Federal Life Group, Inc.

A Pennsylvania Corporation

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I.R.S. Employer Identification No.: 82-4944172

QUARTERLY REPORT

FOR THE QUARTER ENDED JUNE 30, 2019

Title of each class of security	Trading Symbol(s)	Name of each exchange on which registered
Common stock, par value $.01	FLFG	OTC Pink Open Market

APPLICABLE TO CORPORATE ISSUERS:

As of August 14, 2019, there were 3,530,250 shares of the registrant’s common stock, $.01 par value, outstanding.

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FEDERAL LIFE GROUP, INC.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

	June 30, 2019 (unaudited)	December 31, 2018
Assets		
Investments:		
Fixed maturity securities available for sale, at fair value (amortized cost: 2019, $198,867; 2018, $187,035)	$ 207,416	$ 184,475
Equity securities, at fair value	2,300	6,004
Policy loans	9,238	9,581
Other invested assets	728	202
Total investments	219,682	200,262
Cash and cash equivalents	23,844	33,252
Real estate, property and equipment, net	2,118	2,130
Accrued investment income	1,977	1,908
Accounts receivable	2,093	498
Reinsurance recoverables	3,496	3,556
Prepaid reinsurance premiums	1,430	1,418
Deferred policy acquisition costs, net	11,938	13,533
Deferred sales inducement costs, net	1,439	1,348
Deferred tax asset, net	–	492
Other assets	663	511
Separate account asset	23,618	20,819
Total Assets	$ 292,298	$ 279,727
Liabilities		
Policy liabilities and accruals:		
Policyholder account balance	$ 119,234	$ 116,298
Future life policy benefits	71,145	71,992
Future accident and health policy benefits	339	345
Reserve for deposit type contracts	10,389	10,587
Other policyholder funds	1,026	1,398
Unearned revenue	1,343	1,367
Deferred reinsurance settlements	2,530	2,641
Deferred tax liability, net	1,041	–
Other liabilities	2,094	1,360
Separate account liability	23,618	20,819
Total Liabilities	232,759	226,807
Equity		
Common stock, par value $.01 per share, 4,010,250 shares authorized; issued and outstanding:		
2019 - 3,530,250		
2018 - 3,530,150	35	35
Additional paid-in capital	33,255	33,076
Retained earnings	21,404	21,774
Accumulated other comprehensive income (loss)	4,845	(1,965)
Total Equity	59,539	52,920
Total Liabilities and Equity	$ 292,298	$ 279,727

See accompanying notes to unaudited consolidated financial statements

FEDERAL LIFE GROUP, INC.

CONSOLIDATED STATEMENT OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(Dollars in thousands, except share and per share data)
(Unaudited)

	Three Months Ended June 30, 2019	Three Months Ended June 30, 2018	Six Months Ended June 30, 2019	Six Months Ended June 30, 2018
Revenues				
Insurance revenues	$ 2,040	$ 3,514	$ 4,160	$ 6,258
Net investment income	2,251	2,111	4,452	4,218
Net investment gains	79	234	653	324
Other revenues	45	48	71	97
Total Revenues	4,415	5,907	9,336	10,897
Benefits and expenses				
Policyholder benefits	2,611	3,923	4,565	7,018
Interest credit to policyholders	54	255	124	207
Operating costs and expenses	2,362	2,090	4,821	4,331
Amortization of deferred acquisition and sales inducement costs	564	523	935	897
Taxes, licenses and fees	199	201	388	398
Dividends to policyholders	12	13	30	31
Total Benefits and Expenses	5,802	7,005	10,863	12,882
Net loss before taxes	(1,387)	(1,098)	(1,527)	(1,985)
Tax expense	5	6	3	9
Net Loss	$ (1,392)	$ (1,104)	$ (1,530)	$ (1,994)
Other Comprehensive Income (Loss), net of tax:				
Unrealized holding gains (losses) arising during the period, net of tax	4,241	(1,816)	9,238	(6,663)
Adjustment to deferred acquisition costs, net of tax	(619)	235	(1,268)	817
Other Comprehensive Income (Loss)	3,622	(1,581)	7,970	(5,846)
Comprehensive Income (Loss)	$ 2,230	$ (2,685)	$ 6,440	$ (7,840)

Earnings per common share for the periods (Note 12):	**Three months ended June 30, 2019**	**Pro forma for the three months ended June 30, 2018**	**Six months ended June 30, 2019**	**Pro forma for the six months ended June 30, 2018**
Basic loss per common share	$ (0.39)	$ (0.31)	$ (0.43)	$ (0.56)
Diluted loss per common share	$ (0.39)	$ (0.31)	$ (0.43)	$ (0.56)

See accompanying notes to unaudited consolidated financial statements

FEDERAL LIFE GROUP, INC.

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(Dollars in thousands, except share and per share data)
(Unaudited)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
			(Dollars in thousands)			
Balance, March 31, 2019	3,530,250	$ 35	$ 33,110	$ 1,223	$ 22,796	$ 57,164
Net loss for the period	—	—	—	—	(1,392)	(1,392)
Paid in capital	—	—	145	—	—	145
Other comprehensive income	—	—	—	3,622	—	3,622
Balance, June 30, 2019	3,530,250	$ 35	$ 33,255	$ 4,845	$ 21,404	$ 59,539
Balance, March 31, 2018	—	$ —	$ —	$ 492	$ 25,710	$ 26,202
Net loss for the period	—	—	—	—	(1,104)	(1,104)
Other comprehensive loss	—	—	—	(1,581)	—	(1,581)
Balance, June 30, 2018	—	$ —	$ —	$ (1,089)	$ 24,606	$ 23,517
Balance, December 31, 2018	3,530,150	$ 35	$ 33,076	$ (1,965)	$ 21,774	$ 52,920
Net loss for the period	—	—	—	—	(1,530)	(1,530)
Paid in capital	100	—	179	—	—	179
Cumulative net effect of adoption of new accounting principle	—	—	—	(1,160)	1,160	—
Other comprehensive income	—	—	—	7,970	—	7,970
Balance, June 30, 2019	3,530,250	$ 35	$ 33,255	$ 4,845	$ 21,404	$ 59,539
Balance, December 31, 2017	—	$ —	$ —	$ 4,757	$ 26,600	$ 31,357
Net loss for the period	—	—	—	—	(1,994)	(1,994)
Other comprehensive loss	—	—	—	(5,846)	—	(5,846)
Balance, June 30, 2018	—	$ —	$ —	$ (1,089)	$ 24,606	$ 23,517

See accompanying notes to unaudited consolidated financial statements

FEDERAL LIFE GROUP, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

(Dollars in thousands)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Cash flows from operating activities:				
Net loss	$ (1,392)	$ (1,104)	$ (1,530)	$ (1,994)
Adjustments to reconcile net loss to net cash used in operating activities:				
Investment gains, net	(79)	(234)	(653)	(324)
Amortization on investments	(7)	(19)	(18)	(40)
Depreciation	47	69	94	137
Stock-based compensation	145	—	291	—
Deferred insurance acquisition costs	(428)	(505)	(910)	(1,011)
Deferred sales inducement costs	(50)	(102)	(126)	(201)
Interest and amortization of deferred acquisition and sales inducement costs	564	523	935	897
Change in value of derivatives and other	(119)	(5)	(433)	96
Change in accrued investment income	92	(17)	(70)	(42)
Change in receivables	(1,566)	(1,225)	(1,595)	(1,879)
Change in reinsurance recoverable	25	30	60	105
Change in prepaid reinsurance premiums	37	25	(12)	(21)
Change in policy benefits	(287)	1,547	(1,224)	1,401
Change in unearned revenue	—	6	(25)	(30)
Change in deferred reinsurance settlements	(34)	(48)	(111)	(123)
Change in other	527	232	469	277
Net cash used in operating activities	(2,525)	(827)	(4,858)	(2,752)
Cash flows from investing activities:				
Proceeds from investments sold or matured:				
Fixed maturity securities	2,840	2,583	6,608	8,197
Equity securities	1,575	261	4,402	261
Derivatives	120	78	197	206
Policy loans	250	32	344	134
Costs of investments purchased:				
Fixed maturity securities	(9,141)	(3,933)	(18,427)	(10,026)
Equity securities	—	(41)	(35)	(41)
Derivatives	(168)	(91)	(295)	(202)
Real estate additions	(45)	(42)	(46)	(61)
Purchase of property and equipment	(27)	(68)	(36)	(92)
Other assets	(1)	—	(1)	—
Net cash used in investing activities	(4,597)	(1,221)	(7,289)	(1,624)

See accompanying notes to unaudited consolidated financial statements

FEDERAL LIFE GROUP, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS (Continued)

(Dollars in thousands)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	**2018**	**2019**	**2018**
Cash flows from financing activities:				
Policyholder account balances:				
Deposits	$ 2,746	$ 3,929	$ 6,067	$ 8,388
Withdrawals	(1,622)	(1,767)	(3,329)	(4,184)
Net proceeds received from issuance of shares of common stock	—	—	1	—
Net cash provided by financing activities	1,124	2,162	2,739	4,204
Net increase (decrease) in cash	(5,998)	114	(9,408)	(172)
Cash, beginning of period	29,842	3,799	33,252	4,085
Cash, end of period	$ 23,844	$ 3,913	$ 23,844	$ 3,913
Supplemental disclosures of cash flow information				
Supplemental non-cash activity:				
Deferral of sales inducements	$ 50	$ 102	$ 126	$ 201

See accompanying notes to unaudited consolidated financial statements

FEDERAL LIFE GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2019
(Unaudited)

1. Organization and Basis of Presentation

Federal Life Group, Inc. ("FLG", "we", "us", "our" or the "Company") is a Pennsylvania corporation organized to be the stock holding company for Federal Life Mutual Holding Company and its subsidiaries (the "Predecessor") following the conversion of Federal Life Mutual Holding Company from mutual to stock form on December 11, 2018 (the "Conversion"). As part of the Conversion, FLG issued 3,530,150 shares of common stock at $10.00 per share for gross proceeds of $35.3 million in its initial public offering (the "IPO"). Federal Life Mutual Holding Company was subsequently renamed Federal Life Holding Company. FLG's primary assets are the outstanding capital stock of the Predecessor and a portion of the net proceeds of the IPO. Prior to the Conversion, FLG was not engaged in any significant operations, did not have any assets or liabilities, and was a direct, wholly-owned subsidiary of the Predecessor. Following the Conversion, the Company reorganized its corporate structure so that the Predecessor is a direct, wholly-owned subsidiary of FLG. FLG now contains the accounts of its Predecessor and those accounts are consolidated with those of FLG within the accompanying financial statements. The reorganization is considered a transaction between entities that are under common control. As a result, the consolidated financial statements prior to the IPO and the reorganization have been presented at their historical amounts.

The accompanying consolidated financial statements include the accounts of FLG and its subsidiaries, Federal Life Holding Company; FEDHO Holding Company ("FEDHO"); Federal Life Insurance Company ("Federal Life"); FED Mutual Financial Services, Inc. ("FED Mutual"); and Americana Realty Company ("Americana"). Additionally, the IPO described above resulted in a change in control according to Business Combinations (Topic 805), however, the Company elected not to apply push down accounting. Accordingly, the consolidated financial statements are presented at the Company's historical carrying amounts. All intercompany transactions and balances have been eliminated in consolidation.

Federal Life, a subsidiary of Federal Life Holding Company, completed a reorganization in 2016 in which it converted from a mutual to a stock insurance company within a newly created mutual holding company structure. As part of this reorganization, Federal Life Mutual Holding Company was formed as an Illinois mutual insurance holding company and Federal Life continued its existence as an Illinois stock life insurance company. All of the shares of Federal Life were issued to FEDHO, an intermediate holding company that, in turn, is a wholly-owned subsidiary of the Federal Life Holding Company. Federal Life has two wholly-owned non-insurance subsidiaries, Americana and FED Mutual, discussed further below.

Federal Life's in force business is primarily comprised of traditional life policies (term insurance, whole life insurance, non-medical health insurance, and group life insurance), interest sensitive contracts, and fixed deferred annuity contracts. Federal Life primarily sells its interest sensitive life, whole life, term life, fixed and indexed annuities through a network of independent agents. Federal Life is licensed to sell new business in the District of Columbia and all states except Maine, Massachusetts, New Hampshire, New York and Vermont. Although Federal Life is licensed to sell products in 45 states, its primary markets are Illinois, Michigan, Ohio, California, Florida, Texas, and Wisconsin.

Americana owns mineral rights in Arkansas, Georgia, Oklahoma and Texas. Americana earns royalty revenues from energy producers that are under agreement to drill for and produce oil and gas products on properties where Americana owns mineral rights.

FED Mutual is a FINRA licensed broker/dealer that was established to distribute Federal Life's variable annuity products.

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information. Accordingly, they do not include all the information and notes required by GAAP for complete financial statements. The consolidated financial statements reflect all adjustments, consisting only of normal recurring items, which are necessary to present fairly our financial position and results of operations on a basis consistent with the prior audited consolidated financial statements. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in our Annual Report for the year ended December 31, 2018 (the "2018 Annual Report"), which is available on our website at ir.federallife.com. Operating results for the three and six month periods ended June 30, 2019 are not necessarily indicative of the results that may be expected for the year ended December 31, 2019. The interim consolidated financial statements and accompanying notes presented herein for the periods ended June 30, 2019 and 2018 are unaudited. The December 31, 2018 consolidated balance sheet data was derived from audited consolidated financial statements for the year ended December 31, 2018, which include all disclosures required by GAAP.

For further information related to a description of areas of judgement and estimates and other information necessary to understand our financial position and results of operations, refer to the audited consolidated financial statements and notes included in our 2018 Annual Report.

Investor Information

Investor related information, including periodic reports filed with the OTC Markets, may be found on our website at ir.federallife.com as soon as reasonably practicable after such reports are filed on otciq.com. In addition, we have available on our website our: (i) compliance reporting policy; (ii) code of ethics; (iii) audit committee charter; (iv) compensation committee charter and (v) nominating committee charter.

Reclassifications

Certain prior period amounts have been reclassified for consistency with the current period presentation. An adjustment has been made to the Consolidated Statements of Cash Flows for the three and six month periods ended June 30, 2018, to reclassify the full amount of Other Investing Activities to Deferred Insurance Acquisition Costs and Change in Value of Derivatives and Other. These reclassifications had no effect on the reported results of operations.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to adopt accounting policies and make estimates and assumptions that affect amounts reported in the consolidated financial statements. The most significant estimates include those used in determining the capitalization and amortization of deferred policy acquisition costs (“DAC”), the valuation of investments, future policy benefits (traditional life contracts, immediate annuities, supplemental contracts with life contingencies, and accident and health), the fair value of stock-based compensation awards, and the provision for income taxes. Actual results could differ from those estimates.

Emerging Growth Company

Effective April 15, 2019, the Company voluntarily delisted its common stock from the Nasdaq Capital Market, thereby terminating its obligation to file reports with the U.S. Securities and Exchange Commission (“SEC”) under Section 12(b) of the Securities Exchange Act of 1934 (the “Exchange Act”). Subsequently, on May 28, 2019, the Company filed a Form 15 with the SEC to voluntarily suspend its duty to file reports under Section 15(d) of the Exchange Act. FLG was previously considered an “emerging growth company”, as defined in the Jumpstart Our Business Startups Act of 2012 (the “Jobs Act”), which allowed the Company to utilize extended transition periods for compliance with new or revised accounting standards in relation to financial information publicly filed with the SEC. As FLG is no longer required to file reports with the SEC, the Company is no longer considered an emerging growth company for financial reporting purposes. Accordingly, the Company has retrospectively adopted certain accounting pronouncements based on this status change, as further described in Note 3.

Investments

Realized capital gains and losses on sales of investments include fixed maturity securities with calls and prepayments and are determined on the basis of specific security identification.

Equity securities are carried at fair value. Beginning with the adoption of Accounting Standards Update (“ASU”) No. 2016-01 on January 1, 2019, changes in the fair value of equity securities are recognized through net income. Prior to January 1, 2019, unrealized gains or losses were recorded in accumulated other comprehensive income (loss) (“AOCI”). Additionally, in connection with the adoption of ASU No. 2016-01, effective January 1, 2019, the Company has reclassified its investment in Federal Home Loan Bank (“FHLB”) common stock from equity securities to other invested assets. These investments are carried at redemption value. The carrying value of these investments at December 31, 2018 was $10,000.

3. Recent Accounting Pronouncements

Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued an ASU 2014-09 “Revenue from Contracts with Customers,” related to revenue arising from contracts with customers. This ASU, which replaces most current revenue recognition guidance, including industry specific guidance, prescribes that an entity should recognize revenue to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. We adopted this ASU on January 1, 2019. The adoption of this ASU had no impact on our consolidated financial statements as revenues related to insurance contracts and investment contracts are excluded from its scope.

In January 2016, the FASB issued ASU No. 2016-01 “Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities,” which revises an entity’s accounting related to the classification and measurement of certain equity investments and the presentation of certain fair value changes for financial liabilities measured at fair value. The guidance also amends certain disclosure requirements associated with the fair value of financial instruments. We adopted this guidance effective January 1, 2019 with no material impact to our consolidated financial statements. Changes in fair value of equity securities, previously recognized through other comprehensive income (loss), are now recognized in net investment gains. We also recorded a cumulative effect adjustment to increase retained earnings by $1,160,000, net of tax, as of January 1, 2019 for unrealized gains previously recognized in AOCI. For additional information, please see Note 7.

In February 2016, the FASB issued ASU No. 2016-02 “Leases”, that will require recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. This ASU affects accounting and disclosure more dramatically for lessees as accounting for lessors is mainly unchanged. We retrospectively adopted this ASU as of January 1, 2019 in accordance with our changed emerging growth company status (see Note 2). The adoption of this ASU had no impact on our financial statements as we do not have any leases.

In March 2016, the Financial Accounting Standards Board (the “FASB”) issued ASU No. 2016-09, “Compensation - Stock Compensation”: Improvements to Employee Shared-Based Payment Accounting. The aspects of accounting guidance affected by this ASU are income taxes, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This ASU was effective for annual reporting periods beginning after December 15, 2017. The Company adopted this ASU in the fourth quarter of fiscal 2018 upon the issuance of restricted stock and stock options to our employees. The adoption of the ASU did not have an impact on our financial statements as we did not previously have stock compensation. The Company has elected to account for forfeitures when they occur.

In March 2017, the FASB issued ASU No. 2017-08, “Receivables – Nonrefundable Fees and Other Costs: Premium Amortization of Purchased Callable Debt Securities,” which requires that certain premiums on callable debt securities be amortized to the earliest call date. ASU No. 2017-08 was effective for annual periods beginning after December 15, 2018. We retrospectively adopted this ASU as of January 1, 2019 in accordance with our changed emerging growth company status (see Note 2). The adoption of ASU No. 2017-08 did not have a material impact on the Company’s consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12, “Derivatives and Hedging – Targeted Improvements to Accounting for Hedging Activities,” which changes the recognition and presentation requirements of hedge accounting. ASU No. 2017-12 was effective for annual periods beginning after December 15, 2018. We retrospectively adopted this ASU as of January 1, 2019 in accordance with our changed emerging growth company status (see Note 2). The adoption of ASU No. 2017-12 did not have a material impact on the Company’s consolidated financial statements because the Company does not apply hedge accounting.

In February 2018, the FASB issued ASU No. 2018-02, “Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,” which provides an option to reclassify stranded tax effects within AOCI to retained earnings in each period in which the effect of the change in the U.S. federal corporate income tax rate described in the “Income Tax Reform” section below is recorded. ASU No. 2018-02 is effective for fiscal years beginning after December 15, 2018 and should be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the Tax Act is recognized. The Company early adopted ASU No. 2018-02 effective December 31, 2017 using the portfolio method, which resulted in the reclassification of $805,000 of stranded tax effects from AOCI to retained earnings within the Company’s consolidated financial statements.

Issued Accounting Pronouncements Not Yet Adopted

In June 2016, the FASB issued ASU No. 2016-13 “Financial Instruments – Credit Losses: Measurement of Credit Losses of Financial Instruments,” which provides a new current expected credit loss model to account for credit losses on certain financial assets and off-balance sheet exposure. The model requires an entity to estimate lifetime credit losses related to such assets and exposure based on relevant information about past events, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. The guidance also modifies the current other-than- temporary impairment guidance for available-for-sale debt securities to require the use of an allowance rather than a direct write down of the investment and replaces existing guidance for purchased credit deteriorated loans and debt securities. ASU No. 2016-13 is currently effective for annual reporting periods beginning after December 15, 2020 with early adoption permitted for annual periods beginning after December 15, 2018. On July 17, 2019, the FASB tentatively decided to extend the effective date of this ASU by one year for public business entities that are non-SEC filers. The FASB intends to release an exposure draft, which if adopted, will change the effective date for the Company to January 1, 2022. The Company is currently assessing the impact of the guidance on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-12, “Targeted Improvements to the Accounting for Long – Duration Contracts,” which revises certain aspects of the measurement models and disclosure requirements for long duration insurance and investment contracts. The FASB’s objective in issuing this ASU is to improve, simplify, and enhance the accounting for long-duration contracts. The revisions include updating cash flow assumptions in the calculation of the liability for traditional life products, introducing the term ‘market risk benefit’ (“MRB”) and requiring all contract features meeting the definition of an MRB to be measured at fair value, simplifying the method used to amortize DAC and deferred sales inducement costs (“DSIC”) to a constant basis over the expected term of the related contracts rather than based on gross profits and enhancing disclosure requirements. ASU No. 2018-12 is effective on January 1, 2021, the transition date (the remeasurement date) is January 1, 2019. Early adoption of this ASU is permitted. The Company is currently assessing the impact of the guidance on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-13, “Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement.” This update modifies the disclosure requirements for fair value measurements in ASC Topic 820 Fair Value Measurement. Specific fair value measurement disclosure requirements are removed, modified, or added. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The Company is currently evaluating this guidance. However, it will not impact our earnings or financial position as the modifications only impact disclosures.

In November 2018, the FASB issued ASU No. 2018-19, “Codification Improvements to Topic 326, Financial Instruments – Credit Losses.” The amendments in this update include items brought to the Board’s attention by stakeholders to clarify the guidance in the amendments in ASU 2016-13, “Financial Instruments – Credit Losses” (Topic 326) which was issued in June 2016. The amendments of this update clarify that receivables arising from operating leases are not within the scope of Subtopic 326-20. Under ASU 2016-13, this replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to perform credit loss estimates. This update changes the methodology from an incurred loss to an expected credit loss. An allowance for the expected credit loss will be set up and the net income will be impacted. The credit losses will be evaluated in the current period and an adjustment to the allowance can be made. The effective date will be the same as the effective date in ASU 2016-13. The Company is currently assessing the impact of the guidance on its consolidated financial statements.

In May 2019, the FASB issued ASU No 2019-04, which clarifies certain aspects of accounting for credit losses, hedging activities, and financial instruments. The ASU’s amendments apply to all entities within the scope of the affected guidance. Accrued interest - Amortized cost basis is defined in ASU 2016-13 as "the amount at which a financing receivable or investment is originated or acquired, adjusted for applicable accrued interest, accretion or amortization of premium, discount, and net deferred fees or costs, collection of cash, write-offs, foreign exchange, and fair value hedge accounting adjustments" (emphasis added). To address stakeholders’ concerns that the inclusion of accrued interest in the definition of amortized cost basis could make application of the credit loss guidance operationally burdensome, ASU 2019-04 provides certain alternatives for the measurement of the allowance for credit losses (ALL) on accrued interest receivable (AIR). These measurement alternatives include (1) measuring an ALL on AIR separately, (2) electing to provide separate disclosure of the AIR component of amortized cost as a practical expedient, and (3) making accounting policy elections to simplify certain aspects of the presentation and measurement of such AIR. ASU 2019-04’s amendments should be applied "on a modified-retrospective basis by means of a cumulative-effect adjustment to the opening retained earnings balance in the statement of financial position as of the date an entity adopted the amendments in ASU 2016-13." Certain disclosures are also required. The effective date will be the same as the effective date in ASU 2016-13. The Company is currently assessing the methods and impact of adopting this new standard on our consolidated financial statements.

In May 2019, the FASB issued ASU No. 2019-05, which amends ASU 2016-13 to allow companies to irrevocably elect, upon adoption of ASU 2016-13, the fair value option on financial instruments that (1) were previously recorded at amortized cost and (2) are within the scope of ASC 326-203, if the instruments are eligible for the fair value option under ASC 825-10. The fair value option election does not apply to held-to-maturity debt securities. Entities are required to make this election on an instrument-by-instrument basis. ASU 2019-05’s amendments should be applied "on a modified-retrospective basis by means of a cumulative-effect adjustment to the opening balance of retained earnings balance in the statement of financial position as of the date that an entity adopted the amendments in ASU 2016-13." Certain disclosures are required. The effective date will be the same as the effective date in ASU 2016-13. The Company is currently assessing the methods and impact of adopting this new standard on our consolidated financial statements.

All other new accounting standards and updates of existing standards issued through the date of this filing were considered by management and did not relate to accounting policies and procedures pertinent to us at this time or were not expected to have a material impact to the consolidated financial statements.

4. Investments and Related Income

The Company's principal investments are in fixed income securities, equity securities, and policy loans.

The following table presents the amortized cost, gross unrealized gains (losses) and fair value of the Company's fixed maturity securities as of June 30, 2019 and December 31, 2018. Equity securities were removed from this table upon adoption of ASU No. 2016-01 at January 1, 2019.

	June 30, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. government	$ 2,201	$ 152	$ —	$ 2,353
States, political subdivisions, other	38,094	1,251	(18)	39,327
Corporate	111,503	4,652	(195)	115,960
Residential mortgage-backed securities	41,507	2,430	—	43,937
Commercial mortgage-backed securities	5,562	277	—	5,839
Total fixed maturity securities	$ 198,867	$ 8,762	$ (213)	$ 207,416

	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. government	$ 4,063	$ 142	$ (148)	$ 4,057
States, political subdivisions, other	30,881	472	(364)	30,989
Corporate	108,664	617	(2,995)	106,286
Residential mortgage-backed securities	37,755	455	(688)	37,522
Commercial mortgage-backed securities	5,672	73	(124)	5,621
Total fixed maturity securities	187,035	1,759	(4,319)	184,475
Equity securities	4,514	1,528	(38)	6,004
Total fixed maturity and equity securities	$ 191,549	$ 3,287	$ (4,357)	$ 190,479

The scheduled maturities for fixed income securities as of June 30, 2019 and December 31, 2018 are as follows:

	June 30, 2019		December 31, 2018	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)			
Due in one year or less	$ 7,446	$ 7,539	$ 5,998	$ 6,041
Due after one year through five years	35,023	36,292	37,917	38,032
Due after five years through ten years	76,757	80,290	74,274	72,209
Due after ten years	32,572	33,519	25,419	25,050
Mortgage-backed securities	47,069	49,776	43,427	43,143
Total	$ 198,867	$ 207,416	$ 187,035	$ 184,475

Actual maturities may differ from those scheduled as a result of prepayments by the issuers. Because of the potential for prepayment on mortgage-backed securities, they are not categorized by contractual maturity.

The following table presents the sources of investment proceeds and the related gross realized investment gains (losses) for the three and six month periods ended June 30, 2019 and June 30, 2018, respectively:

	Three Months Ended June 30, 2019			Six Months Ended June 30, 2019		
	Fixed Maturities	Equity Securities	Derivative Instruments	Fixed Maturities	Equity Securities	Derivative Instruments
	(Dollars in thousands)					
Proceeds from sales or maturities	$ 2,840	$ 1,575	$ 120	$ 6,608	$ 4,402	$ 197
Gross gains from sales or maturities	11	496	29	22	1,211	136
Gross losses from sales or maturities	(25)	—	—	(27)	(12)	(140)

	Three Months Ended June 30, 2018			Six Months Ended June 30, 2018		
	Fixed Maturities	Equity Securities	Derivative Instruments	Fixed Maturities	Equity Securities	Derivative Instruments
	(Dollars in thousands)					
Proceeds from sales or maturities	$ 2,583	$ 261	$ 78	$ 8,197	$ 261	$ 206
Gross gains from sales or maturities	27	261	113	75	261	339
Other-than-temporary-impairment (OTTI) losses	(89)	—	—	(89)	—	—
Gross losses from sales or maturities	(6)	—	(72)	(39)	—	(223)

There was $0.4 million and $0.5 million of unrealized losses on equity securities in net investment gains recognized for the three month and sixth month periods ended June 30, 2019, respectively. Of the amount recognized for the six month period ended June 30, 2019, $105,000 was recognized in the first quarter 2019, in accordance with the adoption of ASU 2016-01.

For the three and six month periods ended June 30, 2019, the Company did not recognize any impairment losses. For the three and six month periods ended June 30, 2018, the Company recognized $0.1 million in impairment losses.

The Company has a comprehensive portfolio monitoring process to identify and evaluate each fixed income and equity security whose carrying value may be other-than-temporarily impaired.

For each fixed income security in an unrealized loss position, the Company assesses whether management with the appropriate authority has made a decision to sell or whether it is probable that the Company will be required to sell the security before recovery of the amortized cost basis for reasons such as liquidity, contractual or regulatory purposes. If a security meets any of these criteria, the security's decline in fair value is deemed other than temporary and is recorded in earnings.

If the Company has not made the decision to sell the fixed income security and it is not more likely than not that the Company will be required to sell the fixed income security before recovery of its amortized cost basis, the Company evaluates if it expects to receive cash flows sufficient to recover the entire amortized cost basis of the security by comparing the estimated recovery value calculated by discounting the best estimate of future cash flows at the security's original or current effective rate, as appropriate, with the amortized cost of the security. If the Company does not expect to receive cash flows sufficient to recover the entire amortized cost basis of the fixed income security, the credit loss component of the impairment is recorded in earnings, with the remaining amount of the unrealized loss deemed to be related to other factors and recognized in AOCI.

The Company's portfolio monitoring process includes a quarterly review of all securities through a screening process which identifies instances where the fair value compared to amortized cost for fixed income securities and cost for equity securities is below established thresholds, and also includes the monitoring of other criteria such as ratings, ratings downgrades or payment defaults. The securities identified, in addition to other securities for which the Company may have a concern, are evaluated for potential other-than-temporary impairment using all reasonably available information relevant to the collectability or recovery of the security. Inherent in the Company's evaluation of other-than-temporary impairment for these fixed income and equity securities are assumptions and estimates about the financial condition of the issue or issuer and its future earnings potential. Some of the factors considered in evaluating whether a decline in fair value is other than temporary are: 1) the length of time and extent to which the fair value has been less than amortized cost for fixed income securities, or cost for equity securities; 2) the financial condition, near-term and long-term prospects of the issue or issuer, including relevant industry specific market conditions and trends, geographic location and implications of rating agency actions and offering prices; and 3) the specific reasons that a security is in a significant unrealized loss position, including overall market conditions which could affect liquidity.

The following table shows the fair value and gross unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2019 and December 31, 2018. Equity securities were removed from this table upon adoption of ASU No. 2016-01 at January 1, 2019.

June 30, 2019	Less than 12 months		12 months or longer		Total	
Description of securities	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
	(Dollars in thousands)					
U.S. government	$ —	$ —	$ —	$ —	$ —	$ —
States, political subdivisions, other	3,139	(18)	—	—	3,139	(18)
Corporate	1,065	(1)	5,727	(194)	6,792	(195)
Residential mortgage-backed securities	—	—	—	—	—	—
Commercial mortgage-backed securities	1	—	—	—	1	—
Total	$ 4,205	$ (19)	$ 5,727	$ (194)	$ 9,932	$ (213)

December 31, 2018	Less than 12 months		12 months or longer		Total	
Description of securities	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
	(Dollars in thousands)					
U.S. government	$ —	$ —	$ 2,907	$ (148)	$ 2,907	$ (148)
States, political subdivisions, other	6,106	(103)	9,339	(261)	15,445	(364)
Corporate	49,193	(1,886)	14,228	(1,109)	63,421	(2,995)
Residential mortgage-backed securities	9,401	(158)	13,065	(530)	22,466	(688)
Commercial mortgage-backed securities	2,003	(45)	1,502	(79)	3,505	(124)
Equity securities	379	(38)	—	—	379	(38)
Total	$ 67,082	$ (2,230)	$ 41,041	$ (2,127)	$ 108,123	$ (4,357)

It is not more likely than not that the Company will be required to sell these investments before recovery of their amortized cost bases, which may be maturity.

Net Investment Income

Net investment income for the three and six month periods ended June 30, 2019 and June 30, 2018, respectively, is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(Dollars in thousands)			
Fixed maturity securities	$ 1,908	$ 1,820	$ 3,743	$ 3,689
Equity securities	32	45	63	82
Real estate	27	35	53	72
Cash equivalents	121	11	274	19
Policy loans	170	180	344	356
Other	120	145	248	285
Subtotal	2,378	2,236	4,725	4,503
Investment expense	(127)	(125)	(273)	(285)
Net investment income	$ 2,251	$ 2,111	$ 4,452	$ 4,218

Unrealized Capital Gains (Losses)

The following table shows the unrealized net capital gains and losses included in AOCI at June 30, 2019 and December 31, 2018. Equity securities were removed from this table upon adoption of ASU No. 2016-01 at January 1, 2019.

	June 30, 2019			
	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Net Unrealized Gain (Loss)
	(Dollars in thousands)			
Fixed income securities	$ 207,416	$ 8,762	$ (213)	$ 8,549
Net unrealized capital gains				$ 8,549

	December 31, 2018			
	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Net Unrealized Gain (Loss)
	(Dollars in thousands)			
Fixed income securities	$ 184,475	$ 1,759	$ (4,319)	$ (2,560)
Equity securities	6,004	1,528	(38)	1,490
Net unrealized capital gains				$ (1,070)

At June 30, 2019 and December 31, 2018, securities with a market value of approximately $3.2 million and $4.5 million, respectively, were on deposit with governmental agencies as required by State Insurance Departments. The reason for the decrease in the market value of securities held on deposit is that effective June 2019, Federal Life Holding Company is no longer required to hold a security on deposit with the Illinois Department of Insurance.

Credit Risk

The Company generally strives to maintain a diversified invested asset portfolio but is exposed to credit and other types of risks related to its holding in fixed income and equity securities. Such risk may be related to individual companies, sectors, or entire asset classes. The Company manages this risk by holding a diversified portfolio of securities and sectors and by limiting the amount of exposure to a single issuer of credit. For June 30, 2019 and December 31, 2018, approximately 24% and 23%, respectively, of the Company’s investments in fixed maturities were invested in commercial and residential mortgage-backed securities and approximately 55% and 57% in corporate bonds. Approximately 5% of the fixed income maturities were rated below investment grade. There is certain concentration risk from investments in companies that are engaged in similar activities and have similar economic characteristics. The largest corporate bond sector exposures at June 30, 2019 are consumer non-cyclical consisting of 10% of the total fixed income portfolio, banks 6%, real estate 5%, energy 5%, and consumer cyclicals 5%. The largest corporate bond sector exposures at December 31, 2018 were consumer non-cyclical consisting of 11% of the total fixed income portfolio, banks 6%, communications 6%, energy 5%, and real estate 5%. The Company uses equity index options to manage its equity market exposure to index annuity products. These are exchange-traded options and there is no credit risk.

5. Derivative Instruments

The Company uses derivatives to hedge its equity market exposure to index annuity products which are contracts that earn a return based on the change in the value of the S&P 500 index between annual index point dates. The Company buys and sells listed equity and index call options and call option spreads and there is no credit risk. The net premium is paid up front and there are no additional cash requirements or additional contingent liabilities. These contracts are held at fair market value on the Company’s balance sheet and the Company is not applying hedge accounting. At June 30, 2019 and December 31, 2018, these derivatives had a net market value of $0.7 million and $0.2 million, with notional amounts of $15.2 million and $12.7 million on call options purchased and $10.3 million and $8.8 million on call options written, respectively. Derivative instruments are included in other invested assets on the consolidated balance sheets.

6. Fair Value of Financial Instruments

Fair value estimates are made at specific points in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale, at one time, the Company's entire holding of a particular financial instrument. Although fair value estimates are calculated using assumptions that management believes are appropriate, changes in assumptions could significantly affect estimates.

Fair value estimates are determined for existing financial instruments without attempting to estimate the value of anticipated future business and the value of assets and certain liabilities that are not considered financial instruments. Accordingly, the aggregate fair value estimates presented do not represent the underlying value of the Company.

The Company has procedures in place to validate the fair values received from the independent pricing service. The Company assesses whether prices received represent a reasonable estimate of fair value through various controls designed to ensure that valuations represent a fair price, including calculation of portfolio returns, comparison of returns to corresponding benchmark returns, analysis of periodic changes in market prices, evaluation of corresponding market yields and spread levels, and comparing prices from multiple pricing sources. On an ongoing basis, the Company monitors the pricing service valuation methods and evaluates the various types of securities in its investment portfolio to determine an appropriate fair value hierarchy.

In addition, tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of the estimates. The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

Fixed maturity and equity securities: Fair values were determined by an independent pricing service and are downloaded from Clearwater Analytics. The Company does not own any securities for which a fair value was not provided by the pricing service or a custody statement.

If a fair value had not been provided for a security, the Company would use a fair value estimated from yield data relating to instruments or securities with similar characteristics or as determined in good faith by the Company's investment advisor, DWS.

Policy loans: The carrying value of policy loans approximates fair value.

Other invested assets: Fair values of derivative instruments were determined by an independent pricing service and are downloaded from Clearwater Analytics. FHLB common stock is held at redemption value (see Note 2).

Cash and cash equivalents: The carrying value approximates fair value.

Separate account asset/liability: Fair values are based on net asset values provided daily by fund managers.

Policyholder account balance: For deposit liabilities, the carrying value was based on the amount payable on demand at the reporting date and approximates fair value.

Dividend accumulations and other: The carrying value approximates fair value.

Amounts related to the Company's financial instruments as of June 30, 2019 and December 31, 2018 are as follows:

	Carrying/Fair Value June 30, 2019	Carrying/Fair Value December 31, 2018
	(Dollars in thousands)	
Financial instruments recorded as assets:		
Fixed maturity securities	$ 207,416	$ 184,475
Equity securities	2,300	6,004
Policy loans	9,238	9,581
Other invested assets	728	202
Cash and cash equivalents	23,844	33,252
Separate account	23,618	20,819
Financial instruments recorded as liabilities:		
Policyholder account balance:		
Interest sensitive life contracts	41,937	41,478
Annuities	77,297	74,820
Dividend accumulations and other (1)	6,534	6,705
Separate account	23,618	20,819

(1) included within Reserve for deposit type funds in the consolidated balance sheet

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The hierarchy for inputs used in determining fair value maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available. Assets and liabilities recorded on the Consolidated Balance Sheets at fair value are categorized in the fair value hierarchy based on the observability of inputs to the valuation techniques as follows:

Level 1 – Assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Company can access.

Level 2 – Assets and liabilities whose values are based on the following:

(a) Quoted prices for similar assets or liabilities in active markets;

(b) Quoted prices for identical or similar assets or liabilities in markets that are not active; or

(c) Valuation models whose inputs are observable, directly or indirectly, for substantially the full term of the asset or liability.

Level 3 – Assets and liabilities whose values are based on prices or valuation techniques that are both unobservable and significant to the overall fair value measurement. Unobservable inputs reflect the Company's estimates of the assumptions that market participants would use in valuing the assets and liabilities.

Summary of significant valuation techniques and inputs for assets and liabilities measured at fair value on a recurring basis:

Level 1 measurements:

Fixed maturity securities: Comprised of U.S. Treasury and GNMA agency securities. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.

Equities: Comprised of actively traded, exchange-listed equities. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.

Other invested assets: Comprised of actively traded, exchange-listed derivative instruments. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.

Cash Equivalents: Comprised of money market funds. Market values for the money market funds are obtained daily from the fund managers.

Separate account assets: Comprised of actively traded mutual funds that have daily quoted net asset values for identical assets that the Company can access. Market values for the actively traded mutual funds in which the separate account assets are invested are obtained daily from the fund managers.

Level 2 measurements:

Fixed maturity securities: States, political subdivisions, and corporate securities: As valuation technique the pricing vendor employs multi-dimensional relational application model which uses standard inputs including benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications. The pricing vendor also monitors market indicators, and industry and economic events. For high yield corporate securities, observations of equity and credit default swap curves are also used.

Residential mortgage-backed securities: As valuation technique the pricing vendor employs option-adjusted spread ("OAS") model and prepayment model as well as volatility driven, multi-dimensional spread tables using standard inputs including benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications plus new issue data, monthly prepayment information, and collateral performance. The pricing vendor also monitors market indicators, and industry and economic events.

Commercial mortgage-backed securities: As valuation technique the pricing vendor employs multi-dimensional spread table and price tables using standard inputs including benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications plus new issue data, monthly prepayment information, collateral performance, and real estate analysis from third party. The pricing vendor also monitors market indicators, and industry and economic events.

Level 3 measurements:

Equities: The primary inputs to the valuation include quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2 fair value measurements, contractual cash flows, benchmark yields, collateral performance, credit spreads, and other estimates including custody statements.

The following table presents the Company's securities measured at fair value on a recurring basis as of June 30, 2019 and December 31, 2018:

		Recurring Fair Value Measurements at June 30, 2019 Using:		
Description	**Fair Values**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
		(Dollars in thousands)		
Fixed maturity securities:				
U.S. government	$ 2,353	$ 2,353	$ —	$ —
States, political subdivisions, other	39,327	—	39,327	—
Corporate	115,960	—	115,960	—
Residential mortgage-backed securities	43,937	—	43,937	—
Commercial mortgage-backed securities	5,839	—	5,839	—
Total fixed maturities	207,416	2,353	205,063	—
Equities (1)	28	28	—	—
Other invested assets (2)	717	717	—	—
Cash equivalents (3)	23,844	23,844	—	—
Separate accounts (4)	23,618	23,618	—	—
Total	$ 255,623	$ 50,560	$ 205,063	$ —

Description	Fair Values	Recurring Fair Value Measurements at December 31, 2018 Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(Dollars in thousands)			
Fixed maturity securities:				
U.S. government	$ 4,057	$ 4,057	$ —	$ —
States, political subdivisions, other	30,989	—	30,989	—
Corporate	106,286	—	106,286	—
Residential mortgage-backed securities	37,522	—	37,522	—
Commercial mortgage-backed securities	5,621	—	5,621	—
Total fixed maturities	184,475	4,057	180,418	—
Equities (1)	3,767	3,757	—	10
Other invested assets	202	202	—	—
Cash equivalents (3)	33,252	33,252	—	—
Separate accounts (4)	20,819	20,819	—	—
Total	$ 242,515	$ 62,087	$ 180,418	$ 10

(1) Certain equity investments for which the fair value, of $2.3 million and $2.2 million as of June 30, 2019 and December 31, 2018, respectively, is measured using the net asset value per share (or its equivalent) practical expedient have been excluded from the fair value hierarchy, above.
(2) The Company’s investment in FHLB common stock for which the fair value, of $11,200 at June 30, 2019 and $10,000 at December 31, 2018, is based on its redemption value, effective January 1, 2019 (see Note 2), has been excluded from the fair value hierarchy, above.
(3) Cash equivalents are invested in money market funds with daily liquidity. The estimated fair value of cash equivalents is based on the estimated fair value of the underlying assets as provided by fund managers in daily net asset values and included in Level 1 assets.
(4) Separate account assets are invested in money market funds with daily liquidity. The estimated fair value of separate account assets is based on the estimated fair value of the underlying assets as provided by fund managers in daily net asset values and included in Level 1 assets.

There were no Level 3 purchases, issuances, sales, settlements, or transfers during the three and six month periods ended June 30, 2019 and June 30, 2018.

7. Accumulated Other Comprehensive Income

The components of AOCI are as follows:

	Unrealized Investment Gains (losses)	Shadow DAC	Accumulated Other Comprehensive Income (loss)
	(Dollars in thousands)		
Balance, March 31, 2019	$ 1,589	$ (366)	$ 1,223
Available-for-sale investment			
gains (losses) arising during the period:			
Fixed maturity securities net of tax of $1,128	4,241	—	4,241
Change in Shadow DAC net of tax benefit of $165	—	(619)	(619)
Balance, June 30, 2019	$ 5,830	$ (985)	$ 4,845

Balance, March 31, 2018	$ 512	$ (20)	$ 492
Available-for-sale investment			
gains (losses) arising during the period:			
Fixed maturity securities net of tax benefit of $130	(1,914)	—	(1,914)
Equity securities net of tax of $26	98	—	98
Change in Shadow DAC net of tax of $62	—	235	235
Balance, June 30, 2018	$ (1,304)	$ 215	$ (1,089)

Balance, December 31, 2018	$ (2,248)	$ 283	$ (1,965)
Available-for-sale investment			
gains (losses) arising during the period:			
Fixed maturity securities net of tax of $1,870	9,238	—	9,238
Change in Shadow DAC net of tax benefit of $337	—	(1,268)	(1,268)
Cumulative net effect of adoption of new accounting principle [(1)]	(1,160)	—	(1,160)
Balance, June 30, 2019	$ 5,830	$ (985)	$ 4,845

Balance, December 31, 2017	$ 5,359	$ (602)	$ 4,757
Available-for-sale investment			
gains (losses) arising during the period:			
Fixed maturity securities net of tax benefit of $276	(6,742)	—	(6,742)
Equity securities net of tax of $21	79	—	79
Change in Shadow DAC net of tax of $217	—	817	817
Balance, June 30, 2018	$ (1,304)	$ 215	$ (1,089)

(1) This amount is the net effect of adopting ASU No. 2016-01 as discussed in Note 3.

AOCI includes gross unrealized gains and losses on debt and equity securities, as well as shadow DAC. This value is presented net of tax. Equity securities were removed from this table upon adoption of ASU No. 2016-01 at January 1, 2019.

8. Income Taxes

Effective 2016, the parent holding company and subsidiaries files a consolidated federal income tax return. Tax years 2015 through 2018 are subject to examination by the IRS. Prior to 2016, consolidated federal income tax returns were filed under Federal Life as the ultimate parent.

Internal Revenue Code Section 382 (“Section 382”) limits how much of a loss carryforward can be used to offset taxable income when there is a change of ownership. The Company will be restricted in its ability to utilize loss carryforwards as a result of a 2018 change in ownership. The annual limit is estimated to be approximately $1.0 million and the total limit is estimated to be approximately $15.0 million.

The Company has recorded a net deferred tax liability of $1.0 million reflecting a deferred tax liability of $1.5 million from net unrealized gains on securities offset by a $0.5 million deferred tax asset, the partial benefit of $15.0 million in loss carryforwards, of which $13.1 million expire in varying amounts between 2025 and 2032. Realization of this asset is dependent on generating sufficient taxable income prior to expiration of the loss carryforwards. A valuation allowance has been established to account for the Company’s assessment that the entire loss carryforward will likely not be recovered. Although realization of the net deferred tax asset is not assured, management believes it is more likely than not that all of the net deferred tax asset will be realized. The amount of the net deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced

The Company had no liability for unrecognized tax benefits at June 30, 2019 or December 31, 2018 and believes it is reasonably possible that the liability will not significantly increase within the next twelve months. No amounts have been accrued for interest or penalties.

The Tax Act limits life reserves for tax purposes to the greater of net surrender value or 92.81% of required reserves. It is not estimated that this will have a meaningful impact to the net admitted assets on the Company's balance sheet.

The federal income tax provisions differ from the amounts determined by multiplying pre-tax income attributable to the Company by the statutory federal income tax rate of 21% for June 30, 2019 and June 30, 2018, as shown below.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(Dollars in thousands)			
Income tax benefits at statutory rate	$ (291)	$ (231)	$ (321)	$ (417)
Other	296	237	324	426
Income tax expense	$ 5	$ 6	$ 3	$ 9
Effective tax rate	0.3%	0.5%	0.2%	0.5%

9. Commitments and Contingent Liabilities

The Company is involved in various legal actions for which it will establish liabilities where appropriate. In the opinion of the Company's management, based on the advice of legal counsel, the resolution of such litigation is not expected to have a material adverse effect on the Company's financial position, results of operations or cash flows.

10. Debt and Federal Home Loan Bank Advances

The Company has not issued any debt or other credit obligations as of June 30, 2019 or December 31, 2018. The Company has no commitments in the form of loan guarantees. Federal Life is a member of the FHLB and has access to various advances and other funding products. As of June 30, 2019 and December 31, 2018, there are no advances or other credit outstanding with the FHLB.

11. Related Party Transactions

All the outstanding shares of Americana and FED Mutual are owned by Federal Life. Federal Life is owned by FEDHO Holding Company, which is controlled by Federal Life Holding Company which is owned by Federal Life Group.

For the three months ended June 30, 2019 and June 30, 2018, Americana paid $200,000 and $78,000, respectively, in common stock dividends to Federal Life. For the six months ended June 30, 2019 and June 30, 2018, Americana paid $335,000 and $119,000, respectively, in common stock dividends to Federal Life. As of June 30, 2019, and December 31, 2018, Americana reported $80,000 and $135,000, respectively, as dividends due to its parent company, Federal Life. This amount is generally settled within 60 days. Federal Life provides financial support for FED Mutual to continue its operations. All related party transactions eliminate in consolidation.

12. Earnings Per Share

	Three Months Ended June 30, 2019	Pro Forma for the Three Months Ended June 30, 2018	Six Months Ended June 30, 2019	Pro Forma for the Six Months Ended June 30, 2018
	(Dollars in thousands, except per share data)			
Numerator:				
Net loss - numerator for earnings per common share	$ (1,392)	$ (1,104)	$ (1,530)	$ (1,994)
Denominator:				
Weighted average basic common shares outstanding	3,530,250	3,530,150	3,530,250	3,530,150
Effect of dilutive securities:				
Stock options	215,000	215,000	215,000	215,000
Restricted stock awards	140,000	140,000	140,000	140,000
Denominator for earnings per diluted common share	3,885,250	3,885,150	3,885,250	3,885,150
Basic loss per common share	$ (0.39)	$ (0.31)	$ (0.43)	$ (0.56)
Diluted loss per common share	$ (0.39)	$ (0.31)	$ (0.43)	$ (0.56)

The amounts disclosed above include 140,000 shares that were granted as restricted stock awards to the Company’s executive officers at the closing of the offerings associated with the Company’s IPO. No effect has been given to any issuances of additional shares in connection with the grant of options or awards of stock under the stock-based incentive plan adopted by the Company. Under the stock-based incentive plan, the Company may issue 480,000 shares of its common stock. Of this, 140,000 shares were granted as restricted stock awards and 215,000 shares were used to award stock options under the stock-based incentive plan. The issuance of authorized but unissued shares of common stock upon the exercise of stock options or for purposes of making restricted stock awards under the stock-based incentive plan instead of open market purchases would dilute the voting interests of existing shareholders by approximately 12%.

13. Subsequent Events

We evaluated events that occurred subsequent to June 30, 2019 through August 14, 2019, the date the consolidated financial statements were issued, noting no subsequent events.