Primerica, Inc.
Form 10-Q
May 07, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2015

OR

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

For the transition period from to

Commission File Number: 001-34680

Primerica, Inc.

(Exact name of registrant as specified in its charter)

Delaware	27-1204330
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1 Primerica Parkway	30099

Duluth, Georgia
(Address of principal executive offices) (ZIP Code)

(770) 381-1000

(Registrant's telephone number, including area code)

Not applicable.

(Former name, former address and former fiscal year, if changed since last report)

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. x 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). x Yes ¨ No

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

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	As of April 30, 2015
Common Stock, $0.01 Par Value	51,352,164 shares

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

PRIMERICA, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

	(Unaudited) March 31, 2015	December 31, 2014
	(In thousands)	
Assets		
Investments:		
Fixed-maturity securities available-for-sale, at fair value (amortized cost: $1,696,412 in 2015 and $1,667,500 in 2014)	$1,789,937	$1,759,120
Fixed-maturity securities held-to-maturity, at amortized cost (fair value: $259,761 in 2015 and $228,809 in 2014)	238,000	220,000
Equity securities available-for-sale, at fair value (cost: $42,347 in 2015 and $43,738 in 2014)	51,807	53,390
Trading securities, at fair value (cost: $7,344 in 2015 and $7,710 in 2014)	7,345	7,711
Policy loans	27,679	28,095
Total investments	2,114,768	2,068,316
Cash and cash equivalents	180,207	192,516
Accrued investment income	18,442	17,401
Due from reinsurers	4,094,456	4,115,533
Deferred policy acquisition costs, net	1,377,022	1,351,180
Premiums and other receivables	180,642	181,660
Intangible assets, net (accumulated amortization: $69,277 in 2015 and $68,426 in 2014)	60,870	61,720
Deferred income taxes	32,335	36,082
Other assets	279,207	273,403
Separate account assets	2,386,265	2,440,303
Total assets	$10,724,214	$10,738,114
Liabilities and Stockholders' Equity		
Liabilities:		
Future policy benefits	$5,289,016	$5,264,608
Unearned premiums	821	912
Policy claims and other benefits payable	259,148	264,832
Other policyholders' funds	342,322	344,313
Notes payable	374,545	374,532
Surplus note	238,000	220,000
Income taxes	157,685	140,467
Other liabilities	381,369	392,810
Payable under securities lending	55,622	50,211

Separate account liabilities	2,386,265	2,440,303
Commitments and contingent liabilities (see Commitments and Contingent Liabilities note)		
Total liabilities	9,484,793	9,492,988
Stockholders' equity:		
Common stock ($0.01 par value; authorized 500,000 in 2015 and 2014; issued and outstanding 51,555 shares in 2015 and 52,169 shares in 2014)	516	522
Paid-in capital	323,996	353,337
Retained earnings	830,624	795,740
Accumulated other comprehensive income (loss), net of income tax:		
Unrealized foreign currency translation gains (losses)	1,345	21,681
Net unrealized investment gains (losses):		
Net unrealized investment gains not other-than-temporarily impaired	83,402	74,308
Net unrealized investment losses other-than-temporarily impaired	(462)	(462)
Total stockholders' equity	1,239,421	1,245,126
Total liabilities and stockholders' equity	$10,724,214	$10,738,114

See accompanying notes to condensed consolidated financial statements.

PRIMERICA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Income – Unaudited

	Three months ended March 31,	
	2015	2014
	(In thousands, except per-share amounts)	
Revenues:		
Direct premiums	$577,458	$568,205
Ceded premiums	(397,540)	(402,715)
Net premiums	179,918	165,490
Commissions and fees	132,835	126,933
Net investment income	21,173	21,599
Realized investment gains (losses), including other-than-temporary impairment losses	1,284	263
Other, net	9,929	10,043
Total revenues	345,139	324,328
Benefits and expenses:		
Benefits and claims	82,500	75,191
Amortization of deferred policy acquisition costs	36,213	35,193
Sales commissions	68,457	65,121
Insurance expenses	34,641	28,502
Insurance commissions	3,190	4,083
Interest expense	8,676	8,606
Other operating expenses	44,653	40,800
Total benefits and expenses	278,330	257,496
Income from continuing operations before income taxes	66,809	66,832
Income taxes	23,408	23,347
Income from continuing operations	43,401	43,485
Income from discontinued operations, net of income taxes	-	1,595
Net income	$43,401	$45,080
Basic earnings per share:		
Continuing operations	$0.82	$0.78
Discontinued operations	-	0.03
Basic earnings per share	$0.82	$0.81
Diluted earnings per share:		
Continuing operations	$0.82	$0.78
Discontinued operations	-	0.03
Diluted earnings per share	$0.82	$0.81
Weighted-average shares used in computing earnings per share:		
Basic	52,643	55,211
Diluted	52,691	55,233

Supplemental disclosures:		
Total impairment losses	$(237)	$(149)
Impairment losses recognized in other comprehensive income before income taxes	-	-
Net impairment losses recognized in earnings	(237)	(149)
Other net realized investment gains (losses)	1,521	412
Realized investment gains (losses), including other-than-temporary impairment losses	$1,284	$263
Dividends declared per share	$0.16	$0.12

See accompanying notes to condensed consolidated financial statements.

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PRIMERICA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income (Loss) – Unaudited

	Three months ended March 31,	
	2015	2014
	(In thousands)	
Net income	$43,401	$45,080
Other comprehensive income (loss) before income taxes:		
Unrealized investment gains (losses):		
Change in unrealized holding gains/(losses) on investment securities	15,661	17,930
Reclassification adjustment for realized investment (gains) losses included in net income	(1,670)	(188)
Foreign currency translation adjustments:		
Change in unrealized foreign currency translation gains (losses)	(20,566)	(8,677)
Total other comprehensive income (loss) before income taxes	(6,575)	9,065
Income tax expense (benefit) related to items of other comprehensive income (loss)	4,667	6,104
Other comprehensive income (loss), net of income taxes	(11,242)	2,961
Total comprehensive income (loss)	$32,159	$48,041

See accompanying notes to condensed consolidated financial statements.

PRIMERICA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Stockholders' Equity – Unaudited

	Three months ended March 31, 2015	Three months ended March 31, 2014
	(In thousands)	
Common stock:		
Balance, beginning of period	$522	$548
Repurchases of common stock	(9)	(4)
Net issuance of common stock	3	2
Balance, end of period	516	546
Paid-in capital:		
Balance, beginning of period	353,337	472,633
Share-based compensation	15,307	9,699
Net issuance of common stock	(3)	(2)
Repurchases of common stock	(44,781)	(19,183)
Adjustments to paid-in capital, other	136	(309)
Balance, end of period	323,996	462,838
Retained earnings:		
Balance, beginning of period	795,740	640,840
Net income	43,401	45,080
Dividends	(8,517)	(6,738)
Balance, end of period	830,624	679,182
Accumulated other comprehensive income (loss):		
Balance, beginning of period	95,527	108,006
Change in foreign currency translation adjustment, net of income tax expense (benefit) of $(230) in 2015 and $(106) in 2014	(20,336)	(8,571)
Change in net unrealized investment gains (losses) during the period, net of income taxes:		
Change in net unrealized investment gains (losses) not-other-than temporarily impaired, net of income tax expense (benefit) of $4,897 in 2015 and $6,210 in 2014	9,094	11,532
Change in net unrealized investment losses other-than-temporarily impaired, net of income tax expense (benefit) of $0 in 2015 and 2014	-	-
Balance, end of period	84,285	110,967
Total stockholders' equity	$1,239,421	$1,253,533

See accompanying notes to condensed consolidated financial statements.

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PRIMERICA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows – Unaudited

	Three months ended March 31,	
	2015	2014
	(In thousands)	
Cash flows from operating activities:		
Net income	$43,401	$45,080
Adjustments to reconcile net income to cash provided by (used in) operating activities:		
Change in future policy benefits and other policy liabilities	53,674	54,542
Deferral of policy acquisition costs	(75,434)	(73,045)
Amortization of deferred policy acquisition costs	36,213	35,193
Change in income taxes	18,576	14,905
Realized investment (gains) losses, including other-than-temporary impairments	(1,284)	(263)
Gain from sale of business, net	-	(1,595)
Accretion and amortization of investments	(438)	(597)
Depreciation and amortization	2,633	2,884
Change in due from reinsurers	(6,956)	(32,759)
Change in premiums and other receivables	456	(4,173)
Trading securities sold, matured, or called (acquired), net	365	2,036
Share-based compensation	8,943	2,848
Change in other operating assets and liabilities, net	(13,747)	(7,316)
Net cash provided by (used in) operating activities	66,402	37,740
Cash flows from investing activities:		
Available-for-sale investments sold, matured or called:		
Fixed-maturity securities — sold	23,278	21,094
Fixed-maturity securities — matured or called	72,979	91,596
Equity securities	1,659	188
Available-for-sale investments acquired:		
Fixed-maturity securities	(122,264)	(113,508)
Equity securities	(625)	(5,106)
Purchases of property and equipment and other investing activities, net	(1,635)	(1,491)
Proceeds from sale of business	-	3,000
Cash collateral received (returned) on loaned securities, net	5,411	19,242
Sales (purchases) of short-term investments using securities lending collateral, net	(5,411)	(19,242)
Net cash provided by (used in) investing activities	(26,608)	(4,227)
Cash flows from financing activities:		
Dividends paid	(8,517)	(6,738)
Common stock repurchased	(38,749)	(13,065)
Excess tax benefits on share-based compensation	3,456	2,954
Tax withholdings on share-based compensation	(6,041)	(6,122)
Cash proceeds from stock options exercised	136	-
Net cash provided by (used in) financing activities	(49,715)	(22,971)

Effect of foreign exchange rate changes on cash	(2,388)	(1,293)
Change in cash and cash equivalents	(12,309)	9,249
Cash and cash equivalents, beginning of period	192,516	149,189
Cash and cash equivalents, end of period	$180,207	$158,438

See accompanying notes to condensed consolidated financial statements.

PRIMERICA, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements — Unaudited

(1) Description of Business, Basis of Presentation, and Summary of Significant Accounting Policies

Description of Business. Primerica, Inc. (the "Parent Company"), together with its subsidiaries (collectively, "we", "us" or the "Company"), is a leading distributor of financial products to middle income households in the United States and Canada. We assist our clients in meeting their needs for term life insurance, which we underwrite, and mutual funds, annuities and other financial products, which we distribute primarily on behalf of third parties. Our primary subsidiaries include the following entities: Primerica Financial Services, Inc. ("PFS"), a general agency and marketing company; Primerica Life Insurance Company ("Primerica Life"), our principal life insurance company; Primerica Financial Services (Canada) Ltd., a holding company for our Canadian operations, which includes Primerica Life Insurance Company of Canada ("Primerica Life Canada") and PFSL Investments Canada Ltd. ("PFSL Investments Canada"); and PFS Investments, Inc. ("PFS Investments"), an investment products company and broker-dealer. Primerica Life, domiciled in Massachusetts, owns National Benefit Life Insurance Company ("NBLIC"), a New York insurance company.

We have established Peach Re, Inc. ("Peach Re") and Vidalia Re, Inc. (“Vidalia Re”) as special purpose financial captive insurance companies and wholly owned subsidiaries of Primerica Life. Peach Re and Vidalia Re have each entered into separate coinsurance agreements with Primerica Life whereby Primerica Life has ceded certain level premium term life insurance policies to Peach Re and Vidalia Re (respectively, the “Peach Re Coinsurance Agreement” and the “Vidalia Re Coinsurance Agreement”).

Basis of Presentation. We prepare our financial statements in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"). These principles are established primarily by the Financial Accounting Standards Board ("FASB"). The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect financial statement balances, revenues and expenses and cash flows, as well as the disclosure of contingent assets and liabilities. Management considers available facts and knowledge of existing circumstances when establishing the estimates included in our financial statements.

The accompanying unaudited condensed consolidated financial statements contain all adjustments, generally consisting of normal recurring accruals, which are necessary to fairly present the balance sheets as of March 31, 2015 and December 31, 2014 and the statements of income, comprehensive income (loss), stockholders' equity and cash flows for the three months ended March 31, 2015 and 2014. Results of operations for interim periods are not necessarily indicative of results for the entire year or of the results to be expected in future periods.

These unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are sufficient to make the information not misleading. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto that are included in our Annual Report on Form 10-K for the year ended December 31, 2014 ("2014 Annual Report").

Use of Estimates. The most significant items that involve a greater degree of accounting estimates and actuarial determinations subject to change in the future are the valuation of investments, deferred policy acquisition costs ("DAC"), liabilities for future policy benefits and unpaid policy claims, and income taxes. Estimates for these and other items are subject to change and are reassessed by management in accordance with U.S. GAAP. Actual results could differ from those estimates.

Consolidation. The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and those entities required to be consolidated under applicable accounting standards. All material intercompany profits, transactions, and balances among the consolidated entities have been eliminated.

Reclassifications. Certain reclassifications have been made to prior-period amounts to conform to current-period reporting classifications. These reclassifications had no impact on net income or total stockholders' equity.

Subsequent Events. The Company has evaluated subsequent events for recognition and disclosure for occurrences and transactions after the date of the unaudited condensed consolidated financial statements dated as of March 31, 2015.

Significant Accounting Policies. All significant accounting policies remain unchanged from the 2014 Annual Report.

New Accounting Principles. In April 2015, the FASB issued Accounting Standards Update No. 2015-03, Interest — Imputation of Interest (Subtopic 835-30) – Simplifying the Presentation of Debt Issuance Costs ("ASU 2015-03"). Debt issuance costs related to a recognized debt liability are currently presented as a deferred charge, or asset, within the balance sheet. ASU 2015-03 requires the presentation of debt issuance costs related to a recognized debt liability as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The amendments in ASU 2015-03 are effective retrospectively for the Company beginning in fiscal year 2016, with early adoption permitted. The Company intends to adopt the amendments in ASU 2015-03 beginning in the first quarter of 2016. At March 31, 2015, the Company had debt issuance costs related to recognized liabilities of approximately $3.1 million within Other assets on our unaudited condensed consolidated balance sheets that would be reclassified and presented as a direct deduction from the carrying amount of debt liabilities under ASU 2015-03.

Future Application of Accounting Standards. Recent accounting guidance not discussed is not applicable, is immaterial to our financial statements, or did not or will not have an impact on our business.

(2) Segment and Geographical Information

Segments. We have two primary operating segments — Term Life Insurance and Investment and Savings Products. We also have a Corporate and Other Distributed Products segment.

Results of continuing operations by segment were as follows:

	Three months ended March 31,	
	2015	2014
	(In thousands)	
Revenues:		
Term life insurance segment	$198,365	$182,980
Investment and savings products segment	129,074	123,270
Corporate and other distributed products segment	17,700	18,078
Total revenues	$345,139	$324,328
Income (loss) from continuing operations before income taxes:		
Term life insurance segment	$47,820	$47,204
Investment and savings products segment	35,044	34,028
Corporate and other distributed products segment	(16,055)	(14,400)
Total income from continuing operations before income taxes	$66,809	$66,832

Total assets by segment were as follows:

	March 31, 2015	December 31, 2014
	(In thousands)	
Assets:		
Term life insurance segment	$7,255,680	$7,165,373
Investment and savings products segment	2,586,578	2,642,753
Corporate and other distributed products segment	881,956	929,988
Total assets	$10,724,214	$10,738,114

The Investment and Savings Products segment includes assets held in separate accounts. Excluding separate accounts, the Investment and Savings Products segment assets were approximately $200.7 million and $202.9 million as of March 31, 2015 and December 31, 2014, respectively.

See "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this report for more information regarding our operating segments.

Geographical Information. Results of continuing operations by country and long-lived assets — primarily tangible assets reported in Other assets in our unaudited condensed consolidated balance sheets —were as follows:

	Three months ended March 31, 2015	2014
	(In thousands)	
Revenues by country:		
United States	$286,141	$262,204
Canada	58,998	62,124
Total revenues	$345,139	$324,328
Income from continuing operations before income taxes by country:		
United States	$48,856	$48,912
Canada	17,953	17,920
Total income from continuing operations before income taxes	$66,809	$66,832

	March 31, 2015	December 31, 2014
	(In thousands)	
Long-lived assets by country:		
United States	$28,223	$ 25,897
Canada	592	566
Total long-lived assets	$28,815	$ 26,463

(3) Investments

Available-for-sale Securities. The period-end cost or amortized cost, gross unrealized gains and losses, and fair value of available-for-sale fixed-maturity and equity securities follow:

	March 31, 2015			
	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(In thousands)			
Securities available-for-sale, carried at fair value:				
Fixed-maturity securities:				
U.S. government and agencies	$ 13,925	$ 629	$ (69)	$ 14,485
Foreign government	122,919	4,142	(7,856)	119,205
States and political subdivisions	37,892	3,089	(292)	40,689
Corporates	1,265,977	90,503	(10,044)	1,346,436
Mortgage- and asset-backed securities	255,699	13,633	(210)	269,122
Total fixed-maturity securities[1]	1,696,412	111,996	(18,471)	1,789,937
Equity securities	42,347	10,473	(1,013)	51,807
Total fixed-maturity and equity securities	$ 1,738,759	$ 122,469	$ (19,484)	$ 1,841,744

[1] Includes approximately $0.7 million of other-than-temporary impairment losses related to corporates and mortgage- and asset-backed securities recognized in accumulated other comprehensive income.

	December 31, 2014			
	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(In thousands)			
Securities available-for-sale, carried at fair value:				
Fixed-maturity securities:				
U.S. government and agencies	$ 15,145	$ 557	$ (55)	$ 15,647
Foreign government	120,910	5,388	(3,801)	122,497
States and political subdivisions	38,163	2,719	(188)	40,694
Corporates	1,241,526	82,167	(7,825)	1,315,868
Mortgage- and asset-backed securities	251,756	13,050	(392)	264,414
Total fixed-maturity securities[1]	1,667,500	103,881	(12,261)	1,759,120
Equity securities	43,738	10,711	(1,059)	53,390
Total fixed-maturity and equity securities	$ 1,711,238	$ 114,592	$ (13,320)	$ 1,812,510

[1] Includes approximately $0.7 million of other-than-temporary impairment losses related to corporates and mortgage- and asset-backed securities recognized in accumulated other comprehensive income.

All of our available-for-sale mortgage- and asset-backed securities represent variable interests in variable interest entities ("VIEs"). We are not the primary beneficiary of these VIEs because we do not have the power to direct the activities that most significantly impact the entities' economic performance. The maximum exposure to loss as a result of our involvement in these VIEs equals the carrying value of the securities.

The scheduled contractual maturity distribution of the available-for-sale fixed-maturity portfolio at March 31, 2015 follows:

	Amortized cost	Fair value
	(In thousands)	
Due in one year or less	$115,705	$117,276
Due after one year through five years	580,952	624,827
Due after five years through 10 years	695,841	727,136
Due after 10 years	48,215	51,576
	1,440,713	1,520,815
Mortgage- and asset-backed securities	255,699	269,122
Total fixed-maturity securities	$1,696,412	$1,789,937

Expected maturities may differ from scheduled contractual maturities because issuers of securities may have the right to call or prepay obligations with or without call or prepayment penalties.

Unrealized Gains and Losses on Investments. The net effect on stockholders’ equity of unrealized gains and losses on investments was as follows:

	March 31, 2015	December 31, 2014
	(In thousands)	
Net unrealized investment gains including foreign currency translation adjustment and other-than-temporary impairments:		
Fixed-maturity and equity securities	$102,985	$101,272
Currency swaps	10	23
Foreign currency translation adjustment	24,605	12,314
Other-than-temporary impairments	710	710
Net unrealized investment gains excluding foreign currency translation adjustment and other-than-temporary impairments	128,310	114,319
Deferred income taxes	(44,908)	(40,011)
Net unrealized investment gains excluding foreign currency translation adjustment and other-than-temporary impairments, net of tax	$83,402	$74,308

Trading Securities. We maintain a portfolio of fixed-maturity securities that are classified as trading securities. The carrying values of the fixed-maturity securities classified as trading securities were approximately $7.3 million and $7.7 million as of March 31, 2015 and December 31, 2014, respectively.

Held-to-maturity Security. Concurrent with the execution of the Vidalia Re Coinsurance Agreement, Vidalia Re entered into a Surplus Note Purchase Agreement (the "Surplus Note Purchase Agreement") with Hannover Life Reassurance Company of America and certain of its affiliates (collectively, “Hannover Re”) and a newly formed limited liability company (the "LLC") owned by a third party service provider. Under the Surplus Note Purchase Agreement, Vidalia Re issued a surplus note (the “Surplus Note”) to the LLC in exchange for a credit enhanced note from the LLC with an equal principal amount (the “LLC Note”). The principal amount of both the LLC Note and the Surplus Note will fluctuate over time to coincide with the amount of reserves contractually supported under the Vidalia Re Coinsurance Agreement. Both the LLC Note and the Surplus Note mature on December 31, 2029 and bear interest at an annual interest rate of 4.50%. The LLC Note is guaranteed by Hannover Re through a credit enhancement feature in exchange for a fee.

The LLC is a variable interest entity as its owner does not have an equity investment at risk that is sufficient to permit the LLC to finance its activities without Vidalia Re or Hannover Re. The Parent Company, Primerica Life, and Vidalia Re share the power to direct the activities of the LLC with Hannover Re, but do not have the obligation to absorb losses or the right to receive any residual returns related to the LLC’s primary risks or sources of variability. Through the credit enhancement feature, Hannover Re is the ultimate risk taker in this transaction and bears the obligation to absorb the LLC’s losses in the event of a Surplus Note default in exchange for the fee. Accordingly, the Company is not the primary beneficiary of the LLC and does not consolidate the LLC within its consolidated financial statements.

The LLC Note is classified as a held-to-maturity debt security in the Company’s invested asset portfolio as we have the positive intent and ability to hold the security until maturity. As of March 31, 2015, the LLC Note, which was rated AA- by Fitch Ratings, had an estimated unrealized holding gain of $21.8 million based on its amortized cost and estimated fair value, which is derived using the valuation techniques described in Note 4 (Fair Value of Financial Instruments).

See Note 6 (Debt) for more information on the Surplus Note.

Investments on Deposit with Governmental Authorities. As required by law, we have investments on deposit with governmental authorities and banks for the protection of policyholders. The fair values of investments on deposit were approximately $19.7 million and $19.9 million as of March 31, 2015 and December 31, 2014, respectively.

Securities Lending Transactions. We participate in securities lending transactions with broker-dealers and other financial institutions to increase investment income with minimal risk. We require minimum collateral on securities loaned equal to 102% of the fair value of the loaned securities. We accept collateral in the form of securities, which we are not able to sell or encumber, and to the extent the collateral declines in value below 100%, we require additional collateral from the borrower. Any securities collateral received is not reflected on our unaudited condensed consolidated balance sheets. We also accept collateral in the form of cash, all of which we reinvest. For loans involving unrestricted cash collateral, the collateral is reported as an asset with a corresponding liability representing our obligation to return the collateral. We continue to carry the loaned securities as invested assets on our unaudited condensed consolidated balance sheets during the terms of the loans, and we do not report them as sales. Cash collateral received and reinvested was approximately $55.6 million and $50.2 million as of March 31, 2015 and December 31, 2014, respectively.

Investment Income. The components of net investment income were as follows:

	Three months ended March 31, 2015	2014
	(In thousands)	
Fixed-maturity securities (available-for-sale)	$19,795	$21,032
Fixed-maturity security (held-to-maturity)	2,475	-
Equity securities	516	385
Policy loans and other invested assets	359	388
Cash and cash equivalents	43	53
Market return on deposit asset underlying 10% coinsurance agreement	1,672	953
Gross investment income	24,860	22,811
Investment expenses	(1,212)	(1,212)
Interest expense on Surplus Note	(2,475)	-
Net investment income	$21,173	$21,599

The components of net realized investment gains (losses) as well as details on gross realized investment gains and losses and proceeds from sales or other redemptions were as follows:

	Three months ended March 31, 2015	2014
	(In thousands)	
Net realized investment gains (losses):		
Gross gains from sales	$1,934	$343
Gross losses from sales	(27)	(6)
Other-than-temporary impairment losses	(237)	(149)
Gains (losses) from bifurcated options	(386)	75
Net realized investment gains (losses)	$1,284	$263
Supplemental information:		
Gross realized investment gains (losses) reclassified from accumulated other comprehensive income into earnings	$1,670	$188
Tax expense (benefit) associated with realized investment gains (losses) reclassified from accumulated other comprehensive income into earnings	$585	$66
Proceeds from sales or other redemptions	$97,916	$112,878

Other-Than-Temporary Impairment. We conduct a review each quarter to identify and evaluate impaired investments that have indications of possible other-than-temporary impairment ("OTTI"). An investment in a debt or equity security is impaired if its fair value falls below its cost. Factors considered in determining whether an unrealized loss is temporary include the length of time and extent to which fair value has been below cost, the financial condition and near-term prospects for the issue, and our ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery, which may be maturity for fixed-maturity securities or within a reasonable period of time for equity securities. For additional information, see Note 4 (Investments) to the consolidated financial statements in our 2014 Annual Report.

Available-for-sale fixed-maturity and equity securities with a cost basis in excess of their fair values were approximately $282.0 million and $340.8 million as of March 31, 2015 and December 31, 2014, respectively.

The following tables summarize, for all available-for-sale securities in an unrealized loss position, the aggregate fair value and the gross unrealized loss by length of time such securities have continuously been in an unrealized loss position:

	March 31, 2015					
	Less than 12 months			12 months or longer		
	Fair value	Unrealized losses	Number of securities	Fair value	Unrealized losses	Number of securities
	(Dollars in thousands)					
Fixed-maturity securities:						
U.S. government and agencies	$683	$(12)	1	$197	$(57)	1
Foreign government	49,697	(4,249)	48	19,090	(3,607)	37
States and political subdivisions	1,994	(4)	2	1,612	(288)	3
Corporates	106,770	(5,031)	110	31,239	(5,013)	55
Mortgage-and asset-backed securities	33,624	(84)	29	11,291	(126)	14
Total fixed-maturity securities	192,768	(9,380)		63,429	(9,091)	
Equity securities	6,367	(1,013)	17	-	-	-
Total fixed-maturity and equity securities	$199,135	$(10,393)		$63,429	$(9,091)	

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	December 31, 2014					
	Less than 12 months			12 months or longer		
	Fair value	Unrealized losses	Number of securities	Fair value	Unrealized losses	Number of securities
	(Dollars in thousands)					
Fixed-maturity securities:						
U.S. government and agencies	$7,201	$ (1)	2	$896	$ (54)	2
Foreign government	28,038	(1,317)	35	23,330	(2,484)	40
States and political subdivisions	1,694	(4)	3	2,720	(184)	4
Corporates	144,262	(3,818)	153	43,736	(4,007)	78
Mortgage-and asset-backed securities	49,591	(109)	43	16,847	(283)	20
Total fixed-maturity securities	230,786	(5,249)		87,529	(7,012)	
Equity securities	6,849	(862)	15	2,303	(197)	1
Total fixed-maturity and equity securities	$237,635	$ (6,111)		$89,832	$ (7,209)	

The amortized cost and fair value of available-for-sale fixed-maturity securities in default were as follows:

	March 31, 2015		December 31, 2014	
	Amortized cost	Fair value	Amortized cost	Fair value
	(In thousands)			
Fixed-maturity securities in default	$130	$491	$144	$611

Impairment charges recognized in earnings on available-for-sale securities were as follows:

	Three months ended March 31,	
	2015	2014
	(In thousands)	
Impairments on fixed-maturity securities not in default	$161	$149
Impairments on equity securities	76	-
Total impairment charges	$237	$149

The securities noted above were considered to be other-than-temporarily impaired due to our intent to sell them; adverse credit events, such as news of an impending filing for bankruptcy; analyses of the issuer's most recent financial statements or other information in which liquidity deficiencies, significant losses and large declines in capitalization were evident; or analyses of rating agency information for issuances with severe ratings downgrades that indicated a significant increase in the possibility of default.

As of March 31, 2015, the unrealized losses on our available-for-sale invested asset portfolio were largely caused by interest rate sensitivity, foreign currency exchange rates on our Canadian dollar-denominated investments, and changes in credit spreads. We believe that fluctuations caused by interest rate movement have little bearing on the recoverability of our investments. Because we have the ability to hold these investments until a market price recovery or maturity and we have no present intention to dispose of them, we do not consider these investments to be other-than-temporarily impaired.

Net impairment losses recognized in earnings for available-for-sale securities were as follows:

	Three months ended March 31, 2015	2014
	(In thousands)	
Total impairment losses related to securities which the Company does not intend to sell or more-likely-than-not will not be required to sell:		
Total OTTI losses recognized	$93	$-
Less portion of OTTI loss recognized in accumulated other comprehensive income (loss)	-	-
Net impairment losses recognized in earnings for securities which the Company does not intend to sell or more-likely-than-not will not be required to sell before recovery	93	-
OTTI losses recognized in earnings for securities which the Company intends to sell or more-likely-than-not will be required to sell before recovery	144	149
Net impairment losses recognized in earnings	$237	$149

The rollforward of the credit-related losses recognized in income for all available-for-sale fixed-maturity securities still held follows:

	Three months ended March 31,	
	2015	2014
	(In thousands)	
Cumulative OTTI credit losses recognized for securities still held, beginning of period	$9,550	$7,970
Additions for OTTI securities where no credit losses were recognized prior to the beginning of the period	21	149
Additions for OTTI securities where credit losses have been recognized prior to the beginning of the period	140	-
Reductions due to sales, maturities, calls, amortization or increases in cash flows expected to be collected over the remaining life of credit impaired securities	(956)	(42)
Reductions for exchanges of securities previously impaired	(1,277)	-
Cumulative OTTI credit losses recognized for securities still held, end of period	$7,478	$8,077

As of March 31, 2015, no impairment losses have been recognized on the LLC Note held-to-maturity security.

Derivatives. Embedded conversion options associated with fixed-maturity securities are bifurcated from the fixed-maturity security host contracts and separately recognized as equity securities. The change in fair value of these bifurcated conversion options is reflected in realized investment gains (losses), including OTTI losses. As of March 31, 2015 and December 31, 2014, the fair value of these bifurcated options was approximately $5.6 million and $5.8 million, respectively.

We have a deferred loss related to closed forward contracts, which were settled several years ago, that were used to mitigate our exposure to foreign currency exchange rates that resulted from the net investment in our Canadian operations. The amount of deferred loss included in accumulated other comprehensive income was approximately $26.4 million as of March 31, 2015 and December 31, 2014. While we have no current intention to do so, these deferred losses will not be recognized until such time as we sell or substantially liquidate our Canadian operations.

(4) Fair Value of Financial Instruments

Fair value is the price that would be received upon the sale of an asset in an orderly transaction between market participants at the measurement date. Fair value measurements are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our view of market assumptions in the absence of observable market information. We classify and disclose all invested assets carried at fair value in one of the following three categories:

- Level 1. Quoted prices for identical instruments in active markets. Level 1 primarily consists of financial instruments whose value is based on quoted market prices in active markets, such as exchange-traded common stocks and actively traded mutual fund investments;
-

Level 2. Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets. Level 2 includes those financial instruments that are valued using industry-standard pricing methodologies, models or other valuation methodologies. Various inputs are considered in deriving the fair value of the underlying financial instrument, including interest rate, credit spread, and foreign exchange rates. All significant inputs are observable, or derived from observable information in the marketplace or are supported by observable levels at which transactions are executed in the marketplace. Financial instruments in this category primarily include: certain public and private corporate fixed-maturity and equity securities; government or agency securities; certain mortgage- and asset-backed securities and bifurcated conversion options; and

- Level 3. Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable. Level 3 consists of financial instruments whose fair value is estimated based on industry-standard pricing methodologies and models using significant inputs not based on, nor corroborated by, readily available market information. Valuations for this category primarily consist of non-binding broker quotes. Financial instruments in this category primarily include less liquid fixed-maturity corporate securities.

As of each reporting period, all assets and liabilities recorded at fair value are classified in their entirety based on the lowest level of input (Level 3 being the lowest) that is significant to the fair value measurement. Significant levels of estimation and judgment are required to determine the fair value of certain of our investments. The factors influencing these estimations and judgments are subject to change in subsequent reporting periods.

The estimated fair value and hierarchy classifications for assets and liabilities that are measured at fair value on a recurring basis were as follows: