policy. With respect to policies written by agents that are affiliated with an insurance company or agency, we must also obtain the approval of the insurance company or agency. Currently, four large national insurance companies or agencies permit us to assume policies from Citizens that have been written by their agents—State Farm, Allstate, Brown & Brown and AAA (formerly the American Automobile Association). In an effort to increase the pool of Citizens policies that we may assume, we are seeking similar advance approvals from other insurance companies and agencies. We currently have advance approvals covering more than 5,200 agents. These agents were responsible for writing more than 85% of the eligible personal residential insurance policies held by Citizens as of December 31, 2015.

Recent Developments

On September 29, 2015, the Company entered into a definitive agreement to acquire Zephyr Acquisition Company (“ZAC”) and its wholly-owned subsidiaries, HI Holdings, Inc. and Zephyr Insurance Company, Inc. (“Zephyr”), a specialty insurance provider in Hawaii that writes residential property insurance policies that covers the peril of wind. The acquisition will provide Heritage with an immediate presence in Hawaii with Zephyr holding approximately 30% of the wind-only market share in the state. The purchase price for the acquisition is approximately $120.0 million.

On September 14, 2015, the Company announced that the Board of Directors authorized a $20 million share repurchase program under which purchases may be made from time to time in the open market, or through privately negotiated transactions, block transactions or other techniques, as determined by the Company’s management. This program is available through December 31, 2016. To date, no shares have been repurchased.

In August 2015, the Company announced it received its certificate of Authority (“COA”) to write property and casualty insurance in the state of North Carolina. North Carolina marks the beginning of the Company’s multi-state expansion. The Company wrote its first policy in North Carolina in January 2016. The Company also was received its COA in South Carolina. The Company has been approved in Alabama and Mississippi. The Company has also submitted applications Massachusetts and Georgia.

In July 2015, the Company acquired substantially all of the assets of BRC, a Florida based provider of restoration services and emergency and recovery assistance. At closing, Company paid $6.0 million in cash and 79,850 shares of the Company’s common stock valued at $2.0 million.

Our Strategy

Since our inception, a substantial portion of our revenue has come from policies we assumed from Citizens and Sunshine State Insurance Company (“SSIC”), with the balance of our revenue generated from renewal of these assumed policies and from voluntary policies. Building on these successful transactions, we intend to continue to grow profitably by undertaking the following:

Increase Our Policies in Force in Florida Through Strategic Policy Assumptions and Expansion of Our Voluntary Market Share

We intend to continue assuming policies from Citizens that meet our assumption strategy and underwriting criteria. We also expect continue to pursue opportunities to acquire policies from private insurers. We will also pursue opportunities to increase the number of our voluntary policies by expanding our independent agent distribution network, as well as obtaining approval from national insurance companies to allow their agents to offer our personal residential policies in Florida. We entered into a marketing agreement with National General Insurance Company and began writing homeowners insurance through their distribution network in early 2016 in the state of North Carolina. We also intend to increase our marketing efforts, which we believe will allow us to more effectively penetrate areas of the state where we are not currently writing significant new business.

Opportunistically Diversify Product Offerings

We will continue to grow our commercial residential business, which we launched in the fourth quarter of 2014 with assumption transactions from Citizens, as well as through voluntary sales. As of December 31, 2015, our commercial residential policies represented approximately $113.4 million of in-force premium, which included $66.0 million from Citizens assumptions. We anticipate most of our future growth in commercial residential will come from voluntary sales, as we have already selected most of the commercial policies that meet our underwriting criteria from Citizens. In the fourth quarter of 2014, we also entered into the manufactured housing line of business by assuming approximately 10,100 policies from Citizens. Additional new product lines may include non-residential coverage, such as general liability insurance. We have had no growth in manufacturing housing during 2015, nor do we anticipate any future growth.

Optimize Our Reinsurance Program

We will continue to obtain what we believe to be the most appropriate levels and sources of reinsurance. We believe that the significant additional capital entering portions of the reinsurance market provides us with the opportunity to obtain favorable pricing and contract terms and conditions, including multi-year commitments, which comprise a significant portion of our 2015-2016 reinsurance program. In April 2014 and 2015, we entered into fully collateralized catastrophe reinsurance agreements funded through the issuance of a total of $478.0 million principal amount of catastrophe bonds, and we will continue evaluating such cost-efficient alternatives to traditional reinsurance. Additionally, we will continue to meet certain of our reinsurance needs through the use of our reinsurance subsidiary, Osprey, which mitigates our reinsurance expense and reduces our reliance on third-party reinsurance.

Efficiently Manage Losses and Loss Adjustment Expenses

We are committed to proactively managing our losses and loss adjustment expenses through prudent underwriting and the use of internal claims adjustment and repair services. In March 2014, we acquired the largest vendor in the CAN network, which we believe has allowed us to expand our in-house mitigation and restoration services. We are licensing our CAN employees as adjusters, which we believe will reduce our loss adjustment expenses and shorten the length of time required to resolve claims. Additionally, the acquisition of assets of BRC provides us with additional resources and capabilities to perform restoration services in-house, as well as provide construction resources after a catastrophic event.

Expand to New Geographic Markets

We intend to explore opportunities to enter other coastal states where we believe the market opportunity is most similar to Florida and where we can utilize our underwriting and claims expertise to attract and manage profitable business. We believe further increasing our geographic diversification is an important factor in reducing our potential risk of loss from any catastrophic event, reducing our per policy reinsurance costs and providing an additional area for future growth beyond our expansion in Florida. In 2015, we received COA to write property and casualty insurance in the states of North Carolina and South Carolina. We received approvals to write property and casualty insurance in the states of Alabama and Mississippi in 2016. We also have submitted applications in Massachusetts and Georgia.

Our Competitive Strengths

We believe that our rapid growth to date and our ability to capitalize on our future growth prospects are a result of the following competitive strengths of our business:

Experienced Management Team With a Long History in the Florida Personal Residential Insurance Market

We have a deep and experienced management team led by Bruce Lucas, Chairman and Chief Executive Officer, Richard Widdicombe, President, Stephen Rohde, Chief Financial Officer, Melvin Russell, Chief Underwriting Officer, Ernesto Garateix, Chief Operating Officer, Sharon Binnun, Executive Vice President Finance, Paul Nielsen, Vice President of Claims, Joseph Peiso, Vice President of Compliance, Randy Jones, President Commercial Division and Arlene Luis, Executive Vice President Commercial. Our management team, which averages 31 years of insurance industry experience, has extensive experience in the Florida personal and commercial residential insurance market, has built longstanding relationships with key participants in the insurance industry and is supported by a group of highly qualified individuals with industry expertise, including a Chief Actuary with more than 36 years of industry experience.

Strong, Conservative Capital Structure

As of December 31, 2015, we had stockholders’ equity of $356.6 million. As of December 31, 2015, Heritage P&C had policyholder surplus, as defined by statutory accounting principles, of $216.6 million. We believe that this level of surplus places us among the best capitalized insurance companies focusing primarily on the Florida personal residential insurance market and is significantly in excess of the minimum capital levels required by FLOIR and Demotech for similarly rated in-state insurance companies. In addition, unlike many of our in-state competitors, we have relied exclusively upon common equity to provide our capital.

Selective Underwriting and Policy Acquisition Criteria

We believe our proprietary data analytics capabilities and underwriting processes allow us to better select the insurance policies we are willing to assume from the Citizens depopulation program, leading to strong profitability and reduced risk. In addition, we choose to minimize our exposure to or avoid certain types of coverage if we believe there is significant risk of loss, including coverage for sink-hole related losses in high-risk areas. As a result of our efforts, our gross loss ratio was 26.9% and 28.7% for the years ended December 31, 2015 and 2014, respectively.

Unique Claims Servicing Model and Superior Customer Service

We believe that the vertical integration of our claims adjustment and repair services provides us with a competitive advantage. Because we manage both claims adjusting and repair services, we are generally able to begin the adjustment and mitigation process much earlier than our competitors, thus reducing our loss adjustment expenses and ultimate loss payouts. A significant number of our repair technicians are participating in training and certification programs to become licensed claims adjusters (eight out of the nineteen are now licensed), allowing us to capture additional efficiencies. We also believe our unique model provides a superior level of customer service for our policyholders, enhancing our reputation and increasing the likelihood that our policyholders will renew their policies with us.

Relationships with Highly Rated Reinsurers

We manage our exposure to catastrophic events through, among other things, the purchase of reinsurance. Our relationships with highly rated reinsurers have been developed as a result of our management team’s industry experience and reputation for selective underwriting. Our financial strength, underwriting results and the long-term relationships between our management team and our reinsurance partners help improve the cost-effectiveness of our reinsurance program.

Relationships with Independent Agents and National Underwriters

We have developed relationships with a network of approximately 3,500 independent insurance agents. We believe we have been able to build this network due to our reputation for financial stability, commitment to the Florida market and integrity in the underwriting and claims process. We are also exploring relationships with additional large national insurers and agencies that no longer write substantial personal residential insurance in Florida, which would give us access to their network of Florida agents.

Our Competition

The market for residential property insurance is highly competitive. In Florida, our primary market there are over 164 licensed insurance companies that are actively writing homeowners’ policies. The table below shows year-to-date in-force premium volume and market share for the top 20 companies in Florida as of September 30, 2015, which is the most recent date for which this information is publicly available. We compete to varying degrees with all of these companies and others, including large national carriers, the state-sponsored homeowners’ insurance entity, and single state or regional carriers.

Florida Property Insurance Market - Personal Residential and Commercial Residential - Ranked by Total Premiums Written.*

Company Name [1]	Policies In Force	Total Premiums Written	% of Distribution

CITIZENS PROPERTY INSURANCE CORPORATION	557,378	$	1,131,976,454	11.11%
UNIVERSAL PROPERTY & CASUALTY INSURANCE COMPANY	544,681		817,920,814	8.03%
HERITAGE PROPERTY & CASUALTY INSURANCE COMPANY	247,221		525,973,280	5.16%
FEDERATED NATIONAL INSURANCE COMPANY	231,828		416,422,753	4.09%
HOMEOWNERS CHOICE PROPERTY & CASUALTY INSURANCE COMPANY, INC.	163,808		404,728,434	3.97%
UNITED PROPERTY & CASUALTY INSURANCE COMPANY	172,422		320,886,191	3.15%
AMERICAN COASTAL INSURANCE COMPANY	4,653		320,682,697	3.15%
SECURITY FIRST INSURANCE COMPANY	265,132		288,617,942	2.83%
UNITED SERVICES AUTOMOBILE ASSOCIATION	123,922		281,568,543	2.76%
PEOPLE'S TRUST INSURANCE COMPANY	146,128		272,211,596	2.67%
FLORIDA PENINSULA INSURANCE COMPANY	119,370		267,975,059	2.63%
ST. JOHNS INSURANCE COMPANY, INC.	169,266		263,099,788	2.58%
AMERICAN INTEGRITY INSURANCE COMPANY OF FLORIDA	209,581		242,634,183	2.38%
TOWER HILL PRIME INSURANCE COMPANY	144,845		236,987,264	2.33%
FIRST PROTECTIVE INSURANCE COMPANY	76,973		208,861,567	2.05%
FEDERAL INSURANCE COMPANY	32,456		183,529,011	1.80%
TOWER HILL SIGNATURE INSURANCE COMPANY	93,696		159,136,687	1.56%
AIG PROPERTY CASUALTY COMPANY	14,177		151,703,381	1.49%
OLYMPUS INSURANCE COMPANY	85,406		150,839,928	1.48%
USAA CASUALTY INSURANCE COMPANY	57,770		138,740,749	1.36%
Total - Top 20 Insurers	3,460,713	$	6,784,496,321	66.60%
Total - All Insurers	5,965,572	$	10,187,690,519	100%

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(1) This exhibit excludes State Farm Florida Insurance Company, whose data was not publicly available on September 30, 2015.

* The information displayed in the table above is compiled and published by the Florida Office of Insurance Regulation based on information filings submitted quarterly by all Florida licensed insurance companies. The information above is presented for each individual company and is not consolidated or aggregated.

Products and Distribution

We market and write personal lines voluntary policies through a network of approximately 1,400 independent agents. Of these agents, approximately 56% are affiliated with eight large agency networks with which we have entered into master agency agreements. We intend to pursue additional voluntary business from agents in our existing independent agent network, expand our independent agent network and seek additional opportunities to use insurer-affiliated agents to offer our personal residential policies in Florida. We had 40,131 voluntary policies (15.6% of our total policies in force) as of December 31, 2015, and for the year ended December 31, 2015, we wrote an average of 1,920 new voluntary policies per month. We entered into a marketing agreement with National General Insurance Company and began writing homeowners insurance through their distribution network in early 2016 in the state of North Carolina. The voluntary market is a significant component of our growth strategy.

We market and write commercial residential voluntary policies through a network of approximately 60 independent agents. We intend to pursue additional voluntary business from these agents in our existing independent agent network, expand our independent agent network and seek additional opportunities to increase our commercial residential policies in Florida. We started writing voluntary policies in October 2014. For the year ended December 31, 2015, we wrote 898 policies with an average premium of $50,704, totaling $45.5 million in new voluntary policies. The commercial voluntary market is a major component of our commercial growth strategy.

We seek to underwrite a diverse mix of geographic risks within Florida to manage the potential impact of a catastrophic event and reduce our per policy reinsurance costs. As of December 31, 2015, the geographic distribution of our policies in force and total insured values were as follows (figures may not sum to totals due to rounding):

	As of December 31, 2015 (Total Insured Value in Millions)		
	Total All Lines		
	Policy Count	Total Insured Value (TIV) $	% TIV
South Florida Counties			
Miami-Dade	37,641	$ 15,365	16.2 %
Broward	31,804	15,875	16.7 %
Palm Beach	22,244	9,457	10.0 %
South Florida Exposure	91,689	$ 40,697	42.9 %
Other Significant Counties(1)			
Pinellas	29,012	$ 9,661	10.2 %
Hillsborough	20,605	6,283	6.6 %
Pasco	13,503	3,619	3.8 %
Lee	13,143	4,744	5.0 %
Sarasota	9,686	3,142	3.3 %

Collier	7,144	3,019	3.2 %
Manatee	6,481	2,530	2.7 %
Total Other Significant Counties	99,574	$ 32,998	34.8 %
Summary for all of Florida			
South Florida Exposure	91,689	$ 40,697	42.9 %
Total Other Significant Counties	99,574	32,998	34.8 %
Other Florida Counties	65,868	21,171	22.3 %
TOTAL	257,131	$ 94,866	100.0%

(1) Other significant counties are defined as those counties with a total insured value greater than 2.0% of the $94.9 billion of total insured value as of December 31, 2015. This amount includes policies that do not cover the peril of wind.

In order to limit our potential exposure to individual risks and catastrophic events, we purchase significant reinsurance from third party reinsurers. Purchasing reinsurance is an important part of our risk strategy, and premiums paid (or ceded) to reinsurers is our single largest cost. We have strong relationships with reinsurers which we believe are a result of our management's industry experience and reputation for selective underwriting and effective claim management. For the twelve months beginning June 1, 2014 and 2015, we purchased catastrophe reinsurance from the following sources: (i) the Florida Hurricane Catastrophe Fund, a state-mandated catastrophe fund (“FHCF”), (ii) private reinsurers, all of which were rated “A-” or higher by A.M. Best Company, Inc. (“A.M. Best”) or Standard & Poor’s Financial Services LLC (“S&P”), (iii) sponsorship of multiple catastrophe bonds that provide $478 million of principal limit that can be drawn upon over a three year period, and (iv) our wholly-owned reinsurance subsidiary, Osprey. In addition to purchasing catastrophe reinsurance, we also purchased property risk reinsurance which limits our net exposure in the event of a severe non-catastrophe loss impacting a single location or risk to $1.0 million. We also utilize facultative reinsurance to supplement our per risk reinsurance program where our capacity needs dictate. See “-Reinsurance – 2015 – 2016 Catastrophe Reinsurance Program”.

The FLOIR requires all insurance companies, like us, to have a certain amount of capital reserves and reinsurance coverage in order to cover losses upon the occurrence of a catastrophic event. Our reinsurance program for the twelve months beginning June 1, 2014 and 2015 provides reinsurance in excess of FLOIR’s requirements, which are based on the probable maximum loss that we would incur from an individual catastrophic event estimated to occur once every 100 years based on our portfolio of insured risks. We also purchase reinsurance coverage to protect against the potential for multiple catastrophic events occurring in the same year.

We test the sufficiency of our reinsurance program by subjecting our personal and commercial residential exposures to statistical testing using the AIR U.S. Hurricane Model, which replicates the most severe hurricanes to have occurred historically in Florida, individual storms of severity in excess of such historical levels, and the historical calendar years in which the most severe multiple catastrophic events occurred in Florida. In this regard, the 2004 calendar year, in which four large catastrophic hurricanes made landfall in Florida, is considered to be the worst catastrophic year in Florida’s recorded history. Assuming the reoccurrence of the 2004 calendar year events, the probable maximum net loss to us in 2015, based on the coverage for our 2015-2016 reinsurance program, would be $36.9 million (after tax, net of all reinsurance recoveries and including our retention through Osprey). This loss would have represented 10.4% of our stockholders’ equity at December 31, 2015.

We closely manage all aspects of our claims adjustment process. Claims are initially reviewed by our managers and staff adjusters, who determine the extent of the loss and the resources needed to adjust each claim. In the case of a catastrophic event, we have contracted with four large national claims adjusting firms to assist our adjusters with the increased volume of claims and ensure timely responses to our policyholders. We utilize our wholly-owned subsidiary, CAN, to manage mitigation and restoration services for our customers. CAN primarily handles water damage-related claims, which comprised approximately 73% of our losses and loss adjustment expenses through December 31, 2015. In March 2014, we completed the acquisition of the assets and personnel of our main water mitigation services vendor. This acquisition has allowed us to better service our customers and expand our mitigation and restoration services. In addition, all of our voluntary policies and renewed Citizens policies are enrolled in our Platinum Preferred Savings Program (the “Platinum Program”). Under the Platinum Program, customers receive a 10% discount on their claim deductible, and we obtain control over inspection, claims adjusting and repair services. We believe our approach to claims handling results in a higher level of customer service and reduces our losses and loss adjustment expenses. As a result of our efforts, our gross loss ratio, which expresses our losses and loss adjustment expenses as a percentage of gross earned premiums, was 26.9% and 28.7% for the years ended December 31, 2015 and 2014, respectively. In addition, we utilize our recent acquisition, BRC, to manage and provide restoration services to CAN customers for all types of claims. BRC currently provides services for non-insurance related projects which we expect to decrease in future periods.

Our Market

According to the U.S. Census Bureau, at December 23, 2014, Florida was the third largest U.S. state with an estimated population of approximately 20 million people. The University of Florida Bureau of Economic and Business Research estimates that Florida is expected to reach a population of approximately 26 million people by 2040, an increase of

36% from 2010. Property ownership and development represent key drivers of the Florida economy.

Because of its geography, Florida is exposed to an increased risk of hurricanes during the entire six months of the Atlantic hurricane season, which spans from June 1 through November 30. While a significant hurricane has not made landfall in Florida since 2005, eight hurricanes in 2004 and 2005, including Hurricanes Charley, Katrina, Rita and Wilma, caused a combined estimated property damage of over $110 billion, a significant portion of which occurred in Florida. As a result, personal residential insurance and claims servicing are vitally important to Florida residents.

The Florida residential insurance market is highly fragmented and dominated by in-state insurance companies, including Citizens. Significant dislocation in the Florida property insurance market began following Hurricane Andrew in 1992 and accelerated following the 2004 and 2005 hurricane seasons. In total, national and regional insurers reduced their share of the market in Florida from 84% in 1999 to 26% in 2012. As national and regional insurance companies reduced their exposure in Florida, Citizens increased efforts to provide affordable residential insurance to those residents unable to obtain coverage in the private market. As a result, Citizens' policy count grew from roughly 726,000 policies in 2005 to a peak level of approximately 1.5 million policies in late 2011.

To reduce Citizens' risk exposure, beginning in 2010, Florida elected officials encouraged Citizens to focus on reducing the size of its portfolio by returning policies to the private market. In response, Citizens instituted a number of measures to incentivize the private sector to participate in the depopulation program. Some of these initiatives include increased inspections, improved underwriting, reductions in coverage and annual rate increases. Depopulation efforts have been successful, as Citizens' policy count at December 31, 2015 was approximately 504,000. As of December 31, 2015, approximately 192,000 of Heritage's in force policies were assumed through the depopulation program.

According to data compiled by FLOIR, which excludes State Farm Florida Insurance Company, Citizens was the largest residential insurance carrier in Florida as of September 30, 2015, with a market share of approximately 11.1% based on total in force direct premiums written for personal and commercial residential insurance. As of the same date, we ranked third in Florida within this market, with a market share of approximately 5.2%, and through our depopulation efforts, we have grown substantially since inception in 2012. Assuming further access to capital and reinsurance support, we believe we have the opportunity to significantly expand the size of our personal and commercial residential insurance business in Florida and of our business into other complementary business lines and states. In 2015, we received our COA to write property and casualty insurance in the state of North and South Carolina. We received approval to write property and casualty insurance in Alabama and Mississippi. We have also submitted applications in Massachusetts and Georgia.

In recent years, the property and casualty insurance market has experienced a substantial increase in the availability of property catastrophe reinsurance resulting from the increased supply of capital from non-traditional insurance providers, including private capital and hedge funds. This increased capital supply, coupled with a lack of recent significant catastrophic storm activity in Florida, has reduced the cost of property catastrophe reinsurance, directly benefitting purchasers of this reinsurance, including us.

Underwriting

Our underwriters evaluate and select only those risks that they believe will enable us to achieve an underwriting profit. In order to achieve underwriting profitability on a consistent basis, we focus on (1) the suitability of the risk to be assumed or written, (2) the adequacy of the premium with regard to the risk to be assumed or written and (3) the geographic distribution of existing policies within Florida.

All of our personal lines underwriting is done internally under the supervision of our Chief Underwriting Officer with input from our Chief Actuary and our Director of Risk Management. Our commercial lines underwriting is done internally under the supervision of our Executive Vice President Commercial Division. Our underwriters use our proprietary data analytics capabilities, which include a number of automated processes, to analyze a number of risk evaluation factors, including the age, construction, location and value of the residence and the premiums to be received from insuring the residence. New technological advances in computer generated geographical mapping afford us an enhanced perspective as to geographic concentrations of policyholders. When considering the geographic distribution of existing policies, our underwriters may consider the number of other residences we insure within the same region, county, city and zip code. We also consider the cost of reinsurance when assessing the adequacy of the premium with regard to the risk to be assumed or written. In particular, because we assume policies from Citizens in large quantities, we must evaluate the aggregate impact of the assumed policies on our reinsurance program. The underwriting criteria that we consider will continue to evolve as our business grows and expands.

We also review our expiring policies to determine whether those risks continue to meet our underwriting guidelines. If a given policy no longer meets our underwriting guidelines, we will take appropriate action regarding that policy, including raising premium rates or, to the extent permitted by applicable law and our assumption agreements with Citizens, not offering to renew the policy.

Policy Administration

We have engaged West Point Underwriters, Inc. and Majesco Mastec, providers of web-based software solutions and insurance personnel, to provide us with policy administration services for our business, including processing, billing and policy maintenance. The software is able to adapt to a variety of forms and rates, handle the administration of an increasing number of policies as our Company grows and expands, and provide detailed information about our book of business to our internal underwriters so that they can adjust our underwriting criteria as necessary. The software provides us with daily updates regarding the insurance policies that we have issued. The systems also allow us to provide renewal notices, late payment notices, cancellation notices, endorsements and policies to our policyholders in a timely fashion.

Claims Administration

We closely manage all aspects of the claims process, from processing the initial filing to providing remediation services through our wholly-owned subsidiary, CAN. When a policyholder contacts us to report a claim, members of our claims department create a claim file and aggregate the appropriate supporting documentation. Claims are then reviewed by our managers and staff adjusters, who assess the extent of the loss, including through on-site investigations, and determine the resources needed to adjust each claim. Our claims are generally adjusted by our staff claims professionals, except in the case of a catastrophic event for which we have contracted with four large national claims adjusting firms to assist our adjusters with the increased volume of claims and ensure timely responses to our policyholders. In the final stage of the claims process, we leverage CAN vendor network to provide repair and remediation services to the policyholder.

We perform or supervise the services rendered to our policyholders at all stages of the claims process, which we believe allows us to reduce cost and provide a high level of customer service to our policyholders. To encourage our policyholders to allow us to manage their claims from beginning to end, we developed our Platinum Program. Under the Platinum Program, participating customers receive a 10% discount on their claim deductible, and we obtain control over inspection, claims adjusting and repair services, with the repair services being managed by either CAN or one of our contracted vendors. In March 2014, we acquired the largest vendor in the CAN network, which has allowed us to expand our in-house mitigation and restoration services. In August 2015, we acquired BRC to allow us to further expand our restoration services.

Citizens Assumption Transactions

As of December 31, 2015, we have assumed, net of cancellations, an aggregate of approximately 192,000 policies through participation in the Citizens depopulation program. Citizens generally offers depopulations on a monthly basis. From December 2012 through December 2015, we participated in 22 depopulations. We have also been approved for depopulation during the first quarter of 2016 and continue to seek monthly approvals.

In order to be eligible to participate in an assumption transaction, we first apply to FLOIR for approval to assume a specified number of policies. We prepare and submit a report showing the cumulative pro forma financial impact of assuming all policies for which we have applied and all policies we have been previously approved to assume. Once we have received FLOIR approval indicating the maximum number of policies we may assume, Citizens provides us with a list of policies eligible for assumption and the relevant policy data. We evaluate these policies using our proprietary data analytics capabilities and submit to Citizens a list of policies we would like to assume. Citizens then compares our list of preferred policies with those of other private insurance companies participating in the depopulation and informs us which policies will be assigned to us.

Once Citizens informs us which policies we may assume, we notify each policyholder of our offer to assume their policy, the amount of their estimated premium upon renewal and their right to opt-out of the assumption transaction. On the effective date of such transaction, Citizens transfers to us the unearned premiums for the policies that have not opted out of the assumption transaction. A policyholder may also opt-out during the 30-day period following the effective date of the assumption transaction. If a policyholder opts-out during such period, we return the applicable unearned premiums to Citizens.

Under the terms of our typical assumption agreement with Citizens, we assume all liability and obligation for losses under the assumed policies arising on or after the effective date of the assumption transaction, and we directly service all policyholder claims related to such losses. All terms and conditions of the assumed policies, including coverage and rates, remain unchanged for the remainder of the policy term. Citizens remains liable for all losses under the assumed policies arising prior to the effective date of the assumption transaction and is solely responsible for servicing all policyholder claims related to such losses.

We strive to retain these policies by offering competitive rates and efficient claims handling to our policyholders. Through December 31, 2015, we renewed approximately 85% of the policies we assumed from Citizens upon their initial expiration.

Loss Development

Our losses and loss adjustment expenses ("LAE") represent estimated costs ultimately required to settle all claims for a given period. The following table illustrates development of the estimated liability for losses and loss adjustment expenses as of:

	December 31,		
	2015	2014	2013
	(In thousands)		
Original liability for losses and LAE[1]	$83,722	$51,469	$19,344
Re-estimated losses and LAE[2] as of:			
1 year later	—	46,184	19,121
2 years later	—	—	16,846
3 years later	—	—	—
Cumulative redundancy (deficiency) [3]	—	5,293	2,498
Cumulative amount of liability paid as of:			
1 year later	—	27,265	12,052
2 years later	—	—	13,472
3 years later	—	—	—
Gross premiums earned	$524,740	$311,514	$139,959

(1) Represents management's original best estimated liability of (i) unpaid claims, (ii) incurred but not reported ("IBNR") and (iii) loss adjustment expenses ("LAE").
(2) Represents the re-estimated liabilities in later years of unpaid claims, IBNR and loss adjustment expenses in the respective years.
(3) Represents the difference between the latest re-estimate and the original estimate. A redundancy means the original estimate is higher than the current estimate whereas a deficiency means that the original estimate is lower than the current estimate.

Technology

Our business depends upon the use, development and implementation of integrated technology systems. These systems enable us to provide a high level of service to agents and policyholders by processing business efficiently, communicating and sharing data with agents, providing a variety of methods for the payment of premiums and allowing for the accumulation and analysis of information for our management. We believe the availability and use of these technology systems has resulted in improved service to agents and customers, increased efficiencies in processing Heritage P&C's business and lower operating costs.

We also license software from third parties, including West Point Underwriters, Majesco Mastec and AIR Worldwide, Inc. ("AIR"). AIR's catastrophe modeling software enables us to optimize our insurance portfolio to manage our reinsurance costs. We also own or license other technology systems used by Heritage P&C. These technology systems consist primarily of an integrated central processing computer, a series of server-based computer networks, a back-up server and various Internet-based communications systems.

Reinsurance

In order to limit our potential exposure to catastrophic events, we purchase significant reinsurance from third party reinsurers and sponsor catastrophe bonds (Citrus Re). We also purchase property per risk reinsurance and facultative coverage for non-catastrophe related to losses in excess of $1.0 million. Purchasing reinsurance is an important part of our risk strategy, and premiums paid (or ceded) to reinsurers is our single largest cost. Reinsurance involves transferring, or "ceding", a portion of the risk exposure on policies we write to another insurer, known as a reinsurer. To the extent that our reinsurers are unable to meet the obligations they assume under our reinsurance agreements, we remain liable for the entire insured loss. See in Part I, Item 1A "Risk Factors". We may not be able to collect reinsurance amounts due to us from the reinsurers with which we have contracted.

Our reinsurance agreements are short-term, prospective contracts. We record an asset, prepaid reinsurance premiums, and a liability, reinsurance payable, for the entire contract amount upon commencement of our new reinsurance agreements. We amortize our reinsurance premiums over the 12-month contract period, which is June 1 through May 31.

In the event that we incur losses and loss adjustment expenses recoverable under our reinsurance program, we record amounts recoverable from our reinsurers on paid losses plus an estimate of amounts recoverable on unpaid losses. The estimate of amounts recoverable on unpaid losses is a function of our liability for unpaid losses associated with the reinsured policies; therefore, the amount changes in conjunction with any changes to our estimate of unpaid losses. As a result, a reasonable possibility exists that an estimated recovery may change significantly in the near term from the amounts included in our consolidated financial statements.

FLOIR requires all insurance companies, like us, to have a certain amount of capital and reinsurance coverage in order to cover losses and loss adjustment expenses upon the occurrence of a catastrophic event. Our 2015-2016 reinsurance program provides reinsurance in excess of FLOIR's requirements, which are based on the probable maximum loss that we would incur from an individual catastrophic event estimated to occur once in every 100 years based on our portfolio of insured risks. The nature, severity and location of the event giving rise to such a probable maximum loss differs for each insurer depending on the insurer's portfolio of insured risks, including, among other things, the geographic concentration of insured value within such portfolio. As a result, a particular catastrophic event could be a one-in-100 year loss event for one insurance company while having a greater or lesser probability of occurrence for another insurance company. We also purchase reinsurance coverage to protect against the potential for multiple catastrophic events occurring in the same year.

2015 – 2016 Reinsurance Program

During the second quarter of 2015, we placed our reinsurance program for the period from June 1, 2015 through May 31, 2016. Our reinsurance program, which is segmented into layers of coverage, protects us for excess property catastrophe losses and loss adjustment expenses. Our 2015-2016 reinsurance program incorporates the mandatory coverage required by law to be placed with FHCF. For the 2015 hurricane season, we selected 75% participation in the FHCF. We also purchased private reinsurance below, alongside and above the FHCF layer, as well as aggregate reinsurance coverage. The following describes the various layers of the June 1, 2015 to May 31, 2016 reinsurance program.

- The Company's Retention. For the first catastrophic event, we have a primary retention of the first $35 million of losses and loss adjustment expenses, of which Osprey is responsible for $20 million. For a second event, Heritage P&C's primary retention decreases to $5 million and Osprey is responsible for $10 million. To the extent that there is reinsurance coverage remaining, Heritage P&C has a $5 million primary retention for events beyond the second catastrophic event. Osprey has no primary retention beyond the second catastrophic event.
- Layers Below FHCF. Immediately above our retention, we have purchased $440 million of reinsurance from third party reinsurers. Through the payment of a reinstatement premium, we are able to reinstate the full amount of this reinsurance one time. To the extent that $440 million or a portion thereof is exhausted in a first catastrophic event, we have purchased reinstatement premium protection insurance to pay the required premium necessary for the reinstatement of this coverage. A portion of this coverage wraps around the FHCF and provides coverage alongside and above the FHCF.
- FHCF Layer. Our FHCF coverage includes an estimated maximum provisional limit of 75% of $920 million, or $690 million, in excess of its retention and private reinsurance of $336 million. The limit and retention of the FHCF coverage is subject to upward or downward adjustment based on, among other things, submitted exposures to FHCF by all participants. We purchased coverage alongside from third party reinsurers and through reinsurance agreements with Citrus Re Ltd To the extent the FHCF coverage is adjusted, this private reinsurance with third party reinsurers and Citrus Re Ltd will adjust to fill in any gaps in coverage up to the reinsurers' aggregate limits for this layer. The FHCF coverage cannot be reinstated once exhausted, but it does provide coverage for multiple events.
- CAT Bond Layer alongside the FHCF. During April 2015 Heritage P&C entered into three catastrophe reinsurance agreements with Citrus Re Ltd. The agreements provide for three years of coverage from catastrophic losses caused by named storms, including hurricanes, beginning on June 1, 2015. Heritage P&C pays a periodic premium to Citrus Re Ltd during this three-year risk period. Citrus Re Ltd issued in aggregate of $277.5 million of principal-at-risk variable notes due April 2017 to fund the reinsurance trust account and its obligations to Heritage P&C under the reinsurance agreements. These notes were issued in three classes. The Class A notes provide $150 million of coverage for the layer immediately above the FHCF. The Class B notes provide $97.5 million of coverage, and the Class C notes provide $30 million of coverage. The Class B and Class C notes provide reinsurance coverage for a sliver of the catastrophe coverage that had previously been provided by the FHCF. The limit of coverage is fully collateralized by a reinsurance trust account for the benefit of Heritage P&C. The maturity date of the notes may be extended up to two additional years to satisfy claims for catastrophic events occurring during the three-year term of the reinsurance agreements.

- CAT Bond Layer above the FHCF. Immediately above the FHCF layer is the coverage provided by the 2015 reinsurance agreement entered into with Citrus Re as described above in this footnote. The Citrus Re 2015 Class A notes provide up to $150 million of coverage immediately above the FHCF layer. Coverage immediately above the 2015 Class A notes is provided by the 2014 reinsurance agreements entered into with Citrus Re Ltd. The first contract with Citrus Re Ltd provides $150 million of coverage and the second contract provides an additional $50 million of coverage.
- Aggregate Coverage. In addition to the layers described above, we have also purchased $125 million of aggregate reinsurance coverage for losses and loss adjustment expenses in excess of $1.648 billion for a first catastrophic event. To the extent that this coverage is not fully exhausted in the first catastrophic event, it provides coverage commencing at its reduced retention for second and subsequent events and where underlying coverage has been previously exhausted. There is no reinstatement of the aggregate reinsurance coverage once exhausted, but it does provide coverage for multiple events.

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For a first catastrophic event, our reinsurance program provides coverage for $1.8 billion of losses and loss adjustment expenses, including our retention, and we are responsible for all losses and loss adjustment expenses in excess of such amount. For subsequent catastrophic events, our total available coverage depends on the magnitude of the first event, as we may have coverage remaining from layers that were not previously fully exhausted. We have also purchased reinstatement premium protection insurance to provide an additional $440.0 million of coverage. Our aggregate reinsurance layer also provides coverage for second and subsequent events to the extent not exhausted in prior events. In total, we have purchased $2.3 billion of potential reinsurance coverage, including our retention, for multiple catastrophic events. Our ability to access this coverage, however, will be subject to the severity and frequency of such events. As of August 31, 2015, the peak of the hurricane season, our total insured value was $76.9 billion, and we may experience significant losses and loss adjustment expenses in excess of our retention. The chart below provides a graphic illustration of the structure and operations of our 2015-2016 catastrophe reinsurance program.

In placing our 2015-2016 reinsurance program, we sought to capitalize on favorable reinsurance pricing and mitigate uncertainty surrounding the future cost of our reinsurance by negotiating multi-year arrangements. The $477.5 million of aggregate coverage we have purchased from Citrus Re Ltd, which includes both the 2014 Class A & B notes and 2015 Class A, B, and C notes, extends $200.0 million for another two-year period and $277.5 million for a three-year period. To the extent it is all or partially exhausted before the end of three years, it cannot be reinstated. In the aggregate, multi-year coverage accounts for approximately 45% of our purchases of private reinsurance for the 2015 hurricane season. The terms of each of the multi-year coverage arrangements described above are subject to adjustment depending on, among other things, the size and composition of our portfolio of insured risks in future periods.

Assuming the reoccurrence of Hurricane Andrew, which is considered to be the most catastrophic single event in Florida’s recorded history, the probable maximum net loss to us in 2015, assuming the reinsurance coverage described above, would be $30.8

million (after tax, net of all reinsurance recoveries and including our retention through Osprey Re). This loss would have represented 8.7% of our stockholders' equity at December 31, 2015. We estimate that, based on our portfolio of insured risks as of August 31, 2015, Hurricane Andrew would have represented a catastrophic event likely to occur approximately once every 31 years and would have exhausted approximately 39.5% of our total expected reinsurance coverage.

For the twelve months ending May 31, 2016, we purchased reinsurance from the following sources: (i) FHCF, (ii) Citrus Re Ltd, (iii) 23 third-party private reinsurers, all of which were rated "A-" or higher by A.M. Best or S&P and (iv) our wholly-owned reinsurance subsidiary, Osprey. Allianz Global Corporate & Specialty SE provides approximately 38% of our third-party reinsurance program, including Citrus Re catastrophe bonds. The chart below lists our third-party reinsurers with A.M. Best and S&P ratings:

Reinsurer	A.M. Best Rating	S&P Rating
Allianz Global & Corporate SE	A+	AA
Amlin AG	A	A
Axis Specialty Limited	A+	A+
ACE Tempest Reinsurance Ltd	A++	AA
Everest Reinsurance Company	A+	A+
Fidelis Insurance Bermuda Limited	A-	NA
General Insurance Corporation of India	A-	NA
Hamilton Re, Ltd	A-	NA
Hannover Re (Bermuda) Ltd	A+	AA-
Horseshoe Re Ltd	Fully Collateralized	
Markel Bermuda Limited	A	A
Odyssey Reinsurance Company	A	A-
Partner Reinsurance Co Ltd	A	A+
Poseidon Re	Fully Collateralized	
Qatar Reinsurance Company Limited	A	A
Rubik Re	Fully Collateralized	
Lloyd's Underwriter Syndicate No. 0382	A	A+
Lloyd's Underwriter Syndicate No. 1955	A	A+
Lloyd's Underwriter Syndicate No. 2001	A+	A+
Lloyd's Underwriter Syndicate No. 2003	A	A+
Taiping Reinsurance Co., Ltd	A	A
Tokio Millennium Re Ag	A++	A+
XL Catlin	A	A+

Investments

Our investments are managed by seven third-party asset managers. We have designed our investment policy to provide a balance between current yield, conservation of capital and the liquidity requirements of our operations. As such, our investable assets are primarily held in cash and bonds with relatively short durations. Our investment policy sets guidelines that provide for a well-diversified investment portfolio that is compliant with Florida statutes that emphasizes quality and preservation of capital. The policy limits investments in common and preferred stocks to 15% of Heritage P&C's admitted assets, with no more than 10% in either class. Our bond portfolio must have a minimum weighted average portfolio quality of A, with only $1 million invested in below investment grade bonds. No more than 2% of admitted assets can be invested in any one issuer, excluding government-related securities. Investments in commercial mortgages cannot exceed 10% of admitted assets. Prohibited investments include short sales and margin purchases, oil, gas, mineral or other types of leases, speculative uses of futures and options, unrated corporate securities, non-US denominated securities, convertible securities high risk CMO instruments, repurchase agreements, securities lending transactions and speculative foreign currency valuation transactions. Our investment policy, which may change from time to time, is approved by our Investment Committee and is reviewed on a regular basis in order to ensure that our investment policy evolves in response to changes in the financial market. See Note 3 to our consolidated financial statements for the year ended December 31, 2015 included elsewhere in this Annual Report.

As of December 31, 2015, we held $236.3 million in cash and cash equivalents and $400.1 million in securities, which were comprised of $371.8 million in bonds, $12.7 million in preferred stocks and $15.6 million in common stock.

Government Regulation

The insurance industry is extensively regulated. Heritage P&C is subject to the laws and regulations of Florida and any other state where we may seek to do business. Florida's insurance regulatory regime provides for regulation of virtually all aspects of Heritage P&C's business. Florida, like many states, has adopted several model laws and regulations as promulgated by the NAIC.

State statutes and administrative rules generally require each insurance company that is part of a 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 which 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. In many instances, Florida's insurance laws and regulations are even more stringent that those promulgated by the NAIC or other states.

As an initial matter, Florida routinely places additional restrictions on new insurers as a condition of receiving a certificate of authority. These restrictions are typically memorialized in a consent order entered into between FLOIR and the insurer applying for a certificate of authority. We are subject to such a consent order in which we have agreed to higher or more stringent restrictions than are otherwise required under Florida law. The material restrictions we have agreed to include:

- Florida law requires a residential property writer to maintain surplus of the greater of $15.0 million or 10% of its liabilities. Pursuant to the consent order, we agreed to establish a minimum capital and surplus of $18.0 million. As of December 31, 2015, our insurance subsidiary held surplus of $216.6 million, in full compliance with Florida law and the consent order.
- Florida law restricts the ratio of premiums written to policyholder surplus to 10 to 1 on a gross basis and 4 to 1 on a net of reinsurance basis. As of December 31, 2015, Heritage P&C's gross and net writing ratios were 2.7 to 1 and 1.8 to 1, respectively. Pursuant to the consent order, we also agreed to not exceed the projected premiums in the plan of operation submitted with our original application for licensure without the prior written approval of FLOIR during 2013, 2014 and 2015. As part of the FLOIR approval process for the various Citizens assumption transactions in which we have participated, we have received approval to exceed these projected premiums. We are in full compliance with these provisions of the consent order.
- Florida law places no restrictions on the parent of an insurer, or other upstream entities, with regard to the payment of dividends. Pursuant to the consent order, we agreed to not make any distributions to stockholders prior to July 31, 2015, except such distributions as are required to offset stockholders' tax obligations resulting from the ownership of our equity or such distributions as may be approved by FLOIR in advance and in writing. We are in full compliance with this provision of the consent order.
- Florida law allows an insurer to pay certain dividends to stockholders without approval of FLOIR. Pursuant to the consent order, we agreed that, until July 31, 2017, Heritage P&C would pay only those dividends that have been approved in advance and in writing by FLOIR. Our insurance subsidiary has paid no stockholder dividends since its inception and is in full compliance with this provision of the consent order.

We are also subject to consent orders setting conditions for FLOIR's approval of the Citizens assumption transactions in which we have participated. We are required by consent order to comply with the assumption agreements entered into with Citizens at the time of each assumption transaction, which requires that for the assumed policies, we must offer to renew each policy for a minimum of three years. In addition, three of our assumptions in 2013 limited rate increases to the higher of those approved by FLOIR for Citizens for comparable risks or 10%. We are in full compliance with all consent orders issued with regard to Citizens' depopulation program.

Additionally, we are subject to regulations administered by a department of insurance in each state in which we do business. These regulations relate to, among other things:

- the content and timing of required notices and other policyholder information;
- the amount of premiums the insurer may assume or 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
- requiring reserves.

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 authorities also conduct periodic examinations into insurers' business practices. Additionally, as an insurance company operating in Florida, Heritage P&C is subject to assessments levied by Citizens, the Florida Insurance Guaranty Association and the FHCF.

Employees

As of December 31, 2015, we had 247 employees, all of whom are full time employees. We are not a party to any collective bargaining agreement and have not experienced any work stoppages or strikes as a result of labor disputes. We consider relations with our employees to be satisfactory.

Available Information

Heritage Insurance Holdings Inc.'s, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to reports filed pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") are made available, free of charge, on or through the "Investor Relations" portion of our Internet website https://heritagepci.com. Reports filed with or furnished to the SEC will also be available as soon as reasonably practicable after they are filed with or furnished to the SEC and are available over the internet at the SEC's website at http://www.sec.gov.

Item 1A. Risk Factors

Set forth below are certain risk factors that could harm our business, results of operations and financial condition. You should carefully read the following risk factors, together with the financial statements, related notes and other information contained in this Annual Report on Form 10-K. Our business, financial condition and operating results may suffer if any of the following risks are realized. If any of these risks or uncertainties occur, the trading price of our common stock could decline and you might lose all or part of your investment. This Annual Report on Form 10-K contains forward-looking statements that contain risks and uncertainties. Please refer to the discussion of "Forward-Looking Statements" of this Annual Report in connection with your consideration of the risk factors and other important factors that may affect future results described herein.

Risks Related to Our Business

We have a limited operating history, and our business and future prospects are difficult to evaluate.

We began operations in August 2012 and wrote our first policy in November 2012. Due to our limited operating history, our ability to execute our business strategy is materially uncertain and our operations and prospects are subject to all risks inherent in a developing business enterprise. Our limited operating history also makes it difficult to evaluate our long term commercial viability. As a new business, we must work to establish and develop successful operating procedures, hire staff, tailor and fine-tune our information management and other systems, maintain adequate control of our expenses, develop business relationships, implement our marketing strategies (and adapt and modify them as needed), establish a positive image and reputation in the community, and take any other steps necessary to conduct our business. As a result of these challenges, it is possible that we may not be successful in implementing our business strategy or completing the development of the infrastructure necessary to expand our business.

Our loss reserves are estimates and may be inadequate to cover our actual liability for losses, causing our results of operations to be adversely affected.

We maintain reserves to cover our estimated ultimate liabilities for losses and loss adjustment expenses, also referred to as loss reserves. We have a limited operating history and a limited loss history which may negatively impact our ability to accurately establish loss reserves. Our current loss reserves are based primarily on industry historical data and statistical projections of what we believe the resolution and administration of claims will cost based on facts and circumstances then known to us. As a company with limited operating history, our claims experience and our experience with the risks related to certain claims is inherently limited. We use company historical data to the extent it is available and rely heavily on industry historical data, which may not be indicative of future periods. As a result, our projections and our estimates may be inaccurate, which in turn may cause our actual losses to exceed our loss reserves. If our actual losses exceed our loss reserves, our financial results, our ability to expand our business and to compete in the property and casualty insurance industry may be negatively affected.

Factors that affect unpaid losses and loss adjustment expenses include the estimates made on a claim-by-claim basis known as “case reserves” coupled with bulk estimates known as “incurred but not yet reported” (or “IBNR”). Periodic estimates by management of the ultimate costs required to resolve all claims are based on our analysis of historical data and estimations of the impact of numerous factors such as (i) per claim information, (ii) industry and company historical loss experience and development patterns, (iii) legislative enactments, judicial decisions, legal developments in the awarding of damages and changes in political attitudes, and (iv) trends in general economic conditions, including the effects of inflation. Management revises its estimates based on the results of its analysis. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for estimating the ultimate resolution of all claims. There is no precise method for subsequently evaluating the impact of any specific factor on the adequacy of the reserves because the eventual redundancy or deficiency is affected by multiple factors.

Because of the inherent uncertainties in the reserving process, we cannot be certain that our reserves will be adequate to cover our actual losses and loss adjustment expenses. If our reserves for unpaid losses and loss adjustment expenses are less than actual losses and loss adjustment expenses, we will be required to increase our reserves with a corresponding reduction in our net income in the period in which the deficiency is identified. Future loss experience substantially in excess of our reserves for unpaid losses and loss adjustment expenses could substantially harm our results of operations and financial condition.

Because all of our insurance business was conducted in Florida as of December 31, 2015, any single catastrophic event, or a series of such events, or other condition affecting losses in Florida could adversely affect our financial condition and results of operations.

As of December 31, 2015, all our insurance business was conducted in Florida. The distribution of our policies is generally consistent with that of Florida’s population and is therefore more concentrated in densely-populated coastal areas. A single catastrophic event, or a series of such events, destructive weather pattern, general economic trend, regulatory development or other condition specifically affecting Florida, particularly the more densely populated areas of the state, 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 Florida subjects us to increased exposure to certain catastrophic events and destructive weather patterns such as hurricanes, tropical storms and tornadoes. Changes in the prevailing regulatory, legal, economic, political, demographic and competitive environment, and other conditions in 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 more geographically diversified than we are. Since our business is concentrated in this manner, the occurrence of one or more catastrophic events or other conditions affecting losses in Florida could have an adverse effect on our business, financial condition and 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 commercial residential buildings for losses that result from, among other things, catastrophes. We are therefore subject to losses, including claims under policies we have assumed or written, arising out of catastrophes that may have a significant effect on our business, results of operations and financial condition. A significant catastrophe, or a series of catastrophes, could also have an adverse effect on our reinsurers. Catastrophes can be caused by various events, including hurricanes, tropical storms, tornadoes, earthquakes, hailstorms, explosions, power outages, fires and by man-made events, such as terrorist attacks. 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 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. In total, for the period from June 1, 2015 through May 31, 2016, we have purchased $2.3 billion of reinsurance coverage, including our retention, for multiple catastrophic events. Our ability to access this coverage, however, is subject to the severity and frequency of such events. We may experience significant losses and loss adjustment expenses in excess of our retention.

Our results of operations may fluctuate significantly based on industry factors as well as our participation in the Citizens depopulation program.

The insurance business historically has been a cyclical industry characterized by periods of intense price competition due to excess underwriting capacity, as well as periods when shortages of capacity permitted an increase in pricing. As premium levels increase, there may be new entrants to the market, which could then lead to increased competition, a significant reduction in premium rates, 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, including changes resulting from multiple and/or catastrophic hurricanes, 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.

In addition, the uncertainties inherent in the reserving process, together with the potential for unforeseen developments, including changes in laws and the prevailing interpretation of policy terms, may result in losses and loss adjustment expenses materially different from the reserves initially established. Changes to prior year reserves will affect current underwriting results by increasing net income if the prior year reserves prove to be redundant or by decreasing net income if the prior year reserves prove to be insufficient. We are not allowed to record contingency reserves to account for expected future losses. As a result, we expect volatility in operating results in periods in which significant loss events occur because generally accepted accounting principles do not permit insurers or reinsurers to reserve for loss events until they have occurred and are expected to give rise to a claim. We anticipate that claims arising from future events may require the establishment of substantial reserves from time to time.

Our results of operations may also vary based on our continued participation in the Citizens depopulation program. As part of a typical assumption transaction with Citizens, we acquire the unearned premium associated with the assumed policies, which, depending on the size of the transaction, may cause significant variability in our financial results from period to period. In June 2013, we entered into a retroactive quota share reinsurance agreement with Citizens that resulted in our recognition of $26.0 million of retroactive insurance income for the year ended December 31, 2013, as we realized income equal to the earned premiums, net of associated losses and loss adjustment expenses, from such policies for the period from January 1, 2013 through May 31, 2013 with no corresponding reinsurance cost. We do not expect to enter into similar retroactive arrangements in connection with future policy assumptions from Citizens. See Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Key Components of Our Results of Operations—Retroactive reinsurance income.”

Our successful participation in the Citizens depopulation program depends on the continuation of such program and our ability to select favorable policies to assume.

An element of our growth strategy involves continued participation in the Citizens depopulation program to the extent that such policies meet our underwriting criteria. As of December 31, 2015, approximately 75% of our 257,131 policies in force were assumed from Citizens. Our ability to participate in this program is subject to a variety of factors, including continuation of the program. There can be no assurance that Citizens will decide to continue the depopulation program for a significant period of time, or at all. At our formation, there were approximately 1.6 million policies in force at Citizens. At the end of 2015, Citizens policies in force had dropped to approximately 500,000 primarily due to depopulation activity from 2012 through 2015. Any efforts by the Florida legislature or Citizens to curtail the depopulation program, materially modify the terms of the program as it relates to personal residential policies, or restrict our participation in the program would hurt our growth prospects and will adversely impair our financial condition and results of operations. When we enter into an assumption transaction with Citizens, we have the opportunity to review information about the policies available for assumption. We undertake a robust selection process in which we analyze various aspects of each policy’s risk profile and, based on the results, select the policies we would like to assume. Our successful participation in the depopulation program depends on our ability to select policies that will be accretive to our financial results. However, our selection process involves many different considerations, and there can be no assurances that we will appropriately assess the risks associated with each policy. As a result, we may select unfavorable policies that could result in substantial losses, which may in turn adversely impact our financial condition and results of operations.

We may not be able to collect reinsurance amounts due to us from the reinsurers with which we have contracted.

Reinsurance is a method of transferring part of an insurance company's risk under an insurance policy to another insurance company. To the extent that our reinsurers are unable to meet the obligations they assume under our reinsurance agreements, we remain liable for the entire insured loss. 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. Our ability to recover amounts due from reinsurers under the reinsurance treaties we currently have in effect is subject to the reinsurance company's ability and willingness to pay and to meet its obligations to us. We attempt to select financially strong reinsurers with an A.M. Best or S&P 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 also rely on our reinsurance broker and rating agencies in evaluating our reinsurers' ability to meet their obligations to us.

Our reinsurance coverage in any given year may be concentrated with one or a limited group of reinsurers. For the twelve months ending May 31, 2016, Allianz Global Corporate & Specialty SE provides approximately 38% of our third-party reinsurance coverage, including Citrus Re Catastrophe Bonds which are fully collateralized. 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.

All residential insurance companies that write business in Florida, including us, are required to obtain reinsurance through FHCF, and this coverage comprises a substantial portion of our reinsurance program. The limit and retention of the FHCF coverage is subject to upward or downward adjustment based on, among other things, submitted exposures to FHCF by all participants. We have purchased private reinsurance alongside our FHCF layer to fill in gaps in coverage that may result from the adjustment of the limit or retention of our FHCF coverage; however, such reinsurance would not cover any losses we may incur as a result of FHCF's inability to pay the full amount of our claims. If a catastrophic event occurs in Florida, FHCF may not have sufficient funds to pay all of its claims from insurance companies in full or in a timely manner. This could result in significant financial, legal and operational challenges to our Company. In the event of a catastrophic loss, FHCF's ability to pay may be dependent upon its ability to issue bonds in amounts that would be required to meet its reinsurance obligations. There can be no assurance that FHCF will be able to do this. While we believe FHCF currently has adequate capital and financing capacity to meet its reinsurance obligations, there can be no assurance that it will be able to meet its obligations in the future, and any failure to do so could have a material adverse effect on our liquidity, financial condition and results of operations.

Reinsurance coverage may not be available to us in the future at commercially reasonable rates or at all.

The cost of reinsurance is subject to prevailing market conditions beyond our control such as the amount of capital in the reinsurance market, as well as the frequency and magnitude 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.

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, during times of increased capacity, highly competitive. We compete not only with other stock companies, but also with Citizens, mutual companies, other underwriting organizations and alternative risk sharing mechanisms. Our principal lines of business are written by numerous other insurance companies. Competition for any one account may come from very large, well-established national companies, smaller regional companies, other specialty insurers in our field and other companies that write insurance only in Florida. Some of these competitors have greater financial resources, larger agency networks and greater name recognition than we do. We compete for business not only on the basis of price, but also on the basis of financial strength, types of coverages offered, and 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.

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 as a result of better premium pricing and/or policy terms;

- an increase in programs in which state-sponsored entities provide property insurance in catastrophe-prone areas;
- changes in Florida’s regulatory climate; and
- the passage 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 Heritage P&C.

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.

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

Our results of operations and financial condition depend on our ability to underwrite and set premium rates accurately for a wide variety of risks. Rate adequacy is necessary to generate sufficient premiums to pay losses, loss adjustment expenses, reinsurance costs and underwriting expenses and to earn a profit. In order 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 successfully perform these tasks, and as a result price our products accurately, is subject to a number of risks and uncertainties, some of which are outside our control, including:

- the availability of sufficient reliable data and our ability to properly analyze available data;
- regulatory delays in approving filed rate changes;
- the uncertainties that inherently characterize estimates and assumptions;
- our selection and application of appropriate rating and pricing techniques;
- changes in legal standards, claim resolution 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 the number of policies we write and our competitiveness. In either event, our profitability could be materially and adversely affected.

The inherent uncertainty of models and our reliance on such models as a tool to evaluate risk may have an adverse effect on our financial results.

We license analytic and modeling software from third parties to facilitate our pricing, assess our risk exposure and determine our reinsurance needs. Given the inherent uncertainty of modeling techniques and the application of such techniques, these models and databases may not accurately address the emergence of a variety of matters which might impact our exposure to losses. Accordingly, these models may understate the exposures we are assuming and our financial results may be adversely impacted, perhaps significantly.

The failure of our claims department to effectively manage or remediate claims could adversely affect our insurance business, financial results and capital requirements.

We rely on our claims department to facilitate and oversee the claims adjustment process for our policyholders. Many factors could affect the ability of our claims department to effectively manage claims by our policyholders, including:

- the accuracy of our 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 department to ensure consistent claims handling;
- the ability of our claims department to translate the information provided by adjusters into acceptable claims resolutions; and
- the ability of our claims department to maintain and update its claims handling procedures and systems as they evolve over time based on claims and geographical trends in claims reporting.

Any failure to effectively manage the claims adjustment process, including 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.

Additionally, in the final stage of the claims process, we leverage CAN’s vendor network to provide repair and remediation services to the policyholder. If such services are not performed properly, we may face liability. Although we maintain professional liability insurance to cover losses arising from our repair and remediation services, there can be no assurances that such coverage is adequate. In addition, our failure to timely and properly remediate claims, or the perception of such failure, may damage our reputation and adversely affect our ability to renew existing policies or write new policies.

If actual renewals of our existing contracts do not meet expectations, our premiums written in future years and our future results of operations could be materially adversely affected.

Our insurance policies are written for a one-year term. We make assumptions about the renewal of our prior year's contracts, including for purposes of determining the amount of reinsurance we purchase. If actual renewals do not meet expectations or if we choose not to write on a renewal basis because of pricing conditions, our premiums written in future years and our future operations would be materially adversely affected, and we may purchase reinsurance beyond what we believe is the most appropriate level.

We may not be able to effectively execute our growth strategy.

We may invest significant time and resources to develop and market new lines of business and/or products and services and we may not achieve the return on our investment that we expect. Initial timetables for the introduction and development of new lines of business and/or new products or services may not be achieved and price and profitability targets may not prove feasible. External factors, such as compliance with regulations, competitive alternatives, and shifting customer preferences may also impact the successful implementation of a new line of business or a new product or service. Such external factors and requirements may increase our costs and potentially affect the speed with which we will be able to pursue new market opportunities. There can be no assurance that we will be successful in bringing new insurance products to our marketplace. Additionally, any new line of business and/or new product or service could have a significant impact on the effectiveness of our system of internal controls. Failure to successfully manage these risks could have a material adverse effect on our business, results of operations and financial condition.

Our growth strategy involves expansion of our business to states outside of Florida. Geographic diversification may be hindered by the fact that we have a limited operating history, and we may be unable to satisfy requirements imposed by state regulators and other third parties.

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

Our future growth and future capital requirements will depend on our ability to expand the number of insurance policies we assume or write in Florida, to expand the kinds of insurance products we offer and to expand the geographic markets in which we do business, all balanced by the business risks we choose to assume and cede. All of these growth initiatives require capital. Our existing sources of funds include possible sales of common or preferred stock, incurring debt and our earnings from operations and investments. Unexpected catastrophic events in our coverage areas, such as the hurricanes experienced in Florida in the past decade, 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 are able to raise additional capital.

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 that our 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 the amount and timing of our capital needs, including our growth and profitability, the availability and cost 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 on acceptable terms or at all. In the case of equity financings, dilution to our stockholders could result, and in any case such securities may have rights, preferences and privileges that are senior to those of existing stockholders. If we cannot obtain adequate capital on favorable terms or at all, our business, financial condition or results of operations could be materially adversely affected.

Our information technology systems, or those of our key service providers, may fail or suffer a loss of security 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 actuarial and other modeling functions necessary for writing business, as well as to handle our policy administration process (i.e., handling and adjusting claims, the printing and mailing of our policies, endorsements, renewal notices, etc.). The successful operation of our systems depends on a continuous supply of electricity. The failure of these systems or disruption in the supply of electricity could interrupt our operations and result in a material adverse effect on our business.

The development and expansion of our insurance business is dependent upon the successful development and implementation of advanced technology, including modeling, underwriting and information technology systems. Because we intend to expand our business by writing additional voluntary policies and entering into new lines of business, we are enhancing our information technology systems to handle and process an increased volume of policies. Additionally, we have engaged service providers to provide us with policy and other administration services for certain of our policies and we intend to continue to utilize third party systems as our policy count grows. The failure of any of these systems to function as planned could slow our growth and adversely affect our future business volume and results of operations. In addition, we have licensed certain systems and data from third parties. We cannot be certain that we will have access to these, or comparable systems, or that our technology or applications will continue to operate as intended. Moreover, we cannot be certain that we would be able to replace these systems without slowing our underwriting response time. A major defect or failure in our internal controls or information technology systems could result in management distraction, harm to our reputation, a loss or delay of revenues or increased expense.

In addition, a security breach of our computer systems could damage our reputation or result in liability. We retain confidential business and policyholder information in our computer systems. We may be required to spend significant capital and other resources to protect against security breaches or to alleviate problems caused by such breaches. It is critical that our facilities and infrastructure remain secure. Despite the implementation of security measures, our infrastructure may be vulnerable to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. In addition, we could be subject to liability if hackers were able to penetrate our network security or otherwise misappropriate confidential information.

The development and implementation of new technologies will require an additional investment of our capital resources in the future.

Frequent technological changes, new products and services and evolving industry standards are all influencing the insurance business. We believe that the development and implementation of new technologies will require additional investment of our capital resources in the future. We have not determined, however, the amount of resources and the time that this development and implementation may require, which may result in short-term, unexpected interruptions to our business, or may result in a competitive disadvantage in price and/or efficiency, as we endeavor to develop or implement new technologies.

We do not have significant redundancy in our operations.

We conduct our business primarily from offices located on the west coast of Florida where hurricanes 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, as we do not have significant redundancies to replace our facilities if functionality is impaired. We contract with a third party vendor to maintain complete daily backups of our systems, however, we have not fully tested our plan to recover data in the event of a disaster.

We may be unable to attract and retain qualified employees.

We depend on our ability to attract and retain experienced underwriting talent and other skilled employees who are knowledgeable about our business. If the quality of our underwriters and other personnel decreases, we may be unable to maintain our current competitive position in the specialized markets in which we operate and be unable to expand our operations, which could adversely affect our results.

The loss of, or failure to attract, key personnel could have a more significant impact on our business as compared to some of our competitors that are larger or have longer operating histories. We believe that our ability to grow and fully execute our business plan will depend in large part on our ability to attract and retain additional skilled and qualified personnel and to expand, train and manage our employees. We may not be successful in doing so, because the competition for experienced personnel in the insurance industry is intense.

We are dependent on key executives, the loss of whom could adversely affect our business.

Our future success depends to a significant extent on the efforts of our senior management. We believe there are only a limited number of available and qualified executives with substantial experience in our industry. Accordingly, the loss of the services of one or more of the members of our senior management could delay or prevent us from fully implementing our business strategy and, consequently, significantly and negatively affect our business.

Currently, we only maintain key man life insurance with respect to Bruce Lucas, our Chairman and Chief Executive Officer. If any other member of senior management dies or becomes incapacitated, or leaves the company to pursue employment opportunities elsewhere, we would be solely responsible for locating an adequate replacement for such senior management and for bearing any related cost. To the extent that we are unable to locate an adequate replacement or are unable to do so within a reasonable period of time, our business may be significantly and negatively affected.

Our financial results may be negatively affected by the fact that a portion of our income is generated by the investment of our company's capital, premiums and loss reserves.

A portion of our income is, and likely will continue to be, generated by the investment of our capital, premiums and loss reserves. The amount of income so generated is a function of our investment policy, available investment opportunities and the amount of available cash invested. We are also constrained by investment limitations contained in the Florida Insurance Code. At December 31, 2015, approximately 63% of our total investments, cash and cash equivalents was invested in fixed-maturity and equity securities with the balance in cash and cash equivalents. We may, under certain circumstances, be required to liquidate our investments in securities at prices below book value, which may adversely affect our financial results. We currently hold all of our cash in accounts with four financial institutions and, as a result of this concentration, a portion of the balances in such accounts exceeds the FDIC insurance limits. While we monitor and adjust the balances in our accounts as appropriate, these balances could be impacted if any of these financial institutions fail and could be subject to other adverse conditions in the financial markets.

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 impossible to estimate accurately the amount of investment income that will be realized. In fact, we may realize losses on our investments.

Our inability to maintain our financial stability rating may have a material adverse effect on our competitive position, the marketability of our product offerings, and our liquidity, operating results and financial condition.

Financial stability ratings are important factors in establishing the competitive position of insurance companies and can have a significant effect on an insurance company's business. Many insurance buyers, agents, brokers and secured lenders use the ratings assigned by rating agencies to assist them in assessing the financial stability and overall quality of the companies from which they are considering purchasing insurance or in determining the financial stability of the company that provides insurance. We currently have a Demotech rating of "A" ("Exceptional"). This is the third highest financial stability rating of the six financial stability ratings utilized by Demotech. These financial stability ratings provide an objective baseline for assessing solvency and should not be interpreted as (and are not intended to serve as) an assessment of, a recommendation to buy, sell, or hold, any securities of an insurance company or its parent holding company, including shares of our common stock.

On an ongoing basis, rating agencies review the financial performance and condition of insurers and can downgrade or change the outlook on an insurer's ratings due to, for example, a change in an insurer's statutory capital, a reduced confidence in management or a host of other considerations that may or may not be under the insurer's control. All ratings are subject to continuous review; therefore, the retention of these ratings cannot be assured. A downgrade in any of these ratings could have a material adverse effect on our competitive position, the marketability of our product offerings and our ability to grow in the marketplace.

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

Loss frequency and severity in the property and casualty insurance industry in general and for our company specifically has continued to increase in recent years, principally driven by litigation and assignment of benefits. In addition, many legal actions and proceedings have been brought on behalf of classes of complainants, which can 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 the loss reserves of our insurance subsidiary inadequate for current and future losses. In addition, as industry practices and 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 policies that are affected by the changes. As a result, the full extent of liability under our insurance policies may not be known at the time such policies are issued or renewed, and our financial position and results of operations may be adversely affected.

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 our risk exposure including:

- employing proper underwriting procedures;
- carefully evaluating the terms and conditions of our policies;
- geographic diversification; and

- ceding insurance risk to reinsurance companies.

However, there are inherent limitations in all of these tactics. No assurance can be given that an event or series of unanticipated events will not result in loss levels which could have a material adverse effect on our financial condition or results of operations.

Lack of effectiveness of exclusions and other loss limitation methods in the insurance policies we assume or write could have a material adverse effect on our financial condition or our results of operations.

Various provisions of our policies, such as limitations or exclusions from coverage which are designed to limit our risks, may not be enforceable in the manner we intend. 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 limitation, 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 could have a material adverse effect on our financial condition or results of operations.

We rely on independent agents to write voluntary insurance policies for us, and if we are not able to attract and retain independent agents, our revenues would be negatively affected.

We write voluntary personal and commercial insurance policies through a network of independent agents. Of our network of approximately 3,533 independent agents, approximately 56% are affiliated with eight large agency networks with which we have entered into master agency agreements. As of December 31, 2015, voluntary policies written through independent agents, including the policies we acquired from SSIC, constituted approximately 25.3% of our total policies in force and represented approximately $146.6 million in annualized premiums. We expect to increase the number of voluntary policies we write as our business expands, which will further increase our reliance on our network of independent agents. In fact, in the future, we may rely on independent agents to be the primary source for our property insurance policies. If any of our independent agents cease writing policies for us, or if any of our master agency agreements are terminated, we may suffer a reduction in the amount of products we are able to sell, which would negatively impact our results.

Many of our competitors also rely on independent agents. As a result, 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.

Changing climate conditions may adversely affect our financial condition, profitability or cash flows.

Climate change, to the extent it produces extreme changes in temperatures and changes in weather patterns, could affect the frequency or severity of weather events. Further, it could reduce the affordability and availability of personal residential insurance, which could have an effect on pricing. Changes in weather patterns could also affect the frequency and severity of other natural catastrophe events to which we may be exposed.

If we are unable to implement and maintain effective internal controls over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock may be negatively affected.

As a public company, we are required to maintain internal controls over financial reporting and to report any material weaknesses in such internal controls. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of a company's annual or interim financial statements will not be prevented or detected on a timely basis. Section 404 of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act") requires that we evaluate and determine the effectiveness of our internal controls over financial reporting and, beginning with this Annual Report on Form 10-K, provide a management report on the internal controls over financial reporting.

We are in the process of designing and implementing the internal controls over financial reporting required to comply with the Sarbanes-Oxley Act requirements, which may take a significant amount of time and may require specific compliance training of our personnel. In the future, we may discover areas of our internal controls that need improvement. If we or our independent registered public accounting firm discover a material weakness, the disclosure of that fact, even if quickly remediated, could reduce the market's confidence in our financial statements and harm our stock price. We may not be able to effectively and timely implement necessary control changes and employee training to ensure continued compliance with the Sarbanes-Oxley Act and other regulatory and reporting requirements. If we fail to maintain effective internal controls, we could be subject to regulatory scrutiny and sanctions and investors could lose confidence in the accuracy and completeness of our financial reports.

The requirements of being a public company have increased certain of our costs and require significant management focus.

As a public company, our legal, accounting and other expenses associated with compliance related and other activities have increased. For example, in connection with our initial public offering, we created new board committees and appointed independent directors to comply with the corporate governance requirements of the NYSE. In addition, our management team and board of directors have limited experience implementing public company compliance requirements, and therefore, since our initial public offering, our management and other personnel have diverted attention from operational and other business matters to devote substantial time to such efforts. In particular, we have incurred significant expenses and devoted substantial management effort toward ensuring compliance with the requirements of Section 404 of the Sarbanes-Oxley Act, which will increase when we are no longer an emerging growth company, as defined in The Jumpstart Our Business Act of 2012 (the “JOBS Act”). We have hired additional accounting and financial staff with appropriate public company experience and technical accounting knowledge and have established an internal audit function. Costs to obtain director and officer liability insurance also contribute to our increased costs. As a result of the associated liability, it may be more difficult for us to attract and retain qualified persons to serve on our board of directors or as executive officers. Advocacy efforts by stockholders and third parties may also prompt even more changes in governance and reporting requirements, which could further increase our compliance costs.

We are an “emerging growth company” and we cannot be certain if the reduced disclosure and other requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an “emerging growth company,” as defined in the JOBS Act, and we currently and may in the future take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act with respect to our internal control over financial reporting, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We may take advantage of these provisions for up to five years from our initial public offering or such earlier time that we are no longer an “emerging growth company.” We would cease to be an “emerging growth company” upon the earliest to occur of: (i) the last day of the year in which we have more than $1.0 billion in annual revenues; (ii) the date we qualify as a “large accelerated filer,” with at least $700 million of equity securities; (iii) the issuance, in any three-year period, by our company of more than $1.0 billion in non-convertible debt securities held by non-affiliates; and (iv) the last day of the year ending after the fifth anniversary of our initial public offering. We may choose to take advantage of some but not all of these reduced reporting and other burdens. To the extent we take advantage of any of the reduced reporting burdens in this annual report or in future filings, the information that we provide our security holders may be different than you might get from other public companies in which you hold equity interests. We cannot predict if investors will find our common stock less attractive because we may rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

In addition, Section 107 of the JOBS Act provides that an “emerging growth company” can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. In other words, an “emerging growth company” can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have chosen to “opt-out” of such extended transition period, however, and, as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. Section 107 of the JOBS Act provides that our decision to opt-out of the extended transition period for complying with new or revised accounting standards is irrevocable.

Risks Related to Regulation of our Insurance Operations

We 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.

We are subject to extensive state regulation. Heritage P&C is subject to supervision and regulation that is primarily designed to protect our policyholders rather than our stockholders, and such regulation is imposed by both the state in which it is domiciled (Florida) and the states in which it does business. These regulations relate to, among other things, the approval of policy forms and premium rates, our conduct in the marketplace, our compliance with solvency and financial reporting requirements, transactions with our affiliates, and limitations on the amount of business we can write, the amount of dividends we can pay to stockholders, and the types of investments we can make. Insurance holding company regulations generally provide that transactions between an insurance company and its affiliates must be fair and reasonable, and must be clearly and accurately disclosed in the records of the respective parties, with expenses and payments allocated between the parties in accordance with customary accounting practices. Many types of transactions between an insurance company and its affiliates, such as transfers of assets, loans, reinsurance agreements, service agreements, certain dividend payments by the insurance company and certain other material transactions, 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. These regulatory requirements may adversely affect or inhibit our ability to achieve some or all of our business objectives. In addition, regulatory authorities also may conduct periodic examinations into insurers' business practices. These reviews may reveal deficiencies in our insurance operations or differences between our interpretations of regulatory requirements and those of the regulators.

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. For example, Florida law requires that a person may not, individually or in conjunction with any affiliated person of such person, acquire directly or indirectly, conclude a tender offer or exchange offer for, enter into any agreement to exchange securities for, or otherwise finally acquire 5% or more of the outstanding voting securities of a Florida domiciled stock insurer or of a controlling company, unless it is in compliance with certain notice and approval requirements. Such restriction may inhibit our ability to grow our business or achieve our business objectives.

Further, 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.

Heritage P&C is subject to additional regulation imposed by consent orders entered into with FLOIR in connection with our formation.

In addition to compliance with statutes and regulations, Florida routinely places additional restrictions on new insurers as a condition of receiving their certificate of authority. These restrictions are typically memorialized in a consent order entered into between FLOIR and the insurer applying for a certificate of authority. We are subject to such a consent order. We have, in certain cases, agreed to higher or more stringent restrictions than are otherwise required under Florida law. The material restrictions we have agreed to include:

- Florida law requires a residential property writer to maintain surplus of the greater of $15.0 million or 10% of its liabilities. Pursuant the consent order, we agreed to establish a minimum capital and surplus of $18.0 million.
- Florida law restricts the ratio of premiums written to policyholder surplus to 10 to 1 on a gross basis and 4 to 1 on a net of reinsurance basis. Pursuant to the consent order, we agreed to not exceed the projected premiums in the plan of operation submitted with our original application for licensure without the prior written approval of FLOIR during 2012, 2013 and 2014. As part of the FLOIR approval process for the various Citizens assumption transactions in which we have participated, we have received approval to exceed these projected premiums.
- Florida law places no restrictions on the parent of an insurer, or other upstream entities, with regard to the payment of dividends. Pursuant to the consent order, we agreed to not make any distributions to stockholders prior to July 31, 2015, except such distributions as are required to offset stockholders’ tax obligations resulting from the ownership of our equity or such distributions as may be approved by FLOIR in advance and in writing.
- Florida law allows an insurer to pay certain dividends to stockholders without approval of FLOIR. Pursuant to the consent order, we agreed that, until July 31, 2017, Heritage P&C would pay only those dividends that have been approved in advance and in writing by FLOIR.

In addition, we are subject to several consent orders setting conditions upon FLOIR’s approval of the various Citizens assumption transactions in which we have participated. For example, beginning with our June 2013 assumption transaction, we are required to offer to renew each assumed policy for a minimum of three years and limit rate increases to the higher of those offered by Citizens for comparable risks or 10%.

In the event we are unable to comply with the additional regulation imposed by these consent orders, it may adversely affect our ability to operate our business.

Changes in regulation may reduce our profitability and limit our growth.

We are subject to extensive regulation in Florida, the only state in which we currently conduct business through December 31, 2015. The National Association of Insurance Commissioners (“NAIC”) and state insurance regulators are constantly reexamining existing laws and regulations, generally focusing on modifications to holding company regulations, interpretations of existing laws and the development of new laws. For example, in 2013 FLOIR asked the Florida legislature to amend the Florida Insurance Code in conformity with the latest amendments to the NAIC Model Holding Company System Regulatory Act. Among other things, such amendment requires the ultimate controlling person of any Florida insurance company to file an Annual Report identifying the material risks within the insurance holding company system that could pose enterprise risk to the insurance company.

From time to time, states consider and/or enact laws that may alter or increase state authority to regulate insurance companies and insurance holding companies. States also consider and/or enact laws that impact the competitive environment and marketplace for property and casualty insurance. Our insurance company subsidiary currently transacts insurance only in Florida, where the political environment has sometimes led to aggressive regulation of property and casualty insurance companies. For example, in 2007, Florida enacted legislation that led to rate levels in the private insurance market that we believe, in many instances in the past, were inadequate to cover the related underwriting risk. This same legislation required Citizens to reduce its premium rates and begin competing against private insurers in the Florida residential property insurance market. Florida lawmakers may continue to enact or retain legislation that suppresses the rates of Citizens, further adversely impacting the private insurance market and increasing the likelihood that it must levy assessments on private insurance companies and ultimately on Florida consumers. These and other aspects of the political environment in jurisdictions where we operate may reduce our profitability, limit our growth, or otherwise adversely affect our operations.

During the past several years, various regulatory and legislative bodies have adopted or proposed new laws or regulations to address the cyclical nature of the insurance industry, catastrophic events and insurance capacity and pricing. These regulations include (i) the creation of “market assistance plans” under which insurers are induced to provide certain coverages, (ii) restrictions on the ability of insurers to rescind or otherwise cancel certain policies in mid-term or to nonrenew policies at their scheduled expirations, (iii) advance notice requirements or limitations imposed for certain policy non-renewals, (iv) limitations upon or decreases in rates permitted to be charged, (v) expansion of governmental involvement in the insurance market and (vi) increased regulation of insurers’ policy administration and claims handling practices.

Currently, the federal government does not directly regulate the insurance business. However, in recent years the state insurance regulatory framework has come under increased federal scrutiny. Congress and some federal agencies from time to time investigate the current condition of insurance regulation in the United States to determine whether to impose federal regulation or to allow an optional federal charter, similar to banks. In addition, changes in federal legislation and administrative policies in several areas, including changes in the Gramm-Leach-Bliley Act, financial services regulation and federal taxation, can significantly impact the insurance industry and us.

We cannot predict with certainty the effect any enacted, proposed or future state or federal legislation or NAIC initiatives may have on the conduct of our business. Furthermore, there can be no assurance that the regulatory requirements applicable to our business will not become more stringent in the future or result in materially higher costs than current requirements, or that creation of a federal insurance regulatory system will not adversely affect our business or disproportionately benefit our competitors. Changes in the regulation of our business may reduce our profitability, limit our growth or otherwise adversely affect our operations.

Our insurance subsidiary is subject to minimum capital and surplus requirements, and our failure to meet these requirements could subject us to regulatory action.

Our insurance subsidiary is subject to risk-based capital standards and other minimum capital and surplus requirements imposed under applicable state laws, currently the laws of Florida. The risk-based capital standards, based upon the Risk-Based Capital Model Act adopted by the NAIC, require our insurance subsidiary to report its results of risk-based capital calculations to FLOIR and the NAIC. These risk-based capital standards provide for different levels of regulatory attention depending upon the ratio of an insurance company’s total adjusted capital, as calculated in accordance with NAIC guidelines, to its authorized control level risk-based capital. Authorized control level risk-based capital is determined using the NAIC’s risk-based capital formula, which measures the minimum amount of capital that an insurance company needs to support its overall business operations.

An insurance company with total adjusted capital that is less than 200% of its authorized control level risk-based capital is at a company action level, which would require the insurance company to file a risk-based capital plan that, among other things, contains proposals of corrective actions the company intends to take that are reasonably expected to result in the elimination of the company action level event. Additional action level events occur when the insurer’s total adjusted capital falls below 150%, 100%, and 70% of its authorized control level risk-based capital. The lower the percentage, the more severe the regulatory response, including, in the event of a mandatory control level event (total adjusted capital falls below 70% of the insurer’s authorized control level risk-based capital), placing the insurance company into receivership. As of December 31, 2015, Heritage P&C’s risk-based capital ratio was 368%.

In addition, our insurance subsidiary is required to maintain certain minimum capital and surplus and to limit its written premiums to specified multiples of its capital and surplus. The insurance subsidiary could exceed these ratios if its volume increases faster than anticipated or if its surplus declines due to catastrophe or non-catastrophe losses or excessive underwriting and operational expenses.

Florida law requires a residential property writer to maintain surplus of the greater of $15.0 million or 10% of its liabilities. Pursuant to the consent order we entered into in connection with receiving our certificate of authority, we agreed to establish a minimum capital and surplus of $18.0 million. As of December 31, 2015, our insurance subsidiary held surplus of $216.6 million. Florida law also restricts the ratio of premiums written to policyholder surplus to 10 to 1 on a gross basis and 4 to 1 on a net of reinsurance basis. As of December 31, 2015, our insurance subsidiary's gross and net writing ratios were 2.7 to 1 and 1.8 to 1, respectively. Pursuant to the consent order, we agreed to not exceed the projected premiums in the plan of operation submitted with our original application for licensure without the prior written approval of FLOIR during 2012, 2013, and 2014. As part of the FLOIR approval process for the various Citizens assumption transactions in which we have participated, we have received approval to exceed these projected premiums.

Any failure by our insurance subsidiary to meet the applicable risk-based capital or minimum statutory capital requirements or the writings ratio limitations imposed by the laws of Florida (or other states where we may eventually conduct business) could subject it to further examination or corrective action imposed by state regulators, including limitations on our writing of additional business, state supervision or liquidation.

Any changes in existing risk-based capital requirements, minimum statutory capital requirements, or applicable writings ratios may require us to increase our statutory capital levels, which we may be unable to do.

Regulation limiting rate increases and requiring us to participate in loss sharing may decrease our profitability.

From time to time, political dispositions affect the insurance market, including efforts to effectively suppress rates at a level that may not allow us to reach targeted levels of profitability. Despite efforts to remove politics from insurance regulation, facts and history demonstrate that public policymakers, when faced with untoward events and adverse public sentiment, can act in ways that impede a satisfactory correlation between rates and risk. Such acts may affect our ability to obtain approval for rate changes that may be required to attain rate adequacy along with targeted levels of profitability and returns on equity. Our ability to afford reinsurance required to reduce our catastrophe risk may be dependent upon the ability to adjust rates for our cost.

Additionally, we are required to participate in guaranty funds for insolvent insurance companies. The funds periodically assess losses against all insurance companies doing business in the state. Our operating results and financial condition could be adversely affected by any of these factors.

Risks Relating to Ownership of Our Common Stock

The price of our common stock may fluctuate significantly, and you could lose all or part of your investment.

Volatility in the market price of our common stock may prevent you from being able to sell your shares at or above the price you paid for them. The market price for our common stock could fluctuate significantly for various reasons, including:

- our operating and financial performance and prospects;
- our quarterly or annual earnings or those of other companies in our industry;
- the public's reaction to our press releases, our other public announcements and our filings with the SEC;
- changes in, or failure to meet, earnings estimates or recommendations by research analysts who track our common stock or the stock of other companies in our industry;
- the failure of research analysts to cover our common stock;
- general economic, industry and market conditions;
- strategic actions by us, our customers or our competitors, such as acquisitions or restructurings;
- new laws or regulations or new interpretations of existing laws or regulations applicable to our business;
- changes in accounting standards, policies, guidance, interpretations or principles;
- material litigation or government investigations;
- changes in general conditions in the U.S. and global economies or financial markets, including those resulting from war, incidents of terrorism or responses to such events;
- changes in key personnel;
- sales of common stock by us, our principal stockholders or members of our management team;
- the granting or exercise of employee stock options;
- volume of trading in our common stock; and
- impact of the facts described elsewhere in "Risk Factors."

In addition, in recent years, the stock market has regularly experienced significant price and volume fluctuations. This volatility has had a significant impact on the market price of securities issued by many companies, including companies in our industry. The changes frequently appear to occur without regard to the operating performance of the affected companies. Hence, the price of our common stock could fluctuate based upon factors that have little or nothing to do with us and these fluctuations could materially reduce our share price.

We may not continue to pay dividends on our common stock.

In the fourth quarter of 2015 and in the first quarter of 2016, our Board of Directors initiated a quarterly cash dividends on our common stock; however, we can provide no assurance or guarantee that we will continue to pay dividends in the future. Therefore, investors who purchase our common stock may only realize a return on their investment if the value of our common stock appreciates. The declaration and payment of any future dividends will be at the discretion of our Board of Directors and will be dependent upon our profits, financial requirements and other factors including regulatory restrictions on the payment of dividends from our subsidiaries, general business conditions and such other factors as our Board of Directors considers relevant.

Certain provisions of our certificate of incorporation and our bylaws may make it difficult for stockholders to change the composition of our board of directors and may discourage hostile takeover attempts that some of our stockholders may consider to be beneficial.

Certain provisions of our certificate of incorporation and bylaws may have the effect of delaying or preventing changes in control if our board of directors determines that such changes in control are not in the best interests of us and our stockholders. The provisions in such certificate of incorporation and bylaws include, among other things, the following:

- the ability of our board of directors to issue shares of preferred stock and to determine the price and other terms, including preferences and voting rights, of those shares without stockholder approval;
- stockholder action can only be taken at a special or regular meeting and not by written consent;
- advance notice procedures for nominating candidates to our board of directors or presenting matters at stockholder meetings; and
- allowing only our board of directors to fill vacancies on our board of directors.

We have elected in our certificate of incorporation not to be subject to Section 203 of the DGCL, an anti-takeover law. In general, Section 203 prohibits a publicly held Delaware corporation from engaging in a business combination, such as a merger, with a person or group owning 15% or more of the corporation's voting stock for a period of three years following the date the person became an interested stockholder, unless (with certain exceptions) the business combination or the transaction in which the person became an interested stockholder is approved in a prescribed manner. Accordingly, we will not be subject to any anti-takeover effects of Section 203.

While these provisions have the effect of encouraging persons seeking to acquire control of our company to negotiate with our board of directors, they could enable the board of directors to hinder or frustrate a transaction that some, or a majority, of the stockholders might believe to be in their best interests, including an acquisition that would result in a price per share at a premium over the market price, and, in that case, may prevent or discourage attempts to remove and replace incumbent directors.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management.

Applicable insurance laws may make it difficult to effect a change of control of our company.

State insurance holding company laws require prior approval by the state insurance department of any change of control of an insurer that is domiciled in that respective state. "Control" is generally defined as the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a company, whether through the ownership of voting securities, by contract or otherwise. Control is generally presumed to exist through the direct or indirect ownership of 10% or more of the voting securities of a domestic insurance company or any entity that controls a domestic insurance company. Because Heritage P&C is domiciled in Florida, we are subject to Florida law, which prohibits any person from acquiring 5% or more of our outstanding voting securities without the prior approval of FLOIR. However, a party acquiring more than 5% but less than 10% of our voting securities that does not otherwise exercise control may make such acquisition without prior approval by filing a disclaimer of affiliation and control with FLOIR. These laws may discourage potential acquisition proposals and may delay, deter or prevent a change of control of us, including through transactions, and in particular unsolicited transactions, that some or all of our stockholders might consider to be desirable.

Any issuance of preferred stock could make it difficult for another company to acquire us or could otherwise adversely affect holders of our common stock, which could depress the price of our common stock.

Our board of directors has the authority to issue preferred stock and to determine the preferences, limitations and relative rights of shares of preferred stock and to fix the number of shares constituting any series and the designation of such series, without any further vote or action by our stockholders. Our preferred stock could be issued with voting, liquidation, dividend and other rights superior to the rights of our common stock. The potential issuance of preferred stock may delay or prevent a change in control of us, discouraging bids for our common stock at a premium over the market price, and adversely affect the market price and the voting and other rights of the holders of our common stock.

Our business and stock price may suffer as a result of our limited public company operating experience. In addition, if securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

We completed our initial public offering in May 2014. Our limited public company operating experience may make it difficult to forecast and evaluate our future prospects. If we are unable to execute our business strategy, either as a result of our inability to effectively manage our business in a public company environment or for any other reason, our business, prospects, financial condition and results of operations may be harmed. In addition, if no or very few securities or industry analysts cover of our company, the trading price for our stock would be negatively impacted. If one or more of the analysts who covers us downgrades our stock or publishes inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts ceases coverage of us or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

Item 1B. Unresolved Staff Comments

None

Item 2. Properties

We, through Skye Lane, our wholly-owned subsidiary, own a two-building 13-acre campus located in Clearwater, Florida. Approximately 80% of the property is occupied by unaffiliated tenants.

Item 3. Legal Proceedings

We are subject to routine legal proceedings in the ordinary course of business. We believe that the ultimate resolution of these matters will not have a material adverse effect on our business, financial condition or results of operations.

Item 4. Mine Safety Disclosures

Not applicable

PART II

Item 5. Market For Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock trades on the New York Stock Exchange ("NYSE") under the symbol "HRTG". The following table sets forth the high and low sale prices as reported on the NYSE, and the amount of our dividends declarations, for 2015 and 2014, respectively. These reported prices reflect inter-dealer prices without adjustments for retail markups, markdowns or commissions.

Year	Quarter	High	Low	Dividends paid per share
2015	First	$22.80	$18.58	$ —
	Second	$23.23	$19.88	$ —
	Third	$27.28	$16.81	$ —
	Fourth	$24.98	$18.73	$ 0.05

Year	Quarter	High	Low	Dividends paid per share
2014	First	$—	$—	$ —
	Second	$15.38	$11.29	$ —
	Third	$15.70	$13.60	$ —
	Fourth	$19.84	$14.03	$ —

The closing sale price of our common stock as reported on the NYSE on March 1, 2016 was $19.76 per share. As of such date there were 39 holders of record of our common stock based on information provided by our transfer agent.

Dividends

On December 17, 2015, the Company's Board of Directors declared dividends of $0.05 per share. Total dividends paid to date are approximately $1.6 million. No dividends were declared for 2014. Any future dividend payments will be at the discretion of our Board of Directors and will depend on profits, financial requirements and other factors, such as legal and regulatory restrictions on the payment of dividends, overall business condition and other elements the Board of Directors considers relevant.

Securities Authorized for Issuance under Equity Compensation Plan

For information regarding the securities authorized for issuance under our equity compensation plans, refer to "Security Ownership of Certain Beneficial Owners and Management and Related Stockholders Matters" included in Part III, Item 12 of this Annual Report.

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 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. The consolidated statements of operations data for the years ended December 31, 2015, 2014 and 2013 and the consolidated balance sheet data at December 31, 2015 and 2014 are derived from our consolidated financial statements appearing in Item 8 of this Annual Report. The historical results shown below are not necessarily indicative of the results to be expected in any future period.

Statements of Operations Data:

	Year Ended December 31,		
	2015	2014	2013
	(In thousands, except per share data)		
Revenue:			
Gross premiums written	$586,098	$436,407	$218,537
Gross premiums earned	$524,740	$311,514	$139,959
Net premiums earned	$376,268	$223,612	$95,159
Net investment income and realized gains	$8,929	$4,153	$726
Other revenue	$9,595	$6,055	$28,947
Total revenue	$394,792	$233,820	$124,832
Expenses:			
Loss and loss adjustment expenses	$141,191	$89,560	$38,501
Other operating expenses	$103,311	$70,008	$30,870
Total expenses	$244,502	$159,568	$69,371
Income before income taxes	$150,290	$74,252	$55,461
Provision for income taxes	$57,778	$27,155	$21,248
Net income	$92,512	$47,097	$34,213
Earnings per share:			
Basic	$3.08	$1.92	$2.39
Diluted	$3.05	$1.82	$2.36
Ratios to net premiums earned:			
Net loss ratio	37.5 %	40.1 %	40.5 %
Net expense ratio	27.5 %	31.3 %	32.4 %
Combined ratio	65.0 %	71.4 %	72.9 %

Balance Sheet Data

	As of December 31,	
	2015	2014
	(In thousands)	
Cash and invested assets	$636,373	$491,640
Prepaid reinsurance premiums	$78,517	$43,148
Deferred policy acquisition costs	$34,800	$24,370
Total Assets	$837,398	$615,031
Unpaid loss and loss adjustment expense	$83,722	$51,469
Unearned premiums	$302,493	$241,136
Reinsurance payable	$60,210	$17,113

Total Liabilities	$480,845	$359,942
Total Stockholders' Equity	$356,553	$255,089

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations
The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this Annual Report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. The actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those which are not within our control.

Overview: We are a property and casualty insurance holding company headquartered in Clearwater, Florida and, through our insurance subsidiary, we provide personal residential insurance for single-family homeowners and condominium owners, rental property insurance and commercial residential insurance in the state of Florida and North Carolina. We are vertically integrated and control or manage substantially all aspects of insurance underwriting, customer service, actuarial analysis, distribution and claims processing and adjusting. We are led by an experienced senior management team with an average of 31 years of insurance industry experience. Heritage P&C is currently rated "A" ("Exceptional") by Demotech, Inc. ("Demotech"), a rating agency specializing in evaluating the financial stability of insurers.

In addition to Heritage P&C, our other subsidiaries include: Heritage MGA, LLC, the managing general agent that manages substantially all aspects of our insurance subsidiary's business; Contractors' Alliance Network, LLC, ("CAN") our vendor network manager that also houses with BRC Restoration Specialists ("BRC") our provider of restoration, emergency and recovery services; Skye Lane Properties, LLC, our property management subsidiary; First Access Insurance Group, LLC, our retail agency; Osprey Re Ltd ("Osprey"); our reinsurance subsidiary that provides a portion of the reinsurance protection purchased by our insurance subsidiary; and Heritage Insurance Claims, LLC an inactive subsidiary reserved for future development.

We intend the discussion of our financial condition and results of operations that follows to provide information that will assist the reader in understanding our consolidated financial statements, the changes in certain key items in those financial statements from year to year, and the primary factors that accounted for those changes, as well as how certain accounting principles, policies and estimates affect our consolidated financial statements. This discussion should be read in conjunction with our consolidated financial statements and the related notes that appear elsewhere in this document.

Discussion of our business and overall financial results, and other highlights related to our results of operations for the periods presented.

Financial Results Highlights for the Year Ended December 31, 2015

- There were 257,131 policies in-force at December 31, 2015, of which approximately 74.6% were assumed from Citizens, 9.8% were assumed from SSIC and 15.6% were from voluntary sales
- Gross premiums written of $586.1 million and total revenue of $394.8 million
- Net premiums earned of $376.3 million
- Net income of $92.5 million
- Combined ratio of 74.9% on a gross basis and 65.0% on a net basis
- Cash, cash equivalents and investments of $636.4 million, with total assets of $837.4 million

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Consolidated Results of Operations

The following table summarizes our results of operations for the periods indicated (in thousands, except per share amounts):

	Year Ended December 31,		
	2015	2014	2013
	(in thousands)		
REVENUE:			
Gross premiums written	$586,098	$436,407	$218,537
Increase in gross unearned premiums	(61,358)	(124,893)	(78,578)
Gross premiums earned	524,740	311,514	139,959
Ceded premiums	(148,472)	(87,902)	(44,800)
Net premiums earned	376,268	223,612	95,159
Retroactive reinsurance [(1)]	—	—	26,046
Net investment income	7,421	3,849	1,049
Net realized gains (losses)	1,508	304	(323)
Other revenue	9,595	6,055	2,901
Total revenue	$394,792	$233,820	$124,832
EXPENSES:			
Losses and loss adjustment expenses	141,191	89,560	38,501
Policy acquisition costs	57,186	36,510	6,150
General and administrative expenses	46,125	33,498	24,720
Total expenses	244,502	159,568	69,371
Income before income taxes	150,290	74,252	55,461
Provision for income taxes	57,778	27,155	21,248
Net income	$92,512	$47,097	$34,213
Earnings per share			
Basic	$3.08	$1.92	$2.39
Diluted	$3.05	$1.82	$2.36
Selected Other Data			
Book value per share	$11.71	$8.56	$7.20
Growth in book value per share	36.8 %	18.9 %	113.0 %
Return on average equity	30.2 %	26.5 %	45.0 %

	Year Ended December 31,		
	2015	2014	2013
Ratios to Gross Premiums Earned:	(unaudited)		
Ceded premium ratio	28.3%	28.2%	32.0%
Loss ratio	26.9%	28.7%	27.5%
Expense ratio	19.7%	22.5%	22.1%

Combined ratio	74.9%	79.4%	81.6%
Ratios to Net Premiums Earned:			
Loss ratio	37.5%	40.1%	40.5