

HCI Group, Inc.  
Form 10-Q  
August 03, 2017  
[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**Form 10-Q**

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

**For the quarterly period ended June 30, 2017**

**OR**

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

**Commission File Number 001-34126**

**HCI Group, Inc.**

**(Exact name of Registrant as specified in its charter)**

**Florida**  
**(State of**  
**Incorporation)**

**20-5961396**  
**(IRS Employer**  
**Identification No.)**

**5300 West Cypress Street, Suite 100**  
**Tampa, FL 33607**

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

**(813) 849-9500**

**(Registrant's telephone number, including area code)**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.

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

The aggregate number of shares of the Registrant's Common Stock, no par value, outstanding on July 27, 2017 was 9,986,330.



Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****TABLE OF CONTENTS**

|                                            | <b>Page</b>                                                                                               |
|--------------------------------------------|-----------------------------------------------------------------------------------------------------------|
| <b><u>PART I FINANCIAL INFORMATION</u></b> |                                                                                                           |
| <b>Item 1</b>                              | <b><u>Financial Statements</u></b>                                                                        |
|                                            | <u>Consolidated Balance Sheets:</u>                                                                       |
|                                            | June 30, 2017 (unaudited) and December 31, 2016 1                                                         |
|                                            | <u>Consolidated Statements of Income:</u>                                                                 |
|                                            | Three and six months ended June 30, 2017 and 2016 (unaudited) 2                                           |
|                                            | <u>Consolidated Statements of Comprehensive Income:</u>                                                   |
|                                            | Three and six months ended June 30, 2017 and 2016 (unaudited) 3                                           |
|                                            | <u>Consolidated Statements of Cash Flows:</u>                                                             |
|                                            | Six months ended June 30, 2017 and 2016 (unaudited) 4-5                                                   |
|                                            | <u>Consolidated Statements of Stockholders' Equity:</u>                                                   |
|                                            | Six months ended June 30, 2017 and 2016 (unaudited) 6-7                                                   |
|                                            | <u>Notes to Consolidated Financial Statements (unaudited)</u> 8-40                                        |
| <b>Item 2</b>                              | <b><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b> 41-55 |
| <b>Item 3</b>                              | <b><u>Quantitative and Qualitative Disclosures about Market Risk</u></b> 55-57                            |
| <b>Item 4</b>                              | <b><u>Controls and Procedures</u></b> 57                                                                  |
| <b><u>PART II OTHER INFORMATION</u></b>    |                                                                                                           |
| <b>Item 1</b>                              | <b><u>Legal Proceedings</u></b> 58                                                                        |
| <b>Item 1A</b>                             | <b><u>Risk Factors</u></b> 58                                                                             |
| <b>Item 2</b>                              | <b><u>Unregistered Sales of Equity Securities and Use of Proceeds</u></b> 59-60                           |
| <b>Item 3</b>                              | <b><u>Defaults upon Senior Securities</u></b> 60                                                          |
| <b>Item 4</b>                              | <b><u>Mine Safety Disclosures</u></b> 60                                                                  |
| <b>Item 5</b>                              | <b><u>Other Information</u></b> 60                                                                        |
| <b>Item 6</b>                              | <b><u>Exhibits</u></b>                                                                                    |
|                                            | <b><u>Signatures</u></b>                                                                                  |
|                                            | <b><u>Certifications</u></b>                                                                              |

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1 Financial Statements****HCI GROUP, INC. AND SUBSIDIARIES****Consolidated Balance Sheets****(Dollar amounts in thousands)**

|                                                                                                                      | <b>June 30,<br/>2017<br/>(Unaudited)</b> | <b>December 31,<br/>2016</b> |
|----------------------------------------------------------------------------------------------------------------------|------------------------------------------|------------------------------|
| <b>Assets</b>                                                                                                        |                                          |                              |
| Fixed-maturity securities, available for sale, at fair value (amortized cost: \$247,147 and \$167,231, respectively) | \$ 248,646                               | \$ 166,248                   |
| Equity securities, available for sale, at fair value (cost: \$52,785 and \$47,750, respectively)                     | 56,152                                   | 53,035                       |
| Limited partnership investments, at equity                                                                           | 19,900                                   | 29,263                       |
| Investment in unconsolidated joint venture, at equity                                                                | 1,680                                    | 2,102                        |
| Real estate investments (Note 4 Consolidated Variable Interest Entity)                                               | 49,286                                   | 48,086                       |
| Total investments                                                                                                    | 375,664                                  | 298,734                      |
| Cash and cash equivalents (Note 4 Consolidated Variable Interest Entity)                                             | 296,520                                  | 280,531                      |
| Accrued interest and dividends receivable                                                                            | 2,081                                    | 1,654                        |
| Income taxes receivable                                                                                              | 973                                      | 2,811                        |
| Premiums receivable                                                                                                  | 26,621                                   | 17,276                       |
| Prepaid reinsurance premiums                                                                                         | 36,032                                   | 24,554                       |
| Deferred policy acquisition costs                                                                                    | 20,251                                   | 16,639                       |
| Property and equipment, net                                                                                          | 12,080                                   | 11,374                       |
| Intangible assets, net                                                                                               | 4,656                                    | 4,899                        |
| Deferred income taxes, net                                                                                           |                                          | 250                          |
| Other assets (Note 4 Consolidated Variable Interest Entity)                                                          | 17,840                                   | 11,342                       |
| Total assets                                                                                                         | \$ 792,718                               | \$ 670,064                   |
| <b>Liabilities and Stockholders Equity</b>                                                                           |                                          |                              |
| Losses and loss adjustment expenses                                                                                  | \$ 73,089                                | \$ 70,492                    |
| Unearned premiums                                                                                                    | 199,970                                  | 175,803                      |
| Advance premiums                                                                                                     | 14,967                                   | 4,651                        |
| Assumed reinsurance balances payable                                                                                 | 181                                      | 3,294                        |
| Accrued expenses (Note 4 Consolidated Variable Interest Entity)                                                      | 10,828                                   | 6,513                        |
| Deferred income taxes, net                                                                                           | 4,383                                    |                              |
| Long-term debt                                                                                                       | 234,817                                  | 138,863                      |
| Other liabilities (Note 4 Consolidated Variable Interest Entity)                                                     | 16,058                                   | 26,702                       |

|                                                                                                                                                                       |            |            |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------|------------|
| Total liabilities                                                                                                                                                     | 554,293    | 426,318    |
| Commitments and contingencies (Note 16)                                                                                                                               |            |            |
| Stockholders' equity:                                                                                                                                                 |            |            |
| 7% Series A cumulative convertible preferred stock (no par value, 1,500,000 shares authorized, no shares issued and outstanding)                                      |            |            |
| Series B junior participating preferred stock (no par value, 400,000 shares authorized, no shares issued or outstanding)                                              |            |            |
| Preferred stock (no par value, 18,100,000 shares authorized, no shares issued or outstanding)                                                                         |            |            |
| Common stock (no par value, 40,000,000 shares authorized, 9,172,802 and 9,662,761 shares issued and outstanding at June 30, 2017 and December 31, 2016, respectively) |            |            |
| Additional paid-in capital                                                                                                                                            |            | 8,139      |
| Retained income                                                                                                                                                       | 235,436    | 232,964    |
| Accumulated other comprehensive income, net of taxes                                                                                                                  | 2,989      | 2,643      |
| Total stockholders' equity                                                                                                                                            | 238,425    | 243,746    |
| Total liabilities and stockholders' equity                                                                                                                            | \$ 792,718 | \$ 670,064 |

See accompanying Notes to Consolidated Financial Statements.

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Consolidated Statements of Income****(Unaudited)****(Dollar amounts in thousands, except per share amounts)**

|                                                                        | <b>Three Months<br/>Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |             |
|------------------------------------------------------------------------|--------------------------------------------|-------------|--------------------------------------|-------------|
|                                                                        | <b>2017</b>                                | <b>2016</b> | <b>2017</b>                          | <b>2016</b> |
| <b>Revenue</b>                                                         |                                            |             |                                      |             |
| Gross premiums earned                                                  | \$ 90,088                                  | \$ 94,912   | \$ 181,707                           | \$ 193,731  |
| Premiums ceded                                                         | (28,241)                                   | (36,384)    | (56,824)                             | (76,756)    |
| Net premiums earned                                                    | 61,847                                     | 58,528      | 124,883                              | 116,975     |
| Net investment income                                                  | 2,810                                      | 1,725       | 5,644                                | 3,215       |
| Net realized investment gains                                          | 1,787                                      | 391         | 2,502                                | 316         |
| Net other-than-temporary impairment losses recognized in income:       |                                            |             |                                      |             |
| Total other-than-temporary impairment losses                           | (177)                                      | (228)       | (390)                                | (636)       |
| Portion of loss recognized in other comprehensive income, before taxes |                                            | (314)       |                                      | (581)       |
| Net other-than-temporary impairment losses                             | (177)                                      | (542)       | (390)                                | (1,217)     |
| Policy fee income                                                      | 908                                        | 988         | 1,816                                | 1,995       |
| Gain on repurchases of convertible senior notes                        |                                            |             |                                      | 153         |
| Other                                                                  | 405                                        | 430         | 838                                  | 830         |
| Total revenue                                                          | 67,580                                     | 61,520      | 135,293                              | 122,267     |
| <b>Expenses</b>                                                        |                                            |             |                                      |             |
| Losses and loss adjustment expenses                                    | 27,665                                     | 26,272      | 53,194                               | 53,352      |
| Policy acquisition and other underwriting expenses                     | 10,070                                     | 10,879      | 19,719                               | 21,989      |
| Salaries and wages                                                     | 5,443                                      | 5,680       | 10,446                               | 11,064      |
| Interest expense                                                       | 4,378                                      | 2,611       | 7,920                                | 5,440       |
| Loss on repurchases of senior notes                                    | 743                                        |             | 743                                  |             |
| Other operating expenses                                               | 4,976                                      | 4,849       | 9,824                                | 9,496       |
| Total operating expenses                                               | 53,275                                     | 50,291      | 101,846                              | 101,341     |
| Income before income taxes                                             | 14,305                                     | 11,229      | 33,447                               | 20,926      |
| Income tax expense                                                     | 4,763                                      | 4,205       | 11,885                               | 7,846       |
| Net income                                                             | \$ 9,542                                   | \$ 7,024    | \$ 21,562                            | \$ 13,080   |

Edgar Filing: HCI Group, Inc. - Form 10-Q

|                            |    |      |    |      |    |      |    |      |
|----------------------------|----|------|----|------|----|------|----|------|
| Basic earnings per share   | \$ | 1.05 | \$ | 0.71 | \$ | 2.32 | \$ | 1.31 |
| Diluted earnings per share | \$ | 0.93 | \$ | 0.71 | \$ | 2.07 | \$ | 1.31 |
| Dividends per share        | \$ | 0.35 | \$ | 0.30 | \$ | 0.70 | \$ | 0.60 |

See accompanying Notes to Consolidated Financial Statements.



Table of Contents

**HCI GROUP, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Comprehensive Income**  
**(Unaudited)**  
**(Amounts in thousands)**

|                                                              | <b>Three Months</b> |             | <b>Six Months Ended</b> |             |
|--------------------------------------------------------------|---------------------|-------------|-------------------------|-------------|
|                                                              | <b>Ended</b>        |             | <b>June 30,</b>         |             |
|                                                              | <b>2017</b>         | <b>2016</b> | <b>2017</b>             | <b>2016</b> |
| Net income                                                   | \$ 9,542            | \$ 7,024    | \$ 21,562               | \$ 13,080   |
| Other comprehensive income:                                  |                     |             |                         |             |
| Change in unrealized (loss) gain on investments:             |                     |             |                         |             |
| Net unrealized gain arising during the period                | 654                 | 5,893       | 2,667                   | 8,056       |
| Other-than-temporary impairment loss charged to income       | 177                 | 542         | 390                     | 1,217       |
| Call and repayment losses charged to investment income       | 8                   | 10          | 9                       | 11          |
| Reclassification adjustment for net realized gains           | (1,787)             | (391)       | (2,502)                 | (316)       |
| Net change in unrealized (loss) gain                         | (948)               | 6,054       | 564                     | 8,968       |
| Deferred income taxes on above change                        | 365                 | (2,336)     | (218)                   | (3,460)     |
| Total other comprehensive (loss) income, net of income taxes | (583)               | 3,718       | 346                     | 5,508       |
| Comprehensive income                                         | \$ 8,959            | \$ 10,742   | \$ 21,908               | \$ 18,588   |

See accompanying Notes to Consolidated Financial Statements.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Consolidated Statements of Cash Flows****(Unaudited)****(Amounts in thousands)**

|                                                                                          | <b>Six Months Ended<br/>June 30,</b> |               |
|------------------------------------------------------------------------------------------|--------------------------------------|---------------|
|                                                                                          | <b>2017</b>                          | <b>2016</b>   |
| <b>Cash flows from operating activities:</b>                                             |                                      |               |
| Net income                                                                               | \$ 21,562                            | \$ 13,080     |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b> |                                      |               |
| Stock-based compensation                                                                 | 2,139                                | 1,948         |
| Net amortization of premiums on investments in fixed-maturity securities                 | 535                                  | 255           |
| Depreciation and amortization                                                            | 4,380                                | 2,656         |
| Deferred income tax benefits                                                             | (1,430)                              | (1,388)       |
| Net realized investment gains                                                            | (2,502)                              | (316)         |
| Other-than-temporary impairment losses                                                   | 390                                  | 1,217         |
| Income from unconsolidated joint venture                                                 | (142)                                | (228)         |
| Distribution received from unconsolidated joint venture                                  | 147                                  |               |
| Gain on repurchases of convertible senior notes                                          |                                      | (153)         |
| Loss on repurchases of senior notes                                                      | 743                                  |               |
| Net (income) loss from limited partnership interests                                     | (1,332)                              | 1,065         |
| Distributions received from limited partnership interests                                | 426                                  | 44            |
| Foreign currency remeasurement (gain) loss                                               | (51)                                 | 19            |
| Other                                                                                    | 116                                  |               |
| <b>Changes in operating assets and liabilities:</b>                                      |                                      |               |
| Accrued interest and dividends receivable                                                | (427)                                | 1             |
| Income taxes                                                                             | 1,838                                | (3,213)       |
| Premiums receivable                                                                      | (9,345)                              | (7,597)       |
| Prepaid reinsurance premiums                                                             | (11,478)                             | 4,954         |
| Deferred policy acquisition costs                                                        | (3,612)                              | (2,489)       |
| Other assets                                                                             | (6,971)                              | 28,442        |
| Losses and loss adjustment expenses                                                      | 2,597                                | 3,037         |
| Unearned premiums                                                                        | 24,167                               | 21,310        |
| Advance premiums                                                                         | 10,316                               | 8,841         |
| Assumed reinsurance balances payable                                                     | (3,113)                              | (1,084)       |
| Accrued expenses and other liabilities                                                   | 2,411                                | 34            |
| <b>Net cash provided by operating activities</b>                                         | <b>31,364</b>                        | <b>70,435</b> |
| <b>Cash flows from investing activities:</b>                                             |                                      |               |
| Investments in limited partnership interests                                             | (1,489)                              | (2,448)       |
| Distributions received from limited partnership interests                                | 11,758                               |               |

Edgar Filing: HCI Group, Inc. - Form 10-Q

|                                                                             |          |          |
|-----------------------------------------------------------------------------|----------|----------|
| Distribution from unconsolidated joint venture                              | 417      |          |
| Purchase of property and equipment                                          | (1,295)  | (485)    |
| Purchase of real estate investments                                         | (1,931)  | (878)    |
| Purchase of fixed-maturity securities                                       | (91,354) | (39,673) |
| Purchase of equity securities                                               | (22,738) | (8,410)  |
| Proceeds from sales of fixed-maturity securities                            | 6,873    | 33,524   |
| Proceeds from calls, repayments and maturities of fixed-maturity securities | 3,937    | 1,074    |
| Proceeds from sales of equity securities                                    | 20,902   | 9,155    |
| Net cash used in investing activities                                       | (74,920) | (8,141)  |

(continued)

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Consolidated Statements of Cash Flows, continued****(Unaudited)****(Amounts in thousands)**

|                                                                             | <b>Six Months Ended<br/>June 30,</b> |                   |
|-----------------------------------------------------------------------------|--------------------------------------|-------------------|
|                                                                             | <b>2017</b>                          | <b>2016</b>       |
| <b>Cash flows from financing activities:</b>                                |                                      |                   |
| Cash dividends paid                                                         | (7,026)                              | (6,310)           |
| Cash dividends received under share repurchase forward contract             | 503                                  | 374               |
| Proceeds from exercise of common stock options                              | 75                                   |                   |
| Proceeds from issuance of long-term debt                                    | 143,859                              | 9,200             |
| Repurchases of convertible senior notes                                     |                                      | (11,347)          |
| Repurchases of senior notes                                                 | (40,250)                             |                   |
| Repayment of debt                                                           | (465)                                | (150)             |
| Repurchases of common stock                                                 | (30,636)                             | (447)             |
| Repurchases of common stock under share repurchase plan                     | (1,590)                              | (12,015)          |
| Debt issuance costs                                                         | (4,975)                              | (177)             |
| Tax benefits on stock-based compensation                                    |                                      | 131               |
| <b>Net cash provided by (used in) financing activities</b>                  | <b>59,495</b>                        | <b>(20,741)</b>   |
| Effect of exchange rate changes on cash                                     | 50                                   | (17)              |
| <b>Net increase in cash and cash equivalents</b>                            | <b>15,989</b>                        | <b>41,536</b>     |
| Cash and cash equivalents at beginning of period                            | 280,531                              | 267,738           |
| <b>Cash and cash equivalents at end of period</b>                           | <b>\$ 296,520</b>                    | <b>\$ 309,274</b> |
| <b>Supplemental disclosure of cash flow information:</b>                    |                                      |                   |
| Cash paid for income taxes                                                  | \$ 11,476                            | \$ 12,315         |
| Cash paid for interest                                                      | \$ 3,620                             | \$ 3,746          |
| <b>Non-cash investing and financing activities:</b>                         |                                      |                   |
| Unrealized gain on investments in available-for-sale securities, net of tax | \$ 346                               | \$ 5,508          |
| Conversion of revolving credit facility to long-term debt                   | \$ 9,441                             | \$                |
| Receivable from sales of available-for-sale securities                      | \$                                   | \$ 95             |

|                                                       |    |     |    |     |
|-------------------------------------------------------|----|-----|----|-----|
| Payable on purchases of available-for-sale securities | \$ | 694 | \$ | 127 |
|-------------------------------------------------------|----|-----|----|-----|

See accompanying Notes to Consolidated Financial Statements.

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Consolidated Statement of Stockholders Equity****Six Months Ended June 30, 2017****(Unaudited)****(Dollar amounts in thousands)**

|                                                                                           | <b>Common Stock<br/>Shares</b> | <b>Common Stock<br/>Amount</b> | <b>Additional<br/>Paid-In<br/>Capital</b> | <b>Retained<br/>Income</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income,<br/>Net of Tax</b> | <b>Total<br/>Stockholders<br/>Equity</b> |
|-------------------------------------------------------------------------------------------|--------------------------------|--------------------------------|-------------------------------------------|----------------------------|---------------------------------------------------------------------------|------------------------------------------|
| Balance at December 31, 2016                                                              | 9,662,761                      | \$                             | \$ 8,139                                  | \$ 232,964                 | \$ 2,643                                                                  | \$ 243,746                               |
| Net income                                                                                |                                |                                |                                           | 21,562                     |                                                                           | 21,562                                   |
| Total other comprehensive income,<br>net of income taxes                                  |                                |                                |                                           |                            | 346                                                                       | 346                                      |
| Exercise of common stock options                                                          | 30,000                         |                                | 75                                        |                            |                                                                           | 75                                       |
| Issuance of restricted stock                                                              | 154,936                        |                                |                                           |                            |                                                                           |                                          |
| Forfeiture of restricted stock                                                            | (10,874)                       |                                |                                           |                            |                                                                           |                                          |
| Repurchase and retirement of<br>common stock                                              | (434,505)                      |                                | (21,236)                                  |                            |                                                                           | (21,236)                                 |
| Repurchase and retirement of<br>common stock under share repurchase<br>plan               | (38,416)                       |                                | (1,590)                                   |                            |                                                                           | (1,590)                                  |
| Repurchase of common stock under<br>prepaid forward contract                              | (191,100)                      |                                | (9,400)                                   |                            |                                                                           | (9,400)                                  |
| Equity component on 4.25%<br>convertible senior notes (net of<br>offering costs of \$543) |                                |                                | 15,151                                    |                            |                                                                           | 15,151                                   |
| Deferred taxes on debt discount                                                           |                                |                                | (5,845)                                   |                            |                                                                           | (5,845)                                  |
| Common stock dividends                                                                    |                                |                                |                                           | (6,523)                    |                                                                           | (6,523)                                  |
| Stock-based compensation                                                                  |                                |                                | 2,139                                     |                            |                                                                           | 2,139                                    |
| Additional paid-in capital shortfall<br>allocated to retained income                      |                                |                                | 12,567                                    | (12,567)                   |                                                                           |                                          |
| Balance at June 30, 2017                                                                  | 9,172,802                      | \$                             | \$                                        | \$ 235,436                 | \$ 2,989                                                                  | \$ 238,425                               |

See accompanying Notes to Consolidated Financial Statements.

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Consolidated Statement of Stockholders Equity - continued****Six Months Ended June 30, 2016****(Unaudited)****(Dollar amounts in thousands)**

|                                                                             | <b>Common Stock<br/>Shares</b> | <b>Common Stock<br/>Amount</b> | <b>Additional<br/>Paid-In<br/>Capital</b> | <b>Retained<br/>Income</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>(Loss)<br/>Income,<br/>Net of Tax</b> | <b>Total<br/>Stockholders<br/>Equity</b> |
|-----------------------------------------------------------------------------|--------------------------------|--------------------------------|-------------------------------------------|----------------------------|--------------------------------------------------------------------------------------|------------------------------------------|
| Balance at December 31, 2015                                                | 10,292,256                     | \$                             | \$ 23,879                                 | \$ 215,634                 | \$ (1,791)                                                                           | \$ 237,722                               |
| Net income                                                                  |                                |                                |                                           | 13,080                     |                                                                                      | 13,080                                   |
| Total other comprehensive income,<br>net of income taxes                    |                                |                                |                                           |                            | 5,508                                                                                | 5,508                                    |
| Issuance of restricted stock                                                | 102,440                        |                                |                                           |                            |                                                                                      |                                          |
| Forfeiture of restricted stock                                              | (5,897)                        |                                |                                           |                            |                                                                                      |                                          |
| Cancellation of restricted stock                                            | (160,000)                      |                                |                                           |                            |                                                                                      |                                          |
| Repurchase and retirement of<br>common stock                                | (14,400)                       |                                | (447)                                     |                            |                                                                                      | (447)                                    |
| Repurchase and retirement of<br>common stock under share<br>repurchase plan | (376,796)                      |                                | (12,015)                                  |                            |                                                                                      | (12,015)                                 |
| Common stock dividends                                                      |                                |                                |                                           | (5,936)                    |                                                                                      | (5,936)                                  |
| Tax benefits on stock-based<br>compensation                                 |                                |                                | 131                                       |                            |                                                                                      | 131                                      |
| Tax shortfalls on stock-based<br>compensation                               |                                |                                | (234)                                     |                            |                                                                                      | (234)                                    |
| Stock-based compensation                                                    |                                |                                | 1,948                                     |                            |                                                                                      | 1,948                                    |
| Balance at June 30, 2016                                                    | 9,837,603                      | \$                             | \$ 13,262                                 | \$ 222,778                 | \$ 3,717                                                                             | \$ 239,757                               |

See accompanying Notes to Consolidated Financial Statements.

---

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

**Note 1 Nature of Operations**

HCI Group, Inc., together with its majority-owned and controlled subsidiaries (collectively, the Company), is primarily engaged in the property and casualty insurance business through Homeowners Choice Property & Casualty Insurance Company, Inc. (HCPCI), its principal operating subsidiary. HCPCI is authorized to underwrite various homeowners' property and casualty insurance products and allied lines business in the state of Florida. HCPCI also offers flood-endorsed and wind-only policies to new and pre-existing Florida customers. HCPCI's operations are supported by HCI Group, Inc. and certain HCI subsidiaries. During the second quarter of 2017, HCPCI received regulatory approval to write residential property and casualty insurance in the states of Arkansas and Pennsylvania.

**Note 2 Summary of Significant Accounting Policies**

***Basis of Presentation***

The accompanying unaudited, consolidated financial statements for the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information, and the Securities and Exchange Commission (SEC) rules for interim financial reporting. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with U.S. GAAP have been omitted pursuant to such rules and regulations. However, in the opinion of management, the accompanying consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the Company's financial position as of June 30, 2017 and the results of operations and cash flows for the periods presented. The results of operations for the interim periods presented are not necessarily indicative of the results of operations to be expected for any subsequent interim period or for the fiscal year ending December 31, 2017. The accompanying unaudited consolidated financial statements and notes thereto should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2016 included in the Company's Form 10-K, which was filed with the SEC on February 22, 2017.

In preparing the interim unaudited consolidated financial statements, management was required to make certain judgments, assumptions, and estimates that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the financial reporting date and throughout the periods being reported upon. Certain of the estimates result from judgments that can be subjective and complex and consequently actual results may differ from these estimates.

Material estimates that are particularly susceptible to significant change in the near term are related to the Company's losses and loss adjustment expenses, which include amounts estimated for claims incurred but not yet reported. The Company uses various assumptions and actuarial data it believes to be reasonable under the circumstances to make these estimates. In addition, accounting policies for reinsurance contracts with retrospective provisions, deferred income taxes, and stock-based compensation expense involve significant judgments and estimates material to the Company's consolidated financial statements.

All significant intercompany balances and transactions have been eliminated.





**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

***Adoption of New Accounting Standards***

Effective January 1, 2017, the Company adopted Accounting Standards Update No. 2016-09, Compensation – Stock Compensation (Topic 718), which amends the accounting for share-based payment transactions including the related income taxes, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Amendments related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements, and forfeitures, which is applied using a modified retrospective transition method, have no impact on the Company's comparative consolidated financial statements. In addition, the retrospective application of the amendments related to the presentation of employee taxes paid does not have an impact on the Company's comparative consolidated statement of cash flows. Upon adoption of this standard, the Company elected to account for forfeitures of share-based awards when they occur and apply the amendments related to the presentation of excess tax benefits on the statement of cash flows prospectively. Under the new standard, the Company is required to recognize any excess tax benefits and tax deficiencies in the Company's consolidated statement of income.

***Long-Term Debt***

Long-term debt is generally classified as a liability and carried at amortized cost, net of any discount and issuance costs. At issuance, a debt instrument with embedded features such as conversion and redemption options is evaluated to determine whether bifurcation and derivative accounting is applicable. If such instrument is not subject to derivative accounting, it is further evaluated to determine if the Company is required to separately account for the liability and equity components.

To determine the carrying values of the liability and equity components at issuance, the Company measures the fair value of a similar liability, including any embedded features other than the conversion option, and assigns such value to the liability component. The liability component's fair value is then subtracted from the initial proceeds to determine the carrying value of the debt instrument's equity component, which is included in additional paid-in capital.

Any embedded feature other than the conversion option is evaluated at issuance to determine if it is probable that such embedded feature will be exercised. If the Company concludes that the exercisability of that embedded feature is not probable, the embedded feature is considered to be non-substantive and would not impact the initial measurement and expected life of the debt instrument's liability component.

Transaction costs related to issuing a debt instrument that embodies both liability and equity components are allocated to the liability and equity components in proportion to the allocation of the proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. Debt issuance costs are capitalized and presented as a deduction from the carrying value of the debt. Both debt discount and deferred debt issuance costs are amortized to interest expense over the expected life of the debt instrument using the effective interest method. Equity issuance costs are a reduction to the proceeds allocated to the equity component.



**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

***Common Share Repurchases***

The Company primarily repurchases its common stock in the open market through share repurchase programs and from institutional investors in private transactions such as prepaid share repurchase forward contracts and share repurchase agreements.

A prepaid share repurchase forward contract is generally a contract that allows a party to buy from the counterparty a specified number of common shares at a specific time at a given forward price. The Company entered into such a contract and evaluated the characteristics of the forward contract to determine whether it met the definition of a derivative financial instrument pursuant to U.S. GAAP. The Company determined the forward contract is an equity contract on the Company's common shares requiring physical settlement in common shares of the Company. As such, the transaction is recognized as a component of stockholders' equity and there will be no recognition in earnings for changes in fair value in subsequent periods.

In general, the Company first allocates the purchase price or the prepayment amount to additional paid-in capital to the extent available and the remaining balance is allocated to retained income. Due to past and recent share repurchases, the Company's additional paid-in capital has been exhausted and shall remain so until the Company fully recoups the total amount allocated to retained income.

***Reclassifications.*** Certain reclassifications of prior year amounts have been made to conform to the current year presentation.

**Note 3 Recent Accounting Pronouncements**

***Accounting Standards Update No. 2017-09.*** In May 2017, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update No. 2017-09 ( ASU 2017-09 ), Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting, which provides guidance about which changes to the terms or conditions of a share-based payment award require an application of modification accounting. ASU 2017-09 is effective for the Company beginning with the first quarter of 2018. Early adoption is permitted. The Company is currently evaluating the impact of this guidance on the Company's consolidated financial statements.

***Accounting Standards Update No. 2017-08.*** In March 2017, the FASB issued Accounting Standards Update No. 2017-08 ( ASU 2017-08 ), Receivables Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities, which amends guidance on the amortization period of premiums on certain purchased callable debt securities. Specifically, this update shortens the amortization period of certain purchased callable debt securities to the earliest call date. ASU 2017-08 is effective for the Company beginning with the first quarter of 2019. Early adoption is permitted. The Company is currently evaluating the impact of this guidance on the Company's consolidated financial statements.



---

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

**Accounting Standards Update No. 2017-05.** In February 2017, the FASB issued Accounting Standards Update No. 2017-05 ( ASU 2017-05 ), Other Income Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20), which clarifies the scope of asset derecognition guidance and accounting for partial sales of nonfinancial assets. In addition, ASU 2017-15 eliminates the exception in the financial asset guidance for transfers of investments including equity method investments in real estate entities and supersedes the guidance in the Exchanges of a Nonfinancial Asset for a Noncontrolling Ownership Interest subsection (Topic 845). ASU 2017-05 is effective for the Company beginning with the first quarter of 2018. The Company is currently evaluating the impact of this guidance on the Company's consolidated financial statements.

**Accounting Standards Update No. 2017-03.** In January 2017, the FASB issued Accounting Standards Update No. 2017-03 ( ASU 2017-03 ), Accounting Changes and Error Corrections (Topic 250) and Investments Equity Method and Joint Ventures (Topic 323), which adds and amends SEC paragraphs pursuant to the SEC Staff Announcements at the September 22, 2016 and November 17, 2016 Emerging Issues Task Force meetings. The announcement made at the September 22, 2016 meeting provides the SEC staff view on the disclosure of the impact that recently issued accounting standards will have on a public entity's financial statements when the standards are adopted in a future period. This announcement applies to ASU 2014-09, Revenue from Contracts with Customers (Topic 606); ASU 2016-02, Leases (Topic 842); ASU 2016-13, Financial Instruments Credit Losses (Topic 326) and any subsequent amendments to guidance in the ASUs that are issued prior to the adoption of the aforementioned ASUs.

**Accounting Standards Update No. 2017-01.** In January 2017, the FASB issued Accounting Standards Update No. 2017-01 ( ASU 2017-01 ), Business Combination (Topic 805), which clarifies the definition of a business and provides a screen to determine when an integrated set of assets and activities is not a business. If the screen is not met, a set must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output to be considered a business. ASU 2017-01 is effective for the Company beginning with the first quarter of 2018. Early adoption is permitted under certain circumstances. When adopted, this guidance will impact how the Company determines whether a transaction should be accounted for as a business acquisition or disposal in a future period.

*Accounting Standards to be Adopted in Fiscal Year 2018*

In January 2016, the FASB issued Accounting Standards Update No. 2016-01 ( ASU 2016-01 ), Financial Instruments Overall (Subtopic 825-10), primarily requiring all equity investments other than those accounted for under the equity method of accounting or those that result in consolidation of the investee to be measured at fair value with changes in the fair value recognized through net income. The application of ASU 2016-01 could cause the Company to experience significant volatility in earnings. Under current accounting policy, the Company recognizes unrealized holding gains and losses on available-for-sale equity securities in stockholders' equity as a component of accumulated other comprehensive income. In the year of adoption, available-for-sale equity securities' unrealized holding gains and losses reported in accumulated other comprehensive income at December 31, 2017 will be reclassified to beginning retained income. Any subsequent changes in fair value will be recognized in the consolidated statement of income. In addition, the classification of the Company's equity securities with readily determinable fair values as

available-for-sale in the consolidated balance sheet and related disclosures will be eliminated.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 ( ASU 2014-09 ), Revenue from Contracts with Customers (Topic 606). The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance throughout the Industry Topics of the Codification. ASU 2014-09 also amends the existing requirements for the recognition of a gain or loss on the transfer of nonfinancial assets that are not in a contract with a customer to be consistent with the guidance in this ASU. ASU 2014-09 permits two methods of adoption: a full retrospective method or a modified retrospective method. This standard could impact the timing and amounts of revenue recognized. The Company has identified and reviewed impacted revenue generating activities in accordance with the five-step revenue recognition model specified by this standard. The Company elects to use a modified retrospective method for transition to the new revenue recognition standard. Based on the Company's assessment, the impact will be limited to the related disclosures of certain revenue generating activities as its primary source of revenue from insurance premiums is not within the scope of this new standard.

**Note 4 Investments*****Available-for-Sale Securities***

The Company holds investments in fixed-maturity securities and equity securities that are classified as available-for-sale. At June 30, 2017 and December 31, 2016, the cost or amortized cost, gross unrealized gains and losses, and estimated fair value of the Company's available-for-sale securities by security type were as follows:

|                                                   | <b>Cost or<br/>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gain</b> | <b>Gross<br/>Unrealized<br/>Loss</b> | <b>Estimated<br/>Fair<br/>Value</b> |
|---------------------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|-------------------------------------|
| <b><i>As of June 30, 2017</i></b>                 |                                       |                                      |                                      |                                     |
| <i>Fixed-maturity securities</i>                  |                                       |                                      |                                      |                                     |
| U.S. Treasury and U.S. government agencies        | \$ 47,134                             | \$ 7                                 | \$ (95)                              | \$ 47,046                           |
| Corporate bonds                                   | 112,603                               | 969                                  | (1,176)                              | 112,396                             |
| State, municipalities, and political subdivisions | 77,429                                | 1,760                                | (197)                                | 78,992                              |
| Exchange-traded debt                              | 9,744                                 | 254                                  | (39)                                 | 9,959                               |
| Redeemable preferred stock                        | 237                                   | 16                                   |                                      | 253                                 |
| <b>Total</b>                                      | <b>247,147</b>                        | <b>3,006</b>                         | <b>(1,507)</b>                       | <b>248,646</b>                      |
| <i>Equity securities</i>                          |                                       |                                      |                                      |                                     |
|                                                   | 52,785                                | 4,292                                | (925)                                | 56,152                              |
| <b>Total available-for-sale securities</b>        | <b>\$ 299,932</b>                     | <b>\$ 7,298</b>                      | <b>\$ (2,432)</b>                    | <b>\$ 304,798</b>                   |



**As of December 31, 2016***Fixed-maturity securities*

|                                                   |          |     |         |          |
|---------------------------------------------------|----------|-----|---------|----------|
| U.S. Treasury and U.S. government agencies        | \$ 1,975 | \$  | \$ (36) | \$ 1,939 |
| Corporate bonds                                   | 75,538   | 607 | (1,641) | 74,504   |
| State, municipalities, and political subdivisions | 78,018   | 776 | (488)   | 78,306   |
| Exchange-traded debt                              | 11,463   | 36  | (237)   | 11,262   |
| Redeemable preferred stock                        | 237      | 3   | (3)     | 237      |

|       |         |       |         |         |
|-------|---------|-------|---------|---------|
| Total | 167,231 | 1,422 | (2,405) | 166,248 |
|-------|---------|-------|---------|---------|

|                          |        |       |       |        |
|--------------------------|--------|-------|-------|--------|
| <i>Equity securities</i> | 47,750 | 5,769 | (484) | 53,035 |
|--------------------------|--------|-------|-------|--------|

|                                     |            |          |            |            |
|-------------------------------------|------------|----------|------------|------------|
| Total available-for-sale securities | \$ 214,981 | \$ 7,191 | \$ (2,889) | \$ 219,283 |
|-------------------------------------|------------|----------|------------|------------|

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

Expected maturities will differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without penalties. The scheduled contractual maturities of fixed-maturity securities as of June 30, 2017 and December 31, 2016 are as follows:

|                                        | <b>Amortized<br/>Cost</b> | <b>Estimated<br/>Fair<br/>Value</b> |
|----------------------------------------|---------------------------|-------------------------------------|
| <b><u>As of June 30, 2017</u></b>      |                           |                                     |
| <b>Available-for-sale</b>              |                           |                                     |
| Due in one year or less                | \$ 30,824                 | \$ 30,820                           |
| Due after one year through five years  | 122,542                   | 122,184                             |
| Due after five years through ten years | 70,671                    | 71,860                              |
| Due after ten years                    | 23,110                    | 23,782                              |
|                                        | <b>\$ 247,147</b>         | <b>\$ 248,646</b>                   |

|                                        | <b>Amortized<br/>Cost</b> | <b>Estimated<br/>Fair<br/>Value</b> |
|----------------------------------------|---------------------------|-------------------------------------|
| <b><u>As of December 31, 2016</u></b>  |                           |                                     |
| <b>Available-for-sale</b>              |                           |                                     |
| Due in one year or less                | \$ 2,656                  | \$ 2,662                            |
| Due after one year through five years  | 49,915                    | 50,023                              |
| Due after five years through ten years | 90,360                    | 89,332                              |
| Due after ten years                    | 24,300                    | 24,231                              |
|                                        | <b>\$ 167,231</b>         | <b>\$ 166,248</b>                   |

***Sales of Available-for-Sale Securities***

Proceeds received, and the gross realized gains and losses from sales of available-for-sale securities, for the three and six months ended June 30, 2017 and 2016 were as follows:

|                                         | <b>Proceeds</b> | <b>Gross<br/>Realized<br/>Gains</b> | <b>Gross<br/>Realized<br/>Losses</b> |
|-----------------------------------------|-----------------|-------------------------------------|--------------------------------------|
| <u>Three months ended June 30, 2017</u> |                 |                                     |                                      |
| Fixed-maturity securities               | \$ 2,434        | \$ 6                                | \$ (18)                              |
| Equity securities                       | \$ 13,631       | \$ 2,090                            | \$ (291)                             |
| <u>Three months ended June 30, 2016</u> |                 |                                     |                                      |
| Fixed-maturity securities               | \$ 32,424       | \$ 376                              | \$                                   |
| Equity securities                       | \$ 4,801        | \$ 220                              | \$ (205)                             |
| <u>Six months ended June 30, 2017</u>   |                 |                                     |                                      |
| Fixed-maturity securities               | \$ 6,873        | \$ 29                               | \$ (22)                              |
| Equity securities                       | \$ 20,902       | \$ 2,835                            | \$ (340)                             |
| <u>Six months ended June 30, 2016</u>   |                 |                                     |                                      |
| Fixed-maturity securities               | \$ 33,524       | \$ 383                              | \$                                   |
| Equity securities                       | \$ 9,155        | \$ 359                              | \$ (426)                             |

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

***Other-than-temporary Impairment***

The Company regularly reviews its individual investment securities for other-than-temporary impairment. The Company considers various factors in determining whether each individual security is other-than-temporarily impaired, including-

the financial condition and near-term prospects of the issuer, including any specific events that may affect its operations or earnings;

the length of time and the extent to which the market value of the security has been below its cost or amortized cost;

general market conditions and industry or sector specific factors and other qualitative factors;

nonpayment by the issuer of its contractually obligated interest and principal payments; and

the Company's intent and ability to hold the investment for a period of time sufficient to allow for the recovery of costs.

**Fixed-maturity Securities**

Prior to the sale of one intent-to-sell fixed-maturity security, the Company recognized \$38 of impairment loss for this security for the three months ended June 30, 2017. For the six months ended June 30, 2017, the Company recognized \$100 of impairment losses related to the sale of two intent-to-sell fixed-maturity securities. At June 30, 2017, two fixed-maturity securities were considered other-than-temporarily impaired due to their credit risk. The Company intends to hold these two fixed-maturity securities until maturity, but does not expect a full recovery of their carrying value.

In June 2016, the Company sold one impaired fixed-maturity security that was previously intended to hold until maturity due to uncertainties surrounding the issuer's announced restructuring plan. Prior to the sale of this security, the remaining \$202 of unrealized impairment loss was reclassified from comprehensive income and recognized in total other-than-temporary impairment losses in the Company's consolidated statement of income for the three months ended June 30, 2016. For the six months ended June 30, 2016, the Company recognized \$495 of additional impairment loss in the consolidated statement of income, representing \$26 of additional loss recorded during the period and the reclassification of \$469 previously recorded in other comprehensive income. At June 30, 2016, there

was no fixed-maturity security with credit risk issue.

The following table presents a rollforward of the cumulative credit losses in other-than-temporary impairments recognized in income from available for sale fixed-maturity securities.

|                                                                                                                         | <b>2017</b> | <b>2016</b> |
|-------------------------------------------------------------------------------------------------------------------------|-------------|-------------|
| Balance at January 1                                                                                                    | \$ 475      | \$ 111      |
| Additional credit impairments on previously impaired securities                                                         |             | 293         |
| Balance at March 31                                                                                                     | 475         | 404         |
| Credit impaired security fully disposed of for which there was no prior intent or requirement to sell                   |             | (385)       |
| Reduction due to increase in expected cash flows recognized over the remaining life of the previously impaired security |             | (19)        |
| Balance at June 30                                                                                                      | \$ 475      | \$          |

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*Equity Securities

In determining whether equity securities are other than temporarily impaired, the Company considers its intent and ability to hold a security for a period of time sufficient to allow for the recovery of cost, the length of time each security has been in an unrealized loss position, the extent of the decline and the near term prospect for recovery. The Company recognized impairment losses of \$139 and \$340 in the consolidated statement of income for the three months ended June 30, 2017 and 2016, respectively. For the six months ended June 30, 2017 and 2016, the Company recognized impairment losses of \$290 and \$722, respectively. At June 30, 2017 and 2016, the Company had three and 15 equity securities, respectively, that were other-than-temporarily impaired.

Securities with gross unrealized loss positions at June 30, 2017 and December 31, 2016, aggregated by investment category and length of time the individual securities have been in a continuous loss position, are as follows:

|                                                   | Less Than Twelve<br>Months  |                            | Twelve Months or Longer     |                            | Total                       |                            |
|---------------------------------------------------|-----------------------------|----------------------------|-----------------------------|----------------------------|-----------------------------|----------------------------|
|                                                   | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value |
| <b>As of June 30, 2017</b>                        |                             |                            |                             |                            |                             |                            |
| <i>Fixed-maturity securities</i>                  |                             |                            |                             |                            |                             |                            |
| U.S. Treasury and U.S. government agencies        | \$ (95)                     | \$ 45,148                  | \$                          | \$                         | \$ (95)                     | \$ 45,148                  |
| Corporate bonds                                   | (1,169)                     | 76,604                     | (7)                         | 993                        | (1,176)                     | 77,597                     |
| State, municipalities, and political subdivisions | (165)                       | 10,715                     | (32)                        | 2,635                      | (197)                       | 13,350                     |
| Exchange-traded debt                              | (39)                        | 3,428                      |                             |                            | (39)                        | 3,428                      |
| Total fixed-maturity securities                   | (1,468)                     | 135,895                    | (39)                        | 3,628                      | (1,507)                     | 139,523                    |
| <i>Equity securities</i>                          | (869)                       | 15,837                     | (56)                        | 1,295                      | (925)                       | 17,132                     |
| Total available-for-sale securities               | \$ (2,337)                  | \$ 151,732                 | \$ (95)                     | \$ 4,923                   | \$ (2,432)                  | \$ 156,655                 |

At June 30, 2017, there were 140 securities in an unrealized loss position. Of these securities, ten securities had been in an unrealized loss position for 12 months or longer. The gross unrealized loss of corporate bonds in an unrealized loss position for less than twelve months included \$236 of other-than-temporary impairment losses related to non-credit factors.

|                                                   | Less Than Twelve<br>Months  |                            | Twelve Months or Longer     |                            | Total                       |                            |
|---------------------------------------------------|-----------------------------|----------------------------|-----------------------------|----------------------------|-----------------------------|----------------------------|
|                                                   | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value |
| <b>As of December 31, 2016</b>                    |                             |                            |                             |                            |                             |                            |
| <i>Fixed-maturity securities</i>                  |                             |                            |                             |                            |                             |                            |
| U.S. Treasury and U.S. government agencies        | \$ (36)                     | \$ 1,939                   | \$                          | \$                         | \$ (36)                     | \$ 1,939                   |
| Corporate bonds                                   | (1,546)                     | 43,859                     | (95)                        | 2,814                      | (1,641)                     | 46,673                     |
| State, municipalities, and political subdivisions | (441)                       | 26,029                     | (47)                        | 3,036                      | (488)                       | 29,065                     |
| Exchange-traded debt                              | (191)                       | 4,980                      | (46)                        | 1,954                      | (237)                       | 6,934                      |
| Redeemable preferred stock                        | (3)                         | 47                         |                             |                            | (3)                         | 47                         |
| <b>Total fixed-maturity securities</b>            | <b>(2,217)</b>              | <b>76,854</b>              | <b>(188)</b>                | <b>7,804</b>               | <b>(2,405)</b>              | <b>84,658</b>              |
| <i>Equity securities</i>                          | (293)                       | 10,042                     | (191)                       | 3,209                      | (484)                       | 13,251                     |
| <b>Total available-for-sale securities</b>        | <b>\$ (2,510)</b>           | <b>\$ 86,896</b>           | <b>\$ (379)</b>             | <b>\$ 11,013</b>           | <b>\$ (2,889)</b>           | <b>\$ 97,909</b>           |

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

At December 31, 2016, there were 134 securities in an unrealized loss position. Of these securities, 20 securities had been in an unrealized loss position for 12 months or longer. The gross unrealized loss of corporate bonds in an unrealized loss position for twelve months or longer included \$76 of other-than-temporary impairment losses related to non-credit factors.

**Limited Partnership Investments**

The Company has interests in limited partnerships that are not registered or readily tradeable on a securities exchange. These partnerships are private equity funds managed by general partners who make all decisions with regard to financial policies and operations. As such, the Company is not the primary beneficiary and does not consolidate these partnerships. The following table provides information related to the Company's investments in limited partnerships.

| Investment Strategy                                                                                                                                                                                                           | June 30, 2017    |                  |        | December 31, 2016 |                  |        |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|------------------|--------|-------------------|------------------|--------|
|                                                                                                                                                                                                                               | Carrying Value   | Unfunded Balance | (%)(a) | Carrying Value    | Unfunded Balance | (%)(a) |
| Primarily in senior secured loans and, to a limited extent, in other debt and equity securities of private U.S. lower-middle-market companies. (b)(c)(e)                                                                      | \$ 7,203         | \$ 5,505         | 15.37  | \$ 6,246          | \$ 6,428         | 16.50  |
| Value creation through active distressed debt investing primarily in bank loans, public and private corporate bonds, asset-backed securities, and equity securities received in connection with debt restructuring. (b)(d)(e) | 6,942            | 2,217            | 1.76   | 7,358             | 1,360            | 1.76   |
| Maximum long-term capital appreciation through long and short positions in equity and/or debt securities of publicly traded U.S. and non-U.S. issuers, derivative instruments and certain other financial instruments. (f)    |                  |                  |        | 11,333            |                  | 66.58  |
| High returns and long-term capital appreciation through investments in the power, utility and energy industries, and in the infrastructure sector. (b)(g)(h)                                                                  | 5,755            | 4,343            | 0.18   | 4,326             | 5,766            | 0.18   |
| <b>Total</b>                                                                                                                                                                                                                  | <b>\$ 19,900</b> | <b>\$ 12,065</b> |        | <b>\$ 29,263</b>  | <b>\$ 13,554</b> |        |

(a) Represents the Company's percentage investment in the fund at each balance sheet date.

(b)



Except under certain circumstances, withdrawals from the funds or any assignments are not permitted. Distributions, except income from late admission of a new limited partner, will be received when underlying investments of the funds are liquidated.

- (c) Expected to have a 10-year term and the capital commitment is expected to expire on September 3, 2019.
- (d) Expected to have a three-year term from the end of the capital commitment period, which is March 31, 2018.
- (e) At the fund manager's discretion, the term of the fund may be extended for up to two additional one-year periods.
- (f) The withdrawal was effective on February 15, 2017. As a result, the Company's investment in this limited partnership was terminated.
- (g) Expected to have a 10-year term and the capital commitment is expected to expire on June 30, 2020.
- (h) With the consent of a super majority of partners, the term of the fund may be extended for up to three additional one-year periods.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

The following is the aggregated summarized unaudited financial information of limited partnerships included in the investment strategy table above, which in certain cases is presented on a three-month lag due to the unavailability of information at the Company's respective balance sheet dates. In applying the equity method of accounting, the Company uses the most recently available financial information provided by the general partner of each of these partnerships. The financial statements of these limited partnerships are audited annually.

|                           | <b>Three Months Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |              |
|---------------------------|----------------------------------------|-------------|--------------------------------------|--------------|
|                           | <b>2017</b>                            | <b>2016</b> | <b>2017</b>                          | <b>2016</b>  |
| <i>Operating results:</i> |                                        |             |                                      |              |
| Total income              | \$ 157,433                             | \$ (6,987)  | \$ 229,750                           | \$ (23,069)  |
| Total expenses            | (26,177)                               | (27,401)    | (53,819)                             | (130,022)    |
| Net income (loss)         | \$ 131,256                             | \$ (34,388) | \$ 175,931                           | \$ (153,091) |

|                       | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|-----------------------|--------------------------|------------------------------|
| <i>Balance Sheet:</i> |                          |                              |
| Total assets          | \$ 3,891,172             | \$ 2,956,327                 |
| Total liabilities     | \$ 180,945               | \$ 63,813                    |

For the three and six months ended June 30, 2017, the Company recognized net investment income of \$560 and \$1,332, respectively, for these investments. During the second quarter of 2017, the Company received in cash a return on investment totaling \$154. During the first half of 2017, the Company received total cash distributions of \$12,184, representing \$11,758 of returned capital and \$426 of return on investment. Included in the return of capital was \$11,626 from one limited partnership the Company withdrew from in February 2017.

For the three and six months ended June 30, 2016, the Company recognized net investment losses of \$196 and \$1,065, respectively. During the three and six months ended June 30, 2016, the Company received one cash distribution of \$44 of return on investment. At June 30, 2017 and December 31, 2016, the Company's cumulative contributed capital to the partnerships existing at each respective balance sheet date totaled \$18,435 and \$31,946, respectively, and the Company's maximum exposure to loss aggregated \$19,900 and \$29,263, respectively.

**Investment in Unconsolidated Joint Venture**

The Company has an equity investment in FMKT Mel JV, which is a limited liability company treated as a joint venture under U.S. GAAP. In March 2017, FMKT Mel JV sold a portion of its outparcel land for gross proceeds of

\$825 and recognized a \$331 gain on sale of which \$199 was allocated to the Company in accordance with the profit allocation specified in the operating agreement.

At June 30, 2017 and December 31, 2016, the Company's maximum exposure to loss relating to this variable interest entity was \$1,680 and \$2,102, respectively, representing the carrying value of the investment. At June 30, 2017, there was an undistributed gain of \$30 from this equity method investment as compared with an undistributed loss, after an equity distribution, of \$25 at December 31, 2016, the amounts of which were included in the Company's consolidated retained income.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

The limited liability company members received no cash distributions during the three months ended June 30, 2017 and 2016. During the six months ended June 30, 2017, the Company received a cash distribution of \$564, representing a combined distribution of \$147 in earnings and \$417 in capital as compared with no cash distribution during the six months ended June 30, 2016. The following tables provide FMKT Mel JV's summarized unaudited financial results and the unaudited financial positions:

|                                           | <b>Three Months Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |             |
|-------------------------------------------|----------------------------------------|-------------|--------------------------------------|-------------|
|                                           | <b>2017</b>                            | <b>2016</b> | <b>2017</b>                          | <b>2016</b> |
| <b>Operating results:</b>                 |                                        |             |                                      |             |
| Total revenues and gain                   | \$                                     | \$ 181      | \$ 331                               | \$ 714      |
| Total expenses                            | (33)                                   | (247)       | (65)                                 | (483)       |
| Net (loss) income                         | \$ (33)                                | \$ (66)     | \$ 266                               | \$ 231      |
| The Company's share of net (loss) income* | \$ (30)                                | \$ (59)     | \$ 142                               | \$ 228      |

\* Included in net investment income in the Company's consolidated statements of income.

|                                                        | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|--------------------------------------------------------|--------------------------|------------------------------|
| <b>Balance Sheet:</b>                                  |                          |                              |
| Construction in progress real estate                   | \$ 328                   | \$ 334                       |
| Property and equipment, net                            | 1,226                    | 1,654                        |
| Cash                                                   | 144                      | 179                          |
| Other                                                  | 180                      | 180                          |
| Total assets                                           | \$ 1,878                 | \$ 2,347                     |
| Accounts payable                                       | \$ 2                     | \$ 11                        |
| Other liabilities                                      | 10                       |                              |
| Members' capital                                       | 1,866                    | 2,336                        |
| Total liabilities and members' capital                 | \$ 1,878                 | \$ 2,347                     |
| Investment in unconsolidated joint venture, at equity* | \$ 1,680                 | \$ 2,102                     |

\* Included the 90% share of FMKT Mel JV s operating results.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

***Real Estate Investments***

Real estate investments include office and retail space that is leased to tenants, wet and dry boat storage, one restaurant, and two marinas. Real estate investments consist of the following as of June 30, 2017 and December 31, 2016.

|                                                 | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|-------------------------------------------------|--------------------------|------------------------------|
| Land                                            | \$ 17,592                | \$ 17,592                    |
| Land improvements                               | 9,370                    | 9,336                        |
| Buildings                                       | 16,601                   | 16,154                       |
| Tenant and leasehold improvements               | 940                      | 872                          |
| Construction in progress*                       | 4,481                    | 3,404                        |
| Other                                           | 2,945                    | 2,683                        |
| <b>Total, at cost</b>                           | <b>51,929</b>            | <b>50,041</b>                |
| Less: accumulated depreciation and amortization | (2,643)                  | (1,955)                      |
| <b>Real estate investments</b>                  | <b>\$ 49,286</b>         | <b>\$ 48,086</b>             |

\* This project, which was developed by the Company's consolidated variable interest entity, was near completion at June 30, 2017.

Depreciation and amortization expense related to real estate investments was \$351 and \$95 for the three months ended June 30, 2017 and 2016, respectively, and \$688 and \$188 for the six months ended June 30, 2017 and 2016, respectively.

***Consolidated Variable Interest Entity***

At June 30, 2017, the Company had a development project near completion in Riverview, Florida through a limited liability company treated under U.S. GAAP as a joint venture in which the Company's subsidiary has a controlling financial interest and, as a result, it is the primary beneficiary. In addition, the Company is the sole source of funding for the development project. The following table summarizes the assets and liabilities related to this variable interest entity which are included in the accompanying consolidated balance sheets.

Edgar Filing: HCI Group, Inc. - Form 10-Q

|                                                              | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|--------------------------------------------------------------|--------------------------|------------------------------|
| Cash and cash equivalents                                    | \$ 69                    | \$ 65                        |
| Construction in progress included in real estate investments | \$ 4,481                 | \$ 3,404                     |
| Other assets                                                 | \$ 49                    | \$                           |
| Accrued expenses                                             | \$ 117                   | \$ 68                        |
| Other liabilities                                            | \$ 17                    | \$ 11                        |

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)***Net Investment Income**

Net investment income (loss), by source, is summarized as follows:

|                                                 | Three Months Ended<br>June 30, |          | Six Months Ended<br>June 30, |          |
|-------------------------------------------------|--------------------------------|----------|------------------------------|----------|
|                                                 | 2017                           | 2016     | 2017                         | 2016     |
| Available-for-sale securities:                  |                                |          |                              |          |
| Fixed-maturity securities                       | \$ 1,403                       | \$ 1,131 | \$ 2,640                     | \$ 2,230 |
| Equity securities                               | 797                            | 784      | 1,671                        | 1,735    |
| Investment expense                              | (191)                          | (161)    | (350)                        | (323)    |
| Limited partnership investments                 | 560                            | (196)    | 1,332                        | (1,065)  |
| Real estate investments                         | (168)                          | (53)     | (564)                        | (83)     |
| (Loss) income from unconsolidated joint venture | (30)                           | (59)     | 142                          | 228      |
| Cash and cash equivalents                       | 439                            | 268      | 767                          | 470      |
| Other                                           |                                | 11       | 6                            | 23       |
| Net investment income                           | \$ 2,810                       | \$ 1,725 | \$ 5,644                     | \$ 3,215 |

**Note 5 Comprehensive Income (Loss)**

Comprehensive income (loss) includes net income and other comprehensive income or loss, which for the Company includes changes in unrealized gains or losses of investments carried at fair value and changes in the unrealized other-than-temporary impairment losses related to these investments. Reclassification adjustments for realized (gains) losses are reflected in net realized investment gains (losses) on the consolidated statements of income. The components of other comprehensive income or loss and the related tax effects allocated to each component were as follows:

|                                           | Three Months Ended<br>June 30, 2017<br>Income Tax |                      |               | Three Months Ended<br>June 30, 2016<br>Income Tax |                      |               |
|-------------------------------------------|---------------------------------------------------|----------------------|---------------|---------------------------------------------------|----------------------|---------------|
|                                           | Before<br>Tax                                     | Expense<br>(Benefit) | Net of<br>Tax | Before<br>Tax                                     | Expense<br>(Benefit) | Net of<br>Tax |
| Unrealized gain arising during the period | \$ 654                                            | \$ 252               | \$ 402        | \$ 5,893                                          | \$ 2,274             | \$ 3,619      |
| Other-than-temporary impairment loss      | 177                                               | 69                   | 108           | 542                                               | 209                  | 333           |
|                                           | 8                                                 | 3                    | 5             | 10                                                | 4                    | 6             |



|                                                        |          |          |          |          |          |          |  |
|--------------------------------------------------------|----------|----------|----------|----------|----------|----------|--|
| Call and repayment losses charged to investment income |          |          |          |          |          |          |  |
| Reclassification adjustment for realized gains         | (1,787)  | (689)    | (1,098)  | (391)    | (151)    | (240)    |  |
| Total other comprehensive (loss) income                | \$ (948) | \$ (365) | \$ (583) | \$ 6,054 | \$ 2,336 | \$ 3,718 |  |

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

|                                                        | Six Months Ended<br>June 30, 2017 |                      |               | Six Months Ended<br>June 30, 2016 |                      |               |
|--------------------------------------------------------|-----------------------------------|----------------------|---------------|-----------------------------------|----------------------|---------------|
|                                                        | Before<br>Tax                     | Expense<br>(Benefit) | Net of<br>Tax | Before<br>Tax                     | Expense<br>(Benefit) | Net of<br>Tax |
| Unrealized gain arising during the period              | \$ 2,667                          | \$ 1,029             | \$ 1,638      | \$ 8,056                          | \$ 3,108             | \$ 4,948      |
| Other-than-temporary impairment loss                   | 390                               | 150                  | 240           | 1,217                             | 470                  | 747           |
| Call and repayment losses charged to investment income | 9                                 | 4                    | 5             | 11                                | 4                    | 7             |
| Reclassification adjustment for realized gains         | (2,502)                           | (965)                | (1,537)       | (316)                             | (122)                | (194)         |
| Total other comprehensive income                       | \$ 564                            | \$ 218               | \$ 346        | \$ 8,968                          | \$ 3,460             | \$ 5,508      |

**Note 6 Fair Value Measurements**

The Company records and discloses certain financial assets at their estimated fair value. The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows:

- Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2 - Other inputs that are observable for the asset or liability, either directly or indirectly such as quoted prices for identical or similar assets or liabilities that are not observable throughout the full term.
- Level 3 - Inputs that are unobservable.

**Valuation Methodology***Cash and cash equivalents*

Cash and cash equivalents primarily consist of money-market funds and certificates of deposit. Their carrying value approximates fair value due to the short maturity and high liquidity of these funds.

*Available-for-sale securities*

Estimated fair values of the Company's available-for-sale securities are determined in accordance with U.S. GAAP, using valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Fair values are generally measured using quoted prices in active markets for identical securities or other inputs that are observable either directly or indirectly, such as quoted prices for similar securities. In those instances where observable inputs are not available, fair values are measured using unobservable inputs. Unobservable inputs reflect the Company's own assumptions about the assumptions that market participants would use in pricing the security and

are developed based on the best information available in the circumstances. Fair value estimates derived from unobservable inputs are significantly affected by the assumptions used, including the discount rates and the estimated amounts and timing of future cash flows. The derived fair value estimates cannot be substantiated by comparison to independent markets and are not necessarily indicative of the amounts that would be realized in a current market exchange.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

The estimated fair values for securities that do not trade on a daily basis are determined by management, utilizing prices obtained from an independent pricing service and information provided by brokers, which are level 2 inputs. Management reviews the assumptions and methods utilized by the pricing service and then compares the relevant data and pricing to broker-provided data. The Company gains assurance of the overall reasonableness and consistent application of the assumptions and methodologies and compliance with accounting standards for fair value determination through ongoing monitoring of the reported fair values.

*Limited Partnership Investments*

As described in Note 4 Investments under Limited Partnership Investments, the Company has interests in limited partnerships which are private equity funds. Pursuant to U.S. GAAP, these funds are required to use fair value accounting; therefore, the estimated fair value approximates the carrying value of these funds.

*Revolving Credit Facility*

The interest rate on the Company's revolving credit facility was periodically adjusted based on the London Interbank Offered Rate plus a spread. As a result, its carrying value at December 31, 2016 approximated fair value. In February 2017, this credit facility was converted into a 3.95% three-year promissory note. See Note 8 Long-Term Debt under 3.95% Promissory Note.

*Long-term debt*

The following table summarizes components of the Company's long-term debt and methods used in estimating their fair values:

|                                 | <b>Maturity<br/>Date</b> | <b>Valuation Methodology</b>                                                                   |
|---------------------------------|--------------------------|------------------------------------------------------------------------------------------------|
| 8% Senior Notes                 | *                        | Closing price listed on the New York Stock Exchange                                            |
| 3.875% Convertible Senior Notes | 2019                     | Quoted price at June 30, 2017; Discounted cash flow method/Level 3 inputs at December 31, 2016 |
| 4.25% Convertible Senior Notes  | 2037                     | Discounted cash flow method/Level 3 inputs                                                     |
| 3.95% Promissory Note           | 2020                     | Discounted cash flow method/Level 3 inputs                                                     |
| 4% Promissory Note              | 2031                     | Discounted cash flow method/Level 3 inputs                                                     |
| 3.75% Promissory Note           | 2036                     | Discounted cash flow method/Level 3 inputs                                                     |

\* Redeemed on April 3, 2017.



**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)**Assets Measured at Estimated Fair Value on a Recurring Basis*

The following table presents information about the Company's financial assets measured at estimated fair value on a recurring basis. The table indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value as of June 30, 2017 and December 31, 2016:

|                                                   | Fair Value Measurements Using |           |           | Total      |
|---------------------------------------------------|-------------------------------|-----------|-----------|------------|
|                                                   | (Level 1)                     | (Level 2) | (Level 3) |            |
| <b><u>As of June 30, 2017</u></b>                 |                               |           |           |            |
| Financial Assets:                                 |                               |           |           |            |
| <i>Cash and cash equivalents</i>                  | \$ 296,520                    | \$        | \$        | \$ 296,520 |
| <i>Fixed-maturity securities:</i>                 |                               |           |           |            |
| U.S. Treasury and U.S. government agencies        | 45,543                        | 1,503     |           | 47,046     |
| Corporate bonds                                   | 111,402                       | 994       |           | 112,396    |
| State, municipalities, and political subdivisions |                               | 78,992    |           | 78,992     |
| Exchange-traded debt                              | 9,959                         |           |           | 9,959      |
| Redeemable preferred stock                        | 253                           |           |           | 253        |
| Total fixed-maturity securities                   | 167,157                       | 81,489    |           | 248,646    |
| <i>Equity securities</i>                          | 56,152                        |           |           | 56,152     |
| Total available-for-sale securities               | 223,309                       | 81,489    |           | 304,798    |
| Total                                             | \$ 519,829                    | \$ 81,489 | \$        | \$ 601,318 |

|                                            | Fair Value Measurements Using |           |           | Total      |
|--------------------------------------------|-------------------------------|-----------|-----------|------------|
|                                            | (Level 1)                     | (Level 2) | (Level 3) |            |
| <b><u>As of December 31, 2016</u></b>      |                               |           |           |            |
| Financial Assets:                          |                               |           |           |            |
| <i>Cash and cash equivalents</i>           | \$ 280,531                    | \$        | \$        | \$ 280,531 |
| <i>Fixed-maturity securities:</i>          |                               |           |           |            |
| U.S. Treasury and U.S. government agencies | 1,939                         |           |           | 1,939      |

Edgar Filing: HCI Group, Inc. - Form 10-Q

|                                                   |            |           |            |
|---------------------------------------------------|------------|-----------|------------|
| Corporate bonds                                   | 73,519     | 985       | 74,504     |
| State, municipalities, and political subdivisions |            | 78,306    | 78,306     |
| Exchange-traded debt                              | 11,262     |           | 11,262     |
| Redeemable preferred stock                        | 237        |           | 237        |
| Total fixed-maturity securities                   | 86,957     | 79,291    | 166,248    |
| <i>Equity securities</i>                          | 53,035     |           | 53,035     |
| Total available-for-sale securities               | 139,992    | 79,291    | 219,283    |
| Total                                             | \$ 420,523 | \$ 79,291 | \$ 499,814 |

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)**Assets and Liabilities Carried at Other Than Fair Value*

The following tables present fair value information for assets and liabilities that are carried on the balance sheet at amounts other than fair value as of June 30, 2017 and December 31, 2016.

|                                   | Carrying<br>Value | Fair Value<br>Measurements Using<br>(Level 1) | (Level 2) | (Level 3)  | Estimated<br>Fair<br>Value |
|-----------------------------------|-------------------|-----------------------------------------------|-----------|------------|----------------------------|
| <b><u>As of June 30, 2017</u></b> |                   |                                               |           |            |                            |
| Financial Assets:                 |                   |                                               |           |            |                            |
| Limited partnership investments   | \$ 19,900         | \$                                            | \$        | \$ 19,900  | \$ 19,900                  |
| Financial Liabilities:            |                   |                                               |           |            |                            |
| <i>Long-term debt:</i>            |                   |                                               |           |            |                            |
| 3.875% Convertible senior notes   | \$ 83,676         | \$                                            | \$ 88,625 | \$         | \$ 88,625                  |
| 4.25% Convertible senior notes    | 124,723           |                                               |           | 123,302    | 123,302                    |
| 3.95% Promissory note             | 9,363             |                                               |           | 9,442      | 9,442                      |
| 4% Promissory note                | 8,436             |                                               |           | 8,200      | 8,200                      |
| 3.75% Promissory note             | 8,619             |                                               |           | 8,065      | 8,065                      |
| Total long-term debt              | \$ 234,817        | \$ _                                          | \$ 88,625 | \$ 237,634 | \$ 237,634                 |

|                                       | Carrying<br>Value | Fair Value<br>Measurements Using<br>(Level 1) | (Level 2) | (Level 3) | Estimated<br>Fair<br>Value |
|---------------------------------------|-------------------|-----------------------------------------------|-----------|-----------|----------------------------|
| <b><u>As of December 31, 2016</u></b> |                   |                                               |           |           |                            |
| Financial Assets:                     |                   |                                               |           |           |                            |
| Limited partnership investments       | \$ 29,263         | \$                                            | \$        | \$ 29,263 | \$ 29,263                  |
| Financial Liabilities:                |                   |                                               |           |           |                            |
| Revolving credit facility             | \$ 9,463          | \$                                            | \$        | \$ 9,463  | \$ 9,463                   |
| <i>Long-term debt:</i>                |                   |                                               |           |           |                            |
| 8% Senior notes                       | \$ 39,448         | \$                                            | \$ 41,618 | \$        | \$ 41,618                  |
| 3.875% Convertible senior notes       | 81,988            |                                               |           | 84,696    | 84,696                     |
| 4% Promissory note                    | 8,660             |                                               |           | 8,664     | 8,664                      |
| 3.75% Promissory note                 | 8,767             |                                               |           | 8,506     | 8,506                      |



|                      |            |    |           |            |            |
|----------------------|------------|----|-----------|------------|------------|
| Total long-term debt | \$ 138,863 | \$ | \$ 41,618 | \$ 101,866 | \$ 143,484 |
|----------------------|------------|----|-----------|------------|------------|

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)***Note 7 Other Assets**

The following table summarizes the Company's other assets:

|                                                                    | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|--------------------------------------------------------------------|--------------------------|------------------------------|
| Benefits receivable related to retrospective reinsurance contracts | \$ 11,269                | \$ 5,810                     |
| Prepaid expenses                                                   | 2,404                    | 1,581                        |
| Lease acquisition costs, net                                       | 597                      | 615                          |
| Restricted cash                                                    | 709                      | 600                          |
| Other                                                              | 2,861                    | 2,736                        |
| <b>Total other assets</b>                                          | <b>\$ 17,840</b>         | <b>\$ 11,342</b>             |

**Note 8 Long-Term Debt**

The following table summarizes the Company's long-term debt.

|                                                      | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|------------------------------------------------------|--------------------------|------------------------------|
| 8% Senior Notes, redeemed in April 2017              | \$                       | \$ 40,250                    |
| 3.875% Convertible Senior Notes, due March 15, 2019  | 89,990                   | 89,990                       |
| 4.25% Convertible Senior Notes, due March 1, 2037    | 143,750                  |                              |
| 3.95% Promissory note, due through February 17, 2020 | 9,473                    |                              |
| 4% Promissory note, due through February 1, 2031     | 8,587                    | 8,821                        |
| 3.75% Promissory note, due through September 1, 2036 | 8,770                    | 8,924                        |
| <b>Total principal amount</b>                        | <b>260,570</b>           | <b>147,985</b>               |
| Less: unamortized discount and issuance costs        | (25,753)                 | (9,122)                      |
| <b>Total long-term debt</b>                          | <b>\$ 234,817</b>        | <b>\$ 138,863</b>            |

Edgar Filing: HCI Group, Inc. - Form 10-Q

The following table summarizes future maturities of long-term debt as of June 30, 2017, which takes into consideration the assumption that the 4.25% Convertible Senior Notes are repurchased at the earliest call date.

|                                     |            |
|-------------------------------------|------------|
| Due in 12 months following June 30, |            |
| 2017                                | \$ 1,029   |
| 2018                                | 91,060     |
| 2019                                | 9,867      |
| 2020                                | 898        |
| 2021                                | 144,683    |
| Thereafter                          | 13,033     |
| Total                               | \$ 260,570 |

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

Information with respect to interest expense related to long-term debt is as follows:

|                          | <b>Three Months Ended<br/>June 30,</b> |                 | <b>Six Months<br/>Ended<br/>June 30,</b> |                 |
|--------------------------|----------------------------------------|-----------------|------------------------------------------|-----------------|
|                          | <b>2017</b>                            | <b>2016</b>     | <b>2017</b>                              | <b>2016</b>     |
| <b>Interest Expense:</b> |                                        |                 |                                          |                 |
| Contractual interest     | \$ 2,680                               | \$ 1,767        | \$ 5,104                                 | \$ 3,656        |
| Non-cash expense (a)     | 1,718                                  | 844             | 2,877                                    | 1,784           |
| Capitalized interest (b) | (20)                                   |                 | (61)                                     |                 |
| <b>Total</b>             | <b>\$ 4,378</b>                        | <b>\$ 2,611</b> | <b>\$ 7,920</b>                          | <b>\$ 5,440</b> |

(a) Represents amortization of debt discount and issuance costs.

(b) Interest was capitalized for a construction project in Riverview, Florida which is intended for lease.

**Convertible Senior Notes**

The Company's Convertible Senior Notes consist of 3.875% Convertible Senior Notes due 2019 ( 3.875% Convertible Notes ) and 4.25% Convertible Senior Notes due 2037 ( 4.25% Convertible Notes ). The 3.875% Convertible Notes were issued in late 2013 in a private offering for an aggregate principal amount of \$103,000. During the first quarter of 2016, the Company repurchased an aggregate of \$13,010 in principal, thereby decreasing the aggregate principal balance of its 3.875% Convertible Notes to \$89,990. On March 3, 2017, the Company issued 4.25% Convertible Notes in a private offering for an aggregate principal amount of \$143,750. The net proceeds of the 4.25% Convertible Notes were \$138,775 after \$4,975 in related issuance and transaction costs. The following table summarizes the principal and interest payment terms of these Convertible Senior Notes:

**Convertible Senior Notes**

3.875% Convertible Notes, due March 15, 2019

4.25% Convertible Notes, due March 1, 2037

**Interest Payment Terms**

Semiannually in arrears: March 15 and September 15

Semiannually in arrears: March 1 and September 1

The Convertible Senior Notes rank equally in right of payment to the Company's existing and future unsecured and unsubordinated obligations. These Convertible Senior Notes do not contain any financial or operating covenants or restrictions on the payments of dividends, the incurrence of indebtedness or the issuance or repurchase of securities by the Company or any of its subsidiaries. The Convertible Senior Notes provide no protection to the note holders in the event of a fundamental change or other corporate transaction involving the Company except those described in each

respective indenture. These Convertible Senior Notes do not require a sinking fund to be established for the purpose of redemption. In conjunction with the issuances of the Convertible Senior Notes, the Company entered into prepaid share repurchase forward contracts and share repurchase agreements providing for the repurchase of shares of the Company's common stock. See Note 14 Stockholders' Equity under *Share Repurchase Agreements* and *Prepaid Share Repurchase Forward Contracts* for additional information.

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

The following table summarizes information regarding the equity and liability components of the Convertible Senior Notes:

|                                                              | <b>June 30,<br/>2017</b> | <b>December 31<br/>2016</b> |
|--------------------------------------------------------------|--------------------------|-----------------------------|
| Principal amount                                             | \$ 233,740               | \$ 89,990                   |
| Unamortized discount                                         | (20,198)                 | (6,795)                     |
| Liability component net carrying value before issuance costs | \$ 213,542               | \$ 83,195                   |
| Equity component conversion, net of offering costs           | \$ 31,051                | \$ 15,900                   |

*Embedded Conversion Feature*

The conversion feature of these Convertible Senior Notes is subject to conversion rate adjustments upon the occurrence of specified events (including payment of dividends above a specified amount) but will not be adjusted for any accrued and unpaid interest.

*3.875% Convertible Notes.* Since January 2015, the Company's cash dividends on common stock have exceeded \$0.275 per share, resulting in adjustments to the conversion rate of the 3.875% Convertible Notes. Accordingly, as of June 30, 2017, the conversion rate of the Company's 3.875% Convertible Notes was 16.1514 shares of common stock for each \$1 in principal amount, which was the equivalent of approximately \$61.91 per share.

*4.25% Convertible Notes.* The conversion rate of the 4.25% Convertible Notes is currently 16.2635 shares of common stock for each \$1 in principal amount, which is the equivalent of approximately \$61.49 per share.

The holders of the Convertible Senior Notes may convert all or a portion of their Convertible Senior Notes during specified periods as follows: (1) during any calendar quarter commencing after the calendar quarter ending on the dates specified in each respective indenture, if the last reported sale price of the Company's common stock for at least 20 trading days during the period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than 130% of the conversion price on each applicable trading day; (2) during the five business-day period after any ten consecutive trading-day period in which the trading price per \$1 principal amount of the Convertible Senior Notes is less than 98% of the product of the last reported sale price and the conversion rate on each such trading day; (3) if specified corporate events, including a change in control, occur; or (4) at any time on or after the dates specified in each respective indenture.

The note holders who elect to convert their Convertible Senior Notes in connection with a fundamental change as described in the indentures will be entitled to a make-whole adjustment in the form of an increase in the conversion rate. Upon conversion, the Company has options to satisfy its conversion obligation by paying or delivering cash, shares of its common stock or a combination of cash and shares of its common stock. As of June 30, 2017, none of the conditions allowing the holders of either class of the Convertible Senior Notes to convert had been met.

The Company determined that the Convertible Senior Notes embedded conversion feature is not a derivative financial instrument but rather is required to be separately accounted for in equity because the Company may elect to settle the conversion option entirely or partially in cash. At issuance, the Company accounted for the equity component of the embedded conversion feature as a reduction in the carrying amount of the debt and an increase in additional paid-in capital.

---

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

*Embedded Redemption Feature Fundamental Change*

The note holders have the right to require the Company to repurchase for cash all or any portion of the Convertible Senior Notes at par prior to the maturity date should any of the fundamental change events described in the indentures occur. The Company concluded that this embedded redemption feature is not a derivative financial instrument and that it is not probable at issuance that any of the specified fundamental change events will occur. Therefore, this embedded redemption feature is not substantive and will not affect the expected life of the liability component.

*Embedded Redemption Feature Put Option of the Note Holder*

At the option of the holders of the 4.25% Convertible Notes, the Company is required to repurchase for cash all or any portion of the 4.25% Convertible Notes at par on March 1, 2022, March 1, 2027 or March 1, 2032. The Company concluded that this embedded feature is not a derivative financial instrument. In addition, based on economic factors at the time when the 4.25% Convertible Notes were issued, the Company determined it is probable that the note holders will exercise this option. Thus, the Company amortizes the liability component and related issuance costs associated with the 4.25% Convertible Notes over the period from March 3, 2017 to March 1, 2022.

The effective interest rates for the 3.875% Convertible Notes and the 4.25% Convertible Notes, taking into account both cash and non-cash components, approximate 8.3% and 7.6%, respectively. Had a 20-year term been used for the amortization of the liability component and issuance costs of the 4.25% Convertible Notes, the annual effective interest rate charged to earnings would have been decreased to approximately 5.4%. As of June 30, 2017, the remaining amortization periods of the debt discounts were expected to be 1.7 years for the 3.875% Convertible Notes and 4.7 years for the 4.25% Convertible Notes.

***8% Senior Notes***

On April 3, 2017, the Company redeemed its 8% publicly traded, unsecured senior notes which had unamortized debt issuance costs of \$743 at par for \$40,805, including accrued and unpaid interest of \$555. For the three and six months ended June 30, 2017, the Company recognized a loss of \$743 associated with the early extinguishment of this debt. The redemption was funded by the net proceeds from the issuance of the 4.25% Convertible Senior Notes.

***3.95% Promissory Note***

On February 27, 2017, the Company converted its outstanding revolving credit facility of \$9,441 into a three-year mortgage loan primarily collateralized by a retail shopping center in Melbourne, Florida. Shortly after the loan conversion, the Company withdrew an additional amount of \$109, thereby increasing the loan amount to \$9,550. The loan bears a fixed annual interest rate of 3.95%. Approximately \$50 of principal and interest is payable in 35 monthly installments beginning March 17, 2017 plus a final balloon payment of \$8,891 including principal and unpaid interest payable on February 17, 2020. The promissory note may be repaid in part or in full at any time without penalty.





**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

**Note 9 Reinsurance**

The Company cedes a portion of its homeowners insurance exposure to other entities under catastrophe excess of loss reinsurance treaties and one quota share reinsurance agreement. Under the terms of the quota share reinsurance agreement effective January 1, 2017, the Company is entitled to a 30% ceding commission on ceded premiums written. The Company remains liable for claims payments in the event that any reinsurer is unable to meet its obligations under the reinsurance agreements. Failure of reinsurers to honor their obligations could result in losses to the Company. The Company evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurer insolvencies. The Company contracts with a number of reinsurers to secure its annual reinsurance coverage, which generally becomes effective June 1st each year. The Company purchases reinsurance each year taking into consideration probable maximum losses and reinsurance market conditions.

The impact of the reinsurance treaties on premiums written and earned is as follows:

|                          | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|--------------------------|---------------------------|-------------|-------------------------|-------------|
|                          | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|                          | <b>2017</b>               | <b>2016</b> | <b>2017</b>             | <b>2016</b> |
| <b>Premiums Written:</b> |                           |             |                         |             |
| Direct                   | \$ 134,609                | \$ 139,761  | \$ 206,995              | \$ 215,400  |
| Assumed                  | (160)                     | (280)       | (1,121)                 | (359)       |
| Gross written            | 134,449                   | 139,481     | 205,874                 | 215,041     |
| Ceded                    | (28,241)                  | (36,384)    | (56,824)                | (76,756)    |
| Net premiums written     | \$ 106,208                | \$ 103,097  | \$ 149,050              | \$ 138,285  |
| <b>Premiums Earned:</b>  |                           |             |                         |             |
| Direct                   | \$ 86,308                 | \$ 94,046   | \$ 172,580              | \$ 190,899  |
| Assumed                  | 3,780                     | 866         | 9,127                   | 2,832       |
| Gross earned             | 90,088                    | 94,912      | 181,707                 | 193,731     |
| Ceded                    | (28,241)                  | (36,384)    | (56,824)                | (76,756)    |
| Net premiums earned      | \$ 61,847                 | \$ 58,528   | \$ 124,883              | \$ 116,975  |

During the three and six months ended June 30, 2017, reinsurance recoveries of \$5 were deducted from losses incurred. During the three and six months ended June 30, 2016, there were no recoveries pertaining to reinsurance contracts that were deducted from losses incurred. At June 30, 2017 and December 31, 2016, there were 37 and 35 reinsurers, respectively, participating in the Company's reinsurance program. At June 30, 2017, there was \$5 of reinsurance receivable included in other assets of the consolidated balance sheet compared with \$0 at December 31, 2016. Thus, the concentration of credit risk associated with reinsurance receivable as of June 30, 2017 was insignificant compared with none at December 31, 2016. In addition, based on the insurance ratings and the financial strength of the reinsurers, management believes there was no significant credit risk associated with its reinsurers obligations to perform on any prepaid reinsurance contract as of June 30, 2017 and December 31, 2016.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)**

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

Certain of the reinsurance contracts include retrospective provisions that adjust premiums, increase the amount of future coverage, or result in a profit commission in the event losses are minimal or zero. These adjustments are reflected in the consolidated statements of income as net reductions in ceded premiums of \$3,634 and \$3,001 for the three months ended June 30, 2017 and 2016, respectively, of which \$936 and \$413 related to the Company's contract with Oxbridge Reinsurance Limited, a related party. For the six months ended June 30, 2017 and 2016, these adjustments were \$6,956 and \$5,822, respectively, of which \$1,512 and \$740 related to the Company's contract with Oxbridge. In June 2016, the Company received a total of \$37,800 in cash benefits related to two retrospective reinsurance contracts that terminated May 31, 2016 of which \$7,560 was received from Oxbridge.

In addition, these adjustments are reflected in other assets and prepaid reinsurance premiums. At June 30, 2017 and December 31, 2016, other assets included \$11,269 and \$5,810, respectively, of which \$2,253 and \$1,043 related to the contract with Oxbridge and prepaid reinsurance premiums included \$3,648 and \$2,152, respectively, of which \$639 and \$338 related to the contract with Oxbridge. Management believes the credit risk associated with the collectability of these accrued benefits is minimal as the amount receivable is concentrated with one reinsurer and the Company monitors the creditworthiness of this reinsurer based on available information about the reinsurer's financial position.

**Note 10 Losses and Loss Adjustment Expenses**

The liability for losses and loss adjustment expenses is determined on an individual case basis for all claims reported. The liability also includes amounts for unallocated expenses, anticipated future claim development and losses incurred, but not reported.

Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows:

|                                           | <b>Three Months Ended<br/>June 30,</b> |               | <b>Six Months Ended<br/>June 30,</b> |               |
|-------------------------------------------|----------------------------------------|---------------|--------------------------------------|---------------|
|                                           | <b>2017</b>                            | <b>2016</b>   | <b>2017</b>                          | <b>2016</b>   |
| Gross balance, beginning of period        | \$ 69,911                              | \$ 53,271     | \$ 70,492                            | \$ 51,690     |
| Incurred, net of reinsurance, related to: |                                        |               |                                      |               |
| Current period                            | 22,165                                 | 20,803        | 45,373                               | 47,420        |
| Prior period                              | 5,500                                  | 5,469         | 7,821                                | 5,932         |
| <b>Total incurred, net of reinsurance</b> | <b>27,665</b>                          | <b>26,272</b> | <b>53,194</b>                        | <b>53,352</b> |
| Paid, net of reinsurance, related to:     |                                        |               |                                      |               |
| Current period                            | (12,859)                               | (14,239)      | (19,504)                             | (22,596)      |
| Prior period                              | (11,633)                               | (10,577)      | (31,098)                             | (27,719)      |

Edgar Filing: HCI Group, Inc. - Form 10-Q

|                                |           |           |           |           |
|--------------------------------|-----------|-----------|-----------|-----------|
| Total paid, net of reinsurance | (24,492)  | (24,816)  | (50,602)  | (50,315)  |
| Net balance, end of period     | 73,084    | 54,727    | 73,084    | 54,727    |
| Add: reinsurance recoverable   | 5         |           | 5         |           |
| Gross balance, end of period   | \$ 73,089 | \$ 54,727 | \$ 73,089 | \$ 54,727 |

The establishment of loss reserves is an inherently uncertain process and changes in loss reserve estimates are expected as these estimates are subject to the outcome of future events. Changes in estimates, or differences between estimates and amounts ultimately paid, are reflected in the operating results of the period during which such estimates are adjusted. During the three and six months ended June 30, 2017, the Company experienced unfavorable development of \$5,500 and \$7,821, respectively, of which \$3,249 and \$5,740, respectively, pertain to claims in the 2016 loss year.

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

The Company writes insurance in the state of Florida, which could be exposed to hurricanes or other natural catastrophes. The occurrence of a major catastrophe could have a significant effect on the Company's quarterly results and cause a temporary disruption of the normal operations of the Company. However, the Company is unable to predict the frequency or severity of any such events that may occur in the near term or thereafter.

**Note 11 Segment Information**

The Company's businesses consist of four operating divisions: property and casualty insurance, reinsurance, investment real estate and information technology. The Company's chief executive officer, who serves as the Company's chief operating decision maker, evaluates each division's financial and operating performances based on revenue and operating income. The Company aggregates its operating divisions into segments based on organizational structure and revenue source.

Due to their economic characteristics, the Company's property and casualty insurance division and reinsurance division are grouped together into one reportable segment under insurance operations. For the three months ended June 30, 2017 and 2016, revenues from the Company's insurance operations before intracompany elimination represented 96.7% and 97.4%, respectively, of total revenues of all operating segments. For the six months ended June 30, 2017 and 2016, revenues from the Company's insurance operations before intracompany elimination represented 96.6% and 97.3%, respectively, of total revenues of all operating segments. At June 30, 2017 and December 31, 2016, insurance operations' total assets represented 87.4% and 87.9%, respectively, of the combined assets of all operating segments. There was no other operating division representing ten percent or more of the Company's total revenues or combined assets. In addition, there was no other operating division representing ten percent or more of the greater, in absolute amount, of the combined profits of all operating divisions reporting a profit or the combined losses of all operating divisions reporting a loss. The following tables present segment information reconciled to the Company's consolidated statements of income. Other non-reportable divisions are combined and disclosed in Corporate and Other. Intersegment transactions are not eliminated from segment results. However, intracompany transactions are eliminated in segment results below.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

| <b>Three Months Ended June 30, 2017</b>           | <b>Insurance<br/>Operations</b> | <b>Corporate/<br/>Other(a)</b> | <b>Reclassification/<br/>Elimination</b> | <b>Consolidated</b> |
|---------------------------------------------------|---------------------------------|--------------------------------|------------------------------------------|---------------------|
| <b>Revenue:</b>                                   |                                 |                                |                                          |                     |
| Net premiums earned                               | \$ 61,847                       | \$                             | \$                                       | \$ 61,847           |
| Net investment income                             | 2,217                           | 790                            | (197)                                    | 2,810               |
| Net realized investment gains (losses)            | 1,813                           | (26)                           |                                          | 1,787               |
| Net other-than-temporary impairment losses        | (177)                           |                                |                                          | (177)               |
| Policy fee income                                 | 908                             |                                |                                          | 908                 |
| Other                                             | 138                             | 2,896                          | (2,629)                                  | 405                 |
| <b>Total revenue</b>                              | <b>66,746</b>                   | <b>3,660</b>                   | <b>(2,826)</b>                           | <b>67,580</b>       |
| <b>Expenses:</b>                                  |                                 |                                |                                          |                     |
| Losses and loss adjustment expenses               | 27,665                          |                                |                                          | 27,665              |
| Amortization of deferred policy acquisition costs | 8,785                           |                                |                                          | 8,785               |
| Interest expense                                  |                                 | 4,378                          |                                          | 4,378               |
| Loss on repurchases of senior notes               |                                 | 743                            |                                          | 743                 |
| Depreciation and amortization                     | 33                              | 728                            | (472)                                    | 289                 |
| Other                                             | 8,077                           | 5,692                          | (2,354)                                  | 11,415              |
| <b>Total expenses</b>                             | <b>44,560</b>                   | <b>11,541</b>                  | <b>(2,826)</b>                           | <b>53,275</b>       |
| <b>Income before income taxes</b>                 | <b>\$ 22,186</b>                | <b>\$ (7,881)</b>              | <b>\$</b>                                | <b>\$ 14,305</b>    |

| <b>Three Months Ended June 30, 2016</b>    | <b>Insurance<br/>Operations</b> | <b>Corporate/<br/>Other(a)</b> | <b>Reclassification/<br/>Elimination</b> | <b>Consolidated</b> |
|--------------------------------------------|---------------------------------|--------------------------------|------------------------------------------|---------------------|
| <b>Revenue:</b>                            |                                 |                                |                                          |                     |
| Net premiums earned                        | \$ 58,528                       | \$                             | \$                                       | \$ 58,528           |
| Net investment income                      | 1,736                           | 250                            | (261)                                    | 1,725               |
| Net realized investment gains              | 382                             | 9                              |                                          | 391                 |
| Net other-than-temporary impairment losses | (540)                           | (2)                            |                                          | (542)               |
| Policy fee income                          | 988                             |                                |                                          | 988                 |
| Other                                      | 211                             | 2,156                          | (1,937)                                  | 430                 |
| <b>Total revenue</b>                       | <b>61,305</b>                   | <b>2,413</b>                   | <b>(2,198)</b>                           | <b>61,520</b>       |
| <b>Expenses:</b>                           |                                 |                                |                                          |                     |

Edgar Filing: HCI Group, Inc. - Form 10-Q

|                                                   |                  |                   |                |                  |
|---------------------------------------------------|------------------|-------------------|----------------|------------------|
| Losses and loss adjustment expenses               | 26,272           |                   |                | 26,272           |
| Amortization of deferred policy acquisition costs | 9,528            |                   |                | 9,528            |
| Interest expense                                  |                  | 2,611             |                | 2,611            |
| Depreciation and amortization                     | 50               | 386               | (95)           | 341              |
| Other                                             | 8,545            | 5,097             | (2,103)        | 11,539           |
| <b>Total expenses</b>                             | <b>44,395</b>    | <b>8,094</b>      | <b>(2,198)</b> | <b>50,291</b>    |
| <b>Income before income taxes</b>                 | <b>\$ 16,910</b> | <b>\$ (5,681)</b> | <b>\$</b>      | <b>\$ 11,229</b> |

- (a) Other revenue under corporate and other primarily consisted of rental income from investment properties and revenue from restaurant and marina businesses.



**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

| <b>Six Months Ended June 30, 2017</b>             | <b>Insurance<br/>Operations</b> | <b>Corporate/<br/>Other(a)</b> | <b>Reclassification/<br/>Elimination</b> | <b>Consolidated</b> |
|---------------------------------------------------|---------------------------------|--------------------------------|------------------------------------------|---------------------|
| <b>Revenue:</b>                                   |                                 |                                |                                          |                     |
| Net premiums earned                               | \$ 124,883                      | \$                             | \$                                       | \$ 124,883          |
| Net investment income                             | 4,590                           | 1,476                          | (422)                                    | 5,644               |
| Net realized investment gains                     | 2,419                           | 83                             |                                          | 2,502               |
| Net other-than-temporary impairment losses        | (390)                           |                                |                                          | (390)               |
| Policy fee income                                 | 1,816                           |                                |                                          | 1,816               |
| Other                                             | 343                             | 5,357                          | (4,862)                                  | 838                 |
| <b>Total revenue</b>                              | <b>133,661</b>                  | <b>6,916</b>                   | <b>(5,284)</b>                           | <b>135,293</b>      |
| <b>Expenses:</b>                                  |                                 |                                |                                          |                     |
| Losses and loss adjustment expenses               | 53,194                          |                                |                                          | 53,194              |
| Amortization of deferred policy acquisition costs | 17,637                          |                                |                                          | 17,637              |
| Interest expense                                  |                                 | 7,920                          |                                          | 7,920               |
| Loss on repurchases of senior notes               |                                 | 743                            |                                          | 743                 |
| Depreciation and amortization                     | 61                              | 1,442                          | (931)                                    | 572                 |
| Other                                             | 15,446                          | 10,687                         | (4,353)                                  | 21,780              |
| <b>Total expenses</b>                             | <b>86,338</b>                   | <b>20,792</b>                  | <b>(5,284)</b>                           | <b>101,846</b>      |
| <b>Income before income taxes</b>                 | <b>\$ 47,323</b>                | <b>\$ (13,876)</b>             | <b>\$</b>                                | <b>\$ 33,447</b>    |

| <b>Six Months Ended June 30, 2016</b>           | <b>Insurance<br/>Operations</b> | <b>Corporate/<br/>Other(a)</b> | <b>Reclassification/<br/>Elimination</b> | <b>Consolidated</b> |
|-------------------------------------------------|---------------------------------|--------------------------------|------------------------------------------|---------------------|
| <b>Revenue:</b>                                 |                                 |                                |                                          |                     |
| Net premiums earned                             | \$ 116,975                      | \$                             | \$                                       | \$ 116,975          |
| Net investment income (loss)                    | 3,486                           | (113)                          | (158)                                    | 3,215               |
| Net realized investment gains (losses)          | 324                             | (8)                            |                                          | 316                 |
| Net other-than-temporary impairment losses      | (1,201)                         | (16)                           |                                          | (1,217)             |
| Policy fee income                               | 1,995                           |                                |                                          | 1,995               |
| Gain on repurchases of convertible senior notes |                                 | 153                            |                                          | 153                 |
| Other                                           | 437                             | 3,807                          | (3,414)                                  | 830                 |
| <b>Total revenue</b>                            | <b>122,016</b>                  | <b>3,823</b>                   | <b>(3,572)</b>                           | <b>122,267</b>      |

**Expenses:**

|                                                   |                  |                    |           |                  |
|---------------------------------------------------|------------------|--------------------|-----------|------------------|
| Losses and loss adjustment expenses               | 53,352           |                    |           | 53,352           |
| Amortization of deferred policy acquisition costs | 19,339           |                    |           | 19,339           |
| Interest expense                                  |                  | 5,440              |           | 5,440            |
| Depreciation and amortization                     | 100              | 772                | (188)     | 684              |
| Other                                             | 16,733           | 9,177              | (3,384)   | 22,526           |
| Total expenses                                    | 89,524           | 15,389             | (3,572)   | 101,341          |
| <b>Income before income taxes</b>                 | <b>\$ 32,492</b> | <b>\$ (11,566)</b> | <b>\$</b> | <b>\$ 20,926</b> |

- (a) Other revenue under corporate and other primarily consisted of rental income from investment properties and revenue from restaurant and marina businesses.

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

The following table presents segment assets reconciled to the Company's total assets in the consolidated balance sheets.

|                               | <b>June 30,<br/>2017</b> | <b>December 31,<br/>2016</b> |
|-------------------------------|--------------------------|------------------------------|
| <b>Segment:</b>               |                          |                              |
| Insurance Operations          | \$ 602,474               | \$ 651,927                   |
| Corporate and Other           | 211,473                  | 116,849                      |
| Consolidation and Elimination | (21,229)                 | (98,712)                     |
| <b>Total assets</b>           | <b>\$ 792,718</b>        | <b>\$ 670,064</b>            |

**Note 12 Income Taxes**

During the three months ended June 30, 2017 and 2016, the Company recorded approximately \$4,763 and \$4,205, respectively, of income taxes, which resulted in effective tax rates of 33.3% and 37.4%, respectively. During the six months ended June 30, 2017 and 2016, the Company recorded approximately \$11,885 and \$7,846, respectively, of income taxes, which resulted in effective tax rates of 35.5% and 37.5%, respectively. The decrease in the 2017 effective tax rate was primarily attributable to tax benefits recognized from the exercise of common stock options during the second quarter of 2017. The Company's estimated annual effective tax rate differs from the statutory federal tax rate due to state and foreign income taxes as well as certain nondeductible and tax-exempt items.

In July 2017, the Company received notice from the Internal Revenue Service stating the Company's 2015 federal income tax return will be examined. The examination is expected to begin during the third quarter of 2017.

**Note 13 Earnings Per Share**

U.S. GAAP requires the Company to use the two-class method in computing basic earnings per share since holders of the Company's restricted stock have the right to share in dividends, if declared, equally with common stockholders. These participating securities affect the computation of both basic and diluted earnings per share during periods of net income.

**Table of Contents****HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

A summary of the numerator and denominator of the basic and diluted earnings per common share is presented below.

|                                                       | Three Months Ended<br>June 30, 2017 |                         |                     | Three Months Ended<br>June 30, 2016 |                         |                     |
|-------------------------------------------------------|-------------------------------------|-------------------------|---------------------|-------------------------------------|-------------------------|---------------------|
|                                                       | Income<br>(Numerator)               | Shares<br>(Denominator) | Per Share<br>Amount | Income<br>(Numerator)               | Shares<br>(Denominator) | Per Share<br>Amount |
| Net income                                            | \$ 9,542                            |                         |                     | \$ 7,024                            |                         |                     |
| Less: Income attributable to participating securities | (572)                               |                         |                     | (306)                               |                         |                     |

**Basic Earnings Per Share:**

|                                         |       |       |         |       |       |         |
|-----------------------------------------|-------|-------|---------|-------|-------|---------|
| Income allocated to common stockholders | 8,970 | 8,503 | \$ 1.05 | 6,718 | 9,399 | \$ 0.71 |
|-----------------------------------------|-------|-------|---------|-------|-------|---------|

**Effect of Dilutive Securities:**

|                          |       |       |  |       |       |  |
|--------------------------|-------|-------|--|-------|-------|--|
| Stock options            |       | 41    |  |       | 62    |  |
| Convertible senior notes | 2,514 | 3,790 |  | 1,018 | 1,446 |  |

**Diluted Earnings Per Share:**

|                                                                 |           |        |         |          |        |         |
|-----------------------------------------------------------------|-----------|--------|---------|----------|--------|---------|
| Income available to common stockholders and assumed conversions | \$ 11,484 | 12,334 | \$ 0.93 | \$ 7,736 | 10,907 | \$ 0.71 |
|-----------------------------------------------------------------|-----------|--------|---------|----------|--------|---------|

|                                                       | Six Months Ended<br>June 30, 2017 |                         |                     | Six Months Ended<br>June 30, 2016 |                         |                     |
|-------------------------------------------------------|-----------------------------------|-------------------------|---------------------|-----------------------------------|-------------------------|---------------------|
|                                                       | Income<br>(Numerator)             | Shares<br>(Denominator) | Per Share<br>Amount | Income<br>(Numerator)             | Shares<br>(Denominator) | Per Share<br>Amount |
| Net income                                            | \$ 21,562                         |                         |                     | \$ 13,080                         |                         |                     |
| Less: Income attributable to participating securities | (1,281)                           |                         |                     | (608)                             |                         |                     |

**Basic Earnings Per Share:**

|                                         |        |       |         |        |       |         |
|-----------------------------------------|--------|-------|---------|--------|-------|---------|
| Income allocated to common stockholders | 20,281 | 8,727 | \$ 2.32 | 12,472 | 9,489 | \$ 1.31 |
|-----------------------------------------|--------|-------|---------|--------|-------|---------|

**Effect of Dilutive Securities:**

|                           |       |       |  |  |    |  |
|---------------------------|-------|-------|--|--|----|--|
| Stock options             |       | 43    |  |  | 62 |  |
| Convertible senior notes* | 4,013 | 2,988 |  |  |    |  |

**Diluted Earnings Per Share:**

|                                                                    |           |        |         |           |       |         |
|--------------------------------------------------------------------|-----------|--------|---------|-----------|-------|---------|
| Income available to common stockholders<br>and assumed conversions | \$ 24,294 | 11,758 | \$ 2.07 | \$ 12,472 | 9,551 | \$ 1.31 |
|--------------------------------------------------------------------|-----------|--------|---------|-----------|-------|---------|

\* Excluded in 2016 due to anti-dilutive effect.

---

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

**Note 14 Stockholders Equity**

***Common Stock***

In December 2016, the Company's Board of Directors authorized a one-year plan to repurchase up to \$20,000 of the Company's common shares before commissions and fees. During the three months ended June 30, 2017, the Company repurchased and retired a total of 900 shares at a weighted average price per share of \$44.26 under this repurchase plan. The total cost of shares repurchased, inclusive of fees and commissions, during the three months ended June 30, 2017 was \$40, or \$44.30 per share. During the six months ended June 30, 2017, the Company repurchased and retired a total of 38,416 shares at a weighted average price per share of \$41.36 under this authorized repurchase plan. The total cost of shares repurchased, inclusive of fees and commissions, during the six months ended June 30, 2017 was \$1,590, or \$41.40 per share.

In December 2015, the Company's Board of Directors authorized a one-year plan to repurchase up to \$20,000 of the Company's common shares before commissions and fees. During the three months ended June 30, 2016, the Company repurchased and retired a total of 189,938 shares at a weighted average price per share of \$31.59 under this repurchase plan. The total cost of shares repurchased, inclusive of fees and commissions, during the three months ended June 30, 2016 was \$6,008, or \$31.63 per share. During the six months ended June 30, 2016, the Company repurchased and retired a total of 376,796 shares at a weighted average price per share of \$31.85. The total cost of shares repurchased, inclusive of fees and commissions, during the six months ended June 30, 2016 was \$12,015, or \$31.89 per share.

On July 6, 2017, the Company's Board of Directors declared a quarterly dividend of \$0.35 per common share. The dividends are payable on September 15, 2017 to shareholders of record on August 18, 2017.

***Share Repurchase Agreements***

In conjunction with the issuance of the 4.25% Convertible Notes as described in Note 8 Long-Term Debt under *Convertible Senior Notes*, the Company used \$20,345 of the net proceeds to repurchase and retire an aggregate of 413,600 shares of its common stock at a price of \$49.19 per share from institutional investors.

***Prepaid Share Repurchase Forward Contracts***

The Company has two outstanding prepaid share repurchase forward contracts, one of which was entered into with Deutsche Bank AG, London Branch in conjunction with the issuance of the 3.875% Convertible Notes. The other was entered into with Societe Generale in conjunction with the issuance of the 4.25% Convertible Notes as described in Note 8 Long-Term Debt under *Convertible Senior Notes*. Both Deutsche Bank AG, London Branch and Societe Generale are considered forward counterparties. Under these forward contracts, the Company made initial upfront payments in exchange for the future deliveries of the Company's common stock from the forward counterparties. Pursuant to the forward contract entered into in December 2013 with Deutsche Bank AG, London Branch, the Company prepaid \$29,923 to repurchase 622,751 shares of the Company's



**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

common stock, which shares will be delivered over a settlement period in 2019. Pursuant to the forward contract entered into in March 2017 with Societe Generale, the Company prepaid \$9,400 of the net proceeds of the offering to repurchase 191,100 shares of the Company's common stock, which shares will be delivered over a settlement period in 2022.

Each forward contract is subject to early settlement, in whole or in part, at any time prior to the final settlement date at the option of each forward counterparty, as well as early settlement or settlement with alternative consideration in the event of certain corporate transactions. In the event the Company pays any cash dividends on its common shares, each forward counterparty will pay an equivalent amount to the Company. The shares to be purchased under the forward contracts will be treated as retired for financial statement purposes as of the effective date of each forward contract, but will remain outstanding for corporate law purposes, including for purposes of any future stockholders votes.

The Company determined that each forward contract does not meet the characteristics of a derivative instrument and, as such, the transaction resulted in an immediate reduction of the outstanding shares used to calculate the weighted-average common shares outstanding for both basic and diluted earnings per share.

**Note 15 Stock-Based Compensation**

***Incentive Plans***

The Company currently has outstanding stock-based awards granted under the 2007 Stock Option and Incentive Plan and the 2012 Omnibus Incentive Plan. Only the 2012 Plan is active and available for future grants. On March 17, 2017, the Company's board of directors amended the 2012 Omnibus Incentive Plan and reduced the number of shares reserved under the plan from 5,000,000 shares to 3,000,000 shares. At June 30, 2017, there were 1,982,763 shares available for grant.

***Stock Options***

Stock options granted and outstanding under the incentive plans vest over periods ranging from immediately vested to five years and are exercisable over the contractual term of ten years.



Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

A summary of the stock option activity for the three and six months ended June 30, 2017 and 2016 is as follows (option amounts not in thousands):

|                                | <b>Number of<br/>Options</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Weighted<br/>Average<br/>Remaining<br/>Contractual<br/>Term</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> |
|--------------------------------|------------------------------|----------------------------------------------------|--------------------------------------------------------------------|------------------------------------------|
| Outstanding at January 1, 2017 | 50,000                       | \$ 4.02                                            | 2.3 years                                                          | \$ 1,773                                 |
| Granted                        | 110,000                      | \$ 40.00                                           |                                                                    |                                          |
| Outstanding at March 31, 2017  | 160,000                      | \$ 28.76                                           | 7.4 years                                                          | \$ 2,591                                 |
| Exercised                      | (30,000)                     | \$ 2.50                                            |                                                                    |                                          |
| Outstanding at June 30, 2017   | 130,000                      | \$ 34.82                                           | 8.7 years                                                          | \$ 1,675                                 |
| Exercisable at June 30, 2017   | 20,000                       | \$ 6.30                                            | 4.2 years                                                          | \$ 828                                   |
| Outstanding at January 1, 2016 | 110,000                      | \$ 3.19                                            | 2.3 years                                                          | \$ 3,482                                 |
| Outstanding at March 31, 2016  | 110,000                      | \$ 3.19                                            | 2.1 years                                                          | \$ 3,312                                 |
| Outstanding at June 30, 2016   | 110,000                      | \$ 3.19                                            | 1.8 years                                                          | \$ 2,650                                 |
| Exercisable at June 30, 2016   | 110,000                      | \$ 3.19                                            | 1.8 years                                                          | \$ 2,650                                 |

The aggregate intrinsic value and realized tax benefits of the options exercised during the three and six months ended June 30, 2017 were \$1,319 and \$509. There were no options exercised during the three and six months ended June 30, 2016. For the three months ended June 30, 2017 and 2016, the Company recognized \$53 and \$0, respectively, of compensation expense. For the six months ended June 30, 2017 and 2016, the Company recognized \$149 and \$0, respectively, of compensation expense which was included in other operating expenses. Deferred tax benefits related to stock options were \$21 and \$0 for the three months ended June 30, 2017 and 2016, respectively, and \$58 and \$0 for the six months ended June 30, 2017 and 2016, respectively. At June 30, 2017 and December 31, 2016, there was \$1,098 and \$0, respectively, of unrecognized compensation expense related to nonvested stock options. The Company expects to recognize the remaining compensation expense over a weighted-average period of 3.5 years.

The following table provides assumptions used in the Black-Scholes option-pricing model to estimate the fair value of the stock options granted during the six months ended June 30, 2017:

|                          |        |
|--------------------------|--------|
| Expected dividend yield  | 3.53%  |
| Expected volatility      | 42.86% |
| Risk-free interest rate  | 1.92%  |
| Expected life (in years) | 5      |

***Restricted Stock Awards***

From time to time, the Company has granted and may grant restricted stock awards to its executive officers, other employees and nonemployee directors in connection with their service to the Company. The terms of the Company's outstanding restricted stock grants may include service, performance and market-based conditions. The fair value of the awards with market-based conditions is determined using a Monte Carlo simulation method, which calculates many potential outcomes for an award and then establishes fair value based on the most likely outcome. The determination of fair value with respect to the awards concerning only performance or service-based conditions is based on the market value of the Company's common stock on the grant date.

Table of Contents**HCI GROUP, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (unaudited)***(Amounts in thousands, except share and per share amounts, unless otherwise stated)*

Information with respect to the activity of unvested restricted stock awards during the three and six months ended June 30, 2017 and 2016 is as follows:

|                              | <b>Number of<br/>Restricted<br/>Stock<br/>Awards</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair<br/>Value</b> |
|------------------------------|------------------------------------------------------|---------------------------------------------------------------|
| Nonvested at January 1, 2017 | 542,503                                              | \$ 30.81                                                      |
| Granted                      | 45,000                                               | \$ 40.15                                                      |
| Vested                       | (20,109)                                             | \$ 48.42                                                      |
| Forfeited                    | (926)                                                | \$ 35.52                                                      |
| Nonvested at March 31, 2017  | 566,468                                              | \$ 30.92                                                      |
| Granted                      | 109,936                                              | \$ 44.05                                                      |
| Vested                       | (45,874)                                             | \$ 34.51                                                      |
| Forfeited                    | (9,948)                                              | \$ 40.90                                                      |
| Nonvested at June 30, 2017   | 620,582                                              | \$ 32.82                                                      |
| Nonvested at January 1, 2016 | 620,513                                              | \$ 30.33                                                      |
| Vested                       | (20,917)                                             | \$ 48.42                                                      |
| Cancelled                    | (160,000)                                            | \$ 26.27                                                      |
| Forfeited                    | (750)                                                | \$ 45.25                                                      |
| Nonvested at March 31, 2016  | 438,846                                              | \$ 30.93                                                      |
| Granted                      | 102,440                                              | \$ 32.21                                                      |
| Vested                       | (24,235)                                             | \$ 37.34                                                      |
| Forfeited                    | (5,147)                                              | \$ 42.20                                                      |
| Nonvested at June 30, 2016   | 511,904                                              | \$ 30.77                                                      |

The Company recognized compensation expense related to restricted stock, which is included in other operating expenses, of \$984 and \$967 for the three months ended June 30, 2017 and 2016, respectively, and \$1,990 and \$1,948 for the six months ended June 30, 2017 and 2016, respectively. At June 30, 2017 and December 31, 2016, there was approximately \$11,751 and \$7,531, respectively, of total unrecognized compensation expense related to nonvested

restricted stock arrangements. The Company expects to recognize the remaining compensation expense over a weighted-average period of 26 months. The following table summarizes information about deferred tax benefits recognized and tax benefits realized related to restricted stock awards and paid dividends, and the fair value of vested restricted stock for the three and six months ended June 30, 2017 and 2016.

|                                                               | <b>Three Months Ended<br/>June 30,</b> |             | <b>Six Months<br/>Ended<br/>June 30,</b> |             |
|---------------------------------------------------------------|----------------------------------------|-------------|------------------------------------------|-------------|
|                                                               | <b>2017</b>                            | <b>2016</b> | <b>2017</b>                              | <b>2016</b> |
| Deferred tax benefits recognized                              | \$ 341                                 | \$ 372      | \$ 694                                   | \$ 751      |
| Tax benefits realized for restricted stock and paid dividends | \$ 816                                 | \$ 338      | \$ 1,183                                 | \$ 637      |
| Fair value of vested restricted stock                         | \$ 1,583                               | \$ 905      | \$ 2,557                                 | \$ 1,918    |

---

**Table of Contents**

**HCI GROUP, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (unaudited)**

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

**Note 16 Commitments and Contingencies**

**Obligations under Multi-Year Reinsurance Contracts**

As of June 30, 2017, the Company has contractual obligations related to multi-year reinsurance contracts. These contracts have effective dates of June 1, 2016 and may be cancelled only with the other party's consent. The future minimum aggregate premiums amount payable to the reinsurers due in June 2018 is \$19,400.

**Capital Commitment**

As described in Note 4 Investments under *Limited Partnership Investments*, the Company is contractually committed to capital contributions for three limited partnership interests. At June 30, 2017, there was an aggregate unfunded balance of \$12,065.

**Note 17 Related Party Transactions**

Claddaugh Casualty Insurance Company, Ltd., the Company's Bermuda domiciled reinsurance subsidiary, has a reinsurance agreement with Oxbridge Reinsurance Limited whereby a portion of the business assumed from the Company's insurance subsidiary, Homeowners Choice Property & Casualty Insurance Company, Inc., is ceded by Claddaugh to Oxbridge. With respect to the period from June 1, 2016 through May 31, 2017, Oxbridge assumed \$6,000 of the total covered exposure for approximately \$3,400 in premiums. With respect to the period from June 1, 2017 through May 31, 2018, Oxbridge assumed \$7,400 of the total covered exposure for approximately \$3,400 in premiums. See Note 9 Reinsurance which includes the amounts due from and paid by Oxbridge during the six months ended June 30, 2017 and 2016 with respect to benefits accrued in connection with the Oxbridge agreements. The premiums charged by Oxbridge are at rates which management believes to be competitive with market rates available to Claddaugh. Oxbridge has deposited funds into a trust account to satisfy certain collateral requirements under its reinsurance contract with Claddaugh. Trust assets may be withdrawn by Claddaugh, the trust beneficiary, in the event amounts are due under the Oxbridge reinsurance agreements. Among the Oxbridge shareholders are Paresh Patel, the Company's chief executive officer, who is also chairman of the board of directors for Oxbridge, and members of his immediate family and three of the Company's non-employee directors including Sanjay Madhu who serves as Oxbridge's president and chief executive officer.

---

**Table of Contents**

**ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*You should read the following discussion under this Item 2 in conjunction with our consolidated financial statements and related notes and information included elsewhere in this quarterly report on Form 10-Q and in our Form 10-K filed with the Securities and Exchange Commission ( SEC ) on February 22, 2017. Unless the context requires otherwise, as used in this Form 10-Q, the terms HCI, we, us, our, the Company, our company, and similar references refer to HCI Group, Inc., a Florida corporation incorporated in 2006, and its subsidiaries. All dollar amounts in this Management's Discussion and Analysis of Financial Condition and Results of Operations are in whole dollars unless specified otherwise.*

***Forward-Looking Statements***

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

**OVERVIEW General**

HCI Group, Inc. is a Florida-based company that, through its subsidiaries, is engaged in a variety of business activities, including property and casualty insurance, reinsurance, real estate and information technology. Based on our organizational structure, revenue sources, and evaluation of financial and operating performances by management, we manage four operating divisions, which includes the following operations:

a) Insurance Operations

*Property and casualty insurance*

*Reinsurance*

b) Other Operations

*Real estate*

*Information technology*

For the three months ended June 30, 2017 and 2016, revenues from insurance operations before intracompany elimination represented 96.7% and 97.4%, respectively, of total revenues of all operating segments. For the six months ended June 30, 2017 and 2016, revenues from insurance operations before intracompany elimination represented 96.6% and 97.3%, respectively, of total

## **Table of Contents**

revenues of all operating segments. At June 30, 2017 and December 31, 2016, insurance operations' total assets represented 87.4% and 87.9%, respectively, of the combined assets of all operating segments. There was no other operating division representing ten percent or more of our total revenues or combined assets. See Note 11 Segment Information to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q for additional information.

## **Insurance Operations**

### ***Property and Casualty Insurance***

#### ***Homeowners Choice Property & Casualty Insurance Company, Inc.***

Our principal operating subsidiary, Homeowners Choice Property & Casualty Insurance Company, Inc. ( HCPCI ), is a leading provider of property and casualty insurance in the state of Florida. HCPCI along with certain of our other subsidiaries currently provides property and casualty insurance to homeowners, condominium owners, and tenants in the state of Florida. HCPCI offers flood-endorsed and wind-only policies to eligible new and pre-existing Florida customers. In addition, HCPCI was approved by the Florida Office of Insurance Regulation to write standalone flood insurance policies for Florida homeowners. HCPCI strives to offer insurance products at competitive rates, while pursuing profitability using selective underwriting criteria.

HCPCI began operations in 2007 by participating in a take-out program, which is a legislatively mandated program designed to encourage private insurance companies to assume policies from Citizens Property Insurance Corporation, a Florida state-supported insurer. Our growth since inception has resulted primarily from a series of policy assumptions. This growth track has been beneficial to us although there are fewer policies available for assumption today as a result of increased competition in the Florida market. Thus, we plan to seek other opportunities to expand by providing new or additional product offerings in and outside the state of Florida. Recently, HCPCI received regulatory approval to write residential property and casualty insurance in the states of Arkansas, Pennsylvania and South Carolina. HCPCI expects to begin writing flood policies in those states during 2017.

#### ***TypTap Insurance Company***

TypTap Insurance Company was organized by HCI Group, Inc. and approved by the Florida Office of Insurance Regulation in January 2016 to transact insurance business in the state of Florida. TypTap began writing standalone flood coverage to Florida homeowners in March 2016.

We expect the flood insurance products offered by TypTap and HCPCI to become significant contributors to future financial results.

### ***Reinsurance***

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



**Table of Contents**

**Other Operations**

***Real Estate***

Our real estate operations consist of multiple properties we own and operate. Properties used in operations consist of our Tampa headquarters building and a secondary insurance operations site in Ocala, Florida. Properties held as investments include two retail shopping centers and a combined 24 acres of waterfront property where two marinas and one restaurant are located.

In July 2017, we completed one real estate development and construction project described as a joint venture arrangement under U.S. GAAP, which we consolidate with our operations. See Note 4 Investments to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q for additional information.

***Information Technology***

Our information technology operations include a team of experienced software developers with extensive knowledge in developing web-based products and applications for mobile devices. The operations, which are in Tampa, Florida and Noida, India, are focused on developing cloud-based, innovative products or services that support in-house operations as well as our third party relationships with our agency partners and claim vendors. These products include *Proplet™*, *TypTap™*, *SAMS™*, *Exzeo®*, *Atlas Viewer™*, and *CasaClue™*.

**Recent Events**

On July 6, 2017, our Board of Directors declared a quarterly dividend of \$0.35 per common share. The dividends are payable on September 15, 2017 to stockholders of record on August 18, 2017.

**Table of Contents****RESULTS OF OPERATIONS**

The following table summarizes our results of operations for the three and six months ended June 30, 2017 and 2016 (dollar amounts in thousands, except per share amounts):

|                                                                           | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |            |
|---------------------------------------------------------------------------|--------------------------------|-----------|------------------------------|------------|
|                                                                           | 2017                           | 2016      | 2017                         | 2016       |
| <b>Revenue</b>                                                            |                                |           |                              |            |
| Gross premiums earned                                                     | \$ 90,088                      | \$ 94,912 | \$ 181,707                   | \$ 193,731 |
| Premiums ceded                                                            | (28,241)                       | (36,384)  | (56,824)                     | (76,756)   |
| Net premiums earned                                                       | 61,847                         | 58,528    | 124,883                      | 116,975    |
| Net investment income                                                     | 2,810                          | 1,725     | 5,644                        | 3,215      |
| Net realized investment gains                                             | 1,787                          | 391       | 2,502                        | 316        |
| Net other-than-temporary impairment losses<br>recognized in income:       |                                |           |                              |            |
| Total other-than-temporary impairment<br>losses                           | (177)                          | (228)     | (390)                        | (636)      |
| Portion of loss recognized in other<br>comprehensive income, before taxes |                                | (314)     |                              | (581)      |
| Net other-than-temporary impairment losses                                | (177)                          | (542)     | (390)                        | (1,217)    |
| Policy fee income                                                         | 908                            | 988       | 1,816                        | 1,995      |
| Gain on repurchases of convertible senior<br>notes                        |                                |           |                              | 153        |
| Other income                                                              | 405                            | 430       | 838                          | 830        |
| Total revenue                                                             | 67,580                         | 61,520    | 135,293                      | 122,267    |
| <b>Expenses</b>                                                           |                                |           |                              |            |
| Losses and loss adjustment expenses                                       | 27,665                         | 26,272    | 53,194                       | 53,352     |
| Policy acquisition and other underwriting<br>expenses                     | 10,070                         | 10,879    | 19,719                       | 21,989     |
| Salaries and wages                                                        | 5,443                          | 5,680     | 10,446                       | 11,064     |
| Interest expense                                                          | 4,378                          | 2,611     | 7,920                        | 5,440      |
| Loss on repurchases of senior notes                                       | 743                            |           | 743                          |            |
| Other operating expenses                                                  | 4,976                          | 4,849     | 9,824                        | 9,496      |
| Total operating expenses                                                  | 53,275                         | 50,291    | 101,846                      | 101,341    |
| Income before income taxes                                                | 14,305                         | 11,229    | 33,447                       | 20,926     |
| Income tax expense                                                        | 4,763                          | 4,205     | 11,885                       | 7,846      |
| Net income                                                                | \$ 9,542                       | \$ 7,024  | \$ 21,562                    | \$ 13,080  |

**Ratios to Net Premiums Earned:**

|                |        |        |        |        |
|----------------|--------|--------|--------|--------|
| Loss Ratio     | 44.73% | 44.89% | 42.60% | 45.61% |
| Expense Ratio  | 41.41% | 41.04% | 38.95% | 41.02% |
| Combined Ratio | 86.14% | 85.93% | 81.55% | 86.63% |

**Ratios to Gross Premiums Earned:**

|                |        |        |        |        |
|----------------|--------|--------|--------|--------|
| Loss Ratio     | 30.71% | 27.68% | 29.27% | 27.54% |
| Expense Ratio  | 28.43% | 25.31% | 26.78% | 24.77% |
| Combined Ratio | 59.14% | 52.99% | 56.05% | 52.31% |

**Earnings Per Share Data:**

|         |         |         |         |         |
|---------|---------|---------|---------|---------|
| Basic   | \$ 1.05 | \$ 0.71 | \$ 2.32 | \$ 1.31 |
| Diluted | \$ 0.93 | \$ 0.71 | \$ 2.07 | \$ 1.31 |

**Table of Contents*****Comparison of the Three Months ended June 30, 2017 with the Three Months ended June 30, 2016***

Our results of operations for the three months ended June 30, 2017 reflect income available to common stockholders of approximately \$9,542,000, or \$0.93 earnings per diluted share, compared with approximately \$7,024,000, or \$0.71 earnings per diluted share, for the three months ended June 30, 2016. The quarter-over-quarter increase was primarily due to a \$3,319,000 increase in net premiums earned which was driven by decreased reinsurance costs. In addition, our 2017 results were positively impacted by increased investment-related income of \$2,481,000 offset by a \$1,393,000 increase in losses and loss adjustment expenses.

**Revenue**

*Gross Premiums Earned* for the three months ended June 30, 2017 and 2016 were approximately \$90,088,000 and \$94,912,000, respectively. The decrease in 2017 was attributable to policy attrition as well as a rate decrease effective on new and renewal policies beginning in January 2016.

*Premiums Ceded* for the three months ended June 30, 2017 and 2016 were approximately \$28,241,000 and \$36,384,000, respectively, representing 31.3% and 38.3%, respectively, of gross premiums earned. The \$8,143,000 decrease was primarily attributable to lower costs of our 2016/2017 reinsurance program, which began June 1, 2016 as compared with the costs of the 2015/2016 program that began June 1, 2015. In addition, the reduction to our ceded premiums attributable to retrospective provisions under certain reinsurance contracts was higher as compared with the corresponding period in 2016.

Our premiums ceded represent amounts paid to reinsurers to cover losses from catastrophes that exceed the retention levels defined by our catastrophe excess of loss reinsurance treaties or to assume a proportional share of losses as defined by a quota share arrangement. For the three months ended June 30, 2017 and 2016, premiums ceded reflect net reductions of approximately \$3,634,000 and \$3,001,000, respectively, related to the provisions under certain reinsurance contracts. See *Economic Impact of Reinsurance Contracts with Retrospective Provisions* under *Critical Accounting Policies and Estimates*. The rates we pay for reinsurance are based primarily on policy exposures reflected in gross premiums earned.

*Net Premiums Written* during the three months ended June 30, 2017 and 2016 totaled approximately \$106,208,000 and \$103,097,000, respectively. Net premiums written represent the premiums charged on policies issued during a fiscal period less any applicable reinsurance costs. The \$3,111,000 increase in 2017 resulted from the decrease in premiums ceded during the period described above offset by a decrease of \$5,032,000 in gross premiums written. We had approximately 143,000 policies in force at June 30, 2017 as compared with approximately 150,000 policies in force at June 30, 2016.

*Net Premiums Earned* for the three months ended June 30, 2017 and 2016 were approximately \$61,847,000 and \$58,528,000, respectively, and reflect the gross premiums earned less reinsurance costs as described above.

The following is a reconciliation of our total Net Premiums Written to Net Premiums Earned for the three months ended June 30, 2017 and 2016 (amounts in thousands):

**Table of Contents**

|                               | <b>Three Months Ended<br/>June 30,</b> |                  |
|-------------------------------|----------------------------------------|------------------|
|                               | <b>2017</b>                            | <b>2016</b>      |
| Net Premiums Written          | \$ 106,208                             | \$ 103,097       |
| Increase in Unearned Premiums | (44,361)                               | (44,569)         |
| <b>Net Premiums Earned</b>    | <b>\$ 61,847</b>                       | <b>\$ 58,528</b> |

*Net Investment Income* for the three months ended June 30, 2017 and 2016 was approximately \$2,810,000 and \$1,725,000, respectively. The increase in 2017 was primarily due to \$560,000 of income from limited partnership investments compared with a \$196,000 loss during the second quarter of 2016. See Note 4 Investments under *Net Investment Income* to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q.

*Net Other-Than-Temporary Impairment Losses* for the three months ended June 30, 2017 and 2016 were approximately \$177,000 and \$542,000, respectively. During the second quarter of 2017, we recognized impairment losses specific to one fixed-maturity security and three equity securities. The fixed-maturity security was subject to impairment resulting from our intention to sell this security before its recovery. Three equity securities were impaired because each security had been in an unrealized loss position for a length of time with no near term prospect of recovery. During the quarter ended June 30, 2016, we recognized impairment losses specific to one fixed-maturity security and seven equity securities.

**Expenses**

Our *Losses and Loss Adjustment Expenses* amounted to approximately \$27,665,000 and \$26,272,000 for the three months ended June 30, 2017 and 2016, respectively. During the second quarter of 2017, we continued to strengthen our loss reserves in response to trends involving assignment of insurance benefits and related litigation. See Reserves for Losses and Loss Adjustment Expenses under Critical Accounting Policies and Estimates.

*Policy Acquisition and Other Underwriting Expenses* for the three months ended June 30, 2017 and 2016 of approximately \$10,070,000 and \$10,879,000, respectively, primarily reflect commissions and premium taxes related to the policies that have renewed. The \$809,000 decrease from the corresponding period in 2016 was primarily attributable to a decrease in commissions and premium taxes resulting from policy attrition and the effect of the rate decrease.

*Salaries and Wages* for the three months ended June 30, 2017 and 2016 were approximately \$5,443,000 and \$5,680,000, respectively. The \$237,000 decrease from the corresponding period in 2016 despite an increase in employee headcount was primarily attributable to the capitalization of payroll costs related to a software development project for internal use. As of June 30, 2017, we had approximately 260 employees located at our offices in Florida compared with 242 employees as of June 30, 2016. We also had 78 employees located in Noida, India at June 30, 2017 versus 85 at June 30, 2016.

*Interest Expense* for the three months ended June 30, 2017 and 2016 was approximately \$4,378,000 and \$2,611,000, respectively. The increase was primarily attributable to the net increase in long-term debt resulting from the issuance of 4.25% Convertible Senior Notes in March 2017 and the redemption of 8% Senior Notes in April 2017.



---

**Table of Contents**

*Loss on repurchases of Senior Notes* for the three months ended June 30, 2017 was approximately \$743,000, resulting from the early extinguishment of our 8% Senior Notes. See Note 8 Long-Term Debt under 8% Senior Notes to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q.

*Income Tax Expense* for the three months ended June 30, 2017 and 2016 was approximately \$4,763,000 and \$4,205,000, respectively, for state, federal, and foreign income taxes resulting in an effective tax rate of 33.3% for 2017 and 37.4% for 2016. The decrease in the effective tax rate was primarily attributable to tax benefits recognized for the exercise of common stock options during the second quarter of 2017.

**Ratios:**

The loss ratio applicable to the three months ended June 30, 2017 (losses and loss adjustment expenses incurred related to net premiums earned) was 44.7% compared with 44.9% for the three months ended June 30, 2016.

The expense ratio applicable to the three months ended June 30, 2017 (defined as underwriting expenses, salaries and wages, interest and other operating expenses related to net premiums earned) was 41.4% compared with 41.0% for the three months ended June 30, 2016.

The combined ratio (total of all expenses in relation to net premiums earned) is the measure of overall underwriting profitability before other income. Our combined ratio for the three months ended June 30, 2017 was 86.1% compared with 85.9% for the three months ended June 30, 2016.

Due to the impact our reinsurance costs have on net premiums earned from period to period, our management believes the combined ratio measured to gross premiums earned is more relevant in assessing overall performance. The combined ratio to gross premiums earned for the three months ended June 30, 2017 was 59.1% compared with 53.0% for the three months ended June 30, 2016. The increase was primarily attributable to the combined impact of decreased gross premiums earned and increased operating expenses.

***Comparison of the Six Months ended June 30, 2017 with the Six Months ended June 30, 2016***

Our results of operations for the six months ended June 30, 2017 reflect income available to common stockholders of approximately \$21,562,000, or \$2.07 earnings per diluted share, compared with approximately \$13,080,000, or \$1.31 earnings per diluted share, for the six months ended June 30, 2016. The period-over-period increase was primarily due to a \$19,932,000 decrease in premiums ceded as well as a \$12,024,000 decrease in gross premiums earned, resulting in an increase in net premiums earned of \$7,908,000. In addition, our investment-related income during 2017 compared with the corresponding period in 2016 increased approximately \$4,615,000.

**Revenue**

*Gross Premiums Earned* for the six months ended June 30, 2017 and 2016 were approximately \$181,707,000 and \$193,731,000, respectively. The decrease in 2017 was attributable to policy attrition as well as a rate decrease effective on new and renewal policies beginning in January 2016.

*Premiums Ceded* for the six months ended June 30, 2017 and 2016 were approximately \$56,824,000 and \$76,756,000, respectively, representing 31.3% and 39.6%, respectively, of gross premiums earned. The decrease from the corresponding period in 2016 was primarily attributable to





**Table of Contents**

lower reinsurance costs as described earlier. In addition, the reduction to our ceded premiums attributable to retrospective provisions under certain reinsurance contracts was higher as compared with the corresponding period in 2016. For the six months ended June 30, 2017 and 2016, premiums ceded reflected net reductions of approximately \$6,956,000 and \$5,822,000, respectively, related to these provisions. See *Economic Impact of Reinsurance Contracts with Retrospective Provisions* under *Critical Accounting Policies and Estimates*.

*Net Premiums Written* for the six months ended June 30, 2017 and 2016 totaled approximately \$149,050,000 and \$138,285,000, respectively. The increase in 2017 resulted from a decrease of approximately \$19,932,000 in premiums ceded combined with a decrease of approximately \$9,167,000 in gross premiums written during the year.

*Net Premiums Earned* for the six months ended June 30, 2017 and 2016 were approximately \$124,883,000 and \$116,975,000, respectively, and reflected gross premiums earned less reinsurance costs as described above.

The following is a reconciliation of our total Net Premiums Written to Net Premiums Earned for the six months ended June 30, 2017 and 2016 (amounts in thousands):

|                               | <b>Six Months Ended</b> |             |
|-------------------------------|-------------------------|-------------|
|                               | <b>June 30,</b>         |             |
|                               | <b>2017</b>             | <b>2016</b> |
| Net Premiums Written          | \$ 149,050              | \$ 138,285  |
| Increase in Unearned Premiums | (24,167)                | (21,310)    |
| Net Premiums Earned           | \$ 124,883              | \$ 116,975  |

*Net Investment Income* for the six months ended June 30, 2017 and 2016 was approximately \$5,644,000 and \$3,215,000, respectively. The increase in 2017 was primarily due to \$1,332,000 of income from limited partnership investments compared with a 1,065,000 loss during the corresponding period in 2016. See Note 4 *Investments* under *Net Investment Income* to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q.

*Net Other-Than-Temporary Impairment Losses* for the six months ended June 30, 2017 and 2016 were approximately \$390,000 and \$1,217,000, respectively. During the six months ended June 30, 2017, we recognized impairment losses specific to two fixed-maturity securities and three equity securities. The fixed-maturity securities were subject to impairment resulting from our intention to sell these securities before their recovery. Three equity securities were impaired as a result of the length of time each security had been in an unrealized loss position with no near term prospect of recovery. During the six months ended June 30, 2016, we recognized impairment losses specific to one fixed-maturity security and 15 equity securities.

*Gain on Repurchases of Convertible Senior Notes* for the six months ended June 30, 2016 was approximately \$153,000. The gain was attributable to the repurchase of \$13,010,000 in principal of our 3.875% Convertible Senior Notes during the first quarter of 2016.

**Expenses**

Our *Losses and Loss Adjustment Expenses* amounted to approximately \$53,194,000 and \$53,352,000, respectively, for the six months ended June 30, 2017 and 2016. Our 2017 losses and loss adjustment expenses reflected the

continuation of reserve strengthening in response to trends involving assignment of insurance benefits and related litigation. See Reserves for Losses and Loss Adjustment Expenses under Critical Accounting Policies and Estimates.

---

**Table of Contents**

*Policy Acquisition and Other Underwriting Expenses* for the six months ended June 30, 2017 and 2016 of approximately \$19,719,000 and \$21,989,000, respectively. The \$2,270,000 decrease from the corresponding period in 2016 was primarily attributable to decreased commissions and premium taxes resulting from policy attrition and the effect of the rate decrease.

*Salaries and Wages* for the six months ended June 30, 2017 and 2016 were approximately \$10,446,000 and \$11,064,000, respectively. The \$618,000 decrease from the corresponding period in 2016 was primarily attributable to the capitalization of payroll costs related to a software development project for internal use.

*Loss on repurchases of Senior Notes* for the six months ended June 30, 2017 was approximately \$743,000, resulting from the early extinguishment of our 8% Senior Notes.

*Income Tax Expense* for the six months ended June 30, 2017 and 2016 were \$11,885,000 and \$7,846,000, respectively, for state, federal, and foreign income taxes resulting in an effective tax rate of 35.5% for 2017 and 37.5% for 2016. The decrease in the effective tax rate primarily resulted from the recognition of tax benefits associated with the exercise of common stock options during the second quarter of 2017.

**Ratios:**

The loss ratio applicable to the six months ended June 30, 2017 was 42.6% compared with 45.6% for the six months ended June 30, 2016. The decrease was primarily due to the increase in net premiums earned which was driven in large part by decreased reinsurance costs.

The expense ratio applicable to the six months ended June 30, 2017 was 39.0% compared with 41.0% for the six months ended June 30, 2016. The decrease in our expense ratio is primarily attributable to the increase net premiums earned.

The combined ratio is the measure of overall underwriting profitability before other income. Our combined ratio for the six months ended June 30, 2017 was 81.6% compared with 86.6% for the six months ended June 30, 2016.

Due to the impact our reinsurance costs have on net premiums earned from period to period, our management believes the combined ratio measured to gross premiums earned is more relevant in assessing overall performance. The combined ratio to gross premiums earned for the six months ended June 30, 2017 was 56.1% compared with 52.3% for the six months ended June 30, 2016.

***Seasonality of Our Business***

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

**Table of Contents****LIQUIDITY AND CAPITAL RESOURCES**

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

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

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

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

***Senior Notes and Promissory Note***

The following table summarizes our long-term debt's principal and interest payment obligations at June 30, 2017:

|                                 | <b>Maturity Date</b>   | <b>Interest Payment Due Date</b>  |
|---------------------------------|------------------------|-----------------------------------|
| 3.875% Convertible Senior Notes | March 2019             | March 15 and September 15         |
| 4.25% Convertible Senior Notes  | March 2037             | March 1 and September 1           |
| 4% Promissory Note              | Through February 2031  | 1 <sup>st</sup> day of each month |
| 3.75% Callable Promissory Note  | Through September 2036 | 1 <sup>st</sup> day of each month |
| 3.95% Promissory Note           | Through February 2020  | 17 <sup>th</sup> of each month    |

See Note 8 – Long-Term Debt to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q for additional information.

***Limited Partnership Investments***

Our limited partnership investments consist of three private equity funds managed by their general partners. These funds have unexpired capital commitments which are callable at the discretion of the fund's general partner for funding new investments or expenses of the fund. At June 30, 2017, there was an aggregate unfunded capital balance of \$12,065,000. See *Limited Partnership Investments* under Note 4 – Investments to our unaudited consolidated financial

statements under Item 1 of this Quarterly Report on Form 10-Q for additional information.

## **Table of Contents**

### ***Share Repurchase Plan***

In December 2016, our Board of Directors approved a one-year plan to repurchase up to \$20,000,000 of common shares under which we may purchase shares of common stock in open market purchases, block transactions and privately negotiated transactions in accordance with applicable federal securities laws. At June 30, 2017, there was approximately \$18,411,000 available under the plan. See Note 14 **Stockholders Equity** to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q.

### ***Real Estate Development and Acquisition***

We may contemplate the acquisition of land for future development through one of our existing joint ventures. Although we have no outstanding commitment to fund any future project and we expect to finance future development projects with cash from real estate operations and through property financings, we may be required to make additional capital contributions when warranted. In addition, we completed our development project in Riverview, Florida in July 2017. We have the option to acquire the joint venture partner's interest in this project.

### ***Sources and Uses of Cash***

#### *Cash Flows for the Six months ended June 30, 2017*

Net cash provided by operating activities for the six months ended June 30, 2017 was approximately \$31,364,000, which consisted primarily of cash received from net premiums written less cash disbursed for operating expenses, losses and loss adjustment expenses and interest payments. Net cash used in investing activities of \$74,920,000 was primarily due to the purchases of available-for-sale securities of \$114,092,000, the limited partnership investments of \$1,489,000, and the real estate investments of \$1,931,000, offset by the proceeds from sales of available-for-sale securities of \$27,775,000, the distributions of \$11,758,000 from limited partnership investments and the redemptions and repayments of fixed-maturity securities of \$3,937,000. Net cash provided by financing activities totaled \$59,495,000, which was primarily due to the proceeds from issuance of 4.25% Convertible Senior Notes of \$143,750,000, offset by \$40,250,000 used in the repurchases of our 8% senior notes, \$4,975,000 of related underwriting and issuance costs, \$32,226,000 used in our share repurchases and \$6,523,000 of net cash dividend payments.

#### *Cash Flows for the Six months ended June 30, 2016*

Net cash provided by operating activities for the six months ended June 30, 2016 was approximately \$70,435,000, which consisted primarily of cash received from net premiums written less cash disbursed for operating expenses, losses and loss adjustment expenses and interest payments. Net cash used in investing activities of \$8,141,000 was primarily due to the purchases of available-for-sale securities of \$48,083,000, and the limited partnership investments of \$2,448,000, offset by the proceeds from sales of available-for-sale securities of \$42,679,000. Net cash used in financing activities totaled \$20,741,000, which was primarily due to \$11,347,000 used in the repurchases of our convertible senior notes, \$12,015,000 used in our share repurchase plan and \$5,936,000 of net cash dividend payments, offset by the proceeds from issuance of a 4% promissory note of \$9,200,000.

**Table of Contents**

***Investments***

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

At June 30, 2017, we had \$304,798,000 of available-for-sale investments, which are carried at fair value. Changes in the general interest rate environment affect the returns available on new fixed-maturity investments. While a rising interest rate environment enhances the returns available on new investments, it reduces the market value of existing fixed-maturity investments and thus the availability of gains on disposition. A decline in interest rates reduces the returns available on new fixed-maturity investments but increases the market value of existing fixed-maturity investments, creating the opportunity for realized investment gains on disposition.

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

**OFF-BALANCE SHEET ARRANGEMENTS**

As of June 30, 2017, we had unexpired capital commitments for three limited partnerships in which we hold interests. Such commitments are not recognized in the financial statements but are required to be disclosed in the notes to the financial statements. See Note 16 Commitments and Contingencies to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q and Contractual Obligations and Commitment below for additional information.

**Table of Contents****CONTRACTUAL OBLIGATIONS AND COMMITMENTS**

The following table summarizes our material contractual obligations and commitments as of June 30, 2017 (amounts in thousands):

|                                  | Total      | Payment Due by Period |           |           | More than<br>5 Years |
|----------------------------------|------------|-----------------------|-----------|-----------|----------------------|
|                                  |            | Less than<br>1 Year   | 1-3 Years | 3-5 Years |                      |
| Operating lease (1)              | \$ 672     | 165                   | 280       | 227       |                      |
| Service agreement (1)            | 114        | 23                    | 50        | 41        |                      |
| Reinsurance contracts (2)        | 19,400     | 19,400                |           |           |                      |
| Unfunded capital commitments (3) | 12,065     | 12,065                |           |           |                      |
| Long-term debt obligations (4)   | 306,177    | 12,129                | 118,963   | 158,883   | 16,202               |
| Total                            | \$ 338,428 | 43,782                | 119,293   | 159,151   | 16,202               |

- (1) Represents the lease for office space in Miami, Florida and the lease and maintenance service agreement for office space in Noida, India. Liabilities related to our India operations were converted from Indian rupees to U.S. dollars using the June 30, 2017 exchange rate.
- (2) Represents the minimum payment of reinsurance premiums under multi-year reinsurance contracts.
- (3) Represents the unfunded balance of capital commitments under the subscription agreements related to three limited partnerships in which we hold an interest.
- (4) Amounts represent principal and interest payments over the lives of various long-term debt obligations. See Note 8 Long-Term Debt to our unaudited consolidated financial statements under Item 1 of this Quarterly Report on Form 10-Q.

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

We have prepared our consolidated financial statements and related disclosures in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements and related disclosures requires us to make judgments, assumptions and estimates to develop amounts reflected and disclosed in our consolidated financial statements. Management bases its estimates on historical experience and on various other assumptions it believes to be reasonable under the circumstances. Actual results may differ from these estimates and such differences may be material.

We believe our critical accounting policies and estimates are those related to losses and loss adjustment expenses, reinsurance with retrospective provisions, deferred income taxes, and stock-based compensation expense. These policies are critical to the portrayal of our financial condition and operating results. They require management to make judgments and estimates about inherently uncertain matters. Material estimates that are particularly susceptible to significant change in the near term are related to our losses and loss adjustment expense reserves, which include amounts estimated for claims incurred but not yet reported and reinsurance contracts with retrospective provisions.

**Reserves for Losses and Loss Adjustment Expenses**



Our liability for losses and loss adjustment expense ( Reserves ) is specific to property insurance, which is our insurance division s only line of business. The Reserves include both case reserves on reported claims and our reserves for incurred but not reported ( IBNR ) losses. At each period end date, the balance of our Reserves is based on our best estimate of the ultimate cost of each claim for those known cases and the IBNR loss reserves are estimated based primarily on our historical experience. Changes in the estimated liability are charged or credited to operations as the losses and loss adjustment expenses are adjusted.

---

**Table of Contents**

The IBNR represents our estimate of the ultimate cost of all claims that have occurred but have not been reported to us, and in some cases may not yet be known to the insured, and future development of reported claims. Estimating the IBNR component of our Reserves involves considerable judgment on the part of management. At June 30, 2017, \$49,850,000 of the total \$73,089,000 we have reserved for losses and loss adjustment expenses is attributable to our estimate of IBNR. The remaining \$23,239,000 relates to known cases which have been reported but not yet fully settled in which case we have established a reserve based on currently available information and our best estimate of the cost to settle each claim. At June 30, 2017, \$17,397,000 of the \$23,239,000 in reserves for known cases relates to claims incurred during prior years.

Our Reserves increased from \$70,492,000 at December 31, 2016 to \$73,089,000 at June 30, 2017. The \$2,597,000 increase in our Reserves is comprised of \$25,874,000 in reserves related to claims occurring in the 2017 loss year offset by reductions in our Reserves of \$14,908,000 for 2016 and \$3,590,000 for 2015 and prior loss years. The \$25,874,000 in Reserves established for 2017 claims is primarily driven by an allowance for subsequent development of claims reported for the accident year and an allowance for those claims that have been incurred but not reported to the company as of June 30, 2017. The decrease of \$23,277,000 specific to our 2016 and prior loss-year reserves is primarily due to settlement of claims related to those loss years.

Based on all information known to us, we consider our Reserves at June 30, 2017 to be adequate to cover our claims for losses that have occurred as of that date including losses yet to be reported to us. However, these estimates are continually reviewed by management as they are subject to significant variability and may be impacted by trends in claim severity and frequency or unusual exposures that have not yet been identified. As part of the process, we review historical data and consider various factors, including known and anticipated regulatory and legal developments, changes in social attitudes, inflation and economic conditions. As experience develops and other data becomes available, these estimates are revised, as required, resulting in increases or decreases to the existing unpaid losses and loss adjustment expenses. Adjustments are reflected in the results of operations in the period in which they are made and the liabilities may deviate substantially from prior estimates.

**Economic Impact of Reinsurance Contracts with Retrospective Provisions**

Certain of our reinsurance contracts include retrospective provisions that adjust premiums, increase the amount of future coverage, or result in a profit commission in the event losses are minimal or zero. In accordance with accounting principles generally accepted in the United States of America, we will recognize an asset in the period in which the absence of loss experience gives rise to an increase in future coverage or obligates the reinsurer to pay cash or other consideration under the contract. In the event that a loss arises, we will derecognize such asset in the period in which a loss arises. Such adjustments to the asset, which accrue throughout the contract term, will negatively impact our operating results when a catastrophic loss event occurs during the contract term.

For the three months ended June 30, 2017 and 2016, we accrued benefits of \$2,968,000 and \$3,947,000, respectively. For the three months ended June 30, 2017, we deferred recognition of \$665,000 of reinsurance costs. For the three months ended June 30, 2016, we recognized net ceded premiums of \$946,000, representing amortization of \$1,223,000 of previously deferred reinsurance costs for increased coverage offset by \$277,000 of ceded premiums deferred for the period. For the three months ended June 30, 2017 and 2016, net reductions in ceded premiums totaled \$3,634,000 and \$3,001,000, respectively.

## **Table of Contents**

For the six months ended June 30, 2017 and 2016, we accrued benefits of \$5,459,000 and \$8,630,000, respectively. For the six months ended June 30, 2017, we deferred recognition of \$1,496,000 of reinsurance costs. For the six months ended June 30, 2016, we recognized net ceded premiums of \$2,808,000, representing amortization of \$3,085,000 of previously deferred reinsurance costs for increased coverage offset by \$277,000 of ceded premiums deferred for the period. For the six months ended June 30, 2017 and 2016, net reductions in ceded premiums totaled \$6,956,000 and \$5,822,000, respectively. In June 2016, we received cash totaling \$37,800,000 in connection with the benefits accrued for two retrospective reinsurance contracts that were terminated effective May 31, 2016.

As of June 30, 2017, we had \$11,269,000 of accrued benefits and \$3,648,000 of ceded premiums deferred, amounts that would be charged to earnings in the event we experience a catastrophic loss that exceeds the coverage limits provided under such agreements and in the period that the increased coverage is applicable. At December 31, 2016, we had \$5,810,000 of accrued benefits and \$2,152,000 of ceded premiums deferred related to these agreements.

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

The above and other accounting estimates and their related risks that we consider to be our critical accounting estimates are more fully described in our Annual Report on Form 10-K, which we filed with the SEC on February 22, 2017. For the six months ended June 30, 2017, there have been no material changes with respect to any of our critical accounting policies.

## **RECENT ACCOUNTING PRONOUNCEMENTS**

For information with respect to recent accounting pronouncements and the impact of these pronouncements on our consolidated financial statements, see Note 3 to our Notes to Consolidated Financial Statements.

## **ITEM 3 *QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK***

Our investment portfolio at June 30, 2017 included fixed-maturity and equity securities, the purposes of which are not for trading or speculation. Our main objective is to maximize after-tax investment income and maintain sufficient liquidity to meet our obligations while minimizing market risk, which is the potential economic loss from adverse fluctuations in securities prices. We consider many factors including credit ratings, investment concentrations, regulatory requirements, anticipated fluctuation of interest rates, durations and market conditions in developing investment strategies. Our investment securities are managed primarily by outside investment advisors and are overseen by the investment committee appointed by our board of directors.

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

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

**Table of Contents***Interest Rate Risk*

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

The following table illustrates the impact of hypothetical changes in interest rates to the fair value of our fixed-maturity securities at June 30, 2017 (amounts in thousands):

| <b>Hypothetical Change in Interest Rates</b> | <b>Estimated Fair Value</b> | <b>Change in Estimated Fair Value</b> | <b>Percentage Increase (Decrease) in Estimated Fair Value</b> |
|----------------------------------------------|-----------------------------|---------------------------------------|---------------------------------------------------------------|
| 300 basis point increase                     | \$ 224,753                  | \$ (23,893)                           | (9.61)%                                                       |
| 200 basis point increase                     | 232,713                     | (15,933)                              | (6.41)%                                                       |
| 100 basis point increase                     | 240,677                     | (7,969)                               | (3.21)%                                                       |
| 100 basis point decrease                     | 256,620                     | 7,974                                 | 3.21%                                                         |
| 200 basis point decrease                     | 263,917                     | 15,271                                | 6.14%                                                         |
| 300 basis point decrease                     | 268,397                     | 19,751                                | 7.94%                                                         |

*Credit Risk*

Credit risk can expose us to potential losses arising principally from adverse changes in the financial condition of the issuers of our fixed-maturity securities. We mitigate the risk by investing in fixed-maturity securities that are generally investment grade, by diversifying our investment portfolio to avoid concentrations in any single issuer or business sector, and by continually monitoring each individual security for declines in credit quality. While we emphasize credit quality in our investment selection process, significant downturns in the markets or general economy may impact the credit quality of our portfolio.

The following table presents the composition of our fixed-maturity securities, by rating, at June 30, 2017 (amounts in thousands):

| <b>Comparable Rating</b> | <b>Amortized Cost</b> | <b>% of Total Amortized Cost</b> | <b>Estimated Fair Value</b> | <b>% of Total Estimated Fair Value</b> |
|--------------------------|-----------------------|----------------------------------|-----------------------------|----------------------------------------|
| AAA                      | \$ 1,703              | 1                                | \$ 1,709                    | 1                                      |
| AA+, AA, AA-             | 70,220                | 28                               | 70,532                      | 28                                     |
| A+, A, A-                | 92,951                | 38                               | 93,123                      | 37                                     |
| BBB+, BBB, BBB-          | 60,160                | 24                               | 61,465                      | 25                                     |
| BB+, BB, BB-             | 7,537                 | 3                                | 7,422                       | 3                                      |
| B+, B, B-                | 8,033                 | 3                                | 7,794                       | 3                                      |
| CCC+, CC and Not rated   | 6,543                 | 3                                | 6,601                       | 3                                      |

Edgar Filing: HCI Group, Inc. - Form 10-Q

|       |            |     |            |     |
|-------|------------|-----|------------|-----|
| Total | \$ 247,147 | 100 | \$ 248,646 | 100 |
|-------|------------|-----|------------|-----|

56

**Table of Contents***Equity Price Risk*

Our equity investment portfolio at June 30, 2017 included common stocks, perpetual preferred stocks, mutual funds and exchange traded funds. We may incur losses due to adverse changes in equity security prices. We manage the risk primarily through industry and issuer diversification and asset mix.

The following table illustrates the composition of our equity securities at June 30, 2017 (amounts in thousands):

|                                                        | <b>Estimated<br/>Fair Value</b> | <b>% of<br/>Total<br/>Estimated<br/>Fair Value</b> |
|--------------------------------------------------------|---------------------------------|----------------------------------------------------|
| <b>Stocks by sector:</b>                               |                                 |                                                    |
| Financial                                              | \$ 28,001                       | 50                                                 |
| Industrial                                             | 4,685                           | 8                                                  |
| Consumer                                               | 3,891                           | 7                                                  |
| Energy                                                 | 3,920                           | 7                                                  |
| Other (1)                                              | 4,918                           | 9                                                  |
|                                                        | <b>45,415</b>                   | <b>81</b>                                          |
| <b>Mutual funds and Exchange traded funds by type:</b> |                                 |                                                    |
| Debt                                                   | 9,336                           | 17                                                 |
| Equity                                                 | 1,401                           | 2                                                  |
|                                                        | <b>10,737</b>                   | <b>19</b>                                          |
| <b>Total</b>                                           | <b>\$ 56,152</b>                | <b>100</b>                                         |

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

*Foreign Currency Exchange Risk*

At June 30, 2017, we did not have any material exposure to foreign currency related risk.

**ITEM 4 CONTROLS AND PROCEDURES***Evaluation of Disclosure Controls and Procedures*

Under the supervision and with the participation of our chief executive officer (our principal executive officer) and our chief financial officer (our principal financial officer), we have evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report, and, based on this evaluation, our chief executive officer and our chief financial officer have concluded that these disclosure controls and procedures are effective.

*Changes in Internal Control Over Financial Reporting*

There have been no changes in our internal controls over financial reporting during the quarter ended June 30, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

*Limitations on Effectiveness of Controls and Procedures*

In designing and evaluating the disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, implementation of possible controls and procedures depends on management's judgment in evaluating their benefits relative to costs.

**Table of Contents**

**PART II OTHER INFORMATION**

**ITEM 1 LEGAL PROCEEDINGS**

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

**ITEM 1A RISK FACTORS**

There have been no material changes from the risk factors previously disclosed in the section entitled Risk Factors in our Form 10-K, which was filed with the SEC on February 22, 2017.



**Table of Contents****ITEM 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS***(a) Sales of Unregistered Securities and Use of Proceeds*

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

*(b) Repurchases of Securities*

The table below summarizes the number of common shares repurchased during the three months ended June 30, 2017 under a share repurchase plan and also the number of shares of common stock surrendered by employees to satisfy their minimum federal income tax liability associated with the vesting of restricted shares in May 2017 (dollar amounts in thousands, except share and per share amounts):

| <b>For the Month Ended</b> | <b>Total Number<br/>of Shares<br/>Purchased</b> | <b>Average<br/>Price Paid<br/>Per<br/>Share</b> | <b>Total Number of<br/>Shares Purchased as<br/>Part of<br/>Publicly<br/>Announced<br/>Plans<br/>or<br/>Programs<br/>(a)</b> | <b>Maximum<br/>Dollar<br/>Value of Shares That<br/>May Yet Be<br/>Purchased<br/>Under<br/>The Plans<br/>or Programs<br/>(b)</b> |
|----------------------------|-------------------------------------------------|-------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------|
| April 30, 2017             |                                                 | \$                                              |                                                                                                                             | \$ 18,451                                                                                                                       |
| May 31, 2017               | 15,188                                          | \$ 44.17                                        | 900                                                                                                                         | \$ 18,411                                                                                                                       |
| June 30, 2017              |                                                 | \$                                              |                                                                                                                             | \$ 18,411                                                                                                                       |
|                            | 15,188                                          | \$ 44.17                                        | 900                                                                                                                         |                                                                                                                                 |

(a) The share repurchase plan approved by our Board of Directors on December 15, 2016 commenced in January 2017.

(b) Represents the balances before commissions and fees at the end of each month.

*Working Capital Restrictions and Other Limitations on Payment of Dividends*

We are not subject to working capital restrictions or other limitations on the payment of dividends. Our insurance subsidiary, however, is subject to restrictions on the dividends it may pay. Those restrictions could impact HCI's ability to pay future dividends.

Under Florida law, a domestic insurer may not pay any dividend or distribute cash or other property to its stockholder except out of that part of its available and accumulated capital and surplus funds which is derived from realized net operating profits on its business and net realized capital gains. Additionally, a Florida domestic insurer may not make dividend payments or distributions to its stockholder without prior approval of the Florida Office of Insurance

Regulation if the dividend or distribution would exceed the larger of (1) the lesser of (a) 10.0% of its capital surplus or (b) net income, not including realized capital gains, plus a two year carry forward, (2) 10.0% of capital surplus with dividends payable constrained to unassigned funds minus 25% of unrealized capital gains or (3) the lesser of (a) 10.0% of capital surplus or (b) net investment income plus a three year carry forward with dividends payable constrained to unassigned funds minus 25% of unrealized capital gains.

**Table of Contents**

Alternatively, a Florida domestic insurer may pay a dividend or distribution without the prior written approval of the Florida Office of Insurance Regulation (1) if the dividend is equal to or less than the greater of (a) 10.0% of the insurer's capital surplus as regards policyholders derived from realized net operating profits on its business and net realized capital gains or (b) the insurer's entire net operating profits and realized net capital gains derived during the immediately preceding calendar year, (2) the insurer will have policy holder capital surplus equal to or exceeding 115.0% of the minimum required statutory capital surplus after the dividend or distribution, (3) the insurer files a notice of the dividend or distribution with the Florida Office of Insurance Regulation at least ten business days prior to the dividend payment or distribution and (4) the notice includes a certification by an officer of the insurer attesting that, after the payment of the dividend or distribution, the insurer will have at least 115% of required statutory capital surplus as to policyholders. Except as provided above, a Florida domiciled insurer may only pay a dividend or make a distribution (1) subject to prior approval by the Florida Office of Insurance Regulation or (2) 30 days after the Florida Office of Insurance Regulation has received notice of such dividend or distribution and has not disapproved it within such time.

During the six months ended June 30, 2017, HCPCI paid a \$18,000,000 dividend to HCI.

**ITEM 3 *DEFAULTS UPON SENIOR SECURITIES***

None.

**ITEM 4 *MINE SAFETY DISCLOSURES***

None.

**ITEM 5 *OTHER INFORMATION***

None.

**Table of Contents****ITEM 6 EXHIBITS**

The following documents are filed as part of this report:

**EXHIBIT**

| <b>NUMBER</b> | <b>DESCRIPTION</b>                                                                                                                                                                                                                                                                                                                                                                                                                                           |
|---------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3.1           | Articles of Incorporation, with amendments. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 7, 2013.                                                                                                                                                                                                                                                                                                         |
| 3.1.1         | Articles of Amendment to Articles of Incorporation designating the rights, preferences and limitations of Series B Junior Participating Preferred Stock. Incorporated by reference to Exhibit 3.1 to our Form 8-K filed October 18, 2013.                                                                                                                                                                                                                    |
| 3.2           | Bylaws. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 7, 2013.                                                                                                                                                                                                                                                                                                                                             |
| 4.1           | Form of common stock certificate. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed November 7, 2013.                                                                                                                                                                                                                                                                                                                 |
| 4.2           | Supplement No. 1, dated as of January 17, 2013, to the Indenture, dated as of January 17, 2013, between HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) and The Bank of New York Mellon Trust Company, N.A., as Trustee. Incorporated by reference to the correspondingly numbered exhibit to our Form 8-K filed January 17, 2013.                                                                                                               |
| 4.3           | Form of 8.00% Senior Note due 2020 (included in Exhibit 4.2). Incorporated by reference to the correspondingly numbered exhibit to our Form 8-K filed January 17, 2013.                                                                                                                                                                                                                                                                                      |
| 4.4           | Indenture, dated as of January 17, 2013, between HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) and The Bank of New York Mellon Trust Company, N.A. Incorporated by reference to Exhibit 4.4 to Amendment No. 1 to our Registration Statement on Form S-3 (File No. <u>333-185228</u> ) filed December 10, 2012.                                                                                                                                |
| 4.6           | Form of Subordinated Indenture. Incorporated by reference to the correspondingly numbered exhibit to Amendment No. 1 to our Registration Statement on Form S-3 (File No. <u>333-185228</u> ) filed December 10, 2012.                                                                                                                                                                                                                                        |
| 4.7           | Rights Agreement, dated as of October 18, 2013, between HCI Group, Inc. and American Stock Transfer & Trust Company, LLC, which includes as Exhibit A thereto a summary of the terms of the Series B Junior Participating Preferred Stock, as Exhibit B thereto the Form of Right Certificate, and as Exhibit C thereto the Summary of Rights to Purchase Preferred Shares. Incorporated by reference to Exhibit 4.1 to our Form 8-K filed October 18, 2013. |

**Table of Contents**

- 4.7.1 Amendment, dated as of April 18, 2017, to the Rights Agreement, by and between the Company and American Stock Transfer & Trust Company, LLC, dated as of October 18, 2013. Incorporated by reference to Exhibit 4.1 to our Form 8-K filed April 24, 2017.
- 4.8 Indenture, dated December 11, 2013, between HCI Group, Inc. and The Bank of New York Mellon Trust Company, N.A. (including Global Note). Incorporated by reference to Exhibit 4.1 to our Form 8-K filed December 12, 2013.
- 4.9 See Exhibits 3.1, 3.1.1 and 3.2 of this report for provisions of the Articles of Incorporation, as amended, and our Bylaws, as amended, defining certain rights of security holders.
- 4.10 Indenture, dated March 3, 2017, between HCI Group, Inc. and The Bank of New York Mellon Trust Company, N.A. Incorporated by reference to Exhibit 4.1 of our Form 8-K filed March 3, 2017.
- 4.11 Form of Global 4.25% Convertible Senior Note due 2037 (included in Exhibit 4.1). Incorporated by reference to Exhibit 4.2 of our Form 8-K filed March 3, 2017.
- 10.1 Excess of Loss Retrocession Contract (flood), effective June 1, 2014, issued to Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 6, 2014.
- 10.2\*\* Executive Agreement dated May 1, 2007 between HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) and Richard R. Allen. Incorporated by reference to the correspondingly numbered exhibit to our Registration Statement on Form S-1 (File No. 333-150513), originally filed April 30, 2008, effective July 24, 2008, as amended.
- 10.3 Reimbursement Contract effective June 1, 2016 between Homeowners Choice Property & Casualty Insurance Company and the State Board of Administration which administers the Florida Hurricane Catastrophe Fund. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.4 Reimbursement Contract effective June 1, 2017 between Homeowners Choice Property & Casualty Insurance Company and the State Board of Administration which administers the Florida Hurricane Catastrophe Fund.
- 10.5\*\* Restated HCI Group, Inc. 2012 Omnibus Incentive Plan. Incorporated by reference to Exhibit 99.1 of our Form 10-Q filed March 23, 2017.

**Table of Contents**

- 10.6\*\* HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) 2007 Stock Option and Incentive Plan. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 29, 2008.
- 10.7\*\* Executive Employment Agreement dated November 23, 2016 between Mark Harmsworth and HCI Group, Inc.
- 10.8 Working Layer Catastrophe Excess of Loss Reinsurance Contract, effective: June 1, 2016, issued to Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers (National Fire). Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.9 Working Layer Catastrophe Excess of Loss Reinsurance Contract, effective June 1, 2016, issued to Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers (Claddaugh). Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.10 Working Layer Catastrophe Excess of Loss Specific Retrocession Contract effective June 1, 2016 issued to Claddaugh Casualty Insurance Company Ltd. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.11 Property Catastrophe Excess of Loss Reinsurance Contract effective June 1, 2016, issued to, Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.12 Property Catastrophe First Excess of Loss Specific Retrocession Contract effective June 1, 2016 issued to Claddaugh Casualty Insurance Company Ltd. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.

---

**Table of Contents**

- 10.13 Reinstatement Premium Protection Reinsurance Contract effective June 1, 2016 by Homeowners Choice Property & Casualty Insurance Company, Inc. and subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.14 Property Catastrophe Third Excess of Loss Reinsurance Contract effective June 1, 2016 issued to Homeowners Choice Property & Casualty Insurance Company, Inc. and subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.15 Property Catastrophe First Excess of Loss Reinsurance Contract effective June 1, 2016 issued to Homeowners Choice Property & Casualty Insurance Company, Inc. and subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-Q filed August 3, 2016.
- 10.16 Working Layer Catastrophe Excess of Loss Specific Retrocession Contract effective June 1, 2017 issued to Claddaugh Casualty Insurance Company Ltd. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment.
- 10.17 Property Catastrophe Excess of Loss Reinsurance Contract effective June 1, 2017 issued to Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment.
- 10.18 Property Catastrophe Second Event Excess of Loss Reinsurance Contract effective June 1, 2017 issued to Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment.
- 10.19 Reinstatement Premium Protection Reinsurance Contract effective June 1, 2017 issued to Homeowners Choice Property & Casualty Insurance Company, Inc. by subscribing reinsurers. Portions of this exhibit have been omitted pursuant to a request for confidential treatment.
- 10.23 Assumption Agreement effective October 15, 2014 by and between Homeowners Choice Property & Casualty Insurance Company, Inc. and Citizens Property Insurance Corporation. Incorporated by reference to Exhibit 10.1 of our Form 8-K filed January 28, 2015.
- 10.28\*\* Restricted Stock Agreement dated May 8, 2012 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 30,000 shares of restricted common stock to Richard R. Allen. Incorporated by reference to Exhibit 10.28 of our Form 8-K filed May 10, 2012.

**Table of Contents**

- 10.30\*\* Restricted Stock Agreement dated May 8, 2012 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 20,000 shares of restricted common stock to Andrew L. Graham. Incorporated by reference to Exhibit 10.30 of our Form 8-K filed May 10, 2012.
- 10.34\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 400,000 shares of restricted common stock to Paresh Patel. Incorporated by reference to Exhibit 10.34 of our Form 8-K filed May 21, 2013. See Exhibit 10.90
- 10.35\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 24,000 shares of restricted common stock to Sanjay Madhu. Incorporated by reference to Exhibit 10.35 of our Form 8-K filed May 21, 2013. See Exhibit 10.91
- 10.36\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 24,000 shares of restricted common stock to George Apostolou. Incorporated by reference to Exhibit 10.36 of our Form 8-K filed May 21, 2013. See Exhibit 10.92
- 10.37\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 24,000 shares of restricted common stock to Harish Patel. Incorporated by reference to Exhibit 10.37 of our Form 8-K filed May 21, 2013. See Exhibit 10.93
- 10.38\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 24,000 shares of restricted common stock to Gregory Politis. Incorporated by reference to Exhibit 10.38 of our Form 8-K filed May 21, 2013. See Exhibit 10.94
- 10.39\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 24,000 shares of restricted common stock to Anthony Saravanos. Incorporated by reference to Exhibit 10.39 of our Form 8-K filed May 21, 2013. See Exhibit 10.95
- 10.40\*\* Restricted Stock Agreement dated May 16, 2013 whereby HCI Group, Inc. (formerly known as Homeowners Choice, Inc.) issued 24,000 shares of restricted common stock to Martin Traber. Incorporated by reference to Exhibit 10.40 of our Form 8-K filed May 21, 2013. See Exhibit 10.96



---

**Table of Contents**

- 10.52\*\* Restricted Stock Agreement dated August 29, 2013 whereby HCI Group, Inc. issued 10,000 shares of restricted common stock to Anthony Saravanos. Incorporated by reference to Exhibit 10.52 of our Form 8-K filed August 29, 2013.
- 10.53\*\* Restricted Stock Agreement dated November 12, 2013 whereby HCI Group, Inc. issued 24,000 shares of restricted common stock to Wayne Burks. Incorporated by reference to Exhibit 10.11 of our Form 8-K filed November 13, 2013. See Exhibit 10.97
- 10.54\*\* Restricted Stock Agreement dated November 12, 2013 whereby HCI Group, Inc. issued 24,000 shares of restricted common stock to James J. Macchiarola. Incorporated by reference to Exhibit 10.12 of our Form 8-K filed November 13, 2013. See Exhibit 10.98
- 10.56 Prepaid Forward Contract, dated December 5, 2013 and effective as of December 11, 2013, between HCI Group, Inc. and Deutsche Bank AG, London Branch. Incorporated by reference to Exhibit 10.1 of our Form 8-K filed December 12, 2013.
- 10.57 Form of executive restricted stock award contract. Incorporated by reference to Exhibit 10.57 of our Form 10-Q for the quarter ended March 31, 2014 filed May 1, 2014.
- 10.58 Purchase Agreement, dated February 28, 2017, by and between HCI Group, Inc. and JMP Securities LLC and SunTrust Robinson Humphrey, Inc., as representatives of the several initial purchasers named therein. Incorporated by reference to Exhibit 10.1 of our Form 8-K filed February 28, 2017.
- 10.59 Prepaid Forward Contract, dated February 28, 2017 and effective as of March 3, 2017, between HCI Group, Inc. and Societe Generale. Incorporated by reference to Exhibit 10.1 of our Form 8-K filed March 3, 2017.
- 10.88\*\* Nonqualified Stock Option Agreement between Paresh Patel and HCI Group, Inc. dated January 7, 2017. Incorporated by reference to exhibit 99.2 to our Form 8-K filed January 11, 2017.
- 10.89\*\* Employment Agreement between Paresh Patel and HCI Group, Inc. dated December 30, 2016. Incorporated by reference to the exhibit numbered 99.1 to our Form 8-K filed December 30, 2016.
- 10.90\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Paresh Patel and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

**Table of Contents**

10.91\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Sanjay Madhu and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.92\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between George Apostolou and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.93\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Harish Patel and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.94\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Gregory Politis and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.95\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Anthony Saravanos and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.96\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Martin Traber and HCI Group, Inc. dated May 16, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.97\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Wayne Burks and HCI Group, Inc. dated November 12, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.98\*\* Amendment dated March 2, 2016 to Restricted Stock Award Contract between Jim Macchiarola and HCI Group, Inc. dated November 12, 2013. Incorporated by reference to the correspondingly numbered exhibit to our Form 10-K filed March 4, 2016.

10.99\*\* Restricted Stock Award Contract between Paresh Patel and HCI Group, Inc. dated January 7, 2017. Incorporated by reference to exhibit 99.1 to our Form 8-K filed January 11, 2017.

10.100\*\* Restricted Stock Award Contract Restricted Stock Award Contract between Mark Harmsworth and HCI Group, Inc. dated December 5, 2016.

31.1 Certification of the Chief Executive Officer

31.2 Certification of the Chief Financial Officer

32.1 Written Statement of the Chief Executive Officer Pursuant to 18 U.S.C.ss.1350

32.2 Written Statement of the Chief Financial Officer Pursuant to 18 U.S.C.ss.1350

**Table of Contents**

101.INS XBRL Instance Document.  
101.SCH XBRL Taxonomy Extension Schema.  
101.CAL XBRL Taxonomy Extension Calculation Linkbase.  
101.DEF XBRL Definition Linkbase.  
101.LAB XBRL Taxonomy Extension Label Linkbase.  
101.PRE XBRL Taxonomy Extension Presentation Linkbase.

\*\* Management contract or compensatory plan.

**Table of Contents**

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, who has signed this report on behalf of the Company.

HCI GROUP, INC.

August 3, 2017

By: /s/ Paresh Patel  
Paresh Patel  
Chief Executive Officer  
(Principal Executive Officer)

August 3, 2017

By: /s/ James Mark Harmsworth  
James Mark Harmsworth  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

A signed original of this document has been provided to HCI Group, Inc. and will be retained by HCI Group, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.