NATIONAL SECURITY GROUP INC
Form 10-K
March 18, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

þ ANNUAL REPORT PURSUANT TO SECTION 13 or 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal Period Ended December 31, 2015

or

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

For the transition period from to .

Commission File Number 0-18649

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

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

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

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

None

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

Common Stock, par value $1.00 per share	The NASDAQ Global Market (EXCHANGE)

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

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 o No þ

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

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

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. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of “large accelerated filler,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller Reporting Company þ

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

The aggregate market value of the voting stock held by non-affiliates of the Registrant as of the last business day of the registrant's most recently completed second fiscal quarter, based upon the bid price of these shares on NASDAQ on such date, was $23,502,497

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the close of the period covered by this report.

Class	Outstanding March 18, 2016
Common Stock $1.00 par value	2,512,425 shares

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THE NATIONAL SECURITY GROUP, INC.

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DOCUMENTS INCORPORATED BY REFERENCE

1. Definitive proxy statement for the 2016 Annual Meeting of Stockholders to be held May 20, 2016 is incorporated by reference into Part III of this report. The proxy statement will be filed no later than 120 days from December 31, 2015.

2. Current Report on Form 8-K for event occurring on February 26, 2016 is incorporated into Part IV of this report.

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PART I

Item 1. Business
Summary Description of The National Security Group, Inc.

The National Security Group, Inc. (the Company, NSG, we, us, our), an insurance holding company, was incorporated in Delaware on March 20, 1990. Our common stock is traded on the NASDAQ Global Market under the symbol NSEC.

Pursuant to regulations of the United States Securities and Exchange Commission (SEC), we are considered a “Smaller Reporting Company” as defined by SEC rules. We have elected to utilize an “a la carte” scaled disclosure which permits smaller reporting companies to elect to comply with scaled financial and non-financial disclosure requirements on an item by item basis. The most significant reporting difference permitted under the scaled disclosures, which we have utilized, is to include two years of audited financial statements.

The Company, through its three wholly owned subsidiaries, operates in two industry segments: property and casualty insurance and life insurance.

The property and casualty subsidiaries of the Company, National Security Fire and Casualty (NSFC), and Omega One Insurance Company (Omega), primarily write personal lines dwelling coverage including dwelling fire and windstorm, homeowners and mobile homeowners lines of insurance in ten states. Property and casualty insurance is the most significant industry segment, accounting for 90.3% of total premium revenues.

The Company's life insurance subsidiary, National Security Insurance Company (NSIC), offers a basic line of life and health and accident insurance products in seven states.

The majority of our assets and investments are held in the insurance company subsidiaries.

The Company's website address is: www.nationalsecuritygroup.com. The “Investors” section of our website (http://www.nationalsecuritygroup.com/public/Investors/Investors.aspx) provides numerous resources for investors seeking additional information about us. Our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our current reports on Form 8-K are made available on our website soon after filing with the SEC. Additionally, stock trades by insiders as filed on Forms 3, 4, and 5 are posted to the website after filing with the SEC. The website also provides information regarding corporate governance, stock quotes and press releases. Investors are encouraged to visit our website for additional information about the Company.

Cautionary Statement Regarding Forward-Looking Statements

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

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

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

The Company is subject to regulation by state governments for each of the states in which it conducts business. The Company cannot predict the subject of any future regulatory initiative(s) or its (their) impact on the Company's business. Company insurance rates are also subject to approval by state insurance departments in each of these states. We are often limited in the level of rate increases we can obtain.

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

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

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

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

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

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

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

Industry Segment and Geographical Area Information

Property and Casualty Insurance Segment

The Company's property and casualty insurance business is conducted through National Security Fire & Casualty Company (NSFC), a wholly owned subsidiary of the Company organized in 1959, and Omega One Insurance Company (Omega), a wholly owned subsidiary of National Security Fire & Casualty Company organized in 1992. This segment will be referred to throughout this report as NSFC, property-casualty segment or P&C segment. NSFC is licensed to write property and casualty insurance in Alabama, Arkansas, Florida, Georgia, Kentucky, Mississippi, Oklahoma, South Carolina, Tennessee and West Virginia, and operates on a surplus lines basis in the state of Louisiana. Omega is licensed to write insurance in Alabama and Louisiana.

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The following table indicates allocation percentages of direct written premium by state for the two years ended December 31, 2015 and 2014:

State	Percent of Direct Written Premium					
	2015			2014		
Alabama	$17,232,000	28.52	%	$17,244,000	29.26	%
Arkansas	2,445,000	4.05	%	2,657,000	4.51	%
Georgia	7,205,000	11.92	%	6,488,000	11.01	%
Louisiana	7,188,000	11.90	%	7,312,000	12.41	%
Mississippi	10,852,000	17.96	%	10,751,000	18.24	%
Oklahoma	5,699,000	9.43	%	4,812,000	8.17	%
South Carolina	6,400,000	10.59	%	6,236,000	10.58	%
Tennessee	3,402,000	5.63	%	3,426,000	5.82	%
	$60,423,000	100.00	%	$58,926,000	100.00	%

In general, the property-casualty insurance business involves the transfer by the insured, to an insurance company of all or a portion of certain risks for the payment, by the insured, of a premium to the insurance company. A portion of such risks is often retained by the insured in the form of deductibles, which vary from policy to policy, but are typically in the range of $500 to $1,000 on NSFC and Omega's primary dwelling property and homeowners lines of business.

The premiums or payments to be made by the insured for insurance policies of the property and casualty subsidiaries are based upon expected costs of providing benefits, underwriting and administering the policies. In determining the premium to be charged, the property and casualty subsidiaries utilize data from past claims experience, modeled catastrophe losses and anticipated claims estimates along with catastrophe reinsurance cost, commissions, taxes and general expenses.

The operating results of the property-casualty insurance industry are subject to significant fluctuations from quarter-to-quarter and from year-to-year. These fluctuations are often due to the effect of competition on pricing, unpredictable losses incurred in connection with weather-related and other catastrophic events, general economic conditions and other factors, such as changes in tax laws and the regulatory environment.

The following table sets forth the premiums earned (net of reinsurance) and pretax income during the periods reported for the property and casualty insurance segment:

	Year Ended December 31,		
	2015		2014
Net premiums earned:			
Fire, allied lines and homeowners	$53,252,000		$50,202,000
Other	(90,000	)	77,000
Total net earned premium	$53,162,000		$50,279,000
Income before taxes	$7,070,000		$11,527,000

Property and Casualty Loss Reserves

Our property and casualty insurance subsidiaries are required to maintain reserves to cover their ultimate liability for losses and adjustment expenses. Our staff periodically conducts reviews throughout the year of projected loss development information in order to adjust estimates. The liability for loss and adjustment expense reserves consists of an estimated liability for the ultimate settlement of claims that have been reported as well as an estimate of loss and adjustment expenses for incurred claims that have not yet been reported (IBNR). IBNR estimates are based primarily on historical development patterns using quantitative data generated from statistical information and qualitative analysis of legal developments, economic conditions and development caused by events deemed to be infrequent in occurrence. The reserves are based on an estimate made by management. Management estimates are based on an analysis of historical paid and incurred loss development patterns for the previous ten loss years. Prior year period-to-period loss development factors are applied to latest reported loss reserve estimates in order to estimate the ultimate

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incurred losses for each given loss year. The amount of loss reserves estimated in excess of current reported case losses are recorded as IBNR reserves.

In addition to loss and loss adjustment expense reserves for specific claims, both reported and unreported, we establish reserves for loss adjustment expenses that are not attributable to specific claims. These reserves consist of estimates for Defense and Cost Containment (DCC) and Adjusting and Other Expenses (AO). These reserves are established for the estimated expenses of internal claims staff and the cost of outside experts, such as attorneys representing our interest, in the final settlement of incurred claims that are still in process of settlement. We conduct annual and interim reviews over the course of each year in order to insure that no significant changes have occurred in our loss development that might adversely impact our loss reserving methodology.

The following Loss Reserve Re-estimates table illustrates the change over time of the net reserves established for property-liability insurance claims and claims expense at the end of the last 10 calendar years. The first section shows the reserves as originally reported at the end of the stated year. The second section, reading down, shows retroactive re-estimates of the original recorded reserve as of the end of each successive year. These re-estimates are the result of the Company's expanded awareness of additional facts and circumstances that pertain to the unsettled claims. The third section, reading down, shows the cumulative amounts paid as of the end of successive years with respect to that year's reserve liability. The last section compares the latest re-estimated reserve to the reserve originally established and indicates whether the original reserve was adequate to cover the estimated costs of unsettled claims. The Loss Reserve Re-estimates table is cumulative, and therefore, ending balances should not be added since the amount at the end of each calendar year includes activity for both the current and prior years.

While the information in the table provides a historical perspective on the adequacy of unpaid losses and loss adjustment expenses established in previous years, it should not be assumed to be predictive of redundancies or deficiencies on current year unpaid losses in future periods. Company management believes that the reserves established at the end of 2015 are adequate. However, due to inherent uncertainties in the loss reserve estimation process, management cannot guarantee that current year reserve balances will prove to be adequate. Due to the relatively short tail nature of the property and casualty subsidiaries' claim liabilities, the Company does not discount loss reserves for the time value of money. Dollar amounts in the following table are in thousands.

Gross unpaid losses per		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Consolidated Balance Sheet		$19,511	$12,498	$11,973	$14,436	$12,646	$13,184	$14,386	$11,214	$8,734	$8,321	$9,6
Ceded reserves		(8,560)	(1,783)	(555)	(2,421)	(549)	(1,329)	(2,381)	(1,229)	(782)	(839)	(1,38
Net unpaid losses		$10,951	$10,715	$11,418	$12,015	$12,097	$11,855	$12,005	$9,985	$7,952	$7,482	$8,2
Cumulative net payments:	1 year later	$7,384	$6,438	$4,797	$5,636	$5,349	$5,738	$4,035	$4,827	$2,900	$2,990	
	2 years later	9,063	8,103	6,496	6,350	6,305	7,239	5,346	6,670	3,539		
	3 years later	10,198	9,652	6,767	6,725	6,764	7,841	6,483	7,426			
	4 years	11,439	10,094	6,976	6,980	7,244	8,382	7,001				

	later										
	5 years later	11,763	10,360	7,202	7,295	7,701	8,419				
	6 years later	11,900	10,662	7,213	7,390	7,725					
	7 years later	12,012	10,810	7,156	7,406						
	8 years later	12,141	10,015	7,164							
	9 years later	11,345	10,022								
	10 years later	11,345									
Net Liability re-estimated:	1 year later	11,844	11,817	9,046	9,438	8,621	11,443	9,606	9,354	6,698	5,597
	2 years later	11,827	11,061	8,739	7,916	8,869	11,064	8,439	9,360	5,185	
	3 years later	12,161	11,121	7,739	8,179	9,033	9,725	8,500	8,483		
	4 years later	12,337	10,792	7,792	8,514	8,418	9,178	7,661			
	5 years later	12,178	11,089	8,010	7,855	8,064	8,854				
	6 years later	12,372	11,413	7,636	7,641	8,092					
	7 years later	12,699	11,175	7,577	7,707						
	8 years later	12,451	10,236	7,390							
	9 years later	11,522	10,038								
	10 years later	11,345									
Net cumulative redundancy		$(394)	$677	$4,028	$4,308	$4,005	$3,001	$4,344	$1,502	$2,767	$1,885

(deficiency)

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Our reported results, financial position and liquidity could be affected by changes in key assumptions that determine our loss reserves. The table below illustrates the change to equity that would occur as a result of a change in loss reserves and reserves for loss adjustment expense:

	For The Years Ended December 31,			
	2015		2014	
Change in Loss and LAE Reserves	Adjusted Loss and LAE Reserves	% Change in Equity	Adjusted Loss and LAE Reserves	% Change in Equity
*Loss and LAE reserves are in thousands				
(10.0)%	$8,681	2.15%	$7,489	1.95%
(7.5)%	8,922	1.61%	7,697	1.46%
(5.0)%	9,163	1.07%	7,905	0.97%
(2.5)%	9,404	0.54%	8,113	0.49%
Reported	9,645	—%	8,321	—%
2.5%	9,886	(0.54)%	8,529	(0.49)%
5.0%	10,127	(1.07)%	8,737	(0.97)%
7.5%	10,368	(1.61)%	8,945	(1.46)%
10.0%	10,610	(2.15)%	9,153	(1.95)%

While our reserve estimates have had more significant variability in the past, we believe that the scenarios presented above are most reasonable as our methodology has become more seasoned, and we have maintained continuity of staff involved in the reserving process.

Life Insurance Segment

National Security Insurance Company (NSIC), a wholly owned subsidiary organized in 1947, conducts the Company's life insurance business. This segment will be referred to throughout this report as NSIC, Life Company, or Life segment. NSIC is licensed to write insurance in seven states: Alabama, Florida, Georgia, Mississippi, South Carolina, Tennessee and Texas.

The following table indicates NSIC's percentage of direct premiums collected by state for the two years ended December 31, 2015 and 2014:

State	Percentage of Total Direct Premiums					
	2015			2014		
Alabama	$3,710,000	58.10	%	$3,827,000	58.63	%
Florida	67,000	1.04	%	74,000	1.14	%
Georgia	1,338,000	20.95	%	1,352,000	20.71	%
Mississippi	659,000	10.32	%	672,000	10.30	%
South Carolina	413,000	6.47	%	418,000	6.40	%
Tennessee	16,000	0.25	%	9,000	0.14	%
Texas	183,000	2.87	%	175,000	2.68	%
	$6,386,000	100.00	%	$6,527,000	100.00	%

NSIC has two primary methods of distribution of insurance products: independent agents and home service (career) agents. The independent agent distribution method accounts for 63.9% of total premium revenue in the life insurance segment. Approximately 200 of the Company's independent agents produced new business during 2015. The home service distribution method of life insurance products accounts for 30.5% of total premium revenue in the life insurance segment. Home service life products consist of products marketed directly at the home or other premises of the insured by an employee agent. The Company employed four career agents and one regional manager as of December 31, 2015. The remaining 5.6% of premium revenue consists of the following: a book of business acquired from a state guaranty association in 2000 (0.9%), premium generated through direct sales of school accident insurance (4.3%), and other miscellaneous business serviced directly through the home office (0.4%).

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NSIC's primary products are life insurance, primarily whole life, and health and accident insurance. NSIC does not sell annuities, interest sensitive whole life or universal life insurance products. Term life insurance policies provide death benefits if the insured's death occurs during the specific premium paying term of the policy. The policies generally do not provide a savings or investment element included as part of the policy premium. Whole-life insurance policies demand a higher premium than term life, but provide death benefits which are payable under effective policies regardless of the time of the insured's death and have a savings and investment element which may result in the accumulation of a cash surrender value. Our accident and health insurance policies provide coverage for losses sustained through sickness or accident and include individual hospitalization and accident policies, group supplementary health policies, and specialty products, such as cancer policies. Our line of health and accident products feature specified fixed benefits, so rapidly rising health care costs do not have as great an impact on our health and accident line as they do on comparable products offered by other companies.

The following table displays a schedule of 2015 life segment premium produced by product and distribution method:

Line of Business	Home Service Agent	Independent Agent	Other
Industrial	$56,000	$—	$34,000
Ordinary	1,638,000	2,697,000	23,000
Group Life	—	12,000	59,000
A&H Group	—	—	270,000
A&H Other	247,000	1,319,000	31,000
Total Premium by Distribution Method	$1,941,000	$4,028,000	$417,000

The following table sets forth certain information with respect to the development of the Life Company's business:

	Year ended December 31,	
	2015	2014
Life insurance in force at end of period:		
Ordinary-whole life	$167,599,000	$173,354,000
Term life	23,340,000	20,977,000
Industrial life	17,232,000	18,039,000
	$208,171,000	$212,370,000
Life insurance issued:		
Ordinary-whole life	$23,000,000	$23,452,000
	$23,000,000	$23,452,000
Net premiums earned:		
Life insurance	$4,423,000	$4,483,000
Accident and health insurance	1,877,000	1,891,000
	$6,300,000	$6,374,000

Life Insurance Segment Reserves

We engage Wakely Actuarial Services of Palm Harbor, Florida as consulting actuary to calculate our reserves for traditional life insurance products. The methodology used requires that the present value of future benefits to be paid under life insurance policies less the present value of future net premiums be calculated. The calculation uses assumptions including estimates of any adverse deviation, investment yields and changes in investment yields, mortality, maintenance expenses and any non-forfeiture options or termination benefits. The assumptions determine the level and sufficiency of reserves which are calculated and reviewed by our consulting actuary at the end of each quarter. The independent consulting actuary also reviews our estimates for other insurance products including claims reserves under accident and health contracts. Management believes that the reserve amounts reflected in the accompanying Consolidated Financial Statements are adequate.

Investments

A significant percentage of the total income for the Company is tied to the performance of its investments. Assets that will eventually be used to pay reserve liabilities and other policyholder obligations along with Company capital are invested to generate investment income while held by the Company. Our investment income is comprised primarily

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of interest and dividend income on debt and equity securities and realized capital gains and losses generated by debt and equity securities. At December 31, 2015, cash and investments comprise 81% of total assets, and investment income (including realized gains) comprises 6.2% of total revenues evidencing the significant impact investments can have on financial results. Because the Company's insurance subsidiaries are regulated as to the types of investments they may make and the amount of funds they may maintain in any one type of investment, the Company has developed a conservative value oriented investment philosophy, in order to meet regulatory requirements. The Company's investment goals are to conserve capital resources and assets, obtain the necessary investment income threshold to meet reserves, and provide a reasonable return. Current yield from invested assets and capital appreciation of investments create this return.

Marketing and Distribution

As mentioned earlier in this report, NSIC products are marketed through a field force of agents who are employees of the Life Company and through a network of independent agents. The Company's use of independent agents is expected to be more cost effective in the long term and has become our primary method of distribution over the past decade. In an effort to boost productivity and better educate agents on the products and services of NSIC, the Life Company marketing team travels throughout our service areas holding training sessions for agents.

NSFC and Omega products are marketed through a network of independent agents and brokers, who are independent contractors and generally maintain relationships with one or more competing insurance companies. NSFC employs field marketing representatives who visit in the offices of our independent agent force regularly to give the agents opportunities for feedback. Our NSFC marketing representatives also host training seminars throughout our service areas. The goal of these seminars is to educate the independent agent sales force about our products and services.

Agents receive compensation for their sales efforts. In the case of life insurance agents, compensation is paid in the form of sales commissions plus a servicing commission. Commissions paid by NSIC in 2015 averaged approximately 11.3% of premiums and are generally higher for new business production and decline each year at subsequent renewals. Commissions rates paid by NSFC in 2015 averaged approximately 15% of premiums on both new and renewal business. During 2015, one independent agent, accounted for more than 10% of total net earned premium of the property-casualty insurance subsidiaries. The net earned premium from this general agent totaled $6,344,000 or 11.9% of total P&C segment net earned premium. NSFC also offers a “profit sharing bonus plan” to independent agents in order to promote better field underwriting and encourage retention of profitable business. This plan not only rewards our agents but also enhances profitability by giving the agent a vested interest in our success and also aids in maintaining price stability for all our customers as agents have a financial incentive to use good field underwriting practices when completing an application for insurance.

At December 31, 2015, NSIC employed five career agents and one regional manager. NSIC also had approximately 200 independent agents actively producing new business in seven states. At December 31, 2015, NSFC had contracts with approximately 1,700 independent agencies in eight states.

Competition

In both of our insurance segments, we operate in a very competitive environment. There are numerous insurance companies competing in the various states in which we offer our products. Many of the companies with which we compete are much larger, have significantly larger volumes of business, offer much broader ranges of products and have more significant financial resources than we do. We compete directly with many of these companies, not only in the sale of products to consumers, but also in the recruitment and retention of qualified agents. We believe the main areas in which a smaller company, like us, can compete is in the areas of providing niche products in under-served areas of the insurance market at competitive prices while providing excellent service to our agents and policyholders during the entire insurance product life cycle from policy issuance to final payment of a claim. We pride ourselves on being accessible to our independent agent force and maintain a presence through the efforts of a field marketing staff and easy access to home office staff. We believe we have made significant advancements in developing a competitive advantage, especially over the last decade. We also have longstanding relationships with many of our agents. We believe we compete effectively within the markets we serve and continue to evolve our processes and procedures in order to garner further competitive advantages.

NSFC's primary insurance products are dwelling fire and homeowners, including mobile homeowners. Dwelling fire and homeowners are collectively referred to as the dwelling property line of business. We focus on providing niche insurance products within the markets we serve. We are in the top twenty-five dwelling property insurance carriers in our two largest states, Alabama and Mississippi. However, due to the large concentration of business among the top five carriers, our total market share in the dwelling fire line of business is approximately 2.5% in Alabama and 1.5%

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in Mississippi. In the homeowners line of business, our market share in both Alabama and Mississippi is less than 1%. The homeowners markets are even more concentrated with the top three homeowners carriers in both Alabama and Mississippi controlling approximately 50% of the market share.

We have actively sought competitive advantages over the last decade in the area of technological advancement. Over the last twelve years, we have replaced our primary policy administration systems in both our property and casualty and life insurance subsidiaries.

The property and casualty administration system is an internally developed end-to-end system that we believe enhances our ability to compete with larger carriers in the markets we serve. The system features a web based portal that allows our independent agents to rate, quote and issue policies directly in their office. The system streamlines the underwriting process with automation of many previous manual processes and enhances our agents' ability to provide excellent service to their clients. The system also enhances the efficiency of our underwriting process allowing for a more thorough evaluation of risks.

Our property and casualty claims administration system automates processes and workflows throughout the claims process and provides a single view of the activity that has occurred on a claim. The system also has an adjuster web portal, which allows adjusters to view policy limits, see reserve history and policy information, and view prior claims and loss history. Communications between adjusters and examiners are centralized on the web portal allowing for any messages to be viewed securely as part of the claims history. Computerized issuance of field checks by staff adjusters was also implemented enforcing reserve and policy limits while reducing the error rates of the previously used hand written checks issued in the field.

Regulation

Our insurance subsidiaries are directly regulated by the insurance department in our state of domicile, Alabama. We are subject to the Alabama Insurance Holding Company System Regulatory Act and report to the Alabama Department of Insurance. Consequently, we are subject to periodic examination and regulation under Alabama Insurance Laws. We underwent our latest periodic regulatory examination which concluded in 2015 with no material issues noted and no financial adjustments made as a result of the examination.

Our insurance subsidiaries are also subject to licensing and supervision by the various governmental agencies in the jurisdictions in which we do business. The nature and extent of such regulation varies, but generally has its source in state statutes which bestow regulatory, supervisory and administrative authority to State Insurance Commissioners and their respective insurance departments. The regulations may require the Company to meet and maintain standards of solvency, comply with licensing requirements, periodically examine market conditions and financial activities and report on the condition of operations and finances. In addition, most of our insurance rates are subject to regulation and approval by regulatory authorities within the respective states in which we offer our products.

Our insurance subsidiaries are subject to various statutory restrictions and limitations relating to the payment of dividends or distributions to stockholders. The restrictions are generally based on certain levels of surplus, net income or operating income as determined by statutory accounting practices. Alabama law permits dividends in any year which, together with other dividends made within the preceding 12 months, do not exceed the greater of (1) 10% of statutory surplus as of the end of the preceding year or (2) for property and casualty insurers, statutory net income for the preceding year or for life companies, statutory net gain from operations for the preceding year. Dividends in excess of the restricted amounts are payable only after obtaining expressed regulatory approval. Future dividends from the insurance subsidiaries may be limited by business or regulatory considerations. The Company relies on the ability of the insurance subsidiaries to pay dividends to fund stockholder dividends and for payment of most operating expenses of the group, including interest and principal payments on debt. Further discussion of dividend payment capacity of subsidiaries can be found in Note 12 of the Consolidated Financial Statements included herein.

Our insurance subsidiaries are subject to risk based capital requirements adopted by the National Association of Insurance Commissioners (NAIC). These requirements direct our insurance companies to calculate and report information according to a risk based formula which attempts to measure statutory capital and surplus needs based on the risk in our product mix and investment portfolio. The formula is designed to allow state insurance regulators to identify companies that are potentially inadequately capitalized. Under the formula, the Company calculates Risk Based Capital (RBC) by taking into account certain risks inherent in an insurer's assets, including investments and an insurer's liabilities. Risk based capital rules provide for different levels of action depending on the ratio of a company's total adjusted capital to its “authorized control level” RBC. Based on calculations made by each of our insurance subsidiaries at December 31, 2015, each subsidiary exceeds any levels that would require regulatory actions.

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A.M. Best Rating

A.M. Best Company is a leading provider of insurance company financial strength ratings and insurance company issuer credit ratings. Best's financial strength ratings and issuer credit ratings provide an independent opinion based on comprehensive quantitative and qualitative evaluation of a company's balance sheet strength, operating performance and business profile. All of our insurance companies have been assigned ratings by A.M. Best Company (Best). On February 10, 2016, Best revised the outlook to stable from negative and affirmed the financial strength rating (FSR) of B++ (Good) and the issuer credit rating (ICR) of "bbb" of NSFC. In addition, Best affirmed the FSR of B+(Good) and ICR of "bbb-" of Omega and NSIC. The outlook for these ratings remained stable. Best also revised the outlook to stable from negative and affirmed the ICR of "bb" of the parent holding company, NSEC. For the latest ratings, you can access www.ambest.com.

Demotech Rating

The property and casualty subsidiaries have been assigned ratings by Demotech, Inc. On December 14, 2015, Demotech affirmed a Financial Stability Rating of A (Exceptional) for both NSFC and Omega.

Employees

The Company itself has no management or operational employees. Instead, all human resource activities are within the subsidiary National Security Insurance Company. NSIC employed 85 staff members as of December 31, 2015, none of which were represented by a labor union. The Company and its property and casualty subsidiary have a Management Service Agreement (“Agreement”) with National Security Insurance Company whereby the Company and the property and casualty subsidiaries reimburse NSIC for salaries and expenses of employees provided under the Agreement. Involved are employees in the areas of Underwriting, Customer Service, Policy Services, Accounting, Marketing, Administration, Document Management, Data Processing, Programming, Personnel, Claims, and Management. We consider our employee relations to be good.

Additional information with respect to The National Security Group's Business

We maintain a website (www.nationalsecuritygroup.com). The National Security Group, Inc.'s annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to such reports that we file or furnish pursuant to Section 13(a) of the Securities Exchange Act of 1934 are available through our website, free of charge, as soon as reasonably practical upon having been electronically filed or furnished to the Securities and Exchange Commission. Our code of ethical conduct is also available on our website and in print to any stockholder who requests copies by contacting The National Security Group, Attn: Investor Relations, P. O. Box 703, Elba, AL 36323. Any of the materials we file with the SEC may also be read and copied at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. Information on the operation of the SEC's Public Reference Room may be obtained by calling the SEC at 1.800.SEC.0330. Our periodic reports filed with the SEC, which include Forms 3, 4 and 5, Form 10-K, Form 10-Q, Form 8-K and any amendments thereto may also be accessed free of charge from the SEC's website at www.sec.gov.

Item 1A. Risk Factors

As a “Smaller Reporting Company,” we are not required to provide any disclosure under Item 1A. In providing these risk factors, we do not represent, and no inference should be drawn, that the disclosures so provided comply with all requirements of Item 1A if we were subject to them. Risk factors are events and uncertainties over which the Company has limited or no control and which can have a material adverse impact on our financial condition or results of operations. We are subject to a variety of risk factors. The following information sets forth our evaluation of the risk factors we deem to be most material. We work to actively manage these risks, but the reader should be cautioned that we are only able to mitigate the impact of most risk factors, not eliminate the risk. Also, there may be other risks which we do not presently deem material that may become material in the future.

Underwriting and product pricing

The insurance subsidiaries maintain underwriting departments that seek to evaluate the risks associated with the issuance of an insurance policy. NSIC accepts standard risks and, to an extent, substandard risks. In the case of the property and casualty subsidiaries, the underwriting staff attempts to assess, in light of the type of insurance sought by an applicant, the risks associated with a prospective insured or insurance situation. The underwriting assessment may involve various components in the risk evaluation process including, but not limited to, potential liability or fire hazards, age of dwelling, loss history, credit history of insured, employment status, location of fire department, home value, home heat source, and general maintenance of the property. In general, the property and casualty subsidiaries specialize in writing nonstandard risks.

The nonstandard market in which the property and casualty subsidiaries operate reacts to general economic conditions in much the same way as the standard market. When insurers' profits and equity are strong, companies sometimes cut rates or do not seek increases. Also, underwriting rules are less restrictive. As profit and/or capital fall, companies may tighten underwriting rules and seek rate increases. Premiums in the nonstandard market are higher than the standard market because of the increased risk, which generally comprises more frequent claims. Lower valued dwellings and mobile homes often warrant higher premiums because of the nature of the risk. The costs of placing such nonstandard policies and making risk determinations are similar to those of the standard market. The added costs due to more frequent claims servicing are reflected in the generally higher premiums that are charged.

Our ability to maintain profitability is contingent upon our ability to actively manage our rates and our underwriting procedures. Premium rate inadequacy may not become apparent quickly, and we will incur lag-time to correct. If our rates or underwriting processes become inadequate, our results of operations and financial condition could be adversely impacted.

Approval of rates

Most lines of business written by our property and casualty insurers are subject to prior approval of premium rates in the majority of the states in which we operate. The process of obtaining regulatory approval can be expensive and time consuming and can impair our ability to make necessary rate adjustments due to changes in loss experience, cost of reinsurance or other factors. If our requests to regulatory bodies for rate increases are not approved in an adequate or timely manner, our results of operations and financial condition may be adversely impacted.

Maintenance of profit margins and potential for margin compression

Our maximum long-term average pretax profit margin on most of our insurance products is approximately five to six percent. In most states, we have limited ability to increase our margins beyond this level for higher risk, and we can incur significant delays in our ability to pass along higher cost that we may incur. Examples of this risk include:

- Our catastrophe reinsurance cost is negotiated annually and effective January 1 of each year. The reinsurance market in which we operate is unregulated, and our reinsurance cost is based on negotiated rates that adjust annually. Due to increased frequency of storms over the past decade and cycles of limited reinsurance market capacity, we often experience rate increases in which we have limited ability to negotiate and often cannot include these increases in our rates until the new reinsurance agreement is negotiated. Due to increased cat loads in more storm prone areas, significant year over year increases in cat cost can often temporarily eliminate our profit margins in some areas and significantly compress our overall profit margins priced into our insurance coverages.
- We have a geographic concentration in the Southeastern U.S. which is exposed to significant hurricane risk. We believe that we are often not adequately compensated for certain heavily exposed risk through a combination of limits on allowable margin and regulatory delays in obtaining rate increases. We often have to manage these exposures using alternatives to pricing, such as limits on new business production, to help us manage exposure concentrations and protect our capital position.
- Due to increasing catastrophe reinsurance cost, we have incurred increases in our reinsurance retentions/deductibles over the past decade. Again, due to limits to profit margins, we are often not adequately compensated for the increased risk associated with these higher reinsurance retentions due to overall limits on margins in some of the states in which we operate.

Reinsurance, risk of loss from catastrophic event and geographic concentration

Both insurance subsidiaries customarily reinsure with other insurers certain portions of the insurance risk. The primary purpose of such reinsurance arrangements is to enable the Company to limit its risk on individual policies, and in the case of property insurance, limit its risk in the event of a catastrophe in various geographic areas. A reinsurance arrangement does not discharge the issuing company from primary liability to the insured, and the issuing company is required to discharge its liability to the insured even if the reinsurer is unable to meet its obligations under the reinsurance arrangements. Reinsurance, however, does make the reinsurer liable to the issuing company to the extent of any reinsurance in force at the time of the loss. Reinsurance arrangements also decrease premiums retained by the issuing company since that company pays the reinsuring company a portion of total premiums based upon the amount of liability reinsured. NSIC generally reinsures all risks in excess of $50,000 with respect to any one insured. NSFC and Omega generally reinsure with third-parties any liability in excess of $225,000 on any single policy. In addition, the property and casualty subsidiaries have catastrophe excess reinsurance, which provided protection in part with respect to aggregate property losses arising out of a single catastrophe, such as a hurricane.

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During 2015, the property and casualty segment maintained a catastrophe contract, which covered losses related to a catastrophic event with multiple policyholders affected. In the event a catastrophe exceeded the $4 million company retention stated in the contract, reinsurers would reimburse the company 100% of gross losses up to the upper limits of the reinsurance agreement, which was $72.5 million in 2015 and 2014. Any losses above the $72.5 million upper limit are the responsibility of our Company. The contract in place during 2015 also allowed one reinstatement for coverage under the contract for a second catastrophic event if needed. This reinsurance structure is expected to remain unchanged in 2016.

The property and casualty subsidiaries utilize our actual in force policy data modeled applying two different industry accepted catastrophe models to structure catastrophe reinsurance and determine upper limits of catastrophe reinsurance agreements. Based on modeling results utilized in 2015 and 2014, the Company was reinsured at approximately a 250 year event level. While this estimate is subject to some uncertainty and model risk, the models indicate that we maintain catastrophe reinsurance upper limits to cover an event that has less than a 0.5% probability of occurring in a given year.

Our inability to procure reinsurance, primarily catastrophe reinsurance, could adversely impact our ability to maintain our level of premium revenue. The increased frequency of catastrophic events also increases our cost of reinsurance pressuring the profit margins of our insurance products. It is generally cost prohibitive to maintain deductibles below levels currently in place. Our current $4 million catastrophe deductible will adversely impact underwriting results in years in which we incur losses from a major hurricane or tornado outbreak.

As described above, we maintain catastrophe reinsurance in amounts that provides protection to the Company's financial condition in all but the most remote likelihood of occurrences. Our most critical catastrophe risk is from hurricanes due to our proximity to the Atlantic Ocean and the Gulf of Mexico. Our results of operations are very likely to be materially impacted in the event of the landfall of a major hurricane striking the Northern Gulf Coast or Southern Atlantic Coast in Georgia or South Carolina where we maintain significant concentrations of business. We are also exposed to the risk of significant tornado activity in many of the states in which we operate. Our most significant catastrophic event risk is the risk of a loss in excess of the Company's upper catastrophe limit which could adversely impact the Company's financial condition if such an event occurs. We are also subject to assessments from windstorm underwriting pools in various states. These risks are often difficult to measure and in the event of a major catastrophe, could exceed the upper limits of our available reinsurance protection. We also face risk from a high frequency of catastrophe events. While these events may not reach the lower limits of our catastrophe reinsurance protection, a large number of smaller events can materially impact our results of operations.

Catastrophe modeling results play a major role in our decision making process regarding the upper limits of our catastrophe reinsurance protection. While the level of sophistication has increased significantly in recent years in the design of computer generated catastrophe modeling, there are risks inherent in the modeling process, and the process continues to evolve. We believe the chance of a catastrophe event exceeding the upper limits of our reinsurance protection is remote; however, with the unpredictability of natural disasters, we are unable to eliminate all risk of exceeding the upper limits of our reinsurance protection. Hurricane Katrina exceeded the upper limits of our coverage in 2005. We have since increased the upper limits of our coverage, but should a future event exceed the upper limits of our reinsurance coverage by a material amount, our financial condition could be adversely impacted.

Climate change
Some scientific evidence supports that there have been and continue to be significant changes in climate including temperature, precipitation and wind resulting from various natural factors, processes, and human activities. Rising temperatures and changes in weather patterns could impact storm frequency and severity in our coverage areas. Increases in storm frequency and severity could negatively impact reinsurance costs impacting product pricing and the areas in which we offer our products. With respect to our property and casualty segment, climate change may impact

the types of storms that impact our coverage areas as well as the frequency and severity of storms, thereby impacting reinsurance placement and rates. With respect to our life insurance segment, climate change may impact life expectancies, thereby influencing mortality assumptions used in pricing assumptions and reserve calculations. Climate change could impact future product offerings, exclusions and/or policy limitations.

The Company may be impacted by domestic legislation and regulation related to climate change. Governmental mandates could impede our ability to make a profit with our current product offerings, limit the products we can offer and/or impact the geographic locations in which we offer our products. The impact of climate change cannot be quantified at this time.

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Reserve liabilities
NSIC maintains life insurance reserves for future policy benefits to meet future obligations under outstanding policies. These reserves are calculated to be sufficient to meet policy and contract obligations as they arise. Liabilities for future policy benefits are calculated using assumptions for interest, mortality, morbidity, expense and withdrawals determined at the time the policies were issued. As of December 31, 2015, the total reserves of NSIC (consisting of reserves for accident and health insurance) were approximately $35,159,000. We believe, based on current available information, reserves for future policy benefits are adequate. However, we are currently in a period of persistent low interest rates, and should this period of low rates be sustained over the long term, it can impair our ability to make sufficient returns to cover future policy liabilities. Also, should actual mortality, morbidity, expense or withdrawal assumption differ materially from assumptions, our operating results could be negatively impacted.

The property and casualty subsidiaries are also required to maintain loss reserves (claim liabilities) for all lines of insurance. Such reserves are intended to cover the probable ultimate cost of settling all claims, including those incurred but not yet reported. The reserves of the property and casualty subsidiaries reflect estimates of the liability with respect to incurred claims and are determined by evaluating reported claims on an ongoing basis and by estimating liabilities for incurred but not reported claims. Such reserves include adjustment expenses to cover the cost of investigating losses and defending lawsuits. The establishment of accurate reserves is complicated by the fact that claims in some lines of insurance are settled many years after the policies have been issued, thus raising the possibility that inflation may have a significant effect on the amount of ultimate loss payment, especially when compared to initial loss estimates. The subsidiaries, however, attempt to restrict their writing to risks that settle within one to four years of issuance of the policy. As of December 31, 2015, the property and casualty subsidiaries had reserves for unpaid claims of approximately $9,645,000, before subtracting unpaid claims due from reinsurers of $1,380,000, leaving net unpaid claims of $8,265,000. The reserves are not discounted for the time value of money. No changes were made in the assumptions used in estimating the reserves during the years ending December 31, 2015 or 2014. The Company believes, based on current available information, such reserves are adequate to provide for settlement of claims.

We incur the risk that we may experience excessive losses due to unanticipated claims frequency, severity or both that may not be factored into our loss reserve liabilities. Unexpected frequency and severity can be adversely impacted by outcomes of claims litigation; adverse jury verdicts related to claims settlements and adverse interpretations of insurance policy provisions which result in increased liabilities. We are also subject to the risk of unanticipated assessments from state underwriting associations or windstorm pools related to losses in excess of the associations or pool's ability to pay. Such costs are often allocated to companies operating in the jurisdiction of the association or windstorm pool, and the likelihood and amount of such assessments are difficult to predict. These events could adversely impact our historical loss reserving methodology and cause financial adjustments that could materially impact our financial condition and results of operations.

Financial Ratings
The insurance subsidiaries are rated by the independent insurance rating agencies A.M. Best and Demotech. A downgrade in our ratings from either of these rating agencies could adversely impact our ability to maintain existing business or generate new business. See page 12 of this Form 10-K for additional information on our current financial ratings.

Regulation
The insurance subsidiaries are each subject to regulation by the insurance departments of those states in which they are licensed to conduct business. Although the extent of regulation varies from state to state, the insurance laws of the various states generally establish supervisory departments having broad administrative powers with respect to, among other matters: the granting and revocation of licenses to transact business, the licensing of agents, the establishment of standards of financial solvency (including reserves to be maintained), the nature of investments and in most cases

premium rates, the approval of forms and policies, and the form and content of financial statements. The primary purpose of these regulations is the protection of policyholders. Compliance with regulations does not necessarily confer a benefit upon shareholders.

Many states in which the insurance subsidiaries operate, including Alabama, have laws requiring that insurers become members of guaranty associations. These associations guarantee that benefits due policyholders of insurance companies will continue to be provided even if the insurance company which wrote the business is financially unable to fulfill its obligations. To provide these benefits, the associations assess the insurance companies licensed in a state that write the line of insurance for which coverage is guaranteed. The amount of an insurer's assessment is generally based on the relationship between that company's premium volume in the state and the premium volume of all companies writing the particular line of insurance in the state. The Company has paid no material amounts to guaranty associations over the past two years. These payments, when made, are principally related to association costs incurred due to the insolvency of various insurance companies. Future assessments depend on the number and magnitude of insurance company insolvencies, and such assessments are therefore difficult to predict.

Most states have enacted legislation or adopted administrative rules and regulations covering such matters as the acquisition of control of insurance companies, transactions between insurance companies and the persons controlling them. The National Association of Insurance Commissioners has recommended model legislation on these subjects, and all states where the Company's subsidiaries transact business have adopted, with some modifications, that model legislation. Among the matters regulated by such statutes are the payments of dividends. These regulations have a direct impact on the Company since its cash flow is substantially derived from dividends from its subsidiaries, and adverse operating results in the insurance subsidiaries or the development of significant additional obligations in the holding company could adversely impact liquidity at the holding company level. Statutory limitations of dividend payments by subsidiaries are disclosed in Note 12 of the accompanying Consolidated Financial Statements.

While most regulation is at the state level, the federal government has increasingly expressed an interest in regulating aspects of the insurance industry. All of these regulations at various levels of government increase the cost of conducting business through increased compliance expenses. Also, existing regulations are constantly evolving through administrative and court interpretations, and new regulations are often adopted. It is difficult to predict what impact changes in regulation may have on the Company in the future. Changes in regulations could occur that might adversely impact our ability to achieve acceptable levels of profitability and limit our growth.

Competition

The insurance subsidiaries are engaged in a highly competitive business and compete with many insurance companies of substantially greater financial resources, including stock and mutual insurance companies. Mutual insurance companies return profits, if any, to policyholders rather than shareholders; therefore, mutual insurance companies may be able to charge lower net premiums than those charged by stock insurers. Accordingly, stock insurers must attempt to achieve competitive premium rates through greater volume, efficiency of operations and control of expenses.

NSIC primarily markets its life and health insurance products through the home service system and independent producers. Direct competition comes from home service companies and other insurance companies that utilize independent producers to sell insurance products, of which there are many. NSIC's life and health products also compete with products sold by ordinary life companies. NSIC writes policies primarily in Alabama, Georgia and Mississippi. The market share of the total life and health premiums written is small because of the number of insurers in this highly competitive field. The primary methods of competition in the field are service and price.

Because of the increased costs associated with a home service company, premium rates are generally higher than ordinary products; as a result, competition from these ordinary insurers must be met through service. Initial costs of distribution through independent agents are generally more than through home service distribution methods, but lower commissions are paid in years subsequent to the first year of the policy so costs decline rapidly as policies renew after the first year. The primary factor in controlling cost under the independent agent distribution method is maintaining a high persistency rate. The persistency rate is the rate at which new business is maintained in renewal periods subsequent to the first year. If a high persistency rate can be maintained, the overall costs of distribution are lowered due to lower commission rate payments on policies in force subsequent to the first year.

The property and casualty subsidiaries market their products through independent agents and brokers, concentrating primarily on dwelling fire and homeowners coverage. NSFC, though one of the larger writers of lower value dwelling fire insurance in Alabama, nevertheless faces a number of competitors in this niche market. Moreover, larger general line insurers also compete with NSFC. The market share in states other than Alabama is small. Price is the primary method of competition. Because the Company utilizes independent agents, commission rates and service to the agent are also important factors in whether the independent agent agrees to offer NSFC products over those of its competitors. The Company primarily relies on an established independent agency force to market our insurance products. The loss of independent agents could adversely impact both the retention of existing business and production of new business.

Significant changes in the competitive environment in which we operate could materially impact our financial condition or results of operations.

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Inflation
The Company shares the same risks from inflation as other companies. Inflation causes operating expenses to increase and erodes the purchasing power of the Company's assets. A large portion of the Company's assets is invested in fixed maturity investments. The purchasing power of these investments will be less at maturity because of inflation. This is generally offset by the reserves that are a fixed liability and will be paid with cheaper dollars. Also, inflation tends to increase investment yields, which may reduce the impact of the increased operating expenses caused by inflation.

Investment Risk and Liquidity
Our invested assets are managed by company personnel. The majority of these investments consist of fixed maturity securities. These securities are subject to price fluctuations due to changes in interest rates, and unfavorable changes could materially reduce the market value of the Company's investment portfolio and adversely impact our financial condition and results of operations. Fixed maturity investments are managed in light of anticipated liquidity needs and duration of liabilities. Should we experience a significant change in liquidity needs for any reason, we may be forced to sell fixed maturity securities at a loss to cover these liquidity needs. Changes in general economic conditions, the stock market and various other external factors could also adversely impact the value of our investments and consequently our results of operations and financial condition.

Impact of economic and credit market conditions on our investments
Our investment portfolio is exposed to economic and financial market risks, including changes in interest rates, credit markets and prices of marketable equity and fixed-income securities. Events that unfolded in the latest recession had a material impact on the valuations of our investments. Economic and credit market conditions during the recession adversely affected the ability of some issuers of investment securities to repay their obligations and may further affect the values of investment securities. If the carrying value of our investments exceeds the fair value, and the decline in fair value is deemed to be other-than-temporary, we will be required to write down the value of our investments, which could adversely impact our results of operations and financial condition.

Litigation
We are routinely involved in litigation related to our insurance products. Litigation can involve claims for damages in excess of stated policy limits and include damages for bad faith. Defense of these claims can often be expensive adding to our loss adjustment expenses, and adverse jury verdicts could materially impact our results of operations and financial position.

Dependence of the Company on Dividends from Insurance Subsidiaries
The Company is an insurance holding company with no significant operations and limited outside sources of income. The primary asset of the Company is its stock in the insurance subsidiaries. The Company relies on dividends from the insurance subsidiaries in order to pay operating expenses, to service debt obligations and to provide liquidity for the payment of dividends to shareholders. The ability of the insurance subsidiaries to pay dividends is subject to regulatory restrictions discussed in detail in Note 12 of the Consolidated Financial Statements included herein. Should the insurance subsidiaries become subject to restrictions imposed by insurance regulations regarding the payment of dividends, the ability of the Company to pay expenses, meet debt service requirements and pay cash dividends to shareholders could be adversely impacted. Additionally, should business conditions deteriorate, we could be forced to further limit or suspend dividend payments in order to protect our capital position.

Low common stock trading volume and liquidity limitations
We are a small public company with a large percentage of common stock outstanding owned by founding family members, employees, officers and directors. Consequently, our average daily trading volume is very low with no shares traded on some days and only a few hundred shares trading in a typical day. This low trading volume can lead to significant volatility in our share price and limit a shareholders ability to dispose of large quantities of stock in a short period of time.

Debt covenants
Should we become unable to remain current on interest payments on our long-term debt, under our debt covenants, we would be forced to suspend the payment of dividends to stockholders until interest payments are current.

Technology
Our insurance subsidiaries are dependent on computer technology and internet based platforms in the delivery of insurance products. Our ability to innovate and manage technological change is a key to remaining competitive in the insurance industry. A breakdown in major systems or failure to maintain up-to-date technology could adversely impact

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our ability to write new business and service existing policyholders, which would adversely impact our results of operations and financial condition. The occurrence of computer viruses, information security breaches, disasters, or unanticipated events could affect the data processing systems of the Company or its service providers which could damage the Company's business and adversely affect our financial condition and results of operations.

Access to capital
We rely on debt and equity capital to operate. Due to a recent litigation settlement, our debt levels are higher than our historical norm. Adverse operating results, general market and economic conditions could impair our ability to raise new capital needed to support our operations.

Key Personnel
As a small company within the insurance industry, we could be adversely impacted by the loss of key personnel. Our ability to remain competitive is contingent upon our ability to attract and retain qualified personnel in all aspects of our operations.

Accounting Standards
Our financial statements are prepared based upon generally accepted accounting standards issued by the Financial Accounting Standards Board along with standards set by other regulatory organizations. We are required to adopt newly issued or revised accounting standards that are issued periodically. Future changes could impact accounting treatment applied to financial statements and could have a material adverse impact on the Company's results of operations and financial conditions. Potential changes in accounting standards that are currently expected to impact the Company are disclosed in the Notes to Financial Statements included herein.

Item 1B. Unresolved Staff Comments
As a smaller reporting company, the Company is not required to furnish the information required in Item 1B.

Item 2. Properties

Our principal executive offices, owned by NSIC, are located at 661 East Davis Street, Elba, Alabama. The executive offices are shared by the insurance subsidiaries. The building was constructed in 1977 with an addition added in 2008. The executive offices total approximately 30,700 square feet. The Company believes this space to be adequate for our immediate needs.

The Company and its subsidiaries own certain real estate investment properties. The Company owns approximately 211 acres of real estate in Coffee County in Alabama. We also own, through our subsidiary NSFC, approximately 85 acres of undeveloped commercial real estate in Greenville, Alabama. We sell undeveloped lots from this development, and the development has no depreciable improvements. The Company incurred impairment losses totaling $552,000 on investment real estate in 2014.

Capitalized along with the Greenville property are site preparation costs, including clearing, filling and leveling of land. There are no improvements such as paving, parking lots or fencing that would be recorded as land improvements and depreciated over the appropriate useful life.

Item 3. Legal Proceedings

The Company and its subsidiaries are named parties to litigation related to the conduct of their insurance operations. Further information regarding details of pending suits can be found in Note 16 to the Consolidated Financial Statements.

Item 4. Mine Safety Disclosures

This section is not applicable.

Part II

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

The capital stock of the Company is traded in the NASDAQ Global Market. Quotations are furnished by the National Association of Security Dealers Automated Quotations System (NASDAQ). The trade symbol is NSEC.

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The following table sets forth the high and low sales prices per share, as reported by NASDAQ, during the period indicated:

	Stock Closing Prices			
	2015		2014	
	High	Low	High	Low
First Quarter	$14.31	$12.82	$10.65	$7.95
Second Quarter	$16.32	$13.85	$12.57	$9.70
Third Quarter	$16.41	$12.51	$13.00	$10.53
Fourth Quarter	$15.16	$13.12	$15.25	$12.50

Shareholders

The number of shareholders of the Company's common stock was approximately 1,200, and the Company had 2,512,425 shares of common stock outstanding on March 18, 2016.

Dividends

The following table sets forth quarterly dividend payment information for the Company for the periods indicated:

	Dividends Per Share	
	2015	2014
First Quarter	$0.04	$0.03
Second Quarter	$0.04	$0.03
Third Quarter	$0.04	$0.03
Fourth Quarter	$0.04	$0.03

Discussion regarding dividend restrictions may be found on page 36 of the Managements' Discussion and Analysis as well as in Note 12 of the Consolidated Financial Statements.

The payment of shareholder dividends is subject to the discretion of our Board of Directors and is dependent upon many factors including our operating results, financial condition, capital requirements and general economic conditions. Total shareholder dividends paid in 2015 totaled $402,000.

Future dividends are dependent on future earnings, the Company's financial condition and other factors evaluated periodically by management and the Board of Directors. The Company is an insurance holding company and depends upon the dividends from the insurance subsidiaries to pay operating expenses and to provide liquidity for the payment of shareholder dividends. The payment of shareholder dividends is subject to the profitability of the insurance subsidiaries and the ability of the insurance subsidiaries to pay dividends to the holding company. Dividends from the insurance subsidiaries are subject to approval of the regulator in the state of domicile, the Alabama Department of Insurance.

Securities authorized for issuance under equity compensation plans

The Company currently only has one equity compensation plan which was approved by security holders at the 2009 Annual Shareholders Meeting. The following table sets forth securities authorized for issuance under the Company's equity compensations plans:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)

Equity compensation plans approved by security holders	—	—	154,175
Equity compensation plans not approved by security holders	—	—	—
Total	—	—	154,175

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Item 6. Selected Financial Data

Under smaller reporting company rules we are not required to disclose information required under Item 6. However, in order to provide information to our investors, we have elected to provide certain selected financial data.

Five-Year Financial Information (dollars in thousands, except per share)

Selected Financial Data:	2015	2014	2013	2012	2011
Net premiums earned	$59,462	$56,653	$52,366	$51,815	$56,243
Net investment income	3,462	3,823	3,746	4,191	4,261
Net realized investment gains	503	100	4,439	2,790	669
Other income	623	3,816	609	720	919
Total revenues	$64,050	$64,392	$61,160	$59,516	$62,092
Net income (loss)	$4,697	$7,616	$5,658	$(6,671)	$(4,956)
Net income (loss) per share	$1.87	$3.04	$2.28	$(2.70)	$(2.01)
Total shareholders' equity	$44,883	$42,757	$33,472	$30,227	$38,015
Book value per share	$17.87	$17.05	$13.42	$12.25	$15.41
Dividends per share	$0.16	$0.12	$0.100	$0.325	$0.550
Net change in unrealized capital gains (losses), net of tax	$(2,128)	$2,061	$(2,801)	$(101,000)	$1,258
Total assets	$148,099	$144,865	$133,980	$135,716	$132,951

Quarterly Information:	Premiums	Investment & Other Income	Realized Investment Gains (Losses)	Claims and Benefit Payments	Net Income (Loss)	Net Income (Loss) Per Share
2015						
First Quarter	$14,706	$1,132	$142	$8,262	$1,308	$0.52
Second Quarter	14,880	940	245	9,435	623	0.25
Third Quarter	15,104	868	130	8,170	1,616	0.64
Fourth Quarter	14,772	1,145	(14)	8,281	1,150	0.46
	$59,462	$4,085	$503	$34,148	$4,697	$1.87
2014						
First Quarter	$13,824	$1,102	$88	$7,864	$999	$0.40
Second Quarter	14,100	2,743	312	9,155	1,934	0.77
Third Quarter	14,374	982	141	7,172	1,797	0.72
Fourth Quarter	14,355	2,727	(441)	6,691	2,886	1.15
	$56,653	$7,554	$100	$30,882	$7,616	$3.04

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

Overview

The following discussion highlights significant factors influencing the consolidated financial position and results of operations of The National Security Group, Inc. (referred to in this document as we, our, us, the Company or NSEC) and its subsidiaries. We are a “smaller reporting company” under Securities and Exchange Commission (SEC) regulations and therefore qualify for the scaled disclosure of smaller reporting companies. In general, the same information is required to be disclosed in the management discussion and analysis by smaller reporting companies except that the discussion need only cover the latest two year period and disclosures relating to contractual obligations are not required. In accordance with the scaled disclosure requirements, this discussion covers the two year period ended December 31, 2015.

The National Security Group, Inc. is made up of two segments: the Life segment and the P&C segment. The Company's life, accident and health insurance business is conducted through National Security Insurance Company (NSIC), a wholly owned subsidiary of the Company organized in 1947. The Company's property and casualty insurance business

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is conducted through National Security Fire & Casualty Company (NSFC), a wholly owned subsidiary of the Company organized in 1959, and Omega One Insurance Company (Omega), a wholly owned subsidiary of National Security Fire & Casualty Company organized in 1992.

This discussion and analysis of the consolidated results of operations and financial condition of the Company should be read in conjunction with the Selected Financial Data and Consolidated Financial Statements and related notes included in this Form 10-K. Please refer to our note regarding forward-looking statements on pages 4-5 of this report. Information in this discussion is presented in whole dollars rounded to the nearest thousand. Tabular amounts are presented in thousands.

The National Security Group operates in the property and casualty and life, accident and supplemental health insurance businesses and markets products primarily through independent agents. The Company operates in ten states with 49.0% of total premium revenue generated in the states of Alabama and Mississippi. Property and casualty insurance is the most significant segment, accounting for 90.3% of gross earned premium revenue in 2015. Revenue generated from the life segment accounted for 9.7% of gross insurance premium revenue in 2015.

National Security Insurance Company (NSIC) is a life, accident and health insurance company founded in 1947. All references to NSIC in the remainder of this management discussion and analysis will refer to the combined life, accident and health insurance operations and will compose the life segment of the Company. NSIC is licensed to underwrite life and accident and health insurance in Alabama, Florida, Georgia, Mississippi, South Carolina, Tennessee and Texas.

The property and casualty segment consists of the consolidated operations of two subsidiaries, National Security Fire and Casualty Company and its wholly owned subsidiary, Omega One Insurance Company. There is no material differentiation between the products underwritten by NSFC and Omega as both underwrite primarily dwelling personal lines coverage. The Property and Casualty segment has premium in-force in the states of Alabama, Arkansas, Georgia, Louisiana, Mississippi, Oklahoma, South Carolina, and Tennessee.

All of the insurance subsidiaries are Alabama domiciled insurance companies; therefore, the Alabama Department of Insurance is the primary insurance regulator. However, each subsidiary is subject to regulation by the respective insurance regulators of each state in which it is licensed to transact business. Insurance rates charged by each of the insurance subsidiaries are typically reviewed and approved by each insurance department for the respective state in which the rates will apply.

All of our insurance companies have been assigned ratings by A.M. Best Co (Best). On February 10, 2016, Best affirmed the financial strength rating (FSR) of B++ (Good) and the issuer credit rating (ICR) of "bbb" of NSFC. In addition, Best affirmed the FSR of B+(Good) and ICR of "bbb-" of Omega and NSIC. The outlook for all of these ratings is stable. Best also affirmed the ICR of "bb" of the parent holding company, NSEC, with a stable outlook. The property and casualty subsidiaries have been assigned ratings by Demotech, Inc. On November 23, 2015, Demotech affirmed a Financial Stability Rating of A (Exceptional) for both NSFC and Omega.

The two primary segments in which we report insurance operations are the personal lines property and casualty segment (NSFC) and the life, accident and health insurance segment (NSIC). Due to Omega producing no earned premium revenue and the fact that Omega is a wholly owned subsidiary of NSFC authorized to underwrite similar lines of business, all references to NSFC in the remainder of this management discussion and analysis will include the insurance operations of both NSFC and Omega. Our income is principally derived from net underwriting profits and investment income. Net underwriting profit is principally derived from earned premiums received less claims paid, sales commissions to agents, costs of underwriting and insurance taxes and fees. Investment income includes interest and dividend income and gains and losses on investment holdings.

The property and casualty segment can be impacted by severe storm activity resulting in incurred losses and loss adjustment expenses primarily from tornado, wind and hail related damage. These storm systems or other natural disasters are classified as catastrophes (referred to as "cat events" or "catastrophe events" throughout the remainder of this document) by Property Claim Service (PCS) when these events cause $25 million or more in industry wide direct insured losses and affect a significant number of policyholders and insurers.

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Overview-Year Ended December 31, 2015 compared to Year Ended December 31, 2014

Summary:
For the year ended December 31, 2015, net income for the Company totaled $4,697,000 or $1.87 per share, compared to net income of $7,616,000, $3.04 per share, for the year ended December 31, 2014, a year over year decrease of $2,919,000. Results for 2014 were positively impacted by a gain on company owned life insurance (COLI) of $3,256,000. No COLI gain was realized in 2015. However, when comparing pretax income from operations, which excludes realized capital gains and gain on COLI (both of which can fluctuate significantly from period to period) along with income taxes, our 2015 results were comparable to our results from 2014. Pretax income from operations in 2015 totaled $5,844,000 compared to $6,019,000 in 2014. Pretax income from operations declined only $175,000 in 2015 despite a $2,724,000 year over year increase in catastrophe losses. Offsetting the increase in catastrophe claims was a 5% increase in net premium earned, driven by our P&C subsidiary, coupled with an 8.5% reduction in general and administrative expenses driven by cost reduction efforts in our life subsidiary.

Financial results for the year ended December 31, 2015 and 2014 were as follows:

Consolidated Financial Summary	Year ended December 31,	
(dollars in thousands)	2015	2014
Gross premiums written	$66,809	$65,453
Net premiums written	$60,389	$58,204
Net premiums earned	$59,462	$56,653
Net investment income	3,462	3,823
Net realized investment gains	503	100
Gain on company owned life insurance	—	3,256
Other income	623	560
Total Revenues	64,050	64,392
Policyholder benefits and settlement expenses	34,148	30,882
Amortization of deferred policy acquisition costs	3,510	3,590
Commissions	7,952	7,459
General and administrative expenses	8,628	9,428
Taxes, licenses and fees	2,086	2,137
Interest expense	1,379	1,521
Total Benefits, Losses and Expenses	57,703	55,017
Income Before Income Taxes	6,347	9,375
Income tax expense	1,650	1,759
Net Income	$4,697	$7,616
Income Per Common Share	$1.87	$3.04
Reconciliation of Net Income to non-GAAP Measurement		
Net income	$4,697	$7,616
Income tax expense	1,650	1,759
Realized investment gains, net	(503)	(100)
Gain on company owned life insurance	—	(3,256)
Pretax Income From Operations	$5,844	$6,019

Premium Revenue:
For the year ended December 31, 2015, net premiums earned were up $2,809,000 at $59,462,000 compared to $56,653,000 in 2014. The primary reasons for the increase were a 12.2% reduction in catastrophe reinsurance costs coupled with increases in gross earned premium. The increase in gross earned premium was due to growth in P&C

segment premium revenue of 3.6% in 2015 compared to 2014.

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Net Income:
For the year ended December 31, 2015, the Company had net income of $4,697,000, $1.87 per share, compared to net income of $7,616,000, $3.04 per share, for the same period in 2014, a decrease of $2,919,000. The primary reason for the decline in 2015 year to date earnings compared to 2014 was a $3,256,000 gain on company owned life insurance realized during 2014.

Pretax income from operations:
For the year ended December 31, 2015, pretax income from operations was $5,844,000 compared to $6,019,000 for the year ended December 31, 2014, a decrease of $175,000. The primary reason for the slight decline in pretax income from operations in 2015 compared to 2014 was an increase in catastrophe related claims in the P&C segment. The P&C segment was impacted by numerous non-hurricane catastrophe events in 2015, the most significant of which was an early October event in South Carolina which generated $1,575,000 in incurred catastrophe losses. In total, catastrophe losses increased policyholder benefits and settlements expenses by $5,373,000 in 2015. The P&C segment ended 2015 with a combined ratio of 91% with catastrophe losses contributing 10.1 percentage points to the combined ratio. In comparison, 2014 cat events added $2,629,000 to prior year policyholder benefits and settlement expenses. The P&C segment ended 2014 with a combined ratio of 87.4% with catastrophe losses contributing 5.2 percentage points to the combined ratio. Offsetting the negative impact of the cat events was an $865,000 decrease in catastrophe reinsurance cost coupled with a 3.6% increase in P&C segment gross earned premiums. Also, due to continued focus on cost reduction measures, we decreased general and administrative expenses by $800,000, primarily in the life insurance subsidiary.

Overview - Balance Sheet highlights at December 31, 2015 compared to December 31, 2014

Selected Balance Sheet Highlights (dollars in thousands)	December 31, 2015	December 31, 2014
Invested Assets	$112,557	$109,549
Cash	$6,763	$6,426
Total Assets	$148,099	$144,865
Policy Liabilities	$77,043	$74,115
Total Debt	$18,215	$19,572
Accumulated Other Comprehensive Income	$525	$2,772
Shareholders' Equity	$44,883	$42,757
Book Value Per Share	$17.87	$17.05

Invested Assets:
Invested assets as of December 31, 2015 were $112,557,000 up $3,008,000, or 2.7%, compared to December 31, 2014. The increase in invested assets was primarily due to $6,880,000 in cash flow from operating activities enabling additional investment in the fixed income investment portfolio.

Cash:
The Company, primarily through its insurance subsidiaries, had $6,763,000 in cash and cash equivalents at December 31, 2015, compared to $6,426,000 at December 31, 2014. Positive cash flow from insurance operations was the primary contributor to the increase in cash for the year ended December 31, 2015.

Total Assets:
Total assets as of December 31, 2015 were $148,099,000 compared to $144,865,000 at December 31, 2014. Positive cash flow from operations of $6,880,000, primarily generated by the P&C subsidiaries, was the primary contributor to the increase in invested assets and total assets at December 31, 2015.

Policy Liabilities:
Policy liabilities were $77,043,000 at December 31, 2015 compared to $74,115,000 at December 31, 2014; an increase of $2,928,000 or 4.0%. The primary reasons for the increase in policy liabilities in 2015 compared to the same period last year were a $1,324,000 increase in property and casualty loss reserves as well as a $999,000 increase in unearned premium reserves. Property and casualty loss reserves were up 15.9% in 2015 compared to 2014 primarily due to

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an increase in storm claims during the fourth quarter of 2015. Unearned premium was up 3.5% as a result of a moderate increase in P&C segment gross written premium.

Debt Outstanding:
Total debt at December 31, 2015 was $18,215,000 compared to $19,572,000 at December 31, 2014. Debt was reduced $1,357,000 during 2015 with the primary reason being the reduction of long term debt. The reduction of debt continues to be a primary focus of management.

Shareholders' Equity:
Shareholders' equity as of December 31, 2015 was $44,883,000 up $2,126,000 compared to December 31, 2014 Shareholders' equity of $42,757,000. Book value per share was $17.87 at December 31, 2015, compared to $17.05 per share at December 31, 2014, an increase of $0.82. The primary factor contributing to the increase in Shareholders' equity was net income of $4,697,000. In addition, shares issued to directors during 2015 totaled $78,000. Offsetting the increase in Shareholders' equity was a decrease in accumulated other comprehensive income of $2,247,000 and dividends paid of $402,000. The decline in accumulated other comprehensive income was primarily driven by interest rate related decreases in market values of available for sale investment securities primarily in our fixed income portfolio.

Industry Segment Data
Net earned premium revenues for The National Security Group's two operating segments (Life segment, Property and Casualty segment) are summarized as follows (amounts in thousands):

(dollars in thousands)	2015	%		2014	%	
Life, accident and health insurance	6,300	10.6	%	6,374	11.3	%
Property and casualty insurance	53,162	89.4	%	50,279	88.7	%
	$59,462	100.0	%	$56,653	100.0	%

The property and casualty segment composed 89.4% of total net earned premium revenue in 2015 compared to 88.7% in 2014. The P&C segment is primarily composed of dwelling fire and homeowners lines of business. The life segment composed 10.6% of net earned premium revenue in 2015 compared to 11.3% in 2014 with revenue produced from life, accident and supplemental health insurance products. While reading this discussion regarding segment information, reference is made to Note 15 to the Consolidated Financial Statements which provides additional segment related information.

The following discussion outlines more specific information with regard to the individual operating segments of the Company along with non-insurance related information (primarily administration expenses and interest expense) associated with the insurance holding company.

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Life and Accident and Health Insurance Operations:
From a revenue standpoint, our life segment is the smaller of our insurance segments contributing 10.6% of total insurance net earned premium revenue in 2015 and 11.3% in 2014. Premium revenues and operating income for the life segment for the year ended December 31, 2015 and 2014 are summarized below (amounts in thousands):

(dollars in thousands)	2015	2014
REVENUE		
Net premiums earned	$6,300	$6,374
Net investment income	1,913	1,925
Net realized investment gains	313	455
Other income	3	10
Total Revenues	8,529	8,764
BENEFITS AND EXPENSES		
Policyholder benefits paid or provided	4,687	5,403
Amortization of deferred policy acquisition costs	809	1,025
Commissions	380	356
General and administrative expenses	1,525	1,893
Insurance taxes, licenses and fees	180	311
Interest expense	61	66
Total Expenses	7,642	9,054
INCOME (LOSS) BEFORE INCOME TAXES	$887	$(290)

Year Ended December 31, 2015 Compared to Year Ended December 31, 2014:
Net earned premium revenue in the life segment was $6,300,000 at December 31, 2015 compared to $6,374,000 at December 31, 2014; a decrease of 1.2%. The $74,000 decrease in net earned premium revenue was primarily due to a decline in new business production in both the traditional life and supplemental accident and health insurance products offered in NSIC.

While NSIC composes only 10.6% of premium revenue, the segment makes up 38.5% of consolidated assets. The majority of these assets consist of fixed income investments. Due to the continued low interest rate environment, net investment income was down slightly at $1,913,000 for the year ended December 31, 2015 compared to $1,925,000 for the same period last year. Management believes the portfolio is well positioned to take advantage of a rising rate environment; however, continued low interest rates could lead to continued moderate declines in interest income.

NSIC ended 2015 with net realized investment gains of $313,000 compared to $455,000 for the same period in 2014. Realized investment gains are highly dependent on several factors including market conditions, tax position and liquidity needs of the Company and can vary significantly from period to period. The primary source of realized investment gains in both 2015 and 2014, were gains from the sale of fixed income and equity investments.

Claims were $4,687,000 through December 31, 2015 compared to $5,403,000 through December 31, 2014; a decrease of $716,000 or 13.3%. NSIC experienced a decrease in both ordinary life and industrial life related claims in 2015 compared to the same period last year.

Deferred policy acquisition cost amortization and commission expenses decreased $192,000 for the year ended December 31, 2015 at $1,189,000 compared to $1,381,000 for the same period in 2014; a decline of 13.9%. As a percent of net premiums earned, policy acquisition cost amortization and commission expense was 18.9% compared to 21.7% in 2014. A decline in the rate of new business production was the primary reason for the decline in policy acquisition costs.

General and administrative expenses were $1,525,000 in 2015 compared to $1,893,000 in 2014. Reduction of general and administrative expenses in NSIC has been a primary focus of management. Historically, general and administrative expenses in our life segment have run higher than industry averages due to the small size of the subsidiary. This disadvantage coupled with the persistent low interest rate environment has eroded earnings in the life segment. In the second half of 2014, management began the process of implementing significant operational changes that included the consolidation of P&C and life segment operations. This consolidation process is virtually complete and was the

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primary contributing factor to reductions in NSIC's general and administrative expenses as employees become cross trained and operational areas become more streamlined.

For the year ended December 31, 2015 and 2014, insurance taxes, licenses and fees were $180,000 and $311,000, respectively. As a percent of earned premium, insurance taxes, licenses and fees were 2.9% in 2015 and 4.9% in 2014. The primary reason for the increase in 2014 taxes, licenses and fees compared to 2015 were fees paid related to our periodic Alabama Department of Insurance examination which took place over most of the year in 2014.

For the year ended December 31, 2015, the life segment had pretax income of $887,000 compared to a pretax loss of $290,000 for the same period in 2014. The decrease in claims related expenses coupled with the reduction in general and administrative expenses were the primary contributors to the increase in pretax income.

Property & Casualty Operations:
Property and casualty operations constitute our largest segment composing 89.4% and 88.7% of our total consolidated premium revenue in 2015 and 2014, respectively. Premium revenues and operating income for the P&C segment for the year ended December 31, 2015 and 2014 are summarized below:

(dollars in thousands)	2015	2014
REVENUE		
Net premiums earned	$ 53,162	$ 50,279
Net investment income	1,473	1,737
Net realized investment gains (losses)	190	(356)
Gain on company owned life insurance	—	3,256
Other income	620	550
Total Revenues	55,445	55,466
BENEFITS AND EXPENSES		
Policyholder benefits paid or provided	29,461	25,479
Amortization of deferred policy acquisition costs	2,701	2,565
Commissions	7,572	7,103
General and administrative expenses	6,735	6,966
Insurance taxes, licenses and fees	1,906	1,826
Total Expenses	48,375	43,939
INCOME BEFORE INCOME TAXES	$ 7,070	$ 11,527

Year Ended December 31, 2015 Compared to Year Ended December 31, 2014:

Premium revenue in the P&C segment is primarily driven by our dwelling fire and homeowner lines of business. The following table provides premiums earned by line of business:

(dollars in thousands)	2015		2014		
Line of Business	Premium Earned	% of NPE	Premium Earned	% of NPE	2015 Increase (Decrease) over 2014
Dwelling Fire/Allied Lines	35,718	67.2 %	33,787	67.2 %	5.7 %
Homeowners	23,800	44.8 %	23,669	47.1 %	0.6 %