

Homeowners Choice, Inc.
Form 10-K
March 29, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2010

OR

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

Commission File Number

001-34126

Homeowners Choice, Inc.

(Exact name of Registrant as specified in its charter)

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Florida
(State of Incorporation)

20-5961396
(IRS Employer
Identification No.)

2340 Drew Street, Suite 200

Clearwater, FL 33765

(Address, including zip code of principal executive offices)

(727) 213-3600

(Registrant's telephone number, including area code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common shares, no par value	NASDAQ Global Select Market
Common stock warrants	NASDAQ Global Market
7% Series A Cumulative Redeemable Preferred Stock, no par value	NASDAQ Capital Market

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

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No (The registrant has not yet been phased into the interactive data requirements)

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 229.10(f)(1) of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Indicate by check mark whether the Registrant is a shell company (as defined in Rule 229.10(f)(1) of the Exchange Act). Yes No

The aggregate market value of the common stock held by non-affiliates of the registrant as of June 30, 2010 was \$29,293,931.

The number of shares outstanding of the registrant's common stock, no par value, on March 21, 2011 was 6,135,281.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's proxy statement for its 2011 annual meeting of shareholders are incorporated by reference into Part III of this Form 10-K.

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PART I

ITEM 1 *Business*

General

Homeowners Choice, Inc. is a property and casualty insurance holding company incorporated in Florida in 2006. Through our subsidiaries, which consist of, Homeowners Choice Managers, Inc., Southern Administration, Inc., Claddaugh Casualty Insurance Company, Ltd., and Homeowners Choice Property & Casualty Insurance Company, Inc. and its subsidiary, HCPCI Holdings LLC, we currently provide property and casualty homeowners insurance, condominium-owners insurance, and tenants insurance to individuals owning property in Florida. We offer these insurance products at competitive rates while pursuing profitability using selective underwriting criteria. Our property and casualty business is our only reportable segment. Our financial information is set forth in Part II, Item 8.

Our principal executive offices are located at 2340 Drew Street, Suite 200, Clearwater, Florida 33765, and our telephone number is (727) 213-3600.

We file annual, quarterly, and current reports with the Securities and Exchange Commission (SEC). These filings are accessible free of charge on our website, www.hcpci.com (click SEC filings at the Investors tab), as soon as reasonably practicable after they have been electronically filed with or furnished to the SEC. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers, which you can access via the SEC's website at www.sec.gov. In addition, these filings are accessible at the SEC's Public Reference Room, which is located at 100 F Street, NE, Washington, DC 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330.

As of December 31, 2010 and 2009, we had total assets of \$140.9 million and \$137.9 million, respectively, and stockholders' equity of \$46.6 million and \$45.4 million, respectively. Our net income was approximately \$5.4 million and \$10.9 million, respectively, for the years ended December 31, 2010 and 2009.

Company History

We began operations in June of 2007 by participating in a take-out program through which we assumed insurance policies held by Citizens Property Insurance Corporation (Citizens), a Florida state-supported insurer. The take-out program is a legislatively mandated program designed to reduce the state's risk exposure by encouraging private companies to assume policies from Citizens. Policies were assumed in eight separate assumption transactions which took place in July and November 2007, February, June, October and December 2008, December 2009, and December 2010. Substantially all of our premium revenue since inception comes from these assumptions. We currently have approximately 65,000 policies in force. Of those policies assumed, approximately 86% are homeowners' insurance policies, and the remaining 14% are a combination of policies written for condominium-owners and tenants. Our current policies in force represent approximately \$135 million in annualized premiums.

Citizens requires us to offer renewals on the policies we acquire for a period of three years subsequent to the initial expiration of the assumed policies. The policyholders have the option to renew with us or they may ask their agent to place their coverage with another insurance company. We strive to retain these policies by offering

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competitive rates to our policyholders.

We face various challenges to implementing our operating and growth strategies. Since we write policies that cover Florida homeowners, condominium owners, and tenants, we cover losses that may arise from, among other things, catastrophes, which could have a significant effect on our business, results of operations, and financial condition. To mitigate our risk of such losses, we cede a portion of our exposure to other entities under catastrophe excess of loss reinsurance treaties. Even without catastrophic events, we may incur losses and loss adjustment expenses that deviate substantially from our estimates and that may exceed our reserves, in which case our net income and capital would decrease. Our operating and growth strategies may also be impacted by regulation of our business by the State of Florida, which must approve our policy forms and premium rates as well as monitor our insurance subsidiary's ability to meet all requirements for regulatory compliance. Additionally, we compete with large, well-established insurance companies as well as other specialty insurers that, in most cases, possess greater financial resources, larger agency networks, and greater name recognition. See Item 1A, Risk Factors, below.

Competition

We operate in highly competitive markets where we face competition from national, regional and residual market insurance companies. Many of our competitors have larger financial capacities, greater resource availability, and more diversification in terms of insurance coverage. Our competitors include companies which market their products through agents, as well as companies which sell insurance directly to their customers. Large national insurers may have certain competitive advantages such as increased name recognition, increased loyalty of their customer base, and reduced policy acquisition costs. Additionally, as described in greater detail below in Government Regulation, the Florida legislature passed a new law in 2007 authorizing Citizens to reduce its premium rates and begin competing against private insurers in the residential property insurance market and expanding the authority of Citizens to write commercial insurance. We may also face competition from new or temporary entrants in our niche markets. In some cases, such entrants may, because of inexperience, desire for new business or other reasons, price their insurance below ours. Although our pricing is inevitably influenced to some degree by that of our competitors, we believe that it is generally not in our best interest to compete solely on price. We compete on the basis of underwriting criteria, our independent agent network, and superior service to our agents and insureds.

Seasonality of Our Business

We expect to experience increases in our losses and loss adjustment expenses during the period from June 1 through November 30 each year as this is typically the period during which hurricanes and other tropical storms may occur. As a result of such seasonal variations in our reported losses, we anticipate our operating profits during the period from June 1 through November 30 each year may be negatively impacted by an increase in losses and loss adjustment expenses.

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Government Regulation

We are subject to the laws and regulations in Florida, and the regulations of any other states in which we may seek to conduct business in the future. The regulations cover all aspects of our business and are generally designed to protect the interests of insurance policyholders as opposed to the interests of shareholders. Such regulations relate to authorized lines of business, capital and surplus requirements, allowable rates and forms, investment parameters, underwriting limitations, transactions with affiliates, dividend limitations, changes in control, market conduct, maximum amount allowable for premium financing service charges and a variety of other financial and non-financial components of our business. Our failure to comply with certain provisions of applicable insurance laws and regulations could have a material adverse effect on our business, results of operations or financial condition. In addition, any changes in such laws and regulations, including the adoption of consumer initiatives regarding rates charged for coverage, could materially and adversely affect our operations or our ability to expand. Recent legislation, among other things, reduces anticipated reinsurance costs and expands the role of Citizens. Other provisions contained in the recent legislation prevent non-renewals and cancellation (except for material misrepresentation and non-payment of premium) and new restrictions on coverage were prohibited until January 2010. We are unaware of any other consumer initiatives which could have a material adverse effect on our business, results of operations or financial condition.

Certain states have recently adopted laws or are considering proposed legislation which, among other things, limit the ability of insurance companies to effect rate increases or to cancel, reduce or non-renew insurance coverage with respect to existing policies. As discussed above, the recent consumer initiatives with Florida's property insurers demonstrate the state's ability to adopt such laws or to effectuate these policies through interpretations of existing laws. Also, the Florida legislature may adopt additional laws of this type in the future, which may adversely affect our business. In most years, the Florida legislature considers bills affecting the residential property insurance market in Florida. Property insurance legislation passed in 2008 increases penalties on insurers for noncompliance with the insurance code, establishes a private cause of action relating to insurers' claims payment practices, and extends the notice period applicable to insurers' nonrenewals of certain residential policies. The legislature also revised procedures governing insurers' rate filings.

Most states, including Florida, require licensure and regulatory approval prior to the marketing of new insurance products. Typically, licensure review is comprehensive and includes a review of a company's business plan, solvency, reinsurance, character of its officers and directors, rates, forms and other financial and non-financial aspects of a company. The regulatory authorities may not allow entry into a new market by not granting a license or by withholding approval. In addition, regulatory authorities may preclude or delay our entry into markets by disapproving or withholding approval of our product filings. As a new insurance company, we are subject to examinations with respect to our first three years in business, which includes the years ended December 31, 2008, 2009 and 2010.

All insurance companies must file quarterly and annual statements with certain regulatory agencies and are subject to regular and special examinations by those agencies. In accordance with the National Association of Insurance Commissioners (NAIC), the Florida Office of Insurance Regulation (Florida OIR) intends to comply with recent initiatives recommending that all insurance companies under the same insurance holding company registration statement be subjected to concurrent triennial examinations. Our subsidiary, Homeowners Choice Property & Casualty Insurance Company, Inc., is subject to Florida OIR examinations.

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Employees

As of March 15, 2011, we employ 80 individuals, all of whom are full-time employees and working primarily from our headquarters in Clearwater, Florida.

Executive Officers

The following table provides information with respect to our executive officers:

Name	Age	Position
Richard R. Allen	64	Chief Financial Officer
Andrew L. Graham	53	Vice President, General Counsel and Corporate Secretary
Francis McCahill, III	63	President and Chief Executive Officer
Jay Madhu	44	Vice President of Marketing and Director of Investor Relations
Paresh Patel	48	Executive Chairman, Strategic Planning and Investments

Richard R. Allen has served as the Chief Financial Officer of our company since November 2006 and also serves as a director of our subsidiary, Claddaugh Casualty Insurance Company, Ltd. Mr. Allen has over thirty years of experience in property/casualty insurance finance and management to include agency/broker relations, reinsurance and financial controls and reporting and third party administration. He has held various positions with several insurance companies as Chief Financial Officer, Controller and Senior Accounting Manager. From 1999 to 2005, Mr. Allen served as the Internal Auditor of Anthem Blue Cross and Blue Shield. From 1996 to 1998, Mr. Allen served as Controller for Symons International Group. From 1994 to 1996, Mr. Allen served as Controller/Treasurer of Coronet Insurance. In addition, Mr. Allen served as the Budget/Cost Manager of Bankers Life and Casualty from 1982 to 1990, and as the Controller of Bankers Standard Insurance Company, an affiliate of CIGNA, from 1969 to 1981. He has experience in forensic accounting and has participated, as a consultant, in numerous projects with state insurance departments. Mr. Allen earned his Bachelor of Science Degree from Quincy University in Quincy, Illinois.

Andrew L. Graham has served as our General Counsel since June 1, 2008 and also currently serves as our Corporate Secretary. Mr. Graham served from 1999 to 2007 in various capacities, including General Counsel, for Trinsic, Inc. (previously named Z-Tel Technologies, Inc.), a publicly-held provider of communications services headquartered in Tampa, Florida. Mr. Graham also serves on the Board of Trustees of Hillsborough Community College. Mr. Graham holds a Bachelor of Science degree from Florida State University and a Juris Doctor, as well as a Master of Laws (L.L.M.) in Taxation, from the University of Florida College of Law.

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Francis McCahill, III has served as our President and Chief Executive Officer and as a director of our company since November 2006. He also currently serves as the President and as a director of each of our five subsidiaries. Mr. McCahill's insurance career began in 1971. His experience includes senior level positions with major insurance brokerage firms including Frank B. Hall and Johnson & Higgins. From 1977 to 1988, he managed the worldwide Risk Management Programs of New York City-based Bristol-Myers Squibb Corp., Norton Simon, Inc. and Florida-based Harris Corporation. In 1991, after managing Johnson & Higgins' Central Florida Region, Mr. McCahill founded Braishfield of Florida, Inc. and Pollution Liability United States, Inc. As founder/president of those organizations, he established both entities as major insurance service providers throughout Florida. Mr. McCahill also founded Cypress Underwriters, Inc. of Port St. Lucie, Florida where he served as President from 1999 to 2006. In addition, Mr. McCahill was Tribunalized at Lloyd's of London. Mr. McCahill attended the United States Merchant Marine Academy, earned his Bachelor's Degree from St. John's University (College of Insurance), and attended Concord University School of Law. He received a number of Certificates in finance and risk management from the Wharton School of Business and the University of Florida.

Jay Madhu is currently Vice President of Marketing and Director of Investor Relations, having served as our Director of Investor Relations since February 2008. Additionally, Mr. Madhu has been a director of our company since May 2007. As an owner and manager of commercial properties, Mr. Madhu has been president of 5th Avenue Group LC since 2002 and President of Forrest Terrace LC since 1999. In addition, Mr. Madhu is an investor in banking and health maintenance organizations. He has also been President of The Mortgage Corporation Network (correspondent lenders) since 1996. Prior to that, Mr. Madhu was Vice President, mortgage division, First Trust Mortgage & Finance, from 1994 to 1996; Vice President, residential first mortgage division, Continental Management Associates Limited, Inc., from 1993 to 1994; and President, S&S Development, Inc. from 1991 to 1993. He attended Northwest Missouri State University, where he studied marketing and management.

Paresh Patel is currently Executive Chairman, Strategic Planning and Investments. Mr. Patel has been a director of our company since November 2006 and has served as the Chairman of our Board since May 2007. His analytical and technology skills were developed through experience with international financial, telecommunications and consulting positions. As a private investor from 2000 to 2006, Mr. Patel used statistical and probability techniques to develop and implement a system for managing money as a business to generate cash flow. Prior to that, Mr. Patel was director of customer care and billing with Global Crossing from 1998 to 2000. In that position, Mr. Patel defined business processes and systems, hired and trained department staff and led the merger of the customer care and billing systems with those of the company's acquisitions. As an independent consultant from 1991 to 1998, Mr. Patel worked with large international telephone companies. Mr. Patel received his bachelor's and master's degrees in Electronic Engineering from Cambridge University, England.

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ITEM 1A *Risk Factors*

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

We currently conduct business in Florida only. Thus, any single catastrophic event or other condition affecting losses in Florida could adversely affect our financial condition and results of operations.

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

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

The insurance business historically has been a cyclical industry characterized by periods of intense price competition due to excessive underwriting capacity, as well as periods when shortages of capacity permitted an increase in pricing and, thus, more favorable underwriting profits. An increase in premium levels is offset over time by an increased supply of insurance capacity, either by capital provided by new entrants or by the commitment of additional capital by existing insurers, which may cause prices to decrease. Any of these factors could lead to a significant reduction in premium rates, less favorable policy terms and fewer opportunities to underwrite insurance risks, which could have a material adverse effect on our results of operations and cash flows. In addition to these considerations, changes in the frequency and severity of losses suffered by insureds and insurers may affect the cycles of the insurance business significantly.

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

We may be unable to attract and retain qualified personnel.

Our operations are highly dependent on the efforts of our senior executive officers, in particular, our President and Chief Executive Officer, Francis McCahill, our Chief Financial Officer, Richard Allen, and our Executive Chairman, Paresh Patel. The loss of their leadership, industry knowledge and experience could negatively impact our operations. With the exception of Mr. McCahill and Mr. Allen, we have no employment agreements with any of our personnel nor do we have any guarantee of any employee's ongoing service.

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We do not have significant redundancy in our operations.

We conduct our business from offices located in Clearwater and Tampa, Florida, an area subject to tropical storms, which could damage our facilities or interrupt our power supply. The loss or significant impairment of functionality in these facilities for any reason could have a material, adverse effect on our business as we do not have significant redundancies to replace either facility if functionality is impaired. We have recently contracted with a third party vendor to maintain complete daily backups of our systems, which are stored at the vendor's facility in Atlanta, Georgia. Access to these databases is strictly controlled and limited to authorized personnel. While we have implemented daily off-site backups, we have not fully tested our plan to recover data in the event of a disaster.

Our information technology systems may fail or suffer a loss of security which could adversely affect our business.

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

The development and expansion of our business is dependent upon the successful development and implementation of advanced computer and data processing systems. Because our insurance subsidiary intends to expand its business by writing additional voluntary policies, we are developing new information technology systems to handle and process an increased volume of voluntary policies. The failure of these systems to function as planned could slow our growth and adversely affect our future business volume and results of operations.

Because we believe that our independent agents will play a key role in our efforts to increase the number of voluntary policies written by our insurance subsidiary, we are also in the process of developing business platforms and distribution initiatives that will allow us to provide information to, and exchange information with, our agents in an effective and efficient manner. These systems are intended to provide us with current information regarding the insurance markets in which we operate, therefore permitting us to adjust our selective underwriting criteria as needed to rapidly respond to market changes. In the event that the development of these systems does not proceed as planned, the expansion of our business could be delayed. Internet disruptions or system failures once these systems are fully operational could also adversely affect our future business volume and results of operations.

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

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

The property and casualty insurance industry in Florida is cyclical and, during times of increased capacity, highly competitive. We compete not only with other stock companies but also with mutual companies, other underwriting organizations and alternative risk sharing mechanisms. Our principal lines of business are written by numerous other insurance companies. Competition for any one account may come from very large, well-established national companies, smaller regional companies, other specialty insurers in our field, and other companies that write insurance only in Florida. Many of these competitors have greater financial resources, larger agency networks and greater name recognition than our company. We compete for business not only on the basis of price, but also on the basis of financial strength, types of coverage offered, availability of coverage desired by customers, commission structure, and quality of service. We may have difficulty continuing to compete successfully on any of these bases in the future. Competitive pressures coupled with market conditions may affect our rate of premium growth and financial results.

Our ability to compete in the property and casualty insurance industry and our ability to expand our business may be negatively affected by the fact that we are a new company. As a new company that has been in business for less than five years, we are not eligible to be rated by A.M. Best. While our insurance subsidiary has obtained a Demotech rating of A Exceptional, which is accepted by mortgage companies operating in the state of Florida, mortgage companies in other states may require homeowners to obtain property insurance from an insurance company with a certain minimum A.M. Best rating. As a result, the minimum A.M. Best rating requirement may also prevent us from expanding our business into other states in the near term, which may in turn limit our ability to compete with large, national insurance companies and certain regional insurance companies.

As a new company, our experience with claims and the risks related to certain claims is inherently limited. These inherent limitations may increase the likelihood that our projections and our estimates may be inaccurate, which in turn may increase the likelihood that our actual losses may exceed our loss reserves. If our actual losses exceed our loss reserves, our financial results, our ability to expand our business, and our ability to compete in the property and casualty insurance industry may be negatively affected. In addition, industry developments could further increase competition in our industry. These developments could include

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

programs in which state-sponsored entities provide property insurance in catastrophe-prone areas or other alternative markets types of coverage;

changes in Florida's regulatory climate; and

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

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

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

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

Our objective is to establish loss reserves that are adequate and represent management's best estimate; that is, the amounts originally recorded as reserves should at least equal the ultimate cost to investigate and settle claims. However, the process of establishing adequate reserves is complex and inherently uncertain, and the ultimate cost of a claim may vary materially from the amounts reserved. We regularly monitor and evaluate loss and loss adjustment expense reserve development to verify reserve adequacy.

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

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

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

The failure of our claims department to pay claims accurately could adversely affect our business, financial results and capital requirements.

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

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

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

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

Our future capital requirements depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover losses. To the extent that our present capital is insufficient to meet future operating requirements or to cover losses, we may need to raise additional funds through financings or curtail our growth. Based on our current operating plan, we believe current capital together with our anticipated retained earnings will support our operations. However, we cannot provide any assurance in that regard, since many factors will affect our capital needs and their amount and timing, including our growth and profitability, and the availability of reinsurance, as well as possible acquisition opportunities, market disruptions and other unforeseeable developments. If we require additional capital, it is possible that equity or debt financing may not be available at all or may be available only on terms that are not favorable to us. In the case of equity financings, dilution to our shareholders could result, and in any case such securities may have rights, preferences and privileges that are senior to those of existing shareholders. If we cannot obtain adequate capital on favorable terms or at all, our business, financial condition or results of operations could be materially adversely affected. On March 25, 2011, we completed our preferred stock offering. We intend to use the net proceeds from this offering primarily for general corporate purposes, which may include contribution of capital to our insurance subsidiary, investments, and the pursuit of growth opportunities.

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

A portion of our income is, and likely will continue to be, generated by the investment of our company's capital and surplus, premiums and loss reserves. The amount of income so generated is a function of our investment policy, available investment opportunities, and the amount of capital and surplus, premium and loss reserves invested. As we continue to grow and to deploy our capital, the proportion of income invested will decrease, and investment income will make up a smaller percentage of our net revenue. At December 31, 2010, approximately 70% of our available cash was invested in money market accounts or in bank deposits (i.e., CDs) that generally mature in no more than thirteen months and approximately 30% was invested in fixed maturity and equity securities. We may alter our investment policy to accept higher levels of risk with the expectation of higher returns. Fluctuating interest rates and other economic factors make it impossible to estimate accurately the amount of investment income that will be realized. In fact, we may realize losses on our investments.

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

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

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results of operations and financial condition. See the risk factor below entitled **Reinsurance coverage may not be available to us in the future at commercially reasonable rates or at all and we risk non-collectibility of reinsurance amounts due us from reinsurers with which we have contracted.**

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

Loss severity in the property and casualty insurance industry has continued to increase in recent years, principally driven by larger court judgments. In addition, many legal actions and proceedings have been brought on behalf of classes of complainants, which can increase the size of judgments. The propensity of policyholders and third party claimants to litigate and the willingness of courts to expand causes of loss and the size of awards may render our loss reserves inadequate for current and future losses.

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

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

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

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

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

engaging in vigorous underwriting;

carefully evaluating terms and conditions of our policies;

focusing on our risk aggregations by geographic zones, credit exposure and other bases; and

ceding insurance risk to reinsurance companies.

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

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

Our underwriting process is designed to limit our exposure to known risks, including but not limited to exclusions relating to homes in close proximity to the coast line. Various provisions of our policies, such as limitations or exclusions from coverage which have been negotiated to limit our risks, may not be enforceable in the manner we intend.

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

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

In the future, we may begin writing a significant number of insurance policies through independent agents unrelated to the Citizens take-out program. We refer to these policies as voluntary policies. Although voluntary policies comprise a minute percentage of our business, we expect to increase the number of voluntary policies we write as our business expands. An inability to sell our products through independent agents would negatively affect our revenues.

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

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

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

the availability of sufficient reliable data and our ability to properly analyze available data;

the uncertainties that inherently characterize estimates and assumptions;

our selection and application of appropriate rating and pricing techniques;

changes in legal standards, claim settlement practices, and restoration costs; and

legislatively imposed consumer initiatives.

Because we assumed substantially all of our current policies from Citizens, our rates are based, to a certain extent, on the rates charged by Citizens. In determining the rates we charge in connection with the policies we assumed from Citizens, our rates must be equal to or less than the rates charged by Citizens during the first full year following the assumption. If Citizens increases its rates, we may not automatically increase our rates. The risk that Citizens will reduce its rates is exacerbated by the fact that, absent certain circumstances, we must continue to provide coverage to the policyholders that we assume from Citizens for a period of three years. Also, inherent in the process of assuming policies from Citizens, there is a risk that a policy or policies that we have assumed from Citizens will opt out of joining us and will return to Citizens, requiring us to refund the unearned policy premium. If this were to occur for a significant number of policies, it could impact our financial results as we would have incurred costs in connection with the assumption of the policies for which we would no longer receive any premium. Consequently, we could under price risk in connection with the policies originating from Citizens, which would negatively affect our profit margins. With respect to the voluntary policies that we write, we could also overprice risks, which could reduce our sales volume and competitiveness. In either event, our profitability could be materially and adversely affected.

Current operating resources are necessary to develop future new insurance products.

We currently intend to expand our product offerings by underwriting additional insurance products and programs, and marketing them through our independent agent network. Expansion of our product offerings will result in increases in expenses due to additional costs incurred in actuarial rate justifications, software and personnel. Offering additional insurance products will also require regulatory approval, further increasing our costs and potentially affecting the speed with which we will be able to pursue new market opportunities. We cannot assure you that we will be successful bringing new insurance products to our marketplace.

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Recent investments in our new headquarters may result in additional and unforeseen costs.

We have taken, and may continue to take, actions that may increase our cost structure in the short-term but are intended to reduce certain portions of our long-term cost structure. For example, we recently purchased a building in Tampa, Florida, and have been remodeling the building to suit our specific needs and requirements. Following completion of the renovations, we will relocate our corporate headquarters to that building and will consolidate redundant office space.

If our long-term cost reduction efforts are ineffective or our estimates of cost savings are inaccurate, our profitability could be negatively impacted. Expected savings from relocating facilities can be highly variable and uncertain. We may experience business disruptions and loss of key personnel associated with the office moves and restructuring, which in turn may negatively affect our productivity and profitability. Further, the costs of implementing this restructuring may be greater than currently anticipated, and we may experience additional costs in connection with remodeling the building, ownership of our headquarters building, relocating offices and consolidation of redundant office space due to delays or other unforeseen circumstances.

As an insurance holding company, we are currently subject to regulation by the state of Florida and in the future may become subject to regulation by certain other states or a federal regulator.

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

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

We currently operate only in the state of Florida. In the future, we may become authorized to transact business in other states and therefore will become subject to the laws and regulatory requirements of those states. These regulations may vary from state to state, and states occasionally may have conflicting regulations. Since Florida is our state of domicile, Florida laws will generally take precedence. Currently, the federal government's role in regulating or dictating the policies of insurance companies is limited. However, Congress, from time to time, considers proposals that would increase the role of the federal government in insurance regulation, either in addition to or in lieu of state regulation. The impact of any future federal insurance regulation on our insurance operations is unclear and may adversely impact our business or competitive position.

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

The insurance industry is highly regulated and supervised. Our insurance subsidiary is subject to the supervision and regulation of the state in which it is domiciled (Florida) and the state(s) in which it does business (currently only Florida). Such supervision and regulation is primarily designed to protect our policyholders rather than our shareholders. These regulations are generally administered by a department of insurance in each state and relate to, among other things

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

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

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

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

business operations and claims practices;

approval of policy forms and premium rates;

standards of solvency, including risk-based capital measurements;

licensing of insurers and their products;

restrictions on the nature, quality and concentration of investments;

restrictions on the ability of our insurance subsidiary to pay dividends to us;

restrictions on transactions between insurance company subsidiaries and their affiliates;

restrictions on the size of risks insurable under a single policy;

requiring deposits for the benefit of policyholders;

requiring certain methods of accounting;

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periodic examinations of our operations and finances;

prescribing the form and content of records of financial condition required to be filed; and

requiring reserves as required by statutory accounting rules.

The Florida Office of Insurance Regulation (OIR) and regulators in other jurisdictions where our insurance subsidiary may become licensed conduct periodic examinations of the affairs of insurance companies and require the filing of annual and other reports relating to financial condition, holding company issues and

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other matters. These regulatory requirements may adversely affect or inhibit our ability to achieve some or all of our business objectives. These regulatory authorities also conduct periodic examinations into insurers' business practices. These reviews may reveal deficiencies in our insurance operations or differences between our interpretations of regulatory requirements and those of the regulators.

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

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

ITEM 1B *Unresolved Staff Comments*

None.

ITEM 2 *Properties*

The Company has a lease for office space located in Clearwater, Florida. This lease commenced in July 2008 and requires the Company to make monthly rent payments of \$12,500, which includes \$2,500 for common area maintenance, to an entity owned by one of the Company's directors. The initial term of this agreement is for five years ending on July 15, 2013 and the lease may be extended for up to three additional five-year periods. In addition to this primary location, the Company leases on a month-to-month basis a small office space in a building adjacent to the corporate office location. This lease requires the Company to pay base rent of approximately \$2,200 per month. The Company is required to provide a 30-day notice to terminate this lease. Rental expense under all facility leases was \$191,000 and \$181,000 during the years ended December 31, 2010 and 2009, respectively.

On June 1, 2010, the Company purchased property in Tampa, Florida for a total purchase price of \$7.1 million. The property consists of 3.5 acres of land, a building with gross area of 122,000 square feet, and a three-story parking garage valued at \$1.2 million, \$5.3 million, and \$0.6 million, respectively. This facility will be used by the Company and its subsidiaries, all of which will be headquartered in the new facility. The Company expects to complete the relocation of its employees and infrastructure during the second quarter of 2011 upon completion of various building improvements, which are expected to cost the Company between \$1.50 million and \$1.75 million. In addition, the Company expects to lease to non-affiliates up to forty-nine percent of the building's office space, which includes space occupied by existing tenants under lease agreements assumed by the Company at acquisition.

Table of Contents**ITEM 3 *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 4 *Reserved***PART II****ITEM 5 *Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*****Market for Common Stock**

Our common stock trades on the NASDAQ Global Select Market under the symbols HCII. Our common stock warrants trade on the NASDAQ Global Market under the symbol HCIIW. The following table represents the high and low sales prices for our common stock as reported by the NASDAQ Global Select Market and the high and low prices for our common stock warrants, as reported by the NASDAQ Global Market, for the periods indicated:

	Common Stock Price		Warrant Price	
	High	Low	High	Low
<u>Calendar Quarter 2010</u>				
First Quarter	\$ 8.26	6.34	2.49	0.52
Second Quarter	\$ 7.25	5.31	0.78	0.16
Third Quarter	\$ 6.93	5.15	0.70	0.23
Fourth Quarter	\$ 9.15	6.27	1.00	0.48
<u>Calendar Quarter 2009</u>				
First Quarter	\$ 6.00	4.12	0.62	0.15
Second Quarter	\$ 5.68	4.43	0.75	0.40
Third Quarter	\$ 8.45	5.06	3.00	0.40
Fourth Quarter	\$ 8.73	7.52	1.50	0.75

 Holders

As of March 21, 2011, the market price for our common stock was \$8.11 and there were 32 holders of record of our common stock. As of March 21, 2011, the market price for our common stock warrants was \$0.83 and there was 1 holder of record of our warrants.

Table of Contents**Dividends**

The declaration and payment of dividends will be at the discretion of our Board of Directors. Our ability to pay dividends depends on many factors, including the Company's operating results, financial condition, capital requirements, and legal and regulatory constraints and requirements on the payment of dividends, which are discussed in Note 14, Regulatory Requirements and Restrictions, to the audited, consolidated financial statements, and such other factors as our Board of Directors deems relevant. On November 2, 2010, the Company's Board of Directors declared a quarterly dividend of \$0.10 per common share and a special dividend of \$0.20 per common share. The dividends were paid December 20, 2010 to stockholders of record on November 20, 2010. On January 26, 2011, the Company's Board of Directors declared a quarterly dividend of \$0.10 per common share. The dividends were paid March 18, 2011 to stockholders of record on February 18, 2011.

Under Florida law, a domestic insurer such as our insurance subsidiary, Homeowners Choice Property & Casualty Insurance Company, Inc. (HCPC), may not pay any dividend or distribute cash or other property to its stockholder, Homeowners Choice, Inc. (HCI), 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. For a three-year period beginning March 30, 2007, HCPC, as a newly licensed Florida insurer, was precluded from paying dividends unless approved in advance by the Florida Office of Insurance Regulation. Additionally, Florida statutes preclude HCPC from making dividend payments or distributions to HCI 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.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table summarizes our equity compensation plan as of December 31, 2010. We currently have no equity compensation plans not approved by stockholders.

Plan Category	A Number of Securities To be Issued Upon Exercise of Outstanding Options	B Weighted Average Exercise Price of Outstanding Options	C Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column A)
Equity Compensation Plans Approved by Stockholders	830,000	\$ 2.50	4,850,000

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As a smaller reporting company as defined by Rule 229.10(f)(1) of the Exchange Act, we are not required to provide the information under this item and, because our stock was not publicly traded prior to July 30, 2008, we have elected not to provide the performance graph, which data typically encompasses a five-year period.

Recent Sales of Unregistered Securities

None.

Issuer Purchases of Equity Securities

Effective March 18, 2009, our Board of Directors authorized a plan to repurchase up to \$3.0 million (inclusive of commissions) of the Company's common shares. The repurchase plan allowed the Company to repurchase shares from time to time through March 19, 2010. This repurchase plan was supplemented in December 2009 upon approval by the Board of Directors to extend the repurchase authority by an additional \$3.0 million and continue until the repurchase plan is terminated by the Company or the maximum number of dollars has been expended. The shares may be purchased for cash in open market purchases, block transactions and privately negotiated transactions in accordance with applicable federal securities laws. The share repurchase plan may be modified, suspended, terminated or extended by the Company any time without prior notice. During the quarter ended December 31, 2010, the Company repurchased and retired a total of 95,270 shares at an average price of \$7.83 per share and a total cost, inclusive of fees and commissions, of \$751,342 or \$7.89 per share, under this authorized repurchase program. The following table provides information with respect to shares repurchased during the quarter ended December 31, 2010:

<u>Period</u>	(a) Total Number Of Shares Repurchased	(b) Average Price Paid Per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plan or Program	(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased
October 1-31, 2010	22,277	6.85	22,277	\$ 1,290,000
November 1-30, 2010	38,895	8.12	38,895	972,000
December 1-31, 2010	34,098	8.14	34,098	693,000
Total	95,270	\$ 7.83	95,270	

ITEM 6 *Selected Financial Data*

As a smaller reporting company as defined by Rule 229.10(f)(1) of the Exchange Act, we are not required to provide the information under this item and we have elected to exclude this information as our operating history does not cover the requisite five-year period.

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

The following discussion should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this annual report on Form 10-K. Unless the context requires otherwise, as used in this Form 10-K, the terms HCI, we, us, our, the Company, our company, and similar references refer to Homeowners Choice, Inc. and its subsidiaries.

Forward-Looking Statements

In addition to historical information, this annual report on Form 10-K contains forward-looking statements as defined under federal securities laws. Such statements 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. Among the important factors that could cause actual results to differ materially from those indicated by such forward-looking statements include but are not limited to the effect of governmental regulation; changes in insurance regulations; the frequency and extent of claims; uncertainties inherent in reserve estimates; catastrophic events; a change in the demand for, pricing of, availability or collectability of reinsurance; restrictions on our ability to change premium rates; increased rate pressure on premiums; changing rates of inflation; and other risks and uncertainties and other factors listed under Item 1A - Risk Factors and elsewhere in this annual report on Form 10-K and in our other Securities and Exchange Commission filings.

OVERVIEW

General

Homeowners Choice, Inc. is a property and casualty insurance holding company incorporated in Florida in 2006. Through our subsidiaries, we provide property and casualty homeowners insurance, condominium-owners insurance, and tenants insurance to individuals owning property in Florida. We offer these insurance products at competitive rates, while pursuing profitability using selective underwriting criteria. Our principal revenues are earned premiums, which are reported net of reinsurance costs, and investment income. We cede a substantial portion of our earned premiums to reinsurers to mitigate risks primarily associated with hurricanes and other catastrophic events. Our principal expenses are claims from policyholders, policy acquisition costs, and other underwriting expenses. As of December 31, 2010, we had total assets of \$140.9 million and stockholders equity of \$46.6 million. Our net income was approximately \$5.4 million for the year ended December 31, 2010. Our book value per share increased to \$7.51 as of December 31, 2010 compared to \$7.03 as of December 31, 2009.

We began operations in June of 2007 by participating in a take-out program through which we assumed insurance policies held by Citizens Property Insurance Corporation (Citizens), a Florida state-supported insurer. The take-out program is a legislatively mandated program designed to reduce the state's risk exposure by encouraging private companies to assume policies from Citizens. Policies were assumed in eight separate assumption transactions which took place in July and November 2007, February, June, October and December 2008, December 2009, and December 2010. Substantially all of our premium revenue since inception comes from these assumptions. We currently have approximately 65,000 policies in force. Of those policies assumed, approximately 86% are homeowners insurance policies, and the remaining 14% are a combination of policies written for condominium-owners and tenants. Our current policies in force represent approximately \$135 million in annualized premiums.

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Citizens requires us to offer renewals on the policies we acquire for a period of three years subsequent to the initial expiration of the assumed policies. The policyholders have the option to renew with us or they may ask their agent to place their coverage with another insurance company. With respect to the assumptions through December 31, 2009, policyholders could also elect to return to Citizens, i.e. opt out, prior to the policy renewal date. With respect to the December 31, 2010 assumption, the opt-out provision was limited to thirty days from the assumption date. We strive to retain these policies by offering competitive rates to our policyholders.

We face various challenges to implementing our operating and growth strategies. Since we write policies that cover Florida homeowners, condominium owners, and tenants, we cover losses that may arise from, among other things, catastrophes, which could have a significant effect on our business, results of operations, and financial condition. To mitigate our risk of such losses, we cede a portion of our exposure to other entities under catastrophe excess of loss reinsurance treaties. Even without catastrophic events, we may incur losses and loss adjustment expenses that deviate substantially from our estimates and that may exceed our reserves, in which case our net income and capital would decrease. Our operating and growth strategies may also be impacted by regulation and supervision of our business by the State of Florida, which must approve our policy forms and premium rates as well as monitor our insurance subsidiary's ability to meet all requirements for regulatory compliance. Additionally, we compete with large, well-established insurance companies as well as other specialty insurers that, in most cases, possess greater financial resources, larger agency networks, and greater name recognition.

Recent Developments

Effective December 7, 2010, Homeowners Choice Property & Casualty Insurance Company, Inc. assumed an additional 8,031 homeowners policies from Citizens.

On January 26, 2011, the Company's Board of Directors declared a quarterly dividend of \$0.10 per common share. The dividends were paid March 18, 2011 to stockholders of record on February 18, 2011.

On February 1, 2011, we filed Amendment No. 2 on Form S-3 with the Securities and Exchange Commission under which we offered for sale a minimum of 1,200,000 shares up to a maximum of 1,500,000 shares of our 7% Series A Cumulative Redeemable Preferred Stock (Series A Preferred). On March 25, 2011, the offering was completed with a total of 1,247,700 shares of Series A Preferred being issued by the Company for gross proceeds of approximately \$12.5 million before deducting offering expenses, which are expected to total approximately \$1.2 million including placement agent fees and expenses. The Company intends to use the net proceeds from this offering of approximately \$11.3 million for general corporate purposes. Dividends on the Series A Preferred will be cumulative from the date of original issue and will accrue on the last day of each month at an annual rate of 7% of the \$10.00 liquidation preference per share. Each share of the Series A Preferred will be convertible, at the holder's option at any time, initially into one share of our common stock based upon an initial conversion price of \$10.00 per share. The Company may terminate this conversion right on or after March 31, 2014, if, for at least twenty trading days within any period of thirty consecutive trading days, the market price of our common stock exceeds the conversion price of the Series A Preferred by more than 20% and our common stock is then traded on the New York Stock Exchange, the NASDAQ Global Select Market, the NASDAQ Global Market, the NASDAQ Capital Market, or the NYSE Amex. Shares of the Series A Preferred will have no voting rights except under limited circumstances.

On February 22, 2011, we announced our intention to enter the Alabama homeowners insurance market. We expect to satisfy Alabama regulatory requirements and begin operations in Alabama by the end of 2011.

Table of Contents**RESULTS OF OPERATIONS**

The following table summarizes our results of operations for the years ended December 31, 2010 and 2009 (dollars in thousands, except per share amounts):

	Year Ended December 31,	
	2010	2009
Operating Revenue		
Gross premiums earned	\$ 119,757	110,011
Premiums ceded	(57,322)	(44,674)
Net premiums earned	62,435	65,337
Net investment income	1,962	1,793
Realized investment gains	2,003	
Other Income	2,215	1,248
Total operating revenue	68,615	68,378
Operating Expenses		
Losses and loss adjustment expenses	37,667	35,230
Policy acquisition and other underwriting expenses	14,878	9,611
Other operating expenses	7,484	5,788
Total operating expenses	60,029	50,629
Income before income taxes	8,586	17,749
Income taxes	3,164	6,839
Net income	\$ 5,422	10,910
Ratios to Net Premiums Earned:		
Loss Ratio	60.33%	53.92%
Expense Ratio	35.82%	23.57%
Combined Ratio	96.15%	77.49%
Ratios to Gross Premiums Earned:		
Loss Ratio	31.45%	32.02%
Expense Ratio	18.67%	14.00%
Combined Ratio	50.12%	46.02%
Per Share Data:		
Basic earnings per share	\$ 0.88	\$ 1.62
Diluted earnings per share	\$ 0.81	\$ 1.52

Comparison of the Year Ended December 31, 2010 to the Year Ended December 31, 2009

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Our results of operations for the year ended December 31, 2010 reflect net income of \$5.4 million, or \$0.81 earnings per diluted share, compared to net income of \$10.9 million, or \$1.52 per diluted share, for the year ended December 31, 2009.

Table of Contents**Revenue**

Gross Premiums Earned for the year ended December 31, 2010 were \$119.8 million and reflect the revenue from policies assumed from Citizens in connection with the eight separate assumption transactions through December 2010 and the revenue on the renewal of these policies. Gross premiums earned for the year ended December 31, 2009 were \$110.0 million and reflect the revenue from policies assumed from Citizens in connection with the seven separate assumption transactions through December 2009 and the revenue on the renewal of these policies.

Premiums Ceded for the years ended December 31, 2010 and 2009 were \$57.3 million and \$44.7 million, respectively. Our premiums ceded represent amounts paid to reinsurers to cover losses from catastrophes that exceed the thresholds defined by our catastrophe excess of loss reinsurance treaties. Our reinsurance rates are based primarily on policy exposures reflected in gross premiums earned. Thus, the \$12.6 million increase in premiums ceded during 2010 is primarily due to the increase in our policy exposure base. Premiums ceded were 47.9% and 40.6% of gross premiums earned during the years ended December 31, 2010 and 2009, respectively.

Net Premiums Earned for the years ended December 31, 2010 and 2009 were \$62.4 million and \$65.3 million, respectively, and reflect the gross premiums earned less reinsurance costs as described above. Net premiums earned decreased by \$2.9 million in 2010 as compared to 2009 as a result of the \$9.7 million increase in gross premiums earned offset by the increase of \$12.6 million in premiums ceded.

Net Premiums Written during the years ended December 31, 2010 and 2009 totaled \$59.0 million and \$66.6 million, respectively. Net premiums written represent the premiums charged on policies issued during a fiscal period less reinsurance costs.

The following is a reconciliation of our total Net Premiums Written to Net Premiums Earned for the years ended December 31, 2010 and 2009 (in thousands):

	Year Ended December 31,	
	2010	2009
Net Premiums Written	\$ 58,960	66,627
Decrease (increase) in Unearned Premiums	3,475	(1,290)
Net Premiums Earned	\$ 62,435	65,337

Net Investment Income for the years ended December 31, 2010 and 2009 was \$2.0 million and \$1.8 million, respectively. There were no other than temporary impairments recorded during the years ended December 31, 2010 and 2009. The \$0.2 million increase in total investment income is primarily due to interest income received from our available-for-sale investments, which were added to our investment portfolio beginning in the second quarter of 2009.

Realized Investment Gains for the year ended December 31, 2010 of \$2.0 million reflects the net gain realized from sales of securities during the year. We had no significant investment gains in the year ended December 31, 2009.

Other Income for the years ended December 31, 2010 and 2009 of \$2.2 million and \$1.2 million, respectively, primarily reflects the policy fee income we earn with respect to our issuance of renewal policies.

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Expenses

Our *Losses and Loss Adjustment Expenses* amounted to \$37.7 million and \$35.2 million, respectively, during the years ended December 31, 2010 and 2009.

Our losses and loss adjustment expense reserves (*Reserves*), which are more fully described below under *Critical Accounting Policies and Estimates*, are specific to homeowners insurance, which is our only line of business. These 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. Our Reserves increased from \$19.2 million at December 31, 2009 to \$22.1 million at December 31, 2010. The \$2.9 million increase in our Reserves during 2010 is comprised of \$14.2 million in new reserves specific to the year ended December 31, 2010 offset by reductions of \$9.9 million and \$1.4 million in our Reserves for 2009 and 2008, respectively. The \$14.2 million in Reserves established for 2010 claims is due to the increase in our policy exposure, which resulted in an increase in the amount of reported losses in 2010. The decrease of \$11.3 million specific to our 2009 and 2008 accident-year reserves is due to favorable development arising from lower than expected loss development during 2010 relative to expectations used to establish our Reserve estimates at the end of 2009. Factors that are attributable to this favorable development may include a lower severity of claims than the severity of claims considered in establishing our Reserves and actual case development may be more favorable than originally anticipated.

Policy Acquisition and Other Underwriting Expenses for the years ended December 31, 2010 and 2009 of \$14.9 million and \$9.6 million, respectively, primarily reflect the amortization of deferred acquisition costs, commissions payable to agents for production and renewal of policies, and premium taxes and policy fees. The \$5.3 million increase in 2010 is primarily attributable to an increase in our commissions, premium taxes, and other underwriting expenses directly attributable to policy renewals and an increase in our payroll and other underwriting expenses required to manage our policies in force.

Other Operating Expenses for the years ended December 31, 2010 and 2009 were \$7.5 million and \$5.8 million, respectively. Such expenses include administrative compensation and related benefits, corporate insurance, professional fees, office lease and related expenses, information system expense, and other general and administrative costs. The \$1.7 million increase is primarily attributable to an increase for administrative compensation and related benefits. As of December 31, 2010, we had 76 employees compared to 58 employees as of December 31, 2009.

Income Taxes for the years ended December 31, 2010 and 2009 were \$3.2 million and \$6.8 million, respectively, for state and federal income taxes resulting in an effective tax rate of 36.9% for 2010 and 38.5% for 2009.

Ratios:

The loss ratio applicable to the year ended December 31, 2010 (loss and loss adjustment expenses related to net premiums earned) was 60.3% compared to 53.9% for the year ended December 31, 2009. Our loss ratio was negatively impacted by a significant increase in our reinsurance costs during 2010, which reduced our net premiums earned.

The expense ratio applicable to the year ended December 31, 2010 (policy acquisition and other underwriting expenses related to net premiums earned plus compensation, employee benefits, and other operating

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expenses) was 35.8% compared to 23.6% for the year ended December 31, 2009. We have experienced an increase in our expense ratio due to increases in our premium taxes, payroll, and other underwriting expenses required to manage our policies in force as we have renewed more policies in 2010 than in 2009 (see *Policy Acquisition and Other Underwriting Expenses* above). In addition, our expense ratio was negatively impacted by a significant increase in our reinsurance costs during 2010, which reduced our net premiums earned.

The combined loss and expense ratio (total of all expenses related to net premiums earned) is the key measure of underwriting performance traditionally used in the property and casualty industry. A combined ratio under 100% generally reflects profitable underwriting results. A combined ratio over 100% generally reflects unprofitable underwriting results. Our combined ratio for the year ended December 31, 2010 was 96.2% compared to 77.5% for the year ended December 31, 2009.

Due to the impact our reinsurance costs have on net premiums earned from period to period, our management believes the combined loss and expense ratio measured to gross premiums earned is more relevant in assessing overall performance. The combined loss and expense ratio to gross premiums earned for the year ended December 31, 2010 was 50.1% compared to 46% for the year ended December 31, 2009.

Seasonality of Our Business

We expect to experience increases in our losses and loss adjustment expenses during the period from June 1 through November 30 each year as this is typically the period during which hurricanes and other tropical storms may occur. As a result of such seasonal variations in our reported losses, we anticipate our operating profits during the period from June 1 through November 30 each year may be negatively impacted by an increase in losses and loss adjustment expenses.

LIQUIDITY AND CAPITAL RESOURCES

Since inception, our liquidity requirements have been met through issuance of our common stock and funds from operations. We expect our future liquidity requirements will be met by funds from operations, primarily the cash received by our insurance subsidiary from premiums written and investment income. In addition, we raised approximately \$11.3 million in net proceeds from our preferred stock offering, which was completed on March 25, 2011. We intend to use the net proceeds from this offering primarily for general corporate purposes, which may include contribution of capital to our insurance subsidiary, investments, and the pursuit of growth 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 loss and loss adjustment expenses are paid out over a period of years. This period of time varies by the circumstances surrounding each claim. A substantial portion of our losses and loss expenses are fully settled and paid within 90 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 our insurance subsidiary's claims and expenses, as well as 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.

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In the future, we anticipate our primary use of funds will be to pay claims and operating expenses. In addition, we expect to spend between \$1.5 million to \$1.75 million on enhancements to our new building.

Inflation and Changing Prices

During our limited operating history, we have not experienced any material impact on revenues or our results of operations due to inflation or changing prices. However, our premiums are established before we know the amount of our losses and the related settlement expenses and before we know the extent to which inflation may impact our expenses. Consequently, we attempt to anticipate the future impact of inflation when establishing our rates, yet our ability to establish and increase rates is subject to regulatory approval and may be further constrained by competitive pressures. In the event we experience prolonged periods of inflation leading to material increases in our expenses without a corresponding increase in our premium rates, such an event could have a material adverse effect on our future results of operations.

Cash Flows

Our cash flows from operating, investing and financing activities for the years ended December 31, 2010 and 2009 are summarized below.

Cash Flows for the Year ended December 31, 2010

Net cash provided by operating activities for the year ended December 31, 2010 was approximately \$16.1 million, which resulted primarily from the \$19.5 million of premiums collected from Citizens offset by \$10.6 million from reinsurance premiums prepaid in 2010 and \$7.2 million cash received from net written premiums less cash disbursed for operating expenses and losses and loss adjustment expenses. Net cash used in investing activities was approximately \$0.2 million of which \$7.3 million was contributed from investment sales net of investment purchases offset by \$7.5 million used to purchase property and equipment. Net cash used in financing activities totaled \$4.5 million, which was primarily due to \$3.6 million used to repurchase our shares and \$1.9 million used to pay dividends offset by approximately \$1.0 million from proceeds and tax benefits related to stock option exercises.

Cash Flows for the Year ended December 31, 2009

Net cash used in operating activities for the year ended December 31, 2009 was approximately \$13.5 million, which resulted primarily from an increase of \$19.5 million in uncollected premiums due from Citizens at December 31, 2009 from the December 2009 assumption transaction partially offset by cash received from net written premiums less cash disbursed for operating expenses and losses and loss adjustment expenses. Net cash used in investing activities of \$21.0 million was primarily due to the \$21.2 million net amount used to purchase various fixed maturity securities and short-term investments. Additionally, we used \$314,000 to purchase property and equipment. These amounts were offset by our receipt of \$450,000 upon repayment of a note receivable. Net cash used in financing activities totaled \$3.1 million, which was primarily due to \$3.2 million used to repurchase our shares and warrants offset by \$49,000 from the exercise of common stock options.

Investments

The main objective of our investment policy is to maximize our after-tax investment income with a minimum of risk given the current financial market. Our excess cash is invested primarily in money market accounts, certificates of deposit (i.e., CDs maturing in less than thirteen months), time deposits (i.e. CDs maturing in more than twelve months), and fixed maturity and equity security available-for-sale investments.

At December 31, 2010, we have \$29.4 million 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

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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 \$5.5 million in any one bank at any time. From time to time, we may have in excess of \$5.5 million of cash designated for investment and on deposit at a single national brokerage firm. In the future, we may alter our investment policy to include or increase investments in federal, state and municipal obligations, preferred and common equity securities and real estate mortgages, as permitted by applicable law, including insurance regulations.

OFF-BALANCE SHEET ARRANGEMENTS

As of December 31, 2010, we had no off-balance sheet arrangements as defined in Item 303(a)(4) of Regulation S-K.

CONTRACTUAL OBLIGATIONS

As a smaller reporting company as defined by Rule 229.10(f)(1) of the Exchange Act, we are not required to provide the information under this item.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

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

We believe our accounting policies specific to premium revenue recognition, losses and loss adjustment expenses, reinsurance, deferred policy acquisition costs, deferred tax assets and liabilities, and stock-based compensation expense involve our most significant judgments and estimates material to our consolidated financial statements.

Premium Revenue. Premium revenue is earned on a daily pro-rata basis over the term of the policies. Unearned premiums represent the portion of the premium related to the unexpired policy term.

Reserves for Losses and Loss Adjustment Expenses. We establish reserves for the estimated total unpaid costs of losses including loss adjustment expenses (LAE). Unless otherwise specified below, the term "loss reserves" shall encompass reserves for both losses and LAE. Loss reserves reflect management's best estimate of the total cost of (i) claims that have been incurred, but not yet paid, and (ii) claims that have been incurred but not yet reported ("IBNR"). Loss reserves established by us are not an exact calculation of our liability. Rather, loss reserves represent management's best estimate of our company's liability based on application of actuarial techniques and other projection methodology and taking into consideration other facts and circumstances known at the balance sheet date. The process of establishing loss reserves is complex and necessarily imprecise, as it

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involves using judgment that is affected by many variables such as past loss experience, current claim trends and the prevailing social, economic and legal environments. The impact of both internal and external variables on ultimate loss and LAE costs is difficult to estimate. Our exposure is impacted by both the risk characteristics of the physical locations where we write policies, such as hurricane and tropical storm-related risks, as well as risks associated with varying social, judicial and legislative characteristics in Florida, the state in which we operate. In determining loss reserves, we give careful consideration to all available data and actuarial analyses, and this process involves significant judgment.

The liability for losses and LAE represents estimates of the ultimate unpaid cost of all losses incurred, including losses for claims that have not yet been reported to our insurance company. The amount of loss reserves for reported claims is based primarily upon a case-by-case evaluation of the kind of risk involved, knowledge of the circumstances surrounding each claim and the insurance policy provisions relating to the type of loss. The amounts of loss reserves for unreported claims and LAE are determined using historical homeowners insurance information as adjusted to current conditions. Inflation is ordinarily implicitly provided for in the reserving function through analysis of costs, trends and reviews of historical reserving results over multiple years.

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

When a claim is reported to us, our claims personnel establish a case reserve for the estimated amount of the ultimate payment. This estimate reflects an informed judgment based upon general insurance reserving practices and on the experience and knowledge of the estimator. The individual estimating the reserve considers the nature and value of the specific claim, the severity of injury or damage, location, and the policy provisions relating to the type of loss. Case reserves are adjusted by us as more information becomes available. It is our policy to settle each claim as expeditiously as possible.

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

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

Reported loss development;

Paid loss development;

Loss ratio method; and

Average outstanding and open claims.

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The results of the reserve calculations using these methods were similar, and therefore, we relied on an average of the four methods.

Description of Ultimate Loss Estimation Methods. The reported loss development method relies on the assumption that, at any given state of maturity, ultimate losses can be predicted by multiplying cumulative reported losses (paid losses plus case reserves) by a cumulative development factor. The validity of the results of this method depends on the stability of claim reporting and settlement rates, as well as the consistency of case reserve levels. Case reserves do not have to be adequately stated for this method to be effective; they only need to have a fairly consistent level of adequacy at all stages of maturity. Because of our limited loss experience, we select loss development factors based on industry data found in current A.M. Best's Aggregates and Averages Property/Casualty United States & Canada. We assume that our loss development patterns will be reasonably consistent with industry averages, and use the selected factors to project the ultimate losses.

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

The validity of the results from using a loss development approach can be affected by many conditions, such as internal claim department processing changes, a shift between single and multiple claim payments, legal changes, or variations in our mix of business from year to year. Also, since the percentage of losses paid for immature years is often low, development factors are volatile. A small variation in the number of claims paid can have a leveraging effect that can lead to significant changes in estimated ultimate losses. Therefore, ultimate values for immature accident years are often based on alternative estimation techniques.

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

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

Finally, we employ the average outstanding and open claims method. We segregate our claims according to when we assumed them from Citizens and conduct a detailed review in order to estimate average future development of open claims and average projected loss on IBNR claims. We combine this estimate with our open claims in order to derive an estimate of expected unreported losses. Paid losses are added to this estimate in order to derive an estimate of ultimate losses. This method is based on the assumption that future IBNR claims and the average severity of open claims and IBNR claims can be reasonably estimated from the experience available.

While the property and casualty industry has incurred substantial aggregate losses from claims related to asbestos-related illnesses, environmental remediation, product and mold, and other uncertain or environmental exposures, we have not experienced significant losses from these types of claims.

Currently, our estimated ultimate liability is calculated monthly using these principles and procedures applicable to the lines of business written. However, because the establishment of loss reserves is an inherently

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uncertain process, we cannot be certain that ultimate losses will not exceed the established loss reserves and have a material adverse effect on our results of operations and financial condition. Changes in estimates, or differences between estimates and amounts ultimately paid, are reflected in the operating results of the period during which such adjustments are made.

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

Year Ended December 31, 2010		
Change in Reserves	Reserves	Percentage change in equity, net of tax
-10.0%	19,931	3.00%
-7.5%	20,485	2.25%
-5.0%	21,039	1.50%
-2.5%	21,592	0.75%
Base	22,146	
2.5%	22,700	-0.75%
5.0%	23,253	-1.50%
7.5%	23,807	-2.25%
10.0%	24,361	-3.00%

Reinsurance. In the normal course of business, we seek to reduce the loss that may arise from catastrophes or other events that cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Amounts recoverable from reinsurers are estimated in a manner consistent with the reinsured policy. Reinsurance premiums and reserves related to reinsured business are accounted for on a basis consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Premiums ceded to other companies have been reported as a reduction of premium income.

Deferred policy acquisition costs. Deferred policy acquisition costs (DAC) primarily represent commissions paid to Citizens or outside agents at the time of collection of the policy premium, salaries and premium taxes and are amortized over the life of the related policy in relation to the amount of gross premiums earned. The method followed in computing DAC limits the amount of such deferred costs to their estimated realizable value, which gives effect to the gross premium earned, related investment income, unpaid losses and LAE and certain other costs expected to be incurred as the premium is earned.

DAC is reviewed to determine if it is recoverable from future income, including investment income. If such costs are determined to be unrecoverable, they are expensed at the time of determination. The amount of

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DAC considered recoverable could be reduced in the near term if the estimates of total revenues discussed above are reduced or permanently impaired as a result of the disposition of a line of business. The amount of amortization of DAC could be revised in the near term if any of the estimates discussed above are revised.

Income Taxes. We account for income taxes in accordance with Accounting Standards Codification (ASC) Topic 740 Income Taxes (ASC 740). ASC 740 results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. We determine deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur. Valuation allowances are provided against assets that are not likely to be realized. We have elected to classify interest and penalties as income tax expense as permitted by current accounting standards.

Stock-Based Compensation. We account for our stock option plan under the fair value recognition provisions of ASC Topic 718 Compensation Stock Compensation, (ASC 718) which requires the measurement and recognition of compensation for all stock-based awards made to employees and directors including stock options and restricted stock issuances based on estimated fair values. Under the fair value recognition provisions of ASC 718, we recognize stock-based compensation in the consolidated statements of earnings on a straight-line basis over the vesting period. We use the Black-Scholes option pricing model, which requires the following variables for input to calculate the fair value of each stock award on the option grant date: 1) expected volatility of our stock price, 2) the risk-free interest rate, 3) expected term of each award, 4) expected dividends, and 5) an expected forfeiture rate.

ITEM 7A Quantitative and Qualitative Disclosures About Market Risk

As a smaller reporting company as defined by Rule 229.10(f)(1) of the Exchange Act, we are not required to provide the information under this item.

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ITEM 8 *Financial Statements and Supplementary Data*

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Report of Independent Registered Public Accounting Firm

Homeowners Choice, Inc.

Clearwater, Florida:

We have audited the accompanying consolidated balance sheets of Homeowners Choice, Inc. and Subsidiaries (the Company) as of December 31, 2010 and 2009, and the related consolidated statements of earnings, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company at December 31, 2010 and 2009, and the results of its operations and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

/s/ Hacker, Johnson & Smith PA

HACKER, JOHNSON & SMITH PA

Tampa, Florida

March 25, 2011

Table of Contents**HOMEOWNERS CHOICE, INC. AND SUBSIDIARIES****Consolidated Balance Sheets**

(Dollars in thousands, except share amounts)

	At December 31, 2010	At December 31, 2009
Assets		
Investments:		
Fixed maturity securities, held-to-maturity, at amortized cost (fair value \$4,250)	\$	4,049
Fixed maturity securities, available-for-sale, at fair value (amortized cost \$28,456 and \$19,763)	28,564	19,266
Equity securities, available-for-sale, at fair value	884	
Time deposits	14,033	13,507
Short-term investments		11,521
Total investments	43,481	48,343
Cash and cash equivalents	54,849	43,453
Accrued interest and dividends receivable	180	176
Premiums receivable	5,822	4,899
Assumed reinsurance balances receivable	26	19,525
Prepaid reinsurance premiums	17,787	7,205
Deferred policy acquisition costs	9,407	10,496
Property and equipment, net	7,755	399
Deferred income taxes	584	2,438
Other assets	1,057	958
Total assets	\$ 140,948	137,892
Liabilities and Stockholders Equity		
Losses and loss adjustment expenses	22,146	19,178
Unearned premiums	65,034	68,509
Advance premiums	1,114	713
Accrued expenses	2,385	2,906
Income taxes payable	310	167
Other liabilities	3,330	1,041
Total liabilities	94,319	92,514
Commitments and contingencies (Notes 1, 5, 8, 13 and 14)		
Stockholders equity:		
Preferred stock (no par value 20,000,000 shares authorized, no shares issued or outstanding)		
Common stock, (no par value, 40,000,000 shares authorized, 6,205,396 and 6,456,635 shares issued and outstanding in 2010 and 2009)		
Additional paid-in capital	18,606	21,164
Retained earnings	28,065	24,520
Accumulated other comprehensive loss	(42)	(306)
Total stockholders equity	46,629	45,378
Total liabilities and stockholders equity	\$ 140,948	137,892

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See accompanying Notes to Consolidated Financial Statements.

Table of Contents**HOMEOWNERS CHOICE, INC. AND SUBSIDIARIES****Consolidated Statements of Earnings**

(Dollars in thousands, except per share amounts)

	Year Ended December 31,	
	2010	2009
Revenue		
Gross premiums earned	\$ 119,757	110,011
Premiums ceded	(57,322)	(44,674)
Net premiums earned	62,435	65,337
Net investment income	1,962	1,793
Realized investment gains	2,003	
Other	2,215	1,248
Total revenue	68,615	68,378
Expenses		
Losses and loss adjustment expenses	37,667	35,230
Policy acquisition and other underwriting expenses	14,878	9,611
Other operating expenses	7,484	5,788
Total expenses	60,029	50,629
Income before income taxes	8,586	17,749
Income taxes	3,164	6,839
Net income	\$ 5,422	10,910
Basic earnings per share	\$ 0.88	1.62
Diluted earnings per share	\$ 0.81	1.52
Dividends per share	\$ 0.30	

See accompanying Notes to Consolidated Financial Statements.

Table of Contents**HOMEOWNERS CHOICE, INC. AND SUBSIDIARIES****Consolidated Statements of Stockholders' Equity****For the Years Ended December 31, 2010 and 2009****(Dollars in thousands, except share amounts)**

	Common stock		Additional	Retained	Accumulated	Total
	Shares	Amount	Paid-In	Earnings	Other	
			Capital		Comprehensive	
					Loss	
Balance at December 31, 2008	6,892,668	\$	23,783	13,610		37,393
Net income				10,910		10,910
Change in unrealized loss on available-for-sale securities, net of income tax benefit					(306)	(306)
Comprehensive income						10,604
Excess tax benefit from stock options exercised			9			9
Repurchases and retirement of common stock	(452,033)		(3,111)			(3,111)
Repurchases of common stock warrants			(40)			(40)
Exercise of stock options	16,000		40			40
Stock-based compensation			483			483
Balance at December 31, 2009	6,456,635	\$	21,164	24,520	(306)	45,378
Net income				5,422		5,422
Change in unrealized loss on available-for-sale securities, net of income taxes					264	264
Comprehensive income						5,686
Excess tax benefit from stock options exercised			301			301
Repurchases and retirement of common stock	(511,239)		(3,596)			(3,596)
Exercise of stock options	260,000		650			650
Cash dividends paid				(1,877)		(1,877)
Stock-based compensation			87			87
Balance at December 31, 2010	6,205,396	\$	18,606	28,065	(42)	46,629

See accompanying Notes to Consolidated Financial Statements.

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HOMEOWNERS CHOICE, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(Dollars in thousands)

	Year Ended December 31,	
	2010	2009
Cash flows from operating activities:		
Net income	\$ 5,422	10,910
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Stock-based compensation	87	483
Amortization of discounts on investments in fixed maturity securities	(28)	(91)
Loss on disposal of property and equipment		