

AMERICAN NATIONAL INSURANCE CO /TX/

Form 10-K

March 12, 2010

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-K**

**Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the fiscal year ended December 31, 2009**  
or

**Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
Commission File No. 001-34280  
American National Insurance Company**  
(Exact name of registrant as specified in its charter)

Texas 74-0484030  
(State or other jurisdiction of (I.R.S. Employer Identification No.)  
incorporation or organization)

One Moody Plaza  
Galveston, Texas 77550-7999  
(Address of principal executive offices) (Zip Code)  
(409) 763-4661  
(Registrant's telephone number, including area code)  
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$1.00 par value	NASDAQ Stock Market LLC
Securities registered pursuant to Section 12(g) of the Act:	
None	
(Title of Class)	

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) 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.  
 Yes  No

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).  Yes  No  
The aggregate market value on June 30, 2009 (the last business day of the registrant's most recently completed second fiscal quarter) of the voting stock held by non-affiliates of the registrant was approximately \$518.0 million. For purposes of the determination of the above-stated amount, only directors, executive officers and 10% shareholders are presumed to be affiliates, but neither the registrant nor any such person concedes that they are affiliates of registrant. As of March 1, 2010, there were 26,820,166 shares of the registrant's voting common stock, \$1.00 par value per share, outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Information called for in Part III of this Form 10-K is incorporated by reference to the Registrants Definitive Proxy Statement to be filed within 120 days of the close of the Registrants fiscal year in conjunction with the Registrants annual meeting of shareholders.

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**Forward-Looking Statements**

Certain statements contained herein are forward-looking statements. The forward-looking statements contained herein are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, and include estimates and assumptions related to economic, competitive and legislative developments. Forward looking statements may be identified by words such as expects, intends, anticipates, plans, believes, estimates, will or words of similar meaning; and include, but are not limited to, statements regarding the outlook of our business and financial performance. These forward-looking statements are subject to change and uncertainty, which are, in many instances, beyond our control and, have been made based upon our expectations and beliefs concerning future developments and their potential effect upon us. There can be no assurance that future developments will be in accordance with our expectations, or that the effect of future developments on us will be anticipated. These forward-looking statements are not a guarantee of future performance and involve risks and uncertainties. There are certain important factors that could cause actual results to differ, possibly materially, from expectations or estimates reflected in such forward-looking statements. These factors include among others: (1) international economic and financial crisis, including the performance and fluctuations of fixed income, equity, real estate, credit capital and other financial markets; (2) interest rate fluctuations; (3) estimates of our reserves for future policy benefits and claims; (4) differences between actual experience regarding mortality, morbidity, persistency, surrender experience, interest rates or market returns, and the assumptions we use in pricing our products, establishing liabilities and reserves or for other purposes; (5) changes in our assumptions related to deferred policy acquisition costs, valuation of business acquired or goodwill; (6) changes in our claims-paying or credit ratings; (7) investment losses and defaults; (8) competition in our product lines and for personnel; (9) changes in tax law; (10) regulatory or legislative changes; (11) adverse determinations in litigation or regulatory matters and our exposure to contingent liabilities, including in connection with our divestiture or winding down of businesses; (12) domestic or international military actions, natural or man-made disasters, including terrorist activities or pandemic disease, or other events resulting in catastrophic loss of life; (13) ineffectiveness of risk management policies and procedures in identifying, monitoring and managing risks; (14) effects of acquisitions, divestitures and restructurings, including possible difficulties in integrating and realizing the projected results of acquisitions; (15) changes in statutory or U.S. generally accepted accounting principles ( GAAP ) practices or policies; and (16) changes in assumptions for retirement expense. It has never been a matter of corporate policy for us to make specific projections relating to future earnings, and we do not endorse any projections regarding future performance made by others. Additionally, we do not publicly update or revise forward-looking statements based on the outcome of various foreseeable or unforeseeable events.

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**PART I**

**ITEM 1. BUSINESS**

***Company Overview***

American National Insurance Company has more than 100 years of experience. We have maintained our home office in Galveston, Texas since our founding in 1905. Historically, our core business has been life insurance. We also offer individual and group health insurance and annuities, credit insurance, pension products, mutual funds, and property and casualty insurance for personal lines, agribusiness, and targeted commercial exposures. We provide personalized service to more than eight million policyholders throughout the United States, the District of Columbia, Puerto Rico, Guam, and American Samoa. Our total assets and stockholders' equity as of December 31, 2009 were \$20.1 billion and \$3.5 billion, respectively.

In this document, we refer to American National Insurance Company, a Texas insurance company, and its subsidiaries, as the Company, we, our, and us.

***Business Strategy***

We are an insurance company with a vision to be a leading provider of financial products and services for current and future generations. For more than a century, we have maintained a conservative business approach and unique corporate culture. We have an unwavering commitment to serve agent, policyholder, and shareholder needs by providing excellent customer service and competitively priced and diversified products. We are committed to profitable growth, which enables us to remain financially strong. Acquisitions that are strategic and that offer synergies are considered, but they are not our primary source of growth. Rather, we invest in our distribution channels and markets to fuel internal growth.

We are committed to excellence and maintaining high ethical standards in all our business dealings. Disciplined adherence to our core values has allowed us to deliver consistently high levels of customer service through talented people, who are at the heart of our business.

***Our Business Segments***

Our family of companies includes five life insurance companies, eight property and casualty insurance companies, and numerous non-insurance subsidiaries. We operate the following five business segments:

- Life;
- Annuity;
- Health;
- Property and Casualty; and
- Corporate and Other.

Revenues for the Life, Annuity, Health, and Property and Casualty segments come primarily from premiums collected on the insurance policies we write. Revenues in the Corporate and Other segment come from investment income on unallocated capital, interest on debt securities, earnings from various investment-related transactions, and the operations of several non-strategic lines of business. Financial information, including revenues, expenses and income and loss per segment is provided below in Management's Discussion and Analysis of Financial Condition and Results of Operations.

Each of our five business segments is discussed further below.

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### ***Life Segment***

A life insurance policy is an agreement between an insurance company and an individual. The typical life insurance contract provides that, in exchange for one or more premium payments, the insurance company promises to pay at the death of the insured (or at another determined time if earlier), a sum of money to the beneficiary.

We provide the following products under our Life segment:

Individual and group life insurance products, including universal life, variable universal life, whole life, and term life; and  
Credit life insurance.

*Whole Life.* Whole life products provide a guaranteed benefit upon the death of the insured in return for the periodic payment of a fixed premium over a predetermined period. Premium payments may be required for the entire life of the contract period, to a specified age or period, or may be level or change in accordance with a predetermined schedule. Whole life insurance includes policies that provide a participation feature in the form of dividends. Policyholders may receive dividends in cash or apply them to increase death benefits, increase cash values available upon surrender, or reduce the premiums required to maintain the contract in-force. Because the use of dividends is specified by the policyholder, this group of products provides significant flexibility to individuals to tailor the product to suit their specific needs and circumstances, while at the same time providing guaranteed benefits. Whole life products are sometimes referred to as ordinary life products.

*Term Life.* Term life provides a guaranteed benefit upon the death of the insured for a specified time period in return for the periodic payment of premiums. Coverage periods typically range from one year to thirty years, but in no event are they longer than the period over which premiums are paid. Term insurance products are sometimes referred to as pure protection products because there are typically no savings or investment elements. Term contracts expire without value at the end of the coverage period. Term life and whole life insurance are sometimes referred to as traditional life insurance products.

*Variable Universal Life.* Variable universal life products provide insurance coverage through a contract that gives the policyholder flexibility in investment choices and, depending on the product, in premium payments and coverage amounts. Most importantly, with variable life products, premiums and account balances can be directed by the policyholder into a variety of separate accounts or directed to our general account. In the separate accounts, the policyholder bears the entire risk of the investment results. We collect specified fees for the management of these various investment accounts and any net return is credited directly to the policyholder's account. With some products, policyholders may have the advantage of guarantees that may protect the death benefit from adverse investment experience.

*Universal Life.* Universal life products provide insurance coverage on the same basis as variable life, except that premiums, and the resulting accumulated balances, are allocated only to our general account. Universal life products may allow the insured to increase or decrease the amount of death benefit coverage over the term of the contract and the owner to adjust the frequency and amount of premium payments. Universal life products are considered interest rate-sensitive. We credit premiums, net of insurance protection expenses and interest, at rates we determine, to an account maintained for the policyholder, subject to a specified minimum interest rate.

*Credit Life Insurance.* Credit insurance is sold in connection with a loan, or other credit account and is designed to make payments to the lender for the borrower if the borrower is unable to make payments. Credit life insurance products pay off the borrower's remaining debt on a loan or credit account if the borrower dies during the term of coverage.

### ***Annuity Segment***

A popular choice in retirement planning, an annuity is any type of periodic (generally monthly) payment made to an individual, called the annuitant. Payment options include lump sum, income for life, or income for a certain period of time.



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We provide the following products under our Annuity segment, both to individuals and to institutional investors:

- Variable annuities; and
- Fixed annuities.

*Variable Annuities.* We offer variable annuities for both asset accumulation and asset distribution needs. Variable annuities allow the contract holder to make deposits into various investment accounts, as determined by the contract holder. The investment accounts are separate accounts, and risks associated with such investments are borne entirely by the contract holder. In certain variable annuity products, contract holders may also choose to allocate all or a portion of their account to our general account and are credited with interest at rates we determine, subject to certain minimums. In addition, contract holders may also elect minimum death benefits or enhanced death benefits under certain contracts, for which additional fees are charged.

*Fixed Annuities.* Fixed annuities are used for both asset accumulation and asset distribution needs. Fixed annuities do not allow the same investment flexibility provided by variable annuities, but they provide guarantees related to the preservation of principal and interest credited. Deposits made into immediate and deferred annuity contracts are allocated to our general account and are credited with interest at rates we determine, subject to certain minimums. For most contracts, credited interest rates are guaranteed not to change for certain limited periods of time, ranging from one to ten years. Fixed income annuities provide a guaranteed monthly income for a specified period of years and/or for the life of the annuitant. Our fixed annuity products include single premium immediate annuities and equity-indexed annuities, among others.

*Single Premium Immediate Annuity.* A single premium immediate annuity is an annuity purchased by one premium payment, providing a periodic (usually monthly or annual) income payment to the owner of the annuity for a specified period, such as for the remainder of the annuitant's life. Generally, once the payments of an immediate annuity have begun, the contract cannot be revised or cashed in, and there is no return of part or all of the original deposit. Annuity payments are usually fixed for the payment period, although they may increase at a predetermined rate, depending upon the terms of the particular contract.

*Equity-Indexed Annuity.* Equity-indexed annuities are usually deferred annuities, meaning that payment of the annuity is not scheduled to commence until a future date. With an equity-indexed annuity, a minimum interest rate is credited at the rates required by state insurance law. Any additional interest credited is typically tied to the performance of a particular stock market index, such as the S&P 500. Crediting of the additional interest, however, may be limited by caps or participation rates prescribed by the particular product.

***Health Segment***

Health insurance provides coverage that protects against the loss of life, loss of earnings, or expenses incurred due to illness or injury.

We provide the following types of products under our Health segment:

- Medicare Supplement;
- Supplemental insurance;
- Hospital surgical;
- Stop-loss; and
- Credit disability.

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*Medicare Supplement.* Medicare Supplement insurance is a type of private health insurance policy designed to supplement or pick up the costs of certain medical services not covered by Medicare. It is also known as gap coverage or Medigap coverage.

*Supplemental Insurance.* Supplemental insurance is designed to provide supplemental coverage for specific events or illnesses, such as cancer, and accidental injury or death.

*Hospital Surgical.* Hospital surgical insurance covers major health expenses associated with hospitalization or surgery.

*Stop-Loss.* Stop-loss coverage is used by employers to limit their exposure under self-insurance medical plans. There are two coverage types available, which are usually offered concurrently:

*Specific Stop-Loss.* Specific stop loss coverage is initiated when claims for an individual reach the threshold selected by the employer. After the threshold is reached, a stop-loss policy reimburses claims paid by the employer up to the lifetime limit per individual.

*Aggregate Stop-Loss.* Aggregate stop-loss coverage is designed to reimburse the employer once the group's total paid claims reach the stipulated threshold.

*Credit Disability.* Credit disability (also called credit accident and health) insurance pays a limited number of monthly payments on a loan or credit account if the borrower becomes disabled during the term of coverage.

***Property and Casualty Segment***

Property insurance provides protection against loss or damage to real or personal property due to fire, windstorm, flood, hail, and other covered perils. Casualty insurance provides coverage for legal liabilities resulting from bodily injury or property damage resulting from an accident caused by the insured.

We provide the following types of products under our Property and Casualty segment:

- Auto insurance;
- Homeowners insurance;
- Agribusiness and commercial insurance; and
- Credit property and casualty insurance.

*Auto Insurance.* Auto insurance provides coverage for specific risks involved in owning and operating an automobile, such as bodily injury, property damage (both to the insured's car and to the car of the other driver, if the loss results from collision), fire, theft and vandalism.

*Homeowners Insurance.* Homeowners insurance provides coverage that protects the insured's property against loss from theft, liability, and most common disasters.

*Agribusiness and Commercial Insurance.* Agribusiness and commercial insurance can encompass property coverage, liability coverage, commercial automobile coverage, workers' compensation coverage, and umbrella coverage tailored for a farm, ranch or other agricultural business operations, contractors, and targeted businesses within the rural and suburban markets.

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*Credit Property and Casualty Insurance.* Through our Property and Casualty segment, we offer the following credit insurance products:

- Credit involuntary unemployment insurance, which pays a limited number of monthly payments on a loan or credit account if the borrower becomes involuntarily unemployed during the term of coverage; and
- Credit property insurance, which pays funds to pay off the entire debt on a piece of property serving as collateral for a loan if the property is lost or damaged.

***Corporate and Other Segment***

Our Corporate and Other segment encompasses primarily our invested assets that are not used to support our insurance activities. It also includes our non-insurance subsidiaries, which consist primarily of mutual fund and investment advisory products and services. This segment provides investment services to each of our other segments and to our non-insurance subsidiaries. Our invested assets include common and preferred stocks, bonds, commercial real estate and mortgages, and participations in private equity funds.

Through our registered investment adviser and wholly-owned broker-dealer subsidiary, we also provide mutual fund products. A mutual fund is a registered investment company with an investment manager that manages a pool of money invested for its shareholders in a variety of instruments, such as stocks, bonds, or government securities, depending on the objectives of the particular mutual fund.

***Our Marketing Channels***

We conduct our sales operations through six marketing channels. Product distribution is aligned to satisfy specific target markets in such a way that channel conflict is minimized and key brand identities are maintained. Whenever possible, products are cross-sold by multiple marketing channels to maximize product offerings and return on investment in products and distribution.

Our six marketing channels are:

- Independent Marketing Group;
- Career Sales & Services Division;
- Multiple Line;
- Health/Senior Age Marketing Division;
- Direct Marketing; and
- Credit Insurance Division.

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The following table illustrates our marketing channels:

<b>Segment</b>	<b>Marketing Channels</b>	<b>Companies</b>	<b>Primary Means of Distribution</b>
Life	Independent Marketing Group; Multiple Line; Career Sales & Service Division; Health/Senior Age Marketing Division; Direct Marketing; Credit Insurance Division	American National Insurance Company; Farm Family Life Insurance Company; Garden State Life Insurance Company; Standard Life and Accident Insurance Company;	Independent agents; Employee agents; Dedicated agents; Internet, mail, print and broadcast media; General agents
Annuity	Independent Marketing Group; Multiple Line; Career Sales & Service Division; Health/Senior Age Marketing Division	American National Insurance Company; Standard Life and Accident Insurance Company; Farm Family Life Insurance Company	Independent agents; Employee agents; Exclusive agents
Property and Casualty	Multiple Line; Credit Insurance Division	American National County Mutual Insurance Company The American National Property and Casualty Companies; (ANPAC) ANPAC Louisiana Insurance Company Pacific Property and Casualty Company American National General Insurance Co. American National Lloyds Insurance Co. Farm Family Casualty Insurance Co. United Farm Family Insurance Company	Multiple Line: Exclusive agents and General agents; Credit Insurance Division: Independent agents
Health	Career Sales & Service Division; Health/Senior Age Marketing Division; Credit Insurance Division	American National Insurance Company; Standard Life and Accident Insurance Company; American National Life Insurance Company of Texas; Farm Family Life Insurance Company	Employee agents; Exclusive agents; Independent agents; Managing general underwriters

Financial information, including revenues, expenses, income and loss, and total assets by segment, is provided in Management's Discussion and Analysis - Results of Operations and Related Information by Segment. Additional information regarding business segments may be found in Management's Discussion and Analysis and the notes to the consolidated financial statements.

**Independent Marketing Group**

Independent Marketing Group distributes life insurance and annuities through independent agents, focusing on a higher-income and affluent marketplace, as well as targeted niche markets such as the small pension plan arena. Independent Marketing Group provides products, service, and concepts to clients in need of wealth protection, accumulation, distribution, and transfer. Independent Marketing Group markets through financial institutions, large marketing organizations, employee benefit firms, broker-dealers, and independent insurance agents and brokers.

**Career Sales & Service Division**

Career Sales & Service Division distributes life insurance, annuities, and limited benefit health insurance products through exclusive employee agents. Career Sales & Service Division primarily serves the lower-to middle-income marketplace.

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**Multiple Line**

Primarily through its Multiple Line exclusive agents, Multiple Line offers a combination of life insurance, annuities, mutual funds, and property and casualty insurance for personal lines, agribusiness, and targeted commercial exposures. Multiple Line is committed to remain an industry leader in tri-line sales (sales of homeowners, auto, and life insurance). Policyholders can do business with a single agent, a concept that has been identified as an important driver to client satisfaction. Multiple Line serves responsible individuals, families, and small business owners at all income levels.

**Health/Senior Age Marketing Division**

The Health/Senior Age Marketing Division, through independent agents and managing general underwriters, primarily serves the needs of middle-income seniors and individuals preparing for retirement. Although the Health/Senior Age Marketing Division offers an array of life insurance, health insurance, and annuity products for this growing segment of the population, including group life products, limited benefit group health insurance products, and health reinsurance, it remains committed to traditional Medicare Supplement products. The Health/Senior Age Marketing Division is also responsible for the administration and management of all health insurance products sold by other marketing channels.

**Direct Marketing**

Direct Marketing focuses on individuals who favor purchasing insurance directly from insurance companies. Direct Marketing offers life insurance products through the Internet, mail, print, and broadcast media, primarily directed at middle and upper income customers.

**Credit Insurance Division**

The Credit Insurance Division offers products that provide protection against specific unpaid debt in the event of loss due to death or disability, or in the event of a loss of ability to repay, such as involuntary unemployment or untimely loss of collateral. Distribution includes general agents who market to financial institutions, automobile dealers, and furniture dealers. These general agents are given non-exclusive authority to solicit insurance within a specified geographic area and to appoint and supervise subagents.

***Policyholder Liabilities***

We establish, and carry as liabilities, actuarially determined amounts that are calculated to meet our policy obligations when an annuitant takes income, a policy matures or surrenders, an insured dies or becomes disabled, or upon the occurrence of other covered events. We compute the amounts for actuarial liabilities reported in our consolidated financial statements in conformity with U.S. generally accepted accounting principles, or GAAP, in the United States of America, and in accordance with standards of practice of the American Academy of Actuaries.

We establish actuarial liabilities for future policy benefits (associated with base policies and riders, unearned mortality charges and future disability benefits), for other policyholder liabilities (associated with unearned revenues and claims payable) and for unearned revenue (the unamortized portion of front-end loads charged). We also establish liabilities for unpaid claims and unpaid claim expenses. In addition, we establish liabilities for minimum death benefit guarantees relating to certain annuity contracts and secondary guarantees relating to certain life policies.

Pursuant to state insurance laws, we establish statutory reserves, reported as liabilities, to meet our obligations on our respective policies. These statutory reserves are established in amounts sufficient to meet policy and contract obligations, when taken together with expected future premiums and interest at assumed rates. Statutory reserves generally differ from actuarial liabilities for future policy benefits determined using GAAP.

Due to the nature of the underlying risks and the high degree of uncertainty associated with the determination of our actuarial liabilities, we cannot precisely determine the amounts we will ultimately pay with respect to these actuarial liabilities, and the ultimate amounts may vary from the estimated amounts, particularly when payments may not occur until well into the future.

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However, we believe our actuarial liabilities for future benefits are adequate to cover the ultimate benefits required to be paid to policyholders. We periodically review our estimates of actuarial liabilities for future benefits and compare them with our actual experience. We revise estimates, to the extent permitted or required under GAAP, if we determine that future expected experience differs from assumptions used in the development of actuarial liabilities. Additional information regarding reserves may be found in Management's Discussion and Analysis - Critical Accounting Estimates - Reserves.

***Risk Management***

A conservative operating philosophy was a founding principle of the Company evidenced in its focus on sustainable, profitable growth. We manage risks throughout the Company by employing controls in our insurance, investment, and operational functions. These controls are designed to both place limits on activities and provide reporting information that helps shape any needed adjustments in our ongoing review of existing controls. We make use of several senior management committees to support the discussion and enforcement of risk controls in the management of the Company.

Our insurance products are designed to offer a balance of features desired by the marketplace with provisions that mitigate exposures so as to allow prudent management across the insurance portfolio. In our life insurance and property & casualty insurance products, we employ underwriting standards to ensure that proper rates are being charged to various classes of insureds. In our life insurance and annuity products, we mitigate against the risk of disintermediation through the use of surrender charges and market value adjustment features. Investment allocations and duration targets also serve to limit the asset-liability risk we are exposed to in our annuity products by limiting the credited rate to a range that is supported by these investments.

One of the significant risks faced by the Company is the management of the linkage between the timing and the amount of obligations related to our insurance contracts and the cash flows and valuations on the invested assets backing those obligations, a process commonly referred to as asset-liability management. This risk is most present in our Life and Annuity segments. Our Asset-Liability Management Committee regularly monitors the level of risk in the interaction of our assets and liabilities and helps shape courses of action that will help the Company attain its desired risk-return profile. Some of the tools employed include deterministic and stochastic interest rate scenario analyses, which help shape investment decision-making. These analyses also use experience analyses related to surrenders and death claims, which influence the timing of our obligations under our life insurance and annuity contracts.

We also manage risk by using reinsurance to limit our exposure on any one insurance contract or any single event. We purchase reinsurance from several providers and are not dependent on any single reinsurer. Further, we believe that our reinsurers are reputable and financially secure, and we regularly review the financial strength ratings of our carriers. Reinsurance does not eliminate our liability to pay our policyholders, and we remain primarily liable to our policyholders for the risks we insure. Reinsurance is a significant element of our Property & Casualty operations. The use of catastrophic event models is an important component of our reinsurance program. These models assist us in the management of our exposure concentration and deductibles to help the Company attain its desired risk-return profile. In an effort to coordinate risk management efforts and ensure alignment between our risk-taking activities and our strategic objectives, several years ago the Company began a formalization of its risk management program on an enterprise-wide basis. Among other things, this included the appointment of a corporate risk management officer. In addition, the Company has created a Management Risk Committee to ensure the consistent application of the enterprise risk management process across all business units.

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***Pricing***

We establish premium rates for our life and health insurance products using assumptions as to future mortality, morbidity, persistency, and expenses, all of which are generally based on our experience, industry data, and projected investment earnings. Premium rates for property and casualty insurance are influenced by many factors, including the frequency and severity of claims, state regulation and legislation, competition, general business and economic conditions, including market rates of interest, and inflation. Profitability is affected to the extent actual experience deviates from the assumptions made in pricing and to the extent investment, income varies from that which is required for policy reserves.

Collections for certain annuity and life products are not recognized as revenues but are added to policyholder account values. Revenues from these products are derived from charges to the account balances for insurance risk and administrative costs as well as charges imposed in some cases upon surrender. Profits are earned to the extent these revenues exceed actual costs. Profits are also earned from investment income on the deposits invested in excess of the amounts credited to policyholder accounts.

Premiums for Medicare Supplement and other accident and health policies must take into account the rising costs of medical care. The annual rate of medical cost inflation has historically been higher than the general rate of inflation, necessitating frequent rate increases, most of which are subject to approval by state regulatory agencies.

***Competition***

We compete principally on the basis of the scope of our distribution systems, the breadth of our product offerings, reputation, marketing expertise and support, our financial strength and ratings, our product features and prices, customer service, claims handling, and in the case of producers, compensation. The market for insurance, retirement and investment products continues to be highly fragmented and competitive. We compete with thousands of domestic and foreign insurance companies, many of which offer one or more similar products. In addition, because many of our products include a savings or investment component, our competition includes domestic and foreign securities firms, investment advisors, mutual funds, banks and other financial institutions. Our wholly-owned subsidiary investment advisor, as well as the mutual funds it manages, are in direct competition with such institutions.

Several competing insurance carriers have brands that are more commonly known and spend significantly more on advertising than we do. We remain competitive with these commonly known brands by relying on our abilities to manage costs, providing attractive coverage and service, maintaining positive relationships with our agents, and maintaining the strength of our financial ratings. Rather than focusing our advertising efforts nationally, we support advertising in the local markets in which our agents live and work.

***Our Ratings***

Insurer financial strength ratings reflect current independent opinions of rating agencies regarding the financial capacity of an insurance company to meet the obligations of its insurance policies and contracts in accordance with their terms. They are based on comprehensive quantitative and qualitative evaluations of a company and its management strategy. The rating agencies do not provide ratings as a recommendation to purchase insurance or annuities, nor are they a warranty of an insurer's current or future ability to meet its contractual obligations. Ratings may be changed, suspended, or withdrawn at any time.



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American National Insurance Company's insurer financial strength ratings from two of the most widely referenced rating organizations as of the date of this filing are as follows:

A.M. Best Company: A (Excellent)<sup>(1)</sup>

Standard & Poor's: AA- (Very Strong)<sup>(3)</sup>

(1) A.M. Best's active company rating scale consists of thirteen ratings ranging from A++ (Superior) to D (poor). A is the third highest of such thirteen ratings and represents companies excellent ability to meet their ongoing insurance obligations.

(2) Standard & Poor's active company rating scale ranges from AAA (Extremely Strong) to CC (Extremely Weak). Plus (+) or Minus (-) modifiers show the relative standing within the categories from AA to CCC. A rating of AA is in the very strong category and represents very strong financial security characteristics, differing only slightly from

those rated  
higher. AA- is  
the fourth  
highest of  
twenty active  
company  
ratings.

### **Regulation**

We are subject to extensive regulation, primarily at the state level. The method, extent, and substance of such regulation varies by state but generally has its source in statutes that establish standards and requirements for conducting the business of insurance and that delegate regulatory authority to a state regulatory agency. These rules have a substantial effect on our business and relate to a wide variety of matters including insurance company licensing and examination, agent and adjuster licensing, price setting, trade practices, policy forms, accounting methods, the nature and amount of investments, claims practices, participation in shared markets and guaranty funds, reserve adequacy, insurer solvency, transactions with affiliates, the payment of dividends, and underwriting standards. Some of these matters are discussed in more detail below.

*Limitations on Dividends By Insurance Subsidiaries.* Dividends paid from subsidiary insurance companies represent one source of cash for us. The ability of various of our insurance company subsidiaries to pay dividends is restricted by state law and impacted by federal income tax considerations.

*Holding Company Regulation.* Our family of companies constitutes an insurance holding company system that is subject to regulation throughout the jurisdictions in which our insurance companies do business. In the U.S., our insurance companies are organized under the insurance codes of Texas, Missouri, New York, Louisiana, and California. Generally, the insurance codes in these states require advance notice to, or in some cases approval by, state insurance regulators prior to certain transactions between insurance companies and other entities within their holding company system. Such requirements may deter or delay certain transactions considered desirable by management.

*Price Regulation.* Nearly all states have insurance laws requiring personal property and casualty and health insurers to file price schedules, policy or coverage forms, and other information with the state's regulatory authority. In many cases, such price schedules, policy forms or both must be approved prior to use. While they vary from state to state, the objectives of these pricing laws are generally the same: a price cannot be excessive, inadequate or unfairly discriminatory. Prohibitions on discriminatory pricing apply in the context of life insurance as well. The speed with which an insurer can change prices in response to competition or in response to increasing costs depends, in part, on the nature of the applicable pricing law.

An insurer's ability to adjust its prices in response to competition or increasing costs is often dependent on an insurer's ability to demonstrate to the regulator that its pricing or proposed pricing meets the requirements of the pricing laws. In those states that significantly restrict an insurer's discretion in selecting the business that it wants to underwrite, an insurer can manage its risk of loss by charging a price that reflects the cost and expense of providing the insurance. In those states that significantly restrict an insurer's ability to charge a price that reflects the cost and expense of providing the insurance, the insurer can manage its risk of loss by being more selective in the type of business it offers. When a state significantly restricts both underwriting and pricing, it becomes more difficult for an insurer to maintain its profitability. These kinds of pricing restrictions can impact our ability to market products to residents of such states.

Changes in our claim settlement process may require us to actuarially adjust loss information used in our pricing process. Some state insurance regulatory authorities may not approve price increases that give full effect to these adjustments.

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From time to time, the private passenger auto insurance industry comes under pressure from state regulators, legislators and special interest groups to reduce, freeze or set prices at levels that do not correspond with our analysis of underlying costs and expenses. Homeowners insurance comes under similar pressure, particularly as regulators in states subject to high levels of catastrophe losses struggle to identify an acceptable methodology to price for catastrophe exposure. We expect this kind of pressure to persist. In addition, our use of insurance scoring based on credit report information for underwriting and pricing regularly comes under attack by regulators, legislators and special interest groups in various states. The result could be legislation or regulation that adversely affects our profitability. We cannot predict the impact on our business of possible future legislative and regulatory measures regarding pricing.

*Involuntary Markets.* As a condition of maintaining our licenses to write personal property and casualty insurance in various states, we are required to participate in assigned risk plans, reinsurance facilities, and joint underwriting associations that provide various types of insurance coverage to individuals or entities that otherwise are unable to purchase such coverage from private insurers. Underwriting results related to these arrangements, which tend to be adverse, have been immaterial to our results of operations.

*Guaranty Funds.* Under state insurance guaranty fund laws, insurers doing business in a state can be assessed, up to prescribed limits, in order to cover certain obligations of insolvent insurance companies.

*Investment Regulation.* Our insurance companies are subject to regulations that require investment portfolio diversification and that limit the amount of investment in certain categories of assets. Failure to comply with these rules leads to the treatment of non-conforming investments as non-admitted assets for purposes of measuring statutory surplus. Further, in some instances, these rules require divestiture of non-conforming investments. As of December 31, 2009, the investment portfolios of our insurance companies complied with such laws and regulations in all material respects.

*Exiting Geographic Markets; Canceling and Non-Renewing Policies.* Most states regulate an insurer's ability to exit a market. For example, states limit, to varying degrees, an insurer's ability to cancel and non-renew policies. Some states prohibit an insurer from withdrawing one or more types of insurance business from the state, except pursuant to a plan that is approved by the state insurance department. Regulations that limit cancellation and non-renewal and that subject withdrawal plans to prior approval requirements could restrict our ability to exit unprofitable markets.

*Variable Life Insurance and Variable Annuities.* The sale and administration of variable life insurance and variable annuities are subject to extensive regulatory oversight at the federal and state level, including regulation and supervision by the Securities and Exchange Commission (the *SEC*) and the Financial Industry Regulatory Authority (*FINRA*). Our variable annuity contracts and variable life insurance policies are issued through separate accounts that are registered with the SEC as investment companies under the Investment Company Act of 1940. Each registered separate account is generally divided into sub-accounts, each of which invests in an underlying mutual fund that is itself a registered investment company under such act. In addition, the variable annuity contracts and variable life insurance policies issued by the separate accounts are registered with the SEC under the Securities Act of 1933. Federal and state regulatory authorities and FINRA from time to time make inquiries and conduct examinations regarding our compliance with securities and other laws and regulations. We cooperate with such inquiries and examinations and take corrective action when warranted.

*Broker-Dealer, Investment Adviser and Investment Companies.* Our wholly-owned subsidiary Securities Management and Research, Inc. is registered with the SEC as a broker-dealer under the Securities and Exchange Act of 1934 and a registered investment adviser under the Investment Advisers Act of 1940. Such company and the registered investment companies that it advises are subject to extensive regulation and supervision by the SEC, FINRA, and/or, in some cases, state securities administrators.

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*Privacy Regulation.* Federal laws, such as the Gramm-Leach-Bliley Act, and the laws of some states require us to protect the security and confidentiality of certain customer information and to notify customers about our policies and practices relating to collection and disclosure of customer information and our policies relating to protecting the security and confidentiality of that information. Federal law and the laws of some states also regulate disclosures of customer information. Furthermore, state and federal laws, such as the federal Health Insurance Portability and Accountability Act, regulate our use and disclosure of certain personal health information. Congress, state legislatures and regulatory authorities are expected to consider additional regulation relating to privacy and other aspects of customer information.

*Environmental Considerations.* As an owner and operator of real property, we are subject to extensive federal, state and local environmental laws and regulations. Inherent in such ownership and operation is also the risk that there may be potential environmental liabilities and costs in connection with any required remediation of such properties. In addition, we hold equity interests in companies that could potentially be subject to environmental liabilities. We routinely have environmental assessments performed with respect to real estate being acquired for investment and real property to be acquired through foreclosure. We cannot provide assurance that unexpected environmental liabilities will not arise. However, based on information currently available to management, management believes that any costs associated with compliance with environmental laws and regulations or any remediation of such properties will not have a material adverse effect on our business, results of operations or financial condition.

***Employees***

As of December 31, 2009, we had approximately 3,211 employees, of which approximately 843 are employed in our Galveston, Texas home office. We consider our employee relations to be good.

**ITEM 1A. RISK FACTORS**

The following describes our most significant risks:

***Difficult conditions in the economy generally may materially adversely affect our business and results of operations, and these conditions may not improve in the near future.***

Our results of operations are materially affected by conditions in the economy in both the U.S. and elsewhere. The stress experienced by global capital markets that began in the second half of 2007 continued and substantially increased during 2008 and continued through 2009. During 2009, adverse economic and market conditions contributed to a consolidated pretax net realized loss of \$75.7 million in our \$16.6 billion investment portfolio.

Included in such loss were other-than-temporary impairment write-downs of \$98.9 million. By comparison, other-than-temporary impairment write-downs during 2008 were \$367.0 million.

Factors such as consumer spending, business investment, energy costs, geopolitical issues, government spending, the volatility and strength of the capital markets, and inflation all affect the business and economic environment and, ultimately, the amount and profitability of our business. In an economic downturn characterized by higher unemployment, declining consumer confidence, lower family income, increased defaults on mortgages and consumer loans, lower corporate earnings, lower business investment and lower consumer spending, the demand for our insurance and financial products could be adversely affected.

Negative economic factors may also affect our ability to receive the appropriate rate for the risks we insure with our policyholders and annuity contract holders. In an economic downturn, our policyholders may choose to defer paying insurance premiums or stop paying insurance premiums altogether, resulting in an elevated incidence of lapses or surrenders of policies. Our individual protection life insurance markets, particularly our Career Sales & Service Division and our Multiple Line distribution channels, which serve primarily the lower and middle income markets, respectively, face competition from alternative uses of the customer's disposable income. All of these outcomes could affect earnings negatively and could have a material adverse effect on our business, results of operations and financial condition.

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The current mortgage crisis also has raised the possibility of future legislative and regulatory actions. We cannot predict whether or when such actions may occur, or what impact, if any, such actions could have on our business, results of operations and financial condition.

The Internal Revenue Code may be changed to address the fiscal challenges currently faced by the federal government. These changes could include changes to the taxation of life insurance, annuities, mutual funds, retirement savings plans, and other investment alternatives offered by us. Such changes could have an adverse impact on the desirability of some of our products.

***Differences between risk assumptions used to price our products and actual experience could materially affect our profitability.***

Our product pricing includes long-term assumptions regarding investment returns, mortality, morbidity (the rate of incidence of illness), persistency (the rate at which our policies remain in force), and operating costs and expenses of our business. The profitability of our business substantially depends on the extent to which our actual experience is consistent with the assumptions we use to price our products. If we fail to appropriately price the risks, we insure, or if our claims experience is more severe than our underlying risk assumptions, our profit margins could be negatively affected. Any potentially overpriced risks could negatively impact new business growth and retention of existing business.

***Increased claims activity resulting from catastrophic events, whether natural or man-made, may result in significant losses.***

We experience increased claims activity when catastrophic events impact geographic locations in which our policyholders live or do business. Catastrophes can be caused by natural events, such as hurricanes, tornadoes, wildfires, earthquakes, snow, hail and windstorms, or other factors, such as terrorism, riots, hazardous material releases, or utility outages. Some scientists believe that in recent years, changing climate conditions have added to the unpredictability, severity and frequency of natural disasters. To the extent climate, change increases the frequency and severity of such weather events, our insurance operating units may face increased claims. Climate change may also affect the affordability and availability of property and casualty insurance and the pricing for such products.

Our life and health insurance operations are additionally exposed to the risk of catastrophic mortality or illness, such as a pandemic, an outbreak of an easily communicable disease, or another event that causes a large number of deaths or high morbidity. Significant influenza pandemics have occurred three times in the last century, but neither the likelihood, timing, nor the severity of a future pandemic can be predicted. The effectiveness of external parties, including governmental and non-governmental organizations, in combating the severity of such a catastrophe could have a material impact on the losses experienced by us.

We cannot accurately predict catastrophes, or the number and type of catastrophic events that will affect us. As a result, our operating and financial results may vary significantly from one period to the next. While we anticipate and plan for catastrophe losses, there can be no assurance that our financial results will not be adversely affected by our exposure to losses arising from catastrophic events in the future that exceed our assumptions. For example, we experienced gross catastrophe losses of \$80.9 million, \$191.6 million, and \$32.4 million during 2009, 2008, and 2007, respectively. In 2008, we experienced abnormally high catastrophes due to Hurricanes Gustav and Ike and a number of tornadoes and hailstorms in the Midwestern and Southeastern states.

The extent of our losses in connection with catastrophic events is a function of the severity of the event and the total amount of policyholder exposure in the affected area. Where we have geographic concentrations of policyholders, a single catastrophe (such as an earthquake) or destructive weather trend affecting a region may have a significant impact on our financial condition and results of operations.

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***As an insurance company, we face a significant risk of litigation and regulatory investigations, which may result in significant financial losses, harm our reputation, and prevent us from implementing our business strategy.***

We face a significant risk of litigation and regulatory investigations in the ordinary course of operating our business, including the risk of class action lawsuits. Our pending legal and regulatory actions include proceedings specific to us and others generally applicable to business practices in the industries in which we operate. In connection with our insurance operations, plaintiffs' lawyers may bring lawsuits, including class actions, alleging, among other things, issues relating to sales or underwriting practices, claims payments and procedures, product design, disclosure, administration, additional premium charges for premiums paid on a periodic basis, denial or delay of benefits, and breaches of fiduciary or other duties to customers. Plaintiffs in class action suits and other types of lawsuits may seek very large or indeterminate amounts, including punitive and treble damages. The damages claimed and the amount of any probable and estimable liability, if any, may remain unknown for substantial periods of time and could result in a material adverse effect on our business, financial condition, results of operation and reputation.

The insurance industry has become the focus of increased scrutiny by regulatory and law enforcement authorities. This scrutiny includes the commencement of investigations and other proceedings relating to allegations of improper conduct in connection with the payment of, and disclosure with respect to, contingent commissions paid by insurance companies to intermediaries, the solicitation and provision of fictitious or inflated quotes, the use of inducements in the sale of insurance products, the issuance of refunds of unearned premiums upon termination of credit insurance, the accounting treatment for finite insurance and reinsurance or other non-traditional or loss mitigation insurance and reinsurance products, and, generally, the marketing of products. One possible result of these investigations and attendant lawsuits is that many insurance industry practices and customs may change. Such changes could adversely affect our ability to implement our business strategy.

In addition, increased regulatory scrutiny and any resulting investigations or proceedings could result in new legal actions and precedents and industry-wide regulations that could adversely affect our business, financial condition, and results of operations and could impact our ability to offer certain products.

***The determination of the amount of allowances and impairments taken on our investments and the valuation allowance on the deferred income tax asset are judgmental and could materially impact our results of operations or financial position.***

The determination of the amount of allowances and impairments vary by investment type and is based upon our periodic evaluation and assessment of known and inherent risks associated with the respective asset class. Such evaluations and assessments are revised as conditions change and new information becomes available. Management updates its evaluations regularly and reflects changes in allowances and impairments in operations as such evaluations are revised. Furthermore, additional impairments may need to be taken or allowances provided for in the future. Historical trends may not be indicative of future impairments or allowances.

For debt and equity securities not subject to ASC 320-10 (formerly, EITF No. 99-20), Investments Debt and Equity Securities an other-than-temporary impairment charge is taken when we do not have the ability and intent to hold the security until the forecasted recovery or based on the probability that we may not be able to receive all contractual payments when due. Debt securities accounted for under ASC 320, (formerly EITF No. 99-20), Investments Debt and Equity Securities may experience other-than-temporary impairment in future periods in the event an adverse change in cash flows is anticipated or probable. Furthermore, equity securities may experience other-than-temporary impairment in the future based on the prospects for recovery in value in a reasonable period.

Many criteria are considered during this process including, but not limited to, our ability and intent to hold the investment for a period of time sufficient to allow for an anticipated recovery in value; the expected recoverability of principal and interest; the length of time and extent to which the fair value has been less than amortized cost for fixed income securities or less than cost for equity securities; the financial condition, near-term and long-term prospects of the issue or issuer, including relevant industry conditions and trends and implications of rating agency actions and offering prices; and the specific reasons that a security is in a significant unrealized loss position, including market conditions, which could affect liquidity. Other-than-temporary impairment losses result in a reduction to the cost basis of the underlying investment.



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***Our investment portfolio includes fixed-income securities, equity securities, and commercial real estate, and fluctuations in these markets could adversely affect the valuation of our investment portfolio, our net investment income, and our overall profitability.***

Our investment portfolio is subject to market risks, such as risks associated with changes in interest rates, market volatility, and deterioration in the credit of companies in which we have invested. Domestic and international equity markets have recently experienced heightened volatility and turmoil. In the event of extreme prolonged market events, such as the current global economic crisis, we could incur significant losses. Even in the absence of a market downturn, however, we are exposed to substantial risk of loss due to market volatility. Investment returns are an important part of our overall profitability, and fluctuations in the fixed-income, equity, or real estate markets could negatively affect the timing and amount of our net investment income and adversely affect our financial condition. When interest rates rise, the value of our investment portfolio may decline due to decreases in the fair value of our fixed-income securities that comprise a substantial portion of our investment portfolio. Generally, we expect to hold all of our fixed maturity investments to maturity, including investments that have declined in value. Our intent can change, however, due to financial market fluctuations, changes in our investment strategy, or changes in our evaluation of the issuer's financial condition and prospects.

In a declining interest rate environment, prepayments and redemptions affecting our investment securities and mortgage loan investments may increase as issuers and borrowers seek to refinance at lower rates. Such a decline in market rates could reduce our investment income as new funds are invested at lower yields.

The prolonged and severe disruptions in the public debt and equity markets, including among other things, widening of credit spreads, bankruptcies and government intervention in a number of large financial institutions, have resulted in significant realized and unrealized losses in our investment portfolio. For the year ended December 31, 2009, we incurred a consolidated pretax net realized loss of \$75.7 million in our \$16.6 billion investment portfolio, including other-than-temporary impairment write-downs of \$98.9 million. By comparison, other-than-temporary impairment write-downs during 2008 were \$367.0 million. Such investment losses are further described in the Investments section of Management's Discussion and Analysis, included below. As a result of volatile, market conditions, we could incur substantial additional realized and unrealized losses in future periods, which could have a material adverse impact on our results of operations, equity, business, and insurer financial strength.

Our investments in commercial real estate, carried on our balance sheet with a value of \$635.1 million at December 31, 2009, which were reduced by \$10.6 million in impairment charge in 2009 due to negative conditions in the economy. Further deterioration in the economy or deterioration in the commercial real estate market could adversely affect our investments in commercial real estate, including our mortgage loans, and have a material adverse effect on our investment portfolio.

***Concentration of our investment portfolios in any particular segment of the economy may have adverse effects on the results of our operations and financial position.***

The concentration of our investment portfolios in any particular industry, group of related industries, or geographic sector could have an adverse effect on our investment portfolios and consequently on our results of operations and financial position. While we seek to mitigate this risk by having a broadly diversified portfolio, events or developments that have a negative impact on any particular industry, group of related industries, or geographic region may have a disproportionate adverse effect on our investment portfolios to the extent that the portfolios are concentrated rather than diversified.



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***Some of our investments are relatively illiquid.***

Our investments in privately placed securities, mortgage loans, and equity covering real estate, including real estate joint ventures and other limited partnership interests, are relatively illiquid.

In addition, the fixed-income markets are experiencing a period of volatility, which has negatively impacted market liquidity conditions. Initially, the concerns on the part of market participants were focused on the sub-prime segment of the mortgage-backed securities (MBS) market. We have limited exposure to commercial mortgage-backed securities (CMBS) and no exposure to other synthetic securities except for our high quality, for the most part agency collateralized mortgage obligation (CMO). We do, however, have exposure to real estate through our mortgage loan and real estate equity investments discussed elsewhere.

***A decline in equity markets or an increase in volatility in the equity markets may adversely affect sales and or financial results of our investment products.***

Significant downturns and volatility in the equity markets could adversely affect our sales of investment products, which may have a material adverse effect on our financial condition and results of operations in three principal ways. First, market downturns and volatility may discourage purchases of variable annuities, variable life insurance, equity-indexed products, and mutual funds that have returns linked to the performance of the equity markets and may cause some of our existing customers to withdraw cash values or reduce investments in such products.

Second, downturns and volatility in the equity markets may have a material adverse effect on the revenues and returns from our savings and investment products and services. Because these products and services depend on fees related primarily to the value of assets under management, a decline in the equity markets could reduce our revenues by reducing the value of the investment assets we manage. In particular, the variable life and annuity business is highly sensitive to equity markets, and a sustained weakness in the markets could decrease revenues and earnings in variable life and annuity products.

Third, we provide certain guarantees within some of our products that protect policyholders against significant downturns in the equity markets. For example, we offer variable annuity products with guaranteed features, such as minimum death and withdrawal benefits. These guarantees may be more costly than expected in volatile or declining equity market conditions, which could cause us to increase liabilities for future policy benefits, negatively affecting our net income.

***Defaults on our mortgage loans may adversely affect our profitability.***

Our mortgage loan investments face default risk. Our mortgage loans are principally collateralized by commercial properties. At December 31, 2009, loans that were either delinquent or in the process of foreclosure were less than 1% of our \$2.23 billion in mortgage loan investments. A significant increase in the default rate of our mortgage loan investments could have a material adverse effect on our business, results of operations, and financial condition.

***We are controlled by a small number of stockholders.***

At December 31, 2009, the Moody Foundation, a charitable trust controlled by members of Robert L. Moody's family, beneficially owns 6,157,822 shares of our common stock. In addition to these shares, Moody National Bank, of which Robert L. Moody is chairman and chief executive officer, in its capacity as trustee or agent votes an additional 12,489,407 shares of our common stock. These two stockholders have the power to vote approximately 70% of our common stock. As a result, these two stockholders have the ability to exercise a controlling influence over all matters affecting us, including:

- The composition of our Board of Directors, subject to applicable legal and regulatory requirements, and through the Board of Directors, any determination with respect to our business direction and policies, including the appointment and removal of officers;
- Any determinations with respect to mergers or other business combinations;

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Our acquisition and disposition of assets; and

Any other matters submitted for stockholder approval.

Concentration of voting power could have the effect of deterring a change of control or other business combination that might otherwise be beneficial to our stockholders. This significant concentration of voting power may also adversely affect the trading price of our common stock, because investors may perceive disadvantages in owning stock in a company that is controlled by a small number of stockholders.

As of December 31, 2009, approximately 19,959,375 shares of our common stock (approximately 74%) were beneficially owned by The Moody Foundation, Moody National Bank, our executive officers, directors, and advisory directors and family members of our executive officers and directors. On that same date, approximately 6,860,791 shares (approximately 26%), with an aggregate market value of \$819,452,877, were held by other stockholders.

***Our future results are dependent in part on our ability to successfully operate in insurance, annuity and investment product industries that are highly competitive.***

The insurance, annuity and investment product industries are highly competitive. The product development and product life cycles have shortened in many product segments, leading to more intense competition with respect to product features. In addition, many of our competitors have well-established national reputations and market similar products. Competition for customers and agents has led to increased marketing and advertising by our competitors, varied agent compensation structures, as well as the introduction of new insurance products and aggressive pricing. We also compete for customers' funds with a variety of investment products offered by financial services companies other than insurance companies, such as banks, investment advisors, mutual fund companies and other financial institutions. Moreover, the ability of banks to be affiliates of insurers may have a material adverse effect on all of our product lines by substantially increasing the number, size and financial strength of potential competitors. If we cannot effectively respond to increased competition for the business of our current and prospective customers, we may not be able to grow our business or we may lose market share. In addition, if we fail to maintain our discipline in pricing and underwriting in the face of this competition, our underwriting profits may be adversely affected.

Furthermore, certain competitors operate using a mutual insurance company structure, which means generally every policyholder has voting rights in addition to their rights as a policyholder. Therefore, such companies may have dissimilar profitability and return targets.

***We may be unable to attract and retain sales representatives and third-party independent agents for our products.***

We must attract and retain productive sales representatives and third-party independent agents to sell our insurance, annuity and investment products. Strong competition exists among insurers for producers with demonstrated ability. We compete with other insurers for producers primarily on the basis of our financial position, stable ownership, support services, compensation, and product features. We continue to undertake several initiatives to grow our agency force while continuing to enhance the efficiency and production of our existing sales force. We cannot provide assurance that these initiatives will succeed in attracting and retaining new sales representatives and agents. Sales of individual insurance, annuities and investment products, and our results of operations and financial condition could be materially adversely affected if we are unsuccessful in attracting and retaining sales representatives and agents. In choosing an insurance provider, an agent may consider ease-of-doing business, reputation, price of product, customer service, claims handling, and the insurer's compensation structure. We may be unable to compete with insurers that adopt more aggressive pricing policies or compensation structures, insurers that offer a broader array of products, or that offer policies similar to ours at lower prices or as part of a package of products, or insurers that have extensive promotional and advertising campaigns. Even though we may establish a contractual relationship with an agent on a short-term basis, there is no certainty that such business arrangement will be continued on a longer-term basis.

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In addition, certain products are distributed under agreements with companies that are not affiliated with us. Termination of one or more of these agreements could have a detrimental effect on our operations and financial condition.

***Our risk management policies and procedures may leave us exposed to unidentified or unanticipated risk, which could negatively affect our business.***

Management of operational, legal, and regulatory risks requires, among other things, policies and procedures to record and verify a large number of transactions and events. We have devoted significant resources to develop risk management policies and procedures, and we expect to continue to do so. Nonetheless, these policies and procedures may not be fully effective. Many of our methods for managing risk and exposures are based upon the use of observed historical market behavior or statistics premised on historical models. As a result, these methods may not accurately predict future exposures, which could be significantly greater than historical measures indicate. Other risk management methods depend upon the evaluation of information that is publicly available or otherwise accessible regarding markets, clients, catastrophe occurrence, or other matters. This information may not always be accurate, complete, up-to-date or properly evaluated. See **Quantitative and Qualitative Disclosures About Market Risk** in **Management's Discussion and Analysis** below.

***Reinsurance may not be available, affordable or adequate to protect us against losses.***

As part of our overall risk management strategy, we purchase reinsurance for certain risks underwritten by our business segments. Market conditions beyond our control determine the availability and cost of reinsurance protection. In certain circumstances, the price of reinsurance for business already reinsured may also increase. Any decrease in the amount of reinsurance will increase our risk of loss, and any increase in the cost of reinsurance will, absent a decrease in the amount of reinsurance, reduce our earnings. Accordingly, we may be forced to incur additional expenses for reinsurance or may not be able to obtain sufficient reinsurance on acceptable terms, which could adversely affect our ability to write future business or result in the assumption of more risk with respect to those policies we issue.

***Emerging claim and coverage issues could negatively impact our business.***

As insurance industry practices and legal, judicial, social, and other conditions outside of our control change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect our business by extending coverage beyond our underwriting intent or increasing the type, number, or size of claims. Such emerging claims and coverage issues include (i) evolving theories of liability and judicial decisions expanding the interpretation of our policy provisions, thereby increasing the amount of damages for which we are liable, and (ii) a growing trend of plaintiffs targeting insurers in purported class action litigation relating to claims handling and other practices in the insurance industry. The effects of these and other related unforeseen emerging issues are extremely hard to predict and could harm our business and adversely affect our operating results and financial condition.

***Our financial results may be adversely affected by the cyclical nature of the property and casualty business in which we participate.***

The property and casualty insurance market is traditionally cyclical, experiencing periods characterized by relatively high levels of price competition, less restrictive underwriting standards, and relatively low premium rates, followed by periods of relatively low levels of competition, more selective underwriting standards, and relatively high premium rates. We are currently operating in a period characterized by significant price competition, which may reduce our margins. While both types of periods pose challenges to us, if we were to relax our underwriting standards or pricing in response to the competitive market, a period of increased claims activity could adversely affect our financial condition and results of operations.

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***Inflationary pressures on medical care costs, auto parts and repair, construction costs, and other economic factors may increase the amount we pay for claims and negatively affect our underwriting results.***

Rising medical costs require us to make higher payouts in connection with health insurance claims and claims of bodily injury under our property and casualty and healthcare policies. Likewise, increases in costs for auto parts and repair services, construction costs, and commodities result in higher loss costs for property damage claims. Thus, inflationary pressures could increase the cost of claims. These inflationary pressures may require us to increase our reserves. Our potential inability to adjust pricing for our products to account for cost increases or find other offsetting supply chain and business efficiencies may negatively impact our underwriting profit and financial results.

***Interest rate fluctuations and other events may require us to accelerate the amortization of deferred policy acquisition costs ( DAC ), which could adversely affect our consolidated financial condition and results of operations.***

DAC represents the costs that vary with and are related primarily to the acquisition of new and renewal insurance and annuity contracts. When interest rates rise, surrenders of policies and withdrawals of life insurance policies and annuity contracts may increase as policyholders seek to buy products with higher or perceived higher returns in exchange for the surrender or withdrawal, requiring us to accelerate the amortization of DAC. To the extent such amortization exceeds surrender or other charges earned as income upon surrender and withdrawals of certain life insurance policies and annuity contracts, our results of operations could be negatively affected.

The rate of amortization of DAC is also contingent upon profitability of the business. Typically, estimated lower levels of profitability require a higher rate of DAC amortization; in contrast, estimated higher levels of profitability require a lower rate of acceleration for DAC amortization. DAC for both insurance-oriented and investment-oriented products is reviewed for recoverability, which involves estimating the future profitability of current business. This review involves significant management judgment. If the actual emergence of future profitability were to be substantially lower than estimated, we could be required to accelerate DAC amortization, and such acceleration could adversely affect our results of operations. See also Management's Discussion and Analysis Critical Accounting Estimates and Notes 2 and 6 to the Consolidated Financial Statements.

***Changes in market interest rates may lead to a significant decrease in the sales and profitability of our spread-based products.***

Some of our products, principally interest sensitive life insurance and fixed annuities, expose us to the risk that changes in interest rates may reduce our spread, or the difference between the amounts that we are required to pay under the contracts and the rate of return we are able to earn on the underlying investment intended to support obligations under such contracts. This spread is a key component of our net income.

Our ability to manage our investment margin for spread-based products is dependent upon maintaining profitable spreads between investment yields and interest crediting rates. When market interest rates decrease or remain at relatively low levels, proceeds from investments that have matured or that have been prepaid or sold may be reinvested at lower yields, reducing investment margin. Lower rates in such an environment can offset decreases in investment yield on some products; however, these changes could be limited by market conditions and regulatory or contractual minimum rate guarantees. Moreover, the new rates may not match the timing or magnitude of changes in asset yields. Furthermore, decreases in the rates offered on products could make those products less attractive, leading to lower sales and/or changes in the level of surrenders and withdrawals for these products. Non-parallel shifts in interest rates, such as increases in short-term rates without accompanying increases in medium- and long-term rates, can influence customer demand for fixed annuities, which could impact the level and profitability of new investments by customers.

Increases in market interest rates can also have negative effects, for example by increasing the attractiveness of other insurance or investment products to our customers, which can lead to higher surrenders at a time when fixed income investment asset values are lower as a result of the increase in interest rates. For certain products, principally fixed annuity and interest-sensitive life products, the earned rate on assets could lag behind rising market yields. We may react to market conditions by increasing rates, which could narrow spreads.



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While we develop and maintain asset/liability management programs and procedures designed to mitigate the effect on spread income of rising or falling interest rates, no assurance can be given that changes in interest rates will not affect such spreads. Additionally, our asset/liability management programs and procedures incorporate assumptions about the relationship between short-term and long-term interest rates (*i.e.*, the slope of the yield curve) and relationships between risk-adjusted and risk-free interest rates, market liquidity, and other factors. The effectiveness of our asset/liability management programs and procedures may be negatively affected whenever actual results differ from these assumptions.

***If the counterparties to our reinsurance arrangements or to the derivative instruments we use to hedge our business risks default or fail to perform, we may be exposed to risks we had sought to mitigate, which could have a material adverse effect on our financial condition and results of operations.***

We use reinsurance and, to a lesser extent, derivative instruments (equity-indexed options) to mitigate our risks in various circumstances. In general, reinsurance does not relieve us of our direct liability to our policyholders, even when the reinsurer is liable to us. Accordingly, we bear credit risk on all of our policies with respect to our reinsurers. We cannot provide assurance that our reinsurers will pay the reinsurance recoverable owed to us or that they will pay these recoverable on a timely basis. A reinsurer's insolvency, inability, or unwillingness to make payments under the terms of reinsurance agreements with us could have a material adverse effect on our financial condition and results of operations.

In addition, we use derivative instruments to hedge various business risks. We enter into derivative instruments, including options, with a number of counterparties. If our counterparties fail or refuse to honor their obligations under these derivative instruments, our hedges of the related risk will be ineffective. Although our use of derivative instruments is not as significant as that of many of our competitors, such counterparty failures nevertheless could have a material adverse effect on our financial condition and results of operations.

***A downgrade or a potential downgrade in our financial strength ratings could result in a loss of business and could adversely affect our financial condition and results of operations.***

We cannot predict what actions rating agencies may take, or what actions we may take in response to the actions of rating agencies, which could adversely affect our business. As with other companies in the financial services industry, our ratings could be downgraded at any time and without any notices by any NRSRO.

Downgrades in our financial strength ratings could have a material adverse effect on our financial condition and results of operations in many ways, including:

- reducing new sales of insurance products, annuities, and investment products;
- adversely affecting our relationships with our sales force and independent sales intermediaries;
- materially increasing the number or amount of policy surrenders and withdrawals by policyholders and contract holders;
- requiring us to reduce prices for many of our products and services to remain competitive;
- adversely affecting our ability to obtain reinsurance at reasonable prices or at all; and
- adversely affecting our relationships with credit counterparties.

***The continued threat of terrorism and ongoing military actions may adversely affect the level of claim losses we incur and the value of our investment portfolio.***

The continued threat of terrorism, both within the U.S. and abroad, ongoing military actions, and heightened security measures in response to these types of threats may cause significant volatility in global financial markets and result in loss of life and property, disruption to commerce, and reduced economic activity. Some of the assets in our investment portfolio may be adversely affected by reduced economic activity caused by the continued threat of terrorism. We cannot predict whether, and the extent to which, companies in which we maintain investments may suffer losses as a result of financial, commercial, or economic disruptions, or how any such disruptions might affect the ability of those companies to pay interest or principal on their securities. The continued threat of terrorism also may result in increased reinsurance prices and reduced insurance coverage and may cause us to retain more risk than we otherwise would retain if we were able to obtain reinsurance at lower prices. In addition, the occurrence of terrorist actions could result in higher claims under our insurance policies than anticipated.



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***We are subject to extensive regulation, and potential further restrictive regulation may increase our operating costs and limit our growth.***

As insurance companies, broker-dealers, investment advisers and/or investment companies, our subsidiaries and affiliates are subject to extensive laws and regulations. The method of such regulation varies, but typically has its source in statutes that delegate regulatory and supervisory powers to an insurance official. The regulation and supervision relate primarily to:

- licensing companies and agents to transact business;
- calculating the value of assets to determine compliance with statutory requirements;
- restricting the size of risks that may be insured under a single contract;
- mandating certain insurance benefits;
- regulating certain premium rates;
- reviewing and approving policy forms and reports of financial condition required to be filed;
- regulating unfair trade and claims practices, including imposing restrictions on marketing and sales practices, distribution arrangements, and payment of inducements;
- regulating advertising;
- protecting privacy;
- establishing statutory capital and reserve requirements and solvency standards;
- determining methods of accounting;
- fixing maximum interest rates on insurance policy loans and minimum rates for guaranteed crediting rates on life insurance policies and annuity contracts;
- approving changes in control of insurance companies;
- restricting the payment of dividends and other transactions between affiliates; and
- regulating the types, amounts and valuation of investments.

These laws and regulations are complex and subject to change. Moreover, they are administered and enforced by a number of different governmental authorities, including state insurance regulators, state securities administrators, the Securities and Exchange Commission, the Internal Revenue Service, the Financial Industry Regulatory Authority, the U.S. Department of Justice, and state attorneys general, each of which exercises a degree of interpretive latitude. Consequently, we are subject to the risk that compliance with any particular regulator's or enforcement authority's interpretation of a legal issue may not result in compliance with another regulator's or enforcement authority's interpretation of the same issue.

In addition, there is risk that any particular regulator's or enforcement authority's interpretation of a legal issue may change over time to our detriment, or that changes in the overall legal environment may, even absent any particular regulator's or enforcement authority's interpretation of a legal issue changing, cause us to change our views regarding the actions we need to take from a legal risk management perspective, thus necessitating changes to our practices that may, in some cases, limit our ability to grow and improve the profitability of our business.



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The regulatory environment could have other significant effects on us and our business. Among other things, we could be fined, prohibited from engaging in some or all of our business activities, or made subject to limitations or conditions on our business activities. Significant regulatory actions against us could have material adverse financial effects, cause significant reputational harm, or harm business prospects. Compliance with applicable laws and regulations is time consuming and personnel-intensive, and changes in these laws and regulations may materially increase our direct and indirect compliance and other expenses of doing business, thus having a material adverse effect on our financial condition and results of operations. In particular, changes in the regulations governing the registration and distribution of variable insurance products, such as changes in the regulatory standards under which the sale of a variable annuity contract or variable life insurance policy is considered suitable for a particular customer, could have a material adverse effect, as could certain state insurance regulations that extend suitability requirements to non-variable products. In addition, with respect to our property and casualty and health business, state departments of insurance regulate and approve underwriting practices and rate changes, which can delay the implementation of premium rate changes or prevent us from making changes we believe are necessary to match rate to risk.

In recent years, the state insurance regulatory framework has come under public scrutiny and members of Congress have discussed proposals to provide for optional federal chartering of insurance companies. The extreme turmoil in the financial markets, combined with a new administration in the U.S. government has increased the likelihood of changes in the way the financial services industry is regulated. It is possible that insurance regulation will be drawn into this process, and that federal regulatory initiatives in the insurance industry could emerge and new regulations could be implemented, possibly on an expedited basis.

In addition, state legislators and insurance regulators continue to examine the appropriate nature and scope of state insurance regulation. Furthermore, we anticipate government involvement in healthcare to increase in the coming years, as it attempts to provide minimum coverage to all individuals. We can make no assurances regarding the potential impact of state or federal measures that may change the nature or scope of insurance regulation.

***Changes in tax laws may decrease sales and profitability of certain products.***

Under current federal and state income tax laws, certain products we offer, primarily life insurance and annuities, receive favorable tax treatment designed to encourage consumers to purchase these products. This favorable treatment may give certain of our products a competitive advantage over non-insurance products. Congress from time to time may consider legislation that would reduce or eliminate the favorable policyholder tax treatment currently applicable to life insurance and annuities.

Congress also may consider proposals to reduce the taxation of certain products or investments that may compete with life insurance and annuities. Legislation that increases the taxation on insurance products and/or reduces the taxation on competing products could lessen the advantage or create a disadvantage for certain of our products, making them less competitive. Such proposals, if adopted, could have a material adverse effect on our financial position and ability to sell such products and could result in the surrender of some existing contracts and policies. In addition, changes in the federal estate tax laws could negatively affect the demand for the types of life insurance used in estate planning.

***Changes in U.S. federal and state securities laws and regulations may affect our operations and our profitability.***

Certain of our variable annuity contracts and variable life insurance policies are subject to federal and state securities laws and regulations that apply to insurance products that are also securities. As a result, some of our activities in offering and selling variable insurance contracts and policies are subject to extensive regulation under these securities laws.

Federal and state securities laws and regulations are primarily intended to ensure the integrity of the financial markets and to protect investors in the securities markets, as well as protect investment advisory or brokerage clients. These laws and regulations generally grant regulatory agencies broad rulemaking and enforcement powers, including the power to limit or restrict the conduct of business for failure to comply with securities laws and regulations. Changes to these laws or regulations that restrict the conduct of our business could have a material adverse effect on our financial condition and results of operations. In particular, changes in the regulations governing the registration and distribution of variable insurance products, such as changes in the regulatory standards for suitability of variable annuity contracts or variable life insurance policies, could have a material adverse effect on our operations and profitability and could ultimately impact our ability to offer certain of these products. Furthermore, recently promulgated SEC regulations

that would require the registration of equity-indexed annuities may impact our ability to offer this product.

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***New accounting rules or changes to existing accounting rules could negatively impact our business.***

We are required to comply with U.S. generally accepted accounting principles. A number of organizations are instrumental in the development and interpretation of GAAP, such as the SEC, the Financial Accounting Standards Board ( FASB ), and the American Institute of Certified Public Accountants ( AICPA ). GAAP is subject to constant review by these organizations and others in an effort to address emerging accounting rules and issue interpretative accounting guidance on a continual basis. We can give no assurance that future changes to GAAP will not have a negative impact on us.

In addition, we are required to comply with statutory accounting principles ( *SAP* ) in our insurance operations. SAP and various components of SAP (such as actuarial reserving methodology) are subject to constant review by the National Association of Insurance Commissioners ( *NAIC* ) and its taskforces and committees, as well as state insurance departments, in an effort to address emerging issues and otherwise improve or alter financial reporting. The NAIC is currently working to reform state regulation in various areas, including comprehensive reforms relating to life insurance reserves and the accounting for such reserves. We cannot predict whether or in what form, reforms will be enacted and, whether the reforms, if enacted, will positively or negatively affect us.

***Prohibition on the use of customer credit information in connection with pricing and underwriting could impact our ability to price policies and consequently our profitability.***

Within the limits of state and federal regulations, our property and casualty personal lines use customer credit information to price policies. Certain groups and regulators have asserted that the use of credit information may have a discriminatory impact and are calling for the prohibition or restriction on the use of credit data in underwriting and pricing. Elimination of the use of this information for underwriting purposes could have an adverse effect on our profitability, because we would have less data upon which to price policies.

***The occurrence of events that are unanticipated in our disaster recovery systems and business continuity planning could impair our ability to conduct business effectively.***

Our home office is located in Galveston, Texas, on the coast of the Gulf of Mexico. We have taken action to protect our ability to service our policyholders in the event of a hurricane or other natural disaster affecting Galveston through our off-site disaster recovery systems and business continuity planning. During the year ended December 31, 2009, we have moved many of our key staff to our South Shore office buildings in League City, Texas. The primary offices of our property and casualty insurance companies are located in Springfield, Missouri and Glenmont, New York. These offices help to insulate our property and casualty operations from coastal catastrophes. Furthermore, we have established a remote processing center in San Antonio, Texas, which will support operations in the event that the Galveston area is affected by natural disaster. There is no assurance, however, that these efforts will prove successful. In the event of a hurricane or other natural disaster, an industrial accident, or acts of terrorism or war that would impact our corporate headquarters, events unanticipated in our disaster recovery systems could have an adverse impact on our ability to conduct business and on our results of operations and financial condition, particularly if those events affect our computer-based data processing, transmission, storage and retrieval systems. In the event that a significant number of our managers, employees, or agents were unavailable following such a disaster, our ability to effectively conduct our business could be compromised.

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***We may not be able to continue to be a low cost provider of property and casualty products due to the potential effects of the use of comparative rating software.***

The increased transparency that arises from the use of comparative rating software in the property and casualty insurance market could work to our competitive disadvantage. Comparative rating software, which already is widely used in personal auto and homeowners insurance, offers competitors the opportunity to model the premiums we charge over the spectrum of personal insurance policies we sell. Increased transparency of our rating structure may allow some competitors to mimic our pricing, thereby possibly reducing our competitive advantage.

***If we are unable to maintain the availability of our systems and safeguard the security of our data, our ability to conduct our business may be compromised and our reputation may be harmed.***

We use computer systems to store, retrieve, evaluate, and utilize customer and company data and information. Our information technology and telecommunications systems, in turn, interface with and rely upon third-party systems. Our business is highly dependent on our ability, and the ability of our employees and agents, to access these systems to perform necessary business functions, such as providing new-business quotes, processing new and renewal business, making changes to existing policies, filing and paying claims, providing customer support, pricing our products and services, establishing reserves, and timely and accurately reporting financial results. Systems failures or outages and our ability to recover from these failures and outages could compromise our ability to perform these functions on a timely basis, which could hurt our business and our relationships with our agents and policyholders. A breach of security with respect to our systems or those of our third-party vendors providing outsourced services could also jeopardize the confidentiality of our customers' personal data, which could harm our reputation and expose us to possible liability. We rely on encryption and authentication technology licensed from third parties to provide security and authentication capabilities, but we cannot guarantee that advances in computer capabilities, computer viruses, programming or human errors, loss or theft of computer equipment, or other events or developments would not result in a breach of our security measures, misappropriation of our proprietary information, misappropriation of customers' personal data, or an interruption of our business operations.

We have invested significant time and resources to mitigate these systems and data security risks; however, we cannot be certain that our efforts to mitigate such risks will be effective in all cases.

***Employee error and misconduct may be difficult to detect and prevent and may result in significant losses.***

Losses may result from, among other things, fraud, errors, failure to document transactions properly, failure to obtain proper internal authorization, or failure to comply with regulatory requirements. There have been a number of highly publicized cases involving fraud or other misconduct by employees in the financial services industry in recent years, and there is a risk that employee misconduct could occur. It is not always possible to deter or prevent employee misconduct, and the precautions we take to prevent and detect this activity may not be effective in all cases.

***Our business operations depend on our ability to appropriately execute and administer our policies and claims.***

Our primary business is writing and servicing life, property and casualty, and health insurance for individuals, families and commercial business. Because we deal with large numbers of similar policies, any problems or discrepancies that arise in our pricing, underwriting, billing, processing, claims handling or other practices, whether as a result of employee error, vendor error, or technological problems, could have negative repercussions on our financial results and our reputation if such problems or discrepancies are replicated through multiple policies.

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***Our Medicare Supplement business could be negatively affected by alternative healthcare providers***

The Medicare Supplement business is impacted by market trends in the senior-aged healthcare industry that provide alternatives to traditional Medicare, such as health maintenance organizations and other managed care or private plans. The success of these alternative healthcare solutions for senior-aged persons could negatively affect the sales and premium growth of traditional Medicare Supplement insurance and could impact our ability to offer such products.

***Our Medicare Supplement business is subject to intense competition and stringent pricing regulation, which could negatively impact future sales and affect our ability to offer this product.***

In recent years, price competition in the traditional Medicare Supplement market has been significant, characterized by some insurers who have been willing to earn very small profit margins or to under-price new sales in order to gain market share. Our Medicare Supplement business is also subject to stringent regulation, which includes price-setting rules that result in a maximum amount of profit that can be made, with no limits on potential loss of the insurer. Under such regulations, we are unable to raise premiums beyond the established set price. Thus, restrictions on the level of our profits could materially adversely affect our ability to offer this product.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

Our home office is located in Galveston, Texas. We own and occupy approximately 420,000 square feet of office space in this building. We also own the following additional properties that are materially important to our operations:

We own and occupy four buildings in League City, Texas, consisting of a total of approximately 298,000 square feet. Approximately one-third of such space is leased to third parties. Our use of these facilities is related primarily to our Life, Health, and Corporate and Other segments.

Our Property and Casualty segment conducts substantial operations through the American National Property and Casualty group of companies in Springfield, Missouri, and the Farm Family companies in Glenmont, New York. The Springfield facility is approximately 232,000 square feet, of which we occupy approximately two-thirds, with the remaining portion leased to third parties. The Glenmont facility is approximately 140,000 square feet, all of which is occupied by us.

We own an approximately 100,000 square foot facility in San Antonio, Texas. We occupy approximately three-fourths of this facility. We use this facility as a remote processing center for customer support and to support other business operations in the event the Galveston home office is evacuated due to catastrophic weather.

We believe our properties are adequate and suitable for our business as currently conducted and are adequately maintained. The above properties do not include properties we own for investment purposes only.

**ITEM 3. LEGAL PROCEEDINGS**

Information required for Item 3 is incorporated by reference to the discussion under the heading "Litigation" in our Commitments and Contingencies footnote within the Consolidated Financial Statements.

**ITEM 4. RESERVED**

**Table of Contents****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****STOCKHOLDER INFORMATION**

Our common stock is traded on the NASDAQ Global Select Market under the symbol ANAT. The following table presents the high and low prices for our common stock for the periods indicated and the quarterly dividends declared per share during such periods.

	<b>High</b>	<b>Low</b>	<b>Dividend Paid Per Share</b>
	<i>(per share)</i>		
<b>2009:</b>			
Fourth quarter	\$ 120.81	\$ 81.05	\$ 0.77
Third quarter	88.68	71.64	0.77
Second quarter	81.65	55.09	0.77
First quarter	74.59	33.74	0.77
			\$ 3.08
<b>2008:</b>			
Fourth quarter	\$ 94.40	\$ 55.00	\$ 0.77
Third quarter	111.76	81.68	0.77
Second quarter	119.65	97.50	0.77
First quarter	133.60	100.00	0.77
			\$ 3.08

Our stock closed at \$119.44 per share on December 31, 2009.

**Security Holders**

As of December 31, 2009, there were approximately 978 holders of record of our issued and outstanding shares of common stock.

**Securities Authorized for Issuance under Equity Compensation Plans**

The following table provides information regarding our common stock that is authorized for issuance under the American National Insurance Company 1999 Stock and Incentive Plan as of December 31, 2009.

<b>Plan category</b>	<b>Equity Compensation Plan Information</b>		
	<b>Number of securities to be issued upon exercise of outstanding</b>	<b>Weighted-average exercise price outstanding options, warrants and rights</b>	<b>Number of securities remaining available for future issuance under equity compensation plans (excluding</b>

	<b>options, warrants and rights (a)</b>	<b>(b)</b>	<b>securities reflected in column (a) (c)</b>
Equity compensation plans approved by security holders	\$	108.53	2,366,390
Equity compensation plans not approved by security holders			
<b>Total</b>	\$	108.53	2,366,390

**Table of Contents*****Performance Graph***

The Company's Common Stock is traded on the NASDAQ Global Select Market under the symbol ANAT. The following graph compares the performance of the cumulative total stockholder return for the Company's stockholders for the last five (5) years with the performance of the NASDAQ Stock Market Index and the NASDAQ Insurance Stock Index. The graph plots the cumulative changes in value of an initial \$100 investment as of December 31, 2004 over the time periods shown.

Value at each year-end of a \$100 initial investment made on December 31, 2004:

	12/31/04	12/31/05	12/31/06	12/31/07	12/31/08	12/31/09
ANICO	\$ 100.000	\$ 115.083	\$ 115.193	\$ 125.023	\$ 82.504	\$ 129.613
NASDAQ Total	\$ 100.000	\$ 102.131	\$ 112.196	\$ 121.670	\$ 58.624	\$ 84.201
NASDAQ Insurance	\$ 100.000	\$ 112.076	\$ 126.722	\$ 126.984	\$ 117.626	\$ 122.845

This performance graph shall not be deemed to be incorporated by reference into our Securities and Exchange Commission filings and should not constitute soliciting material or otherwise be considered filed under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.



**Table of Contents****ITEM 6. SELECTED FINANCIAL DATA****American National Insurance Company (and its subsidiaries)***(dollar amounts in millions, except per share amounts, or unless otherwise noted)*

	<b>Years Ended December 31,</b>				
	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
Revenues	\$ 2,950	\$ 2,519	\$ 3,056	\$ 3,105	\$ 3,036
Income (loss) from continuing operations	15	(173)	245	280	245
Net income (loss)	15	(154)	240	275	238
Net income (loss) attributed to American National Insurance Company and Subsidiaries	16	(154)	241	273	236
<b>Per common share</b>					
Income (loss) from continuing operations:					
- basic	0.57	(6.52)	9.26	10.58	9.27
- diluted	0.57	(6.52)	9.21	10.53	9.23
Net income (loss):					
- basic	0.57	(5.82)	9.07	10.37	8.99
- diluted	0.57	(5.82)	9.02	10.32	8.96
Net income (loss) attributed to American National Insurance Company and Subsidiaries:					
- basic	0.59	(5.82)	9.09	10.32	8.91
- diluted	0.59	(5.82)	9.04	10.27	8.87
Cash dividends per share	3.08	3.08	3.05	3.01	2.97
<b>Selected data</b>					
Return on American National Insurance Company and Subsidiaries stockholders equity	11.3%	(14.0)%	6.9%	8.2%	4.7%
Dividend payout ratio	127.2%	N/A	38.1%	38.7%	43.9%

	<b>Balances at December 31,</b>				
	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
Total assets	\$ 20,150	\$ 18,379	\$ 18,461	\$ 17,932	\$ 17,493
Total American National Insurance Company and Subsidiaries stockholders equity	3,460	3,134	3,737	3,576	3,378
Total equity	3,472	3,142	3,741	3,582	3,380

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**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Set forth on the following pages is management's discussion and analysis (MD&A) of our financial condition. This narrative analysis should be read in conjunction with the forward-looking statement information below, the audited consolidated financial statements and related notes included in Item 8 and *Risk Factors* included in Item 1A.

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**Overview**

We are a diversified insurance and financial services company. Chartered in 1905, we are headquartered in Galveston, Texas. We offer a broad spectrum of life, annuity, health, and property and casualty insurance products. We also offer mutual fund investments through our broker dealer subsidiary. We operate in all 50 states, the District of Columbia, Guam, American Samoa and Puerto Rico.

***Segments***

We manage our business through five business segments, which are comprised of four insurance segments: Life, Annuity, Health and Property and Casualty, and our Corporate and Other segment. The life, annuity, and health insurance segments are primarily operated through five domestic insurance companies. The property and casualty insurance segment is operated through eight domestic property and casualty insurance companies.

***Insurance Segments:***

The insurance segments have revenues, which consist primarily of the following:

- net premiums earned on individual term and whole life insurance, property and casualty insurance, credit insurance, health insurance and single premium immediate annuity products;
- net investment income; and
- insurance and investment product fees and other income, including surrender charges, mortality and expense risk charges, primarily from variable life and annuity, deferred annuities, and universal life insurance policies, management fees and commissions from other investment products, and other administrative charges.

The insurance segment expenses primarily consist of the following:

- benefits provided to policyholders and contract holders and changes in reserves held for future benefits;
- interest credited on account balances;
- acquisition and operating expenses, including commissions, marketing expenses, policy and contract servicing costs, overhead and other general expenses that are not capitalized (shown net of deferrals);
- amortization of deferred policy acquisition costs and other intangible assets; and
- income taxes.

The insurance segments have liabilities for all of the insurance products sold through the segment. Each insurance segment also has an amount of surplus allocated to it sufficient to support the segment's business activities. The insurance segments do not directly own any assets, but assets are allocated to the segments to support the liabilities and surplus of each segment. The mix of assets allocated to each of the insurance segments is modified as necessary to provide the right match of cash flows and earnings to properly support the characteristics of the insurance liabilities. We have utilized this methodology consistently over all periods presented.

***Corporate & Other***

The Corporate and Other segment directly owns all of the invested assets of the Company. As noted above, assets and surplus from the Corporate and Other segment are allocated to the insurance segments as necessary to support the liabilities of those segments. The investment income from the invested assets is also allocated to the insurance segments from the Corporate and Other segment in accordance with the amount of assets allocated to each segment. Earnings of the Corporate and Other segment are derived from our non-insurance businesses as well as earnings from those invested assets that do not support the insurance segments. All realized investment gains and losses are recorded in this segment.

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### **Outlook**

The Outlook sections contain many forward-looking statements, particularly relating to our future financial performance. These forward-looking statements are estimates based on information currently available to us, are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, and are subject to the precautionary statements set forth in the introduction to MD&A above. Actual results are likely to differ materially from those forecast by us, depending on the outcome of various factors.

In recent years, our business has been and likely will continue to be, influenced by a number of industry-wide and segment or product specific trends and conditions. In our discussion below, we first outline the broad macro-economic or industry trends (General Trends) that we expect will have an impact on our overall business. Second, we discuss certain segment specific trends that we believe may impact either individual segments of our business or specific products within these segments.

#### ***General Trends***

*Challenging Financial and Economic Environment:* The current financial crisis that began in mid-2007 is having adverse economic and financial market consequences around the world. In spite of government efforts, economic indicators remain mixed. During 2009, these market conditions contributed to an other-than temporary impairment loss of \$98.9 million in our \$16.6 billion investment portfolio. While we expect to experience continued volatility in the valuation of our investments, we believe that the current credit environment also provides us with opportunities to invest in select asset classes and sectors that may enhance our investment performance over time because of our intent and ability to hold these securities to maturity. Our ability to do so is supported by our strong liquidity position, which cushions us from the need to liquidate securities with significant unrealized losses to meet cash obligations. Due to acquisitions and consolidations principally among financial institutions, we have experienced credit concentrations beyond our normal guidelines. However, we believe those concentrations are manageable as we work to rebalance our investment portfolio to manage risk and investment returns.

We believe that as expectations for global economic growth are lowered, factors such as consumer spending, business investment, the volatility and condition of the capital markets and inflation, will affect the business and economic environment and, in turn, impact the demand for the type of financial and insurance products we offer. Adverse changes in the economy could affect earnings negatively and have a material adverse effect on our business, results of operations and financial condition. However, we believe those risks are somewhat mitigated by our financial strength, active risk management and disciplined underwriting for all of our products. Our diverse product mix across multiple lines of business (life, annuity, health, property and casualty) is a key strength that will help us adapt to current economic times and give us the ability to serve the changing needs of our customer base. For example, recent fluctuations in the stock market have led investors to search for financial products that are insulated from the volatility of the markets. We are well positioned to serve the demand in this marketplace given our success with fixed annuity products. Also, through our conservative business approach, we believe we remain financially strong and we are committed to providing a steady and reliable source of financial protection for policyholders and investors alike.

*Low Interest Rates:* Low interest rate environments are typically challenging for life and annuity companies as the spreads on deposit-type funds and contracts narrow and policies approach their minimum crediting rates. Low market interest rates may reduce the spreads between the amounts we credit to fixed annuity and individual life policyholders and the yield we earn on the investments that support these obligations. We have an established Asset/Liability Management Committee that actively manages the profitability of our in force block of insurance policies. In response to the unusually low interest rates in recent years, we have reduced the guaranteed minimum crediting rates on newly issued fixed annuity contracts and reduced crediting rates on in-force contracts, where permitted to do so. These actions have helped mitigate the adverse impact of low interest rates on our spreads and on the profitability of these products, although sales volume and persistency could diminish as a result. Additionally, the committee maintains assets with various maturities to support product liabilities and ensure liquidity. A gradual increase in longer-term interest rates relative to short-term rates generally will have a favorable effect on the profitability of these products. Although rapidly rising interest rates could result in reduced persistency in our spread-based retail products, as contract holders shift assets into higher yielding investments, we believe that our ability to react quickly to the changing marketplace will allow us to manage this risk.



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*Focus on Operating Efficiencies:* The challenging economic environment and the recent investment related losses across the industry have created a renewed focus on operating cost reductions and efficiencies. We continue to aggressively manage our cost base while maintaining our commitment to provide superior customer service to agents and policyholders. Investments in technology are aligned with activities and are coordinated through a disciplined project management process. In 2009, we consolidated our data centers and Information Technology ( IT ) operations to realize some of the synergies with our subsidiaries. We also anticipate using technology to enhance our web experience for policyholders and agents.

*Changing Regulatory Environment:* The insurance industry is regulated at the state level with some life and annuity products and services also subject to federal regulation. The debate over the federal regulatory role in the insurance industry continues to be a divisive issue within the industry. We proactively monitor this debate to determine its impact on our business. The SEC is attempting to enact new registration requirements for equity-indexed products. American National is prepared to support these products, even with additional registration requirements and regulation.

### ***Life and Annuity***

Due to the recent market and economic turmoil, life insurance companies experienced declining demand for certain products in 2008 and 2009. In response, we developed and began offering in September, 2009 a new Indexed Universal Life product, which we anticipate will be desirable in the current market. Life insurance continues to be a mainstay product for us today, as it has during our long history. We believe that the combination of predictable and decreasing mortality rates, positive cash flow generation for many years after policy issue and favorable persistency characteristics, suggest a viable and profitable future for this line of business. We continue to use a wide variety of marketing channels and plan to expand our traditional distribution models with additional independent agents. While the annuity segment had insignificant sales volume historically, this segment now represents a major and growing contributor to our operations. Although we experienced a slowdown in variable annuity sales in 2009, our fixed annuity sales continued to increase as investors sought less volatile investment vehicles. In light of the current market, we are committed to maintaining our fixed annuity product lines. We have a conservation program to retain policyholders through proactive communication and education when a policyholder is considering surrendering his or her policy. This has resulted in our retaining approximately 10% of policyholders that have submitted surrender requests.

Effective management of billions of dollars of invested assets and associated liabilities involving credited rates and, where applicable, financial hedging instruments (which are utilized as hedges of equity-indexed annuity sales), is crucial to our success in the annuity segment. Asset disintermediation, the risk of large outflows of cash at times when it is disadvantageous to us to dispose of invested assets, is a major risk associated with this segment. This risk is monitored and managed in the Asset Liability Management ( ALM ) Committee. The ALM Committee monitors asset disintermediation risk through the use of statistical measures such as duration and projected future cash flows based on large numbers of possible future interest environments and the use of modeling to identify potential risk areas. These techniques are designed to manage asset/liability cash flow and minimize potential losses.

*Demographics:* We believe that a key driver shaping the actions of the life insurance industry is the rising income protection, wealth accumulation, and insurance needs of the retiring Baby Boomers (those born between 1946 and 1964). According to the U.S. Census published in 2008, about 19.6 percent of the total population will be over 65 by 2030, compared to about 12.4 percent now. Also, the most rapidly growing age group is expected to be the 85 and older population. As a result of increasing longevity and uncertainty regarding the Social Security system, retirees will need to accumulate sufficient savings to support retirement income requirements.

We are well positioned to address the Baby Boomers rapidly increasing need for savings tools and income protection. We believe that our overall financial strength and broad distribution channels will position us to respond with a variety of products needed by Baby Boomers for retirement planning and income requirements. We are ready to respond to individuals approaching retirement age who seek information to plan for and manage their retirement needs. Our products that offer guaranteed income flows for life, including single premium immediate annuities, are well positioned to serve this market.



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*Competitive Pressures:* The life insurance industry remains highly competitive. Product development and product life cycles have shortened in many products, leading to more intense competition with respect to product features. In addition, several of the industry's products can be quite homogeneous and subject to intense price competition. We believe that we possess sufficient scale, financial strength and flexibility to effectively compete in this market.

The annuity market is also highly competitive. In addition to aggressive annuity rates and new product features such as guaranteed living benefit riders, within the industry there is growing competition from other financial service firms. Insurers continue to evaluate their distribution channels and the way they deliver products to consumers. At this time, we have elected not to provide guaranteed living benefits as a part of our variable annuity products. While this may have impeded our ability to sell variable annuities in the short run, this strategy has given us an advantage in terms of profitability in the long run. We believe that these products were not adequately priced historically, and many of our competitors are facing the consequences of mispricing the product.

We believe that we will continue to be competitive in the life and annuity markets through our broad line of products, our distinct distribution channels, and our consistent high level of customer service. We continue to modify our products to meet customer needs and to expand our reach where we believe we can obtain profitable growth. Some of the steps we have taken to improve our competitive position in the market include:

Established in 2009, we have a project under way to establish a New York life insurance subsidiary. We anticipate that sales will begin through this new company in the first half of 2010. A variety of annuity products will be available for sale once the subsidiary is established, followed in subsequent years by our life products. Initial sales are anticipated through independent and multiple-line agents. Based on competitors market experience, we expect annuity deposits from this subsidiary to represent five to ten percent of total deposits received once the market is established.

Sales of traditional life insurance products through our Career Sales and Services Division increased in 2009. This coupled with our focus on policy persistency and expense management allowed us to continue to maintain a stable and profitable block of in force business.

We have repositioned the competitiveness of life products sold through our Independent Marketing Group, particularly at older ages. While this repositioning resulted in a slowing of sales in the last quarter of 2008 and 2009, it has and will help improve the future profitability of these products.

We believe there will be a continuing shift in sales emphasis to utilizing the Internet, endorsed direct mail and innovative product/distribution combinations. Although our direct sales of life insurance products were lower in 2009, we remain committed to traditional life insurance products (term life and whole life) through our Internet and third-party marketing distribution channels.

### ***Health***

We experienced a slight reduction in Medicare Supplement policies in-force in 2009 as the industry continued to move toward Medicare Advantage plans and Part D plans, which redirected much of our agents' focus. We chose to remain committed to the traditional Medicare Supplement plans, which we consider to be viable for the long term. Sales of traditional products decreased during 2009; however, the trend of decreased sales reversed in 2007 and in 2008.

The number of hospital surgical health insurance policies in-force decreased in 2009. The decrease was mainly a result of rate increases. Profitability for our products is dependent on diligent management of policy premiums, relative to benefits paid, and rigid attention to underwriting the health risks of each policyholder. Maintaining adequate scale is a significant contributor to profitability as it allows us to negotiate better arrangements with healthcare providers, thus decreasing unit costs. We consider both new and existing health products on a case-by-case basis, in light of current market and regulatory environments, as well as management expectations.

We anticipate government involvement in healthcare to increase in the coming years, as it attempts to provide minimum coverage to all individuals. We believe that our focus on hospital surgical products may provide additional opportunities as individuals attempt to supplement that basic coverage.





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We anticipate employers will continue to increase offerings of consumer-driven health plans as a way to temper healthcare costs. Our Health/Senior Age marketing division will continue to support independent producers and maintain products that meet their sales needs, while moving toward direct consumer products that will position us for the next generation.

***Property and Casualty***

Since 2007, the property and casualty insurance industry has been experiencing a soft market, characterized by declining premium growth for three consecutive years. U.S. Property/Casualty Review and Preview published by A.M. Best on February 8, 2010 noted that the expected decrease in Net Premiums Written in 2009 has resulted in the first three consecutive year decline in A.M. Best's recorded history. Following the industry's historical decreases the last three years to Net Written Premiums, industry-wide operating results are expected to have improved in 2009. This improvement was due to the decline in catastrophe activity from an estimated \$23 billion industry-wide in 2008 to an estimated \$14 billion in 2009, offset by the prolonged period of competitive market conditions, excess capacity, leakage of premium to non-U.S. companies, alternative forms of risk transfer and the weak economy. A.M. Best expects this competitive pressure will continue in 2010, with an average forecast decline in industry net premiums written of 1.6%. We expect to experience continued pressure on pricing early in 2010, but easing from the levels experienced since 2007, and increasing by the end of 2010. To compete in this tough pricing environment, our long-term plans include developing tiered pricing for our agricultural and commercial lines. Tiered pricing will create a broader range of premiums and is designed to continue to improve our competitive position in the marketplace and our profitability.

With less consumer credit being offered in the market, we anticipate that fewer credit-related insurance products will be purchased. The tightening of credit is more heavily impacting the products written through the auto dealer market. However, the collateral protection production tends to increase in this type of economic environment. We continue to update credit insurance product offerings and pricing to meet these changing market needs, as well as adding new agents to expand our exposure to the credit-related insurance market. We are reviewing and implementing improved procedures to enhance customer service and, at the same time, looking for efficiencies to reduce administrative costs.

*Competition:* Property and casualty insurers are facing a continued competitive pricing environment. The condition of the economy in 2009 prevented the rate hardening most industry leaders were expecting following the declines in previous years. The competitive environment is expected to continue into 2010 as forecasts for an active hurricane season, the low interest rate environment, and an anticipated sluggish economic recovery all undermine any significant improvement in the market.

Despite the challenging pricing environment, we expect to identify profitable opportunities through our strong distribution channels, expanding geographic coverage, target marketing effects and new product development. Through our multiple-line exclusive agents, we will continue to focus on increasing the percentage of clients that buy their home, auto, business, and life insurance from us. Introduction of new products, such as one targeted toward the young family market in 2007, has been a main driver for increased policy counts in homeowners and auto insurance. The integration of the Farm Family companies over the last nine years has allowed us to expand our geographic coverage into the Northeast and our product portfolio to include agribusiness and commercial insurance. Similarly, Farm Family has expanded its product portfolio to include additional personal line property and casualty products. We expect that our agribusiness product will continue to be a leading seller in the Northeast United States. Agribusiness sales in other states are expected to show steady growth.

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### **Critical Accounting Estimates**

The consolidated financial statements have been prepared in conformity with GAAP. The preparation of financial statements requires us to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and their accompanying notes. Actual results could differ from results reported using those estimates.

We have identified the following estimates as critical in that they involve a high degree of judgment and are subject to a significant degree of variability:

- Deferred acquisition costs;
- Reserves;
- Reinsurance recoverable;
- Pension and postretirement benefit plans;
- Other-than-temporary impairment;
- Litigation contingencies; and
- Federal income taxes.

Our accounting estimates inherently require the use of judgments relating to a variety of assumptions, in particular, expectations of current and future mortality, morbidity, persistency, losses and loss adjustment expenses, recoverability of receivables, investment returns and interest rates. In developing these estimates, we make subjective and complex judgments that are inherently uncertain and subject to material changes as facts and circumstances develop. Although variability is inherent in these estimates, we believe that the amounts provided are appropriate, based upon the facts available upon compilation of the consolidated financial statements.

Due to the inherent uncertainty when using assumptions and estimates, the effect of certain accounting policies under different conditions or assumptions could be different from those reported in the consolidated financial statements.

We believe that the estimates used in our deferred acquisition cost calculations provide a representative example of how variations in assumptions and estimates would affect our business. Please see the sensitivity table in the *Deferred Acquisition Costs* section below for further information on how changes in assumptions and estimates would affect our business.

A discussion of these critical accounting estimates is presented below.

#### ***Deferred Acquisition Costs***

We incur significant costs in connection with acquiring insurance business, including commissions and certain other expenses. Such costs are generally deferred and amortized. The deferred costs are recorded as an asset commonly referred to as deferred policy acquisition costs ( DAC ). The DAC asset balance is subsequently charged to income (i.e., amortized) over the lives of the underlying contracts in relation to the anticipated emergence of premiums, gross margins, or gross profits, depending on the type of product.

For traditional life insurance and payout annuities, deferred costs consist of certain underwriting fees, commissions (in excess of ultimate renewal commissions) and certain agent fringe benefit costs, other policy set-up costs, and the cost of insurance in-force gained through acquisitions. The DAC on traditional life and annuity products is amortized with interest over the anticipated premium-paying period of the related policies, in proportion to annual premium revenue to be received over the life of the policies. The present value of expected premium revenue is estimated by using the same mortality, morbidity, persistency and withdrawal assumptions (with provisions for adverse deviation) used in computing liabilities for future policy benefits. These assumptions are not revised after policy issuance or acquisition (i.e., they are locked in ) unless the DAC balance is deemed to be unrecoverable. We periodically perform loss recognition analysis utilizing best estimate assumptions to determine whether or not the DAC balance is recoverable. See the discussion of *Life and Annuity Reserves* below for additional details.

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Costs deferred on universal life, variable universal life, limited pay life and investment-type deferred annuity contracts are amortized as a level percentage of the present value of estimated gross profits. These gross profits are dependent principally upon revenues in excess of the amounts credited to policyholders, death benefits, surrender benefits and expenses to administer the business. Our estimates of future gross profits are influenced by our assumptions including mortality, investment return, expenses and persistency. These assumptions are developed based on our experience. We review and update our assumptions at least annually. Changes to these assumptions result in adjustments which increase or decrease DAC amortization (i.e., they are not locked in ). Actual gross profits in a given reporting period can vary from our initial estimates resulting in an increase or decrease in the rate of amortization. We regularly evaluate the gross profits to determine if actual experience or other evidence suggests that earlier estimates should be revised. See the *Life and Annuity Reserves* discussion below for additional details.

DAC associated with acquisitions of certain blocks of in-force business is referred to as the present value of profits asset. Such DAC consists of the unamortized portion of the present value of profits asset as of the statement date. The initial present value of profits assets were determined based on the present value of projected earnings from the block(s) of business acquired as of the acquisition date. Subsequent to the acquisition date, the present value of profits asset is then amortized in proportion to premiums, gross profits, or gross margins from the acquired block of business. DAC on health products is amortized with interest over the anticipated premium-paying period of the related policies. Expected premium revenue is estimated using the same actuarial assumptions used in computing reserves for future policy benefits. Health insurance products that require DAC consideration are those with contractual obligations, which includes all of our products.

DAC associated with property and casualty insurance business consist of commissions, underwriting and issue costs. These costs are amortized over the coverage period of the related policies in relation to premium revenue recognized. We had a total DAC asset of approximately \$1.33 billion and \$1.48 billion at December 31, 2009 and 2008, respectively.

The following table displays the sensitivity of reasonably likely changes in assumptions included in the amortization of the DAC balance of our long-tail business as of December 31, 2009 (in thousands):

	<b>Increase/(Reduction) in DAC</b>	
Increase in future investment margins of 25 basis points	\$	26,666
Decrease in future investment margins of 25 basis points	\$	(31,810)
Decrease in future life mortality by 1%	\$	1,988
Increase in future life mortality by 1%	\$	(2,045)

**Reserves***Life and Annuity Reserves:*

Liability for Future Policy Benefits and Policy Account Balances For traditional life products, liabilities for future policy benefits have been calculated based on a net level premium method using estimated investment yields, withdrawals, mortality and other assumptions that were appropriate at the time that the policies were issued. Estimates used are based on our experience, adjusted with a provision for adverse deviation. Investment yields used for traditional life products range from 3.0% to 8.0% and vary by issue year. We review experience assumptions at least annually and compare them with our actual experience. When we determine that future expected experience differs such that the DAC asset is not recoverable and/or reserves are not sufficient to provide for policy benefits (after any applicable DAC has been written off), a loss event is recognized, as discussed below.

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Future policy benefits for universal life and investment-type deferred annuity contracts reflect the current account value before applicable surrender charges.

Future policy benefits for group life policies have been calculated using a level interest rate ranging from 3.0% to 5.5%. Mortality and withdrawal assumptions are based on our experience.

Fixed payout annuities included in future policy benefits are calculated using a level interest rate of 5.0%. Mortality assumptions are based on standard industry mortality tables. Liabilities for payout annuities classified as investment contracts (payout annuities without life contingencies) are determined as the present value of future benefits at the breakeven interest rate determined at inception.

Interest assumptions used for future policy benefits on health policies are calculated using graded interest rates ranging from 3.5% to 8.0%. Morbidity and termination assumptions are based on our experience.

At least annually, we test the net benefit reserves (policy benefit reserves less DAC) established for life insurance products, including consideration of future expected premium payments, to determine whether they are adequate to provide for future policyholder benefit obligations. The testing process is referred to as Loss Recognition for traditional products or Unlocking for non-traditional products. The assumptions used to perform the tests are our current best-estimate assumptions as to policyholder mortality, persistency, company maintenance expenses and invested asset returns.

For traditional business, a lock-in principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience differs from the original assumptions.

For non-traditional business, best-estimate assumptions are updated to reflect the observed changes based on experience studies and current economic conditions. We reflect the effect of such assumption changes in DAC and reserve balances accordingly. Due to the long-term nature of many of the liabilities, small changes in certain assumptions may cause large changes in the degree of reserve adequacy or DAC recoverability. In particular, changes in estimates of the future invested asset return assumption have a large effect on the degree of reserve adequacy.

**Life Reserving Methodology** We establish liabilities for amounts payable under life insurance policies, including participating and non-participating traditional life insurance and interest sensitive and variable universal life insurance. In general, amounts are payable over an extended period of time and related liabilities are calculated as the present value of future expected benefits to be paid, reduced by the present value of future expected premiums (for traditional life insurance), or as the account value established for the policyholder (for universal and variable universal life insurance). Such liabilities are established based on methods and underlying assumptions in accordance with GAAP and applicable actuarial standards. Principal assumptions used in the establishment of liabilities for future policy benefits are mortality, policy lapse, investment return, inflation, expenses and other contingent events as appropriate to the respective product type.

For non-participating traditional life insurance policies, future policy benefits are calculated consistent with Accounting Standards Codification ( ASC ) 944-40 (formerly FAS 60 ), *Accounting and Reporting by Insurance Enterprises*, and are equal to the aggregate of the present value of expected future benefit payments and related expenses, less the present value of expected future net premiums. Assumptions as to mortality and persistency are based upon our experience, with provisions for adverse deviation, when the basis of the liability is established. Interest rates for the aggregate future policy benefit liabilities range from 3.0% to 8.0% and vary by issue year.

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Future policy benefit liabilities for participating traditional life insurance policies are calculated consistent with, ASC 944-40 (formerly FAS 97), *Accounting and Reporting by Insurance Enterprise for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*, and are equal to the aggregate of (i) net level premium reserves for death and endowment policy benefits (calculated based upon the non-forfeiture interest rate, ranging from 2.5% to 6.0%, and mortality rates assumed in calculating the cash surrender values described in such contracts); and (ii) the liability for terminal dividends.

Future policy benefits for interest sensitive and variable universal life insurance policies are calculated consistent with ASC 944-40 (formerly FAS 97), *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*, for universal life type products and are equal to the current account value established for the policyholder. Some of our universal life policies contain secondary guarantees, for which an additional liability is established consistent with ASC 944-40 (formerly (SOP 03-01), *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and Separate Accounts*. Liabilities for universal life secondary guarantees and paid-up guarantees are determined by estimating the expected value of death benefits payable when the account balance is projected to be zero and recognizing those benefits over the accumulation period based on total expected assessments.

We regularly evaluate estimates used and adjust the additional liability balances, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised. The assumptions used in estimating the secondary and paid-up guarantee liabilities are consistent with those used for amortizing DAC and are thus subject to the same variability and risk. The benefits used in calculating the liabilities are based on the average benefits payable over a range of scenarios.

**Annuity Reserving Methodology** We establish liabilities for amounts payable under annuity contracts including fixed payout annuities and deferred annuities. An immediate or payout annuity is an annuity contract in the benefit or payout phase. In a fixed payout annuity contract, the insurance company agrees, for a cash consideration, to make specified benefit payments for a fixed period, or for the duration of a designated life or lives. The cash consideration can be funded with a single payment, as is the case with single premium immediate annuities, or with a schedule of payments, as is the case with limited pay products.

Payout annuities with more than an insignificant amount of mortality risk are calculated consistent with guidance under ASC 940-40 for limited pay insurance contracts. Benefit and maintenance expense reserves are established by using assumptions reflecting our expectations, including an appropriate margin for adverse deviation. Payout annuities are reserved using standard industry mortality tables specified for statutory reporting and an interest rate of 5% for life annuities and 3% for shorter duration contracts, such as term certain payouts. If the resulting reserve would otherwise cause profits to be recognized at the issue date, additional reserves are established. The resulting recognition of profits would be gradual over the expected life of the contract.

A deferred annuity is an annuity contract that has not reached the starting date of its periodic benefit payout. The Company establishes liabilities for deferred annuities based on methods and underlying assumptions in accordance with ASC 944-40 for investment contracts. Under ASC 944-40 for investment contracts, reserves for Policyholder Account Balances are established as the account value held on behalf of the policyholder. The possible need for additional reserves for guaranteed minimum death benefits are determined per guidance under SOP 03-01. Currently, no additional reserves are recorded for guaranteed minimum death benefits due to the immaterial amount of this reserve. Our exposure to this risk is minimal. The profit recognition on deferred annuity contracts is gradual over the expected life of the contract. No immediate profit is recognized on the sale of the contract.

**Health Reserves:**

**Overview** We establish policy reserves and claims reserves for known policy-specific liabilities. Further, we establish liabilities for the payment of medical expenses, which have been incurred during the reporting period but have not yet been paid. Additionally, Incurred But Not Reported (IBNR) amounts are determined using actuarial standards of practice which look at the time elapsed between when a claim is first incurred and when the final payment has been made (a completion factor analysis).



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As of year-end 2009 the Health total claim reserve and liability was \$115.9 million, versus \$112.8 million at year-end 2008.

**Reserving Methodology** Several methods are employed to establish claim reserves and liabilities for Health lines of business.

**Completion Factor Approach:** The claim reserves for most health care coverage can be suitably calculated using a Completion Factor Method. This method assumes that the historical lag pattern will be an accurate representation for the payment of claims that have been incurred but not yet completely paid. An estimate of the unpaid claim reserves is calculated by subtracting period-to-date paid claims from an estimate of the ultimate aggregate payment for all incurred claims in the time period. The method is based on the pattern of claims incurred within a given month and paid out in future months until such a point that no more payments are expected. Completion factors are calculated which complete the current period-to-date payment totals for each incurred month to estimate the ultimate expected payout. The method is best used when the incurred date and subsequent paid date is known for each claim and if fairly consistent patterns can be determined from the progression date of incurral until the date paid in full. The completion factor approach is also best used when the time between date of incurral and final payment is short (i.e., less than 24 month) in duration.

For the individual and association medical block (including Medicare Supplement), we use a completion factor approach to generate claim liability and reserves. Group and managing general underwriter claim reserves are also calculated by these methods. Outstanding claim inventories are monitored by management monthly to determine if any adjustment to the completion factor approach is needed.

Some of the larger managing general underwriters that we use engage external actuarial firms to provide an estimate of the claim reserves for their respective blocks. We independently evaluate the external claim reserve estimates provided for reasonableness as well as for consistency with other completion-factor based reserves. These estimates are incorporated into our reserve analysis to determine the booked reserves for the segment.

**Tabular Reserves:** Disability Income and Long Term Care blocks of business utilize a tabular calculation to generate the Present Value of Expected Future Payments. These reserves are called tabular because they rely on the published valuation tables for disability termination as maintained by the Society of Actuaries and validated by the National Association of Insurance Commissions ( NAIC ). Tabular reserves are determined by applying termination assumptions related to mortality or recovery, or for Long Term Care, shifts in the mode of care, to the stream of contractual benefit payments. The present value of these expected benefit payments at the required rate of return establishes the tabular reserve.

Credit Health claim reserves and liabilities are also based on a tabular calculation, using actuarial tables published by the Society of Actuaries and accepted by the NAIC. The reserve for this business is calculated as a function of open claims using the same actuarial tables discussed above. Periodically we test the total claim reserve using a completion factor calculation.

**Case Reserves:** Case reserves are also required for certain lines of business. Case reserves reflect known claims where an estimate of the exposure is readily available and quantifiable based on historical experience or other similar basis. We establish Long Term Care and Nursing Home reserves, on a case-by-case basis, by reviewing the open claims and estimating the remaining liability and applying probabilities derived from continuance tables based on company and industry experience.

**Liability for Future Policy Benefits** Liabilities for future policy benefits have been calculated based on a net level premium method. Future policy benefits are calculated consistent with ASC 944-40 (formerly FAS 60 ) and are equal to the aggregate of the present value of expected future benefit payments, less the present value of expected future premiums. Morbidity and termination assumptions are based on our experience or published valuation tables when available and appropriate. Interest rates for the aggregate future policy benefit liabilities range from 3.5% to 8.0% and vary by issue year.



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**Premium Deficiency Reserves** Deficiency reserves are established when the expected benefit payments for a classification of policies having homogenous characteristics are in excess of the expected premiums for these policies. The determination of a deficiency reserve takes into consideration the likelihood of premium rate increases, the timing of these increases, and the expected benefit utilization patterns. We have a premium deficiency reserve for the Major Medical block of business. This line of business is in run-off and continues to under-perform relative to the original pricing. The assumptions and methods used to determine the deficiency reserves are reviewed periodically for reasonableness and the reserve amount is monitored against emerging losses.

**Property and Casualty Reserves:**

**Reserves for Loss and Loss Adjustment Expense ( LAE )** Property and casualty reserves are established to provide for the estimated costs of paying claims under insurance policies written. These reserves include estimates for both:

Case reserves cost of claims that were reported to us but not yet paid, and

Reserves for IBNR anticipated cost of claims incurred but not reported. IBNR reserves include a provision for potential development on case reserves, losses on claims currently closed which may reopen in the future and claims, which have been incurred but not yet, reported.

These reserves include an estimate of the expense associated with settling claims, including legal and other fees, and the general expenses of administering the claims adjustment process. The two major categories of loss adjustment expense are defense and cost containment expense and adjusting and other expense. Net loss and LAE reserves for case reserves and IBNR as of December 31, 2009 and 2008 are shown in the following table (in thousands):

	December 31, 2009			December 31, 2008		
	Gross	Ceded	Net	Gross	Ceded	Net
Case	\$ 491,163	\$ 11,639	\$ 479,524	\$ 475,738	\$ 47,888	\$ 427,850
IBNR	\$ 425,827	\$ 48,693	\$ 377,134	\$ 437,275	\$ 17,265	\$ 420,010
<b>Total</b>	<b>\$ 916,990</b>	<b>\$ 60,332</b>	<b>\$ 856,658</b>	<b>\$ 913,013</b>	<b>\$ 65,153</b>	<b>\$ 847,860</b>

**Case Reserves:** Reserves for reported losses are established on either a judgment or formula basis, depending on the type of the loss. Formula reserves are used for losses such as credit property, automobile, property damage liability and automobile physical damage. They are based on historical paid loss data for similar claims with provisions for trend changes, such as those caused by inflation. The formula reserve is a fixed amount for each claim of a given type. Judgment reserve amounts are set on a per case basis based on facts and circumstances of each case, the type of claim and the expectation of damages. We regularly monitor the adequacy of judgment reserves and formula reserves on a case-by-case basis and change the amount of such reserves as necessary.

**IBNR:** IBNR reserves are estimated based on many variables, including historical statistical information, inflation, legal developments, economic conditions, and general trends in claim severity, frequency and other factors that could affect the adequacy of loss reserves.

Loss and premium data is aggregated by exposure class and by accident year (i.e., the year in which losses were incurred). IBNR reserves are calculated by projecting ultimate losses on each class of business and subtracting paid losses and case reserves. Unlike case reserves, IBNR is generally calculated at an aggregate level and cannot usually be directly identified as reserves for a particular loss or contract. Our overall reserve practice provides for ongoing claims evaluation and adjustment (if necessary) based on the development of related data and other relevant information pertaining to such claims. Adjustments in aggregate reserves, if any, are reflected in the operating results of the period during which such adjustments are made.

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Our actuaries reflect the potential uncertainty generated by volatility in our loss development profiles when selecting loss development factor patterns for each line of insurance. Therefore, net and gross reserve calculations have shown redundancies for the last several year-ends as a result of losses emerging favorably compared to what is implied by the selected loss development patterns. See *Results of Operations and Related Information by Segment – Property and Casualty, Prior Period Reserve Development* discussion for additional information.

The evaluation process to determine recorded loss and loss adjustment expense reserves involves the collaboration of underwriting, claims and internal actuarial departments. The process also includes consultation with independent actuarial firms on an annual basis. Work performed by independent actuarial firms is an important part of our process of gaining reinsurance that loss and loss adjustment expense reserves determined by our internal actuarial department sufficiently meet all present and future obligations arising out of all claims incurred as of year-end, both reported and unreported. Additionally, the independent actuarial firms complete the Statements of Actuarial Opinion at each year-end, required by state insurance regulators certifying that the recorded loss and loss adjustment expenses reserves appear reasonable.

**Reserving Methodology** The following actuarial methods are utilized in our reserving process during both annual and interim reporting periods:

**Initial Expected Loss Ratio method:** This method calculates an estimate of ultimate losses by applying an estimated loss ratio to an estimate of ultimate earned premium for each accident year. This method is appropriate for classes of business where the actual paid or reported loss experience is not yet mature enough to override initial expectations of the ultimate loss ratios.

**Bornhuetter Ferguson:** This method uses as a starting point an assumed initial expected loss ratio method and blends in the loss ratio implied by the claims experience to date by using loss development patterns based on our own historical experience. This method is generally appropriate where there are few reported claims and a relatively less stable pattern of reported losses.

**Loss or Expense Development (Chain Ladder):** This method uses actual loss or defense and cost containment expense data and the historical development profiles on older accident periods to project more recent, less developed periods to their ultimate position. This method is appropriate when there is a relatively stable pattern of loss and expense emergence and a relatively large number of reported claims.

**Ratio of Paid Defense and Cost Containment Expense to Paid Loss Development:** This method uses the ratio of paid defense and cost containment expense to paid loss data historical development profiles on older accident periods to project more recent, less developed periods to their ultimate position. In this method, an ultimate ratio of paid defense and cost containment expense to paid loss is selected for each accident period. The selected paid defense and cost containment expense to paid loss ratio is then applied to the selected ultimate loss for each accident period to estimate the ultimate defense and cost containment expense. Paid defense and cost containment expense is then subtracted from the ultimate defense and cost containment expense to calculate the unpaid defense and cost containment expense for that accident period.

**Calendar Year Paid Adjusting and Other Expense to Paid Loss:** This method uses the ratio of prior calendar years paid expense to paid loss to project ultimate loss adjustment expenses for adjusting and other expense. The key to this method is the selection of the paid expense to paid loss ratio based on prior calendar years activity. A percentage of the selected ratio is applied to the case reserves (depending on the line of insurance) and 100% to the indicated IBNR reserves. These ratios assume a percentage of the expense is incurred when a claim is opened and the remaining percentage is paid throughout the claim's life.

The basis of our selected single point best estimate on a particular line of business is often a blend of results from two or more methods (e.g. weighted averages). Our estimate is highly dependent on actuarial and management judgment as to which method(s) is most appropriate for a particular accident year and class of business. Our liability for unpaid claims and claim adjustment expense does not materially differ from the amount determined by our independent actuaries. Our methodology changes over time, as new information emerges regarding underlying loss activity and other factors.



**Table of Contents****Key Assumptions:**

Implicit in the actuarial methodologies utilized above are the following critical reserving assumptions:

- The selected loss ratio used in the initial expected loss ratio method and Bornhuetter Ferguson method for each accident year;
- The expected loss development profiles;
- A consistent claims handling process;
- A consistent payout pattern;
- No unusual growth patterns;
- No major shift in liability limits distribution on liability policies; and
- No significant prospective changes in workers compensation laws that would significantly affect future payouts.

The loss ratio selections and loss development profiles are primarily developed using our own historical claims and loss experience. These assumptions have not been modified from the preceding periods and are consistent with historical loss reserve development patterns.

Management believes that our loss reserves at December 31, 2009 are adequate. However, new information, legislation, events or circumstances, unknown at the original valuation date, may result in future development to our ultimate losses significantly greater or less than the reserves provided for at December 31, 2009. As noted in our Key Assumptions above, there are many factors that may impact our reserves, specifically those related to loss ratios for the credit insurance lines of business and those related to a consistent claims handling process for all other lines of business.

For non credit lines of business, our claims handling process is the most likely of those assumptions noted above to vary from the consistency we expect. This assumption was determined to most likely impact our reported results, financial position and liquidity, and we chose to measure the sensitivity to this assumption. The following table presents the range of likely scenarios related to a speed-up or slow-down of five days in the claims handling process and its subsequent impact on our estimate of gross loss reserves. Without certainty of future reporting patterns, we do not consider any change within the range displayed as more reasonably likely than any other.

The table below for the lines of business indicated quantifies the estimated impact on our gross loss reserves of possible scenarios of the speeding-up or slowing-down of claims being processed at December 31, 2009. The results of our analysis below show the cumulative increase (decrease) in gross loss reserves of the lines of business indicated across all accident years combined (in thousands):

	<b>Change in Reporting Pattern</b>	
	<b>5 Day Speed Up</b>	<b>5 Day Slow Down</b>
Personal Auto	\$ (2,499)	\$ 1,171
Homeowner	\$ (913)	\$ 822
Agribusiness	\$ (616)	\$ 2,749
Commercial auto	\$ (1,476)	\$ 4,857
Other	\$ (2,219)	\$ 5,990

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The analysis of our Credit Insurance lines of business quantifies the estimated impact on gross loss reserves of a reasonably likely scenario of varying the ratio applied to the unearned premium to determine the IBNR reserves at December 31, 2009. IBNR reserving methodology for this line of business focuses primarily on the use of a ratio applied to the unearned premium for each Credit Insurance product. The selected ratios are based on historical loss and claim data. In our analysis, we varied this ratio by +/- 5% across all Credit Insurance products combined. The results of our analysis show an increase or decrease, respectively, in gross reserves across all accident years combined of approximately \$6.7 million.

It is not appropriate to add together the total impact shown in the table above, as our lines of business are not directly correlated. It is important to note that the variations set forth in the table above are not meant to be a best-case or worst-case scenario, and therefore, it is possible that future variations may be more or less than the amounts set forth above. While we believe these are possible scenarios based on the information available to us at this time, we do not believe the reader should consider the above sensitivity analysis an actual reserve range.

**Reserving by class of business:**

The weight given to a particular actuarial method is dependent upon the characteristics specific to each class of business, including the types of coverage and the expected claim-tail.

*Short-tail business* Lines of business for which loss data emerge more quickly are referred to as short-tail lines of business. For these lines, emergence of paid losses and case reserves is credible and likely indicative of ultimate losses; therefore, more reliance is placed on the Loss or Expense Development methods.

Large catastrophe and weather events are analyzed separately using information from our claims staff and loss development profiles from similar events and from our own historical experience.

*Long-tail business* For long-tail lines of business, emergence of paid losses and case reserves is less credible in early periods and, accordingly, may not be indicative of ultimate losses. For these lines of business, more reliance is placed on the Bornhuetter Ferguson and Initial Expected Loss Ratio methods.

*Credit business* For credit lines of business, the IBNR is estimated either by applying a selected ratio to the unearned premium reserve or by using the loss development methods described above.

*Loss adjustment expenses* We estimate adjusting and other expense separately from loss reserves using the Calendar Year Paid-to-Paid method. Reserves for defense and cost containment expense are estimated separately from loss reserves, using either the Loss or Expense Development method or Ratio of Paid Defense and Cost Containment Expense to Paid Loss method.

***Reinsurance Recoverable***

Reinsurance recoverable balances include amounts owed to us in respect of paid and unpaid ceded losses and loss expenses and are presented net of a reserve for non-recoverability. At December 31, 2009 and 2008, reinsurance recoverable balances were \$371.7 million and \$482.8 million, respectively.

Recoveries on our gross ultimate losses are determined using distributions of gross ultimate loss by layer of loss retention to estimate ceded IBNR as well as through the review of individual large claims. The most significant assumption we use is the average size of the individual losses for those claims that have occurred but have not yet been recorded by us. The reinsurance recoverable is based on what we believe are reasonable estimates and is disclosed separately in the consolidated financial statements. However, the ultimate amount of the reinsurance recoverable is not known until all losses are settled.

We manage counterparty risk by entering into agreements with reinsurers we generally consider to be highly rated. However, we do not require a specified minimum rating. We monitor the concentrations of the reinsurers and reduce the participation percentage of lower-rated companies when appropriate. We believe we currently have no reinsurance amounts with any significant risk of becoming unrecoverable due to reinsurer insolvency.

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Our reinsurance contracts contain clauses that allow us to terminate the participation with reinsurers who are downgraded. Our risk assessment is comprised of industry ratings, recent news and reports, and a limited review of financials, for any new reinsurer under consideration. We also may require letters of credit, trust agreements, or cash advances from unauthorized reinsurers (reinsurers not licensed in our state of domicile) to fund their share of outstanding losses and LAE. Final assessment is based on the judgment of senior management.

**Pension and Postretirement Benefit Plans**

We maintain one open qualified defined benefit pension plan and one qualified defined benefit pension plan that is closed to new participants. In addition, we also sponsor three non-qualified defined benefit pension plans that restore benefits that would otherwise be curtailed by statutory limits on qualified plan benefits for certain key executives. We also provide certain health and life insurance benefits to qualified current and former employees.

The pension benefit and postretirement benefit obligations and related costs for all plans are calculated using actuarial concepts in accordance with the relevant GAAP pronouncements. Two key assumptions, the discount rate and the expected return on plan assets, are important elements of expense and/or liability measurement. We evaluate these key assumptions annually. Other assumptions involve demographic factors such as retirement age, mortality, turnover and rate of compensation increases.

As described in Note 2 to the Consolidated Financial Statements, effective December 31, 2006, the Company adopted ASC 715-30 (formerly FAS 158), *Employers Accounting for Defined Benefit Pension and Other Postretirement Plan*. In accordance with ASC 715-30, we recognize the funded status of defined benefit pension and other postretirement plans, on our consolidated balance sheet.

We use a discount rate to determine the present value of future benefits on the measurement date. The guideline for setting this rate is a high-quality long-term corporate bond rate. A higher discount rate decreases the present value of benefit obligations and decreases pension expense. To determine the expected long-term rate of return on plan assets, a building-block method is used. The expected rate of return on each asset is broken down into three components: (1) inflation, (2) the real risk-free rate of return (i.e. the long-term estimate of future returns on default-free U.S. government securities), and (3) the risk premium for each asset class (i.e. the expected return in excess of the risk-free rate). Using this approach, the precise expected return derived will fluctuate somewhat from year to year; however, it is our policy to hold this long-term assumption relatively constant.

The assumptions used in the measurement of our pension benefit obligations for 2009 and 2008 are as follows:

	Years Ended December 31,			
	2009		2008	
	Used for Net Benefit Cost in Fiscal Year 1/1/2009 to 12/31/2009	Used for Benefit Obligations as of 12/31/2009	Used for Net Benefit Cost in Fiscal Year 1/1/2008 to 12/31/2008	Used for Benefit Obligations as of 12/31/2008
Discount rate	6.17%	5.73%	6.10%	6.17%
Rate of compensation increase	4.20%	4.20%	4.20%	4.20%
Long-term rate return	7.65%	7.65%	7.65%	7.65%

For additional information regarding our pension plan obligations, see Note 15 to the Consolidated Financial Statements.



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***Other-Than-Temporary Impairment***

Our accounting policy requires that a decline in the fair value of investment securities below their amortized cost basis be evaluated to determine if the decline is other-than-temporary. There are a number of assumptions and estimates inherent in evaluating impairments to determine if they are other-than-temporary including 1) our ability and intent to hold the investment for a period of time sufficient to allow for an anticipated recovery in value; 2) the expected recoverability of principal and interest; 3) the length of time and extent to which the fair value has been less than amortized cost for fixed income securities or less than cost for equity securities; 4) the financial condition, near-term and long-term prospects of the issue or issuer, including relevant industry conditions and trends and implications of rating agency actions and offering prices; and 5) the specific reasons that a security is in a significant unrealized loss position, including market conditions, which could affect liquidity.

Realized gains are attributable to the sale of our invested assets, while realized losses are due to both the sale of investment assets and the write-down of investments from other-than-temporary impairments. In 2009, the consolidated pretax net realized loss on invested assets was \$75.7 million, with pre-tax realized loss of \$379.7 million and pre-tax realized gain of \$41.0 million reported for 2008 and 2007, respectively. Included in these amounts are other-than-temporary impairment write-downs of \$98.9 million, \$367.0 million and \$7.2 million for the years ended 2009, 2008 and 2007, respectively.

***Litigation Contingencies***

We review existing litigation matters and potential litigation items with counsel quarterly to determine if any adjustments to reserves for possible losses are necessary. Reserves for losses are established whenever they are probable and estimable. We establish reserves based on our best estimate of the probable loss. If no one number within the range of possible losses is more probable than any other, we record a reserve at the low end of the estimated range.

Based on information currently available, we believe that amounts ultimately paid, if any, arising from existing and currently potential litigation would not have a material effect on our results of operations and financial position. However, it should be noted that the frequency of large damage awards, which bear little or no relation to the economic damages incurred by plaintiffs continue to create the potential for an unpredictable judgment in any given lawsuit. It is possible that, if the defenses in these lawsuits are not successful, and the judgments are greater than we anticipate, the resulting liability could have a material impact on the consolidated financial results.

***Federal Income Taxes***

Our effective tax rate is based on income, non-taxable and non-deductible items, statutory tax rates and tax planning opportunities available. Inherent in determining our annual tax rate are judgments regarding business plans, planning opportunities and expectations about future outcomes.

Tax regulations require items to be included in the tax return at different times from the items reflected in the financial statements. As a result, the effective tax rate reflected in the financial statements is different than the actual rate applied on the tax return. Some of these differences are permanent such as expenses that are not deductible in our tax return, and some differences are temporary, reversing over time, such as valuation of insurance reserves. Temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that can be used as a tax deduction or credit in future years for which we have already recorded the tax benefit in our income statement. Deferred tax liabilities generally represent tax expense recognized in our consolidated financial statements for which tax payment has been deferred, or expenditures for which we have already taken a deduction in our tax return but have not yet recognized in our consolidated financial statements.



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The application of U.S. GAAP requires us to evaluate the recoverability of our deferred tax assets and establish a valuation allowance if necessary to reduce our deferred tax asset to an amount that is more likely than not to be realized. Considerable judgment is required in determining whether a valuation allowance is necessary, and if so, the amount of such valuation allowance. In evaluating the need for a valuation allowance we consider many factors, including: (1) the nature of the deferred tax assets and liabilities; (2) whether they are ordinary or capital; (3) taxable income in prior carryback years as well as projected taxable earnings exclusive of reversing temporary differences and carryforwards; (4) the length of time that carryovers can be utilized; (5) any unique tax rules that would impact the utilization of the deferred tax assets; and (6) any tax planning strategies that we would employ to avoid a tax benefit from expiring unused. Although realization is not assured, management believes it is more likely than not that, the deferred tax assets, net of valuation allowances, will be realized.

Our accounting represents management's best estimate of future events that can be appropriately reflected in the accounting estimates. Certain changes or future events, such as changes in tax legislation, geographic mix of earnings and completion of tax audits could have an impact on our estimates and effective tax rate. For example, the dividends received deduction or DRD, reduces the amount of dividend income subject to tax and is a significant component of the difference between our actual tax expense and the expected amount determined using the federal statutory tax rate of 35%. The U.S. Treasury Department and the Internal Revenue Service, or IRS, intend to address through regulations the methodology to be followed in determining the DRD related to variable life insurance and annuity contracts. A change in the DRD, including the possible retroactive or prospective elimination of this deduction through regulations or legislation, could increase our actual tax expense and reduce our consolidated net income. Our liability for income taxes includes the liability for unrecognized tax benefits, interest and penalties, which relate to tax years, still subject to review by the IRS or other taxing authorities. Audit periods remain open for review until the statute of limitations has passed. Generally, for tax years, which produce net operating losses, capital losses or tax credit carryforwards, or tax attributes, the statute of limitations does not close, to the extent of these tax attributes, until the expiration of the statute of limitations for the tax year in which they are fully utilized. The completion of review or the expiration of the statute of limitations for a given audit period could result in an adjustment to our liability for income taxes. The statute of limitations for the examination of federal income tax returns by the Internal Revenue Service for years 2005 to 2008 has either been extended or has not expired. In the opinion of management, all prior year deficiencies have been paid or adequate provisions have been made for any tax deficiencies that may be upheld.

**Table of Contents****Consolidated Results of Operations****Comparison of Years Ended December 31, 2009, 2008 and 2007**

The following is a discussion of our consolidated results of operations for the years ended December 31, 2009, 2008 and 2007 and should be read in conjunction with the *Outlook* section. For a discussion of our segment results, see *Results of Operations and Related Information by Segment*. The following table sets forth the consolidated results of operations (in thousands):

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
<b>Premiums and other revenues:</b>							
Premiums	\$ 1,974,024	\$ 1,888,495	\$ 1,999,623	\$ 85,529	4.5	\$ (111,128)	(5.6)
Other policy revenues	179,504	174,899	155,230	4,605	2.6	19,669	12.7
Net investment income	840,105	796,177	812,969	43,928	5.5	(16,792)	(2.1)
Realized investments gains (losses), net	(75,697)	(379,709)	41,027	304,012	(80.1)	(420,736)	(1,025.5)
Other income	31,843	38,779	47,224	(6,936)	(17.9)	(8,445)	(17.9)
<b>Total revenues</b>	<b>2,949,779</b>	<b>2,518,641</b>	<b>3,056,073</b>	<b>431,138</b>	<b>17.1</b>	<b>(537,432)</b>	<b>(17.6)</b>
<b>Benefits, losses and expenses:</b>							
Policy benefits	1,709,899	1,601,854	1,551,698	108,045	6.7	50,156	3.2
Interest credited to policy account balances	370,563	299,833	295,894	70,730	23.6	3,939	1.3
Commissions	459,943	475,345	456,537	(15,402)	(3.2)	18,808	4.1
Other operating costs and expenses	485,409	508,800	465,140	(23,391)	(4.6)	43,660	9.4
Change in deferred policy acquisition costs	(63,611)	(67,439)	(60,442)	3,828	(5.7)	(6,997)	11.6
<b>Total benefits and expenses</b>	<b>2,962,203</b>	<b>2,818,393</b>	<b>2,708,827</b>	<b>143,810</b>	<b>5.1</b>	<b>109,566</b>	<b>4.0</b>
<b>Income (loss) before other items and federal income taxes</b>	<b>\$ (12,424)</b>	<b>\$ (299,752)</b>	<b>\$ 347,246</b>	<b>\$ 287,328</b>	<b>(95.9)</b>	<b>\$ (646,998)</b>	<b>(186.3)</b>

**Summary**

Consolidated revenues increased during 2009 compared to those in 2008 primarily due to:

Decreased realized investment losses and increased investment income; and  
Increase in immediate annuity premiums.

Consolidated revenues declined in 2008 compared to those in 2007 primarily due to:

Investment losses realized during 2008, including \$367.0 million in other-than-temporary impairment write-downs;

Lower sales of our single premium immediate annuity products, caused by the drop in interest rates, which made the product less desirable; and

The declines were partially offset by other policy revenues arising primarily from mortality charges and fees on the in-force block of universal life policies 2008 witnessed a continuation of increased sales of universal life products experienced in 2007.

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Consolidated benefits and expenses increased for the year ended December 31, 2009, compared to the same period in 2008 primarily due to:

Increased policy benefits in annuities due to strong single premium immediate annuity sales resulting in an increase of the related reserve balance;

Increased interest credited to policy account balances due to an 18.2% increase in average account balances; and

These increases were partially offset by the decrease in other operating costs due to non-recurring litigation costs and costs for preparing for compliance with SEC and Sarbanes-Oxley requirements in 2008.

Consolidated benefits and expenses increased for the year ended December 31, 2008, compared to the same period in 2007, primarily due to:

The impact of increased catastrophe losses in our Property and Casualty business; and

Additional operating expenses incurred due to non-recurring litigation costs and costs for preparing for compliance with SEC and Sarbanes-Oxley requirements.

An increase in benefits paid on the growing block of annuity business.

**Table of Contents****Results of Operations and Related Information by Segment****Life****Comparison of Years Ended December 31, 2009, 2008 and 2007**

The Life segment markets traditional life insurance products such as whole life and term life, and interest sensitive life insurance products such as universal life, variable universal life and as well as indexed universal life. These products are marketed on a nationwide basis through employee agents, multiple line agents, independent agents and brokers and direct marketing channels.

Life segment financial results for the periods indicated were as follows (in thousands, except percentages):

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
<b>Revenues:</b>							
Premiums	\$ 284,530	\$ 299,338	\$ 315,893	\$ (14,808)	(4.9)	\$ (16,555)	(5.2)
Other policy revenues	164,748	154,984	130,744	9,764	6.3	24,240	18.5
Net investment income	222,611	226,643	229,092	(4,032)	(1.8)	(2,449)	(1.1)
Other income	2,720	3,767	3,967	(1,047)	(27.8)	(200)	(5.0)
<b>Total revenues</b>	<b>674,609</b>	<b>684,732</b>	<b>679,696</b>	<b>(10,123)</b>	<b>(1.5)</b>	<b>5,036</b>	<b>0.7</b>
<b>Benefits, losses and expenses:</b>							
Policy benefits	297,719	296,078	273,750	1,641	0.6	22,328	8.2
Interest credited to policy account balances	58,983	62,221	63,289	(3,238)	(5.2)	(1,068)	(1.7)
Commissions	91,968	126,813	141,517	(34,845)	(27.5)	(14,704)	(10.4)
Other operating costs and expenses	185,048	222,908	200,361	(37,860)	(17.0)	22,547	11.3
Change in deferred policy acquisition costs	1,536	(42,103)	(57,666)	43,639	(103.6)	15,563	(27.0)
<b>Total benefits, losses and expenses</b>	<b>635,254</b>	<b>665,917</b>	<b>621,251</b>	<b>(30,663)</b>	<b>(4.6)</b>	<b>44,666</b>	<b>7.2</b>
<b>Income (loss) before other items and federal income taxes</b>	<b>\$ 39,355</b>	<b>\$ 18,815</b>	<b>\$ 58,445</b>	<b>\$ 20,540</b>	<b>109.2</b>	<b>\$ (39,630)</b>	<b>(67.8)</b>

For the year ended December 31, 2009, earnings increased compared to 2008. The overall increase we experienced in 2009 can be primarily attributed to the cost of two lawsuit settlements in 2008 and the corresponding impact on other operating costs and expenses. In addition, costs related to our initial SEC registration and expenses related to the implementation of Sarbanes-Oxley compliance decreased compared to 2008. Our benefit to revenue ratio was 52.9% for 2009 compared to 52.3% in 2008. These results are discussed in further detail below.

During the second quarter of 2009, we paid premium refunds as the result of a class action settlement made by us in May 2007. The refunds on the credit life product resulted in issuing \$12.9 million in settlement payments in 2009 comprised of credit life premium refunds and other related damages and fees, to certain previously insured persons.

The Life segment was fully reserved for this settlement and did not incur any related impact to its gain from operations for the year ended December 31, 2009. However, during the second quarter of 2009, several categories of the statement of income were impacted by the recording of the settlement as follows: premiums were decreased by \$4.5 million, other income was decreased by \$0.8 million, commissions were decreased by \$0.9 million, and other operating costs and expenses were decreased by \$4.5 million. For additional information on this settlement, refer to the discussion of the *Perkins* litigation in Note 16 to the Consolidated Financial Statements in our amended Form 10 Registration Statement, filed with the SEC on July 1, 2009.

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Overall, 2008 earnings decreased compared to 2007. The decrease in earnings primarily resulted from certain non-recurring expenses, an increase in the benefit to revenue ratio, a decrease in net investment income, and the declining credit market. The non-recurring expenses related to lawsuit settlements and initial SEC registration expenses and implementation costs related to Sarbanes-Oxley compliance. The life benefits to revenue ratio increased from 49.6% for 2007 to 52.3% for 2008. An unexpected sales increase of higher issue age policies in 2007 resulted from one plan that was very competitively priced at those higher ages. During 2008, we implemented a re-pricing of lifetime guarantee universal life plans to include increases in premiums at the higher issue ages to be more conservatively priced. Also, the declining credit market indirectly caused the loss of funding for a sizable number of life policies that were using a low-interest bank loan program to reduce the net insurance cost of the policies. The source of funding for a portion of the bank loans was discontinued, resulting in the withdrawal of cash values and the subsequent loss of gross margins of the related policies. In addition to the above, net investment income decreased due to a continued decline in overall portfolio rates on investments of the Life segment.

***Premiums***

Revenues from traditional life insurance products include scheduled premium payments from policyholders on whole life and term life products. These premiums are in exchange for financial protection for the policyholder from a specific insurable event, such as death or disability. The change in these premiums is impacted by new sales during the period and the persistency of in-force policies.

Premiums decreased for the years ended December 31, 2009 compared to 2008 and during 2008 compared to 2007. Related to the previously noted settlement payments, we recorded a reversal of \$4.5 million. Excluding the effect of the settlement payments, premiums decreased \$10.3 million for the year ended December 31, 2009. The decrease in premiums can be attributable to an increase in ordinary life ceded reinsurance premiums, which is the result of increasing YRT ( Yearly Renewable Term ) renewal premiums on the higher face amounts issued in 2007 and 2008. We do not expect to see this trend towards higher utilization of reinsurance on large face amounts to continue for new business issued in 2010. Also adding to the decrease was a drop in credit insurance premiums, which was a result of lower credit sales in the declining auto industry.

***Other Policy Revenues***

Other policy revenues include mortality charges, earned policy service fees, and surrender charges on interest sensitive life insurance policies. These charges increased for the year ended December 31, 2009 compared to 2008. Other policy revenues had also increased in 2008 compared to 2007. The increases were primarily due to higher mortality charges and fees, which are a result of the large volume of sales of lifetime secondary guarantee universal life products in 2007 and 2008.

***Net Investment Income***

Net investment income decreased for the year ended December 31, 2009 compared to 2008. The decrease reflects the increased amount of cash we held during the year and the lower yields on the cash. We will continue to hold onto our cash position until appropriate long-term investment opportunities arise. The significant cash position we hold in excess of normal liquidity needs are generally of short duration.

Net investment income in the Life segment decreased slightly for the year ended December 31, 2008 compared to 2007. This decrease was due to a small decline in the investment yield earned on the block of invested assets supporting the Life segment. We continuously manage the crediting rates on interest sensitive products to reflect the lower yields and maintain a suitable interest spread.

Non-interest sensitive life products, such as whole life and term life policies cannot be adjusted to reflect a change in earned investment rates. In a low interest rate environment, the effect of this lower yield earned directly impacts earnings.

***Policy Benefits***

Policy benefits include death claims, surrenders and other benefits paid to traditional whole life and term life policyholders (net of reserves released on terminated policies), reserve increases on existing traditional life policies (reflecting the passage of time on persisting policies in anticipation of future claims), claim benefits in excess of account balances returned to interest sensitive life policyholders, and interest credited on account balances.





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Benefits increased slightly for the year ended December 31, 2009 compared to 2008. The increase was primarily the result of higher claim dollar values. Benefits increased for the 2008 compared to 2007. This increase was due to the claims and reserve costs associated with the \$24.2 million increase in other policy revenues that occurred from the sales of universal life lifetime secondary guarantee policies, including an \$11.0 million increase in reserve accrual expense.

**Commissions**

Commissions decreased for the year ended December 31, 2009 compared to 2008. Related to the previously noted settlement payments, we recorded a reversal of \$0.9 million. Excluding the effect of the settlement payments, commissions decreased \$33.9 million for the year ended December 31, 2009. The decrease was primarily attributable to lower first year universal life premiums. Partially offsetting the decrease in commissions was the increase in renewal commissions at a lower rate on a large volume of business sold in 2008. In addition, credit life business experienced a decrease in sales for 2009 as a result of the downturn in the economy and the constraints of the credit markets. Commissions also decreased in 2008 compared to 2007. During 2008, we implemented a re-pricing of lifetime guarantee universal life plans to include increases in premiums at higher issue. As a result, we experienced a decrease in sales of interest sensitive products from the level of sales established in 2007.

**Other Operating Costs and Expenses**

Other operating costs and expenses decreased for the year ended December 31, 2009 compared to 2008. Related to the previously noted settlement payments, we recorded a reversal of \$4.5 million in previously accrued expenses. Excluding the effect of the settlement payments, other operating costs and expenses decreased \$33.4 million for the year ended December 31, 2009. The decrease was primarily due to a decrease in production bonuses, which is directly a result of lower sales in 2009. Additionally, there was a reduction in marketing expenses for our Direct Marketing channel. Other operating costs and expenses increased for the year ended December 31, 2008, compared to 2007. Much of this increase resulted from the non-recurring legal costs related to the two lawsuits, the *Farm Bureau* litigation in our multiple line marketing division and the *Perkins* litigation in the credit life marketing line. See Note 16 to the Consolidated Financial Statements in our amended Form 10 Registration Statement, filed with the SEC on July 1, 2009 for a discussion on these cases.

**Change in Deferred Policy Acquisition Costs**

The following table presents the components of the change in DAC for the years ended December 31, 2009, 2008 and 2007 (in thousands, except percentages):

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
Acquisition cost capitalized	\$ 77,162	\$ 129,031	\$ 144,936	\$ (51,869)	40.2	\$ (15,905)	11.0
Amortization of DAC	(78,698)	(86,928)	(87,270)	8,230	9.5	342	0.4
<b>Change in deferred policy acquisition costs</b>	<b>\$ (1,536)</b>	<b>\$ 42,103</b>	<b>\$ 57,666</b>	<b>\$ (43,639)</b>	<b>103.6</b>	<b>\$ (15,563)</b>	<b>27.0</b>

We regularly review the underlying DAC assumptions, including future mortality, expenses, lapses, premium persistency, investment yields and interest spreads. Relatively minor adjustments to these assumptions can significantly impact changes in DAC. We monitor the amortization of DAC as a percentage of gross profits before DAC amortization, as a deterioration of this ratio could indicate an emergence of adverse experience affecting the future profitability of a particular block of business and, in turn, affect the recoverability of DAC from such future profits.



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Acquisition costs capitalized decreased for the year ended December 31, 2009 compared to 2008. We also experienced a decrease in 2008 compared to 2007. These decreases resulted from the decline in production related compensation in first year commissions in our Independent Marketing Group. The amortization of DAC as a percentage of gross profits for the years ended December 31, 2009, 2008 and 2007 was 43.3%, 44.5 % and 41.1%, respectively. The change in the ratio for 2009 was primarily attributable to the premium refund lawsuit as previously discussed. The deterioration of the ratio in 2008 was a result of reduced gross profits from overall reduced profitability of the life business. Profitability was down due to decreased investment yields, increased surrenders and higher expenses due to our initial SEC registration and implementation costs related to Sarbanes-Oxley compliance. An increase in the lapse rate would cause acceleration in DAC amortization; therefore, the lapse rate is an important measure of company performance. The average lapse/surrender rates in the Life segment were 10.7%, 10.5% and 10.1% for the years ended December 31, 2009, 2008 and 2007, respectively. These combined rates reflected both first year and renewal business. First year lapse rates are typically much higher on traditional life business than in later years. In general, stable or lower lapse rates are important toward maintaining profitability of the Life segment, as higher lapse rates will reduce the average life expectancy of the in-force block of business and could result in acceleration in the amortization of DAC. Over the course of 2007 through 2009, we experienced normal fluctuations in lapse rates.

**Reinsurance**

The table below summarizes reinsurance reserve and premium amounts assumed and ceded for the years ended December 31, 2009, 2008 and 2007 (in thousands):

	Reserves			Premiums		
	Years Ended December 31,			Years Ended December 31,		
	2009	2008	2007	2009	2008	2007
Reinsurance assumed	\$ 19,514	\$ 25,553	\$ 28,413	\$ 4,512	\$ 8,460	\$ 10,355
Reinsurance ceded	(160,934)	(147,523)	(124,316)	(74,577)	(80,826)	(66,068)
<b>Total</b>	<b>\$ (141,420)</b>	<b>\$ (121,970)</b>	<b>\$ (95,903)</b>	<b>\$ (70,065)</b>	<b>\$ (72,366)</b>	<b>\$ (55,713)</b>

We use reinsurance to mitigate excessive risk to the Company. Our current retention limit is \$700,000 for traditional and universal life. Accidental death benefits and premium waiver benefits are fully retained on new business issued beginning in 2008. Increases in reserves and premium amounts ceded primarily reflect increased use of reinsurance in conjunction with treaties related to universal life products.

We periodically adjust our reinsurance program and retention limits as market conditions warrant, consistent with our corporate risk management strategy. While we have, in the past, reinsured up to 90% of new business, we are currently reinsuring newly developed permanent products on a modified excess retention basis, in which we reinsure mortality risk on a yearly renewable term basis, ceding a 75% quota share of policies with a face value of at least \$500,000 up to our retention and then a 100% quota share in excess of retention. Term products are coinsured between 90% and 100% on a first-dollar quota share basis. The current term portfolio is also coinsured with a 90% quota share up to our retention and then a 100% quota share in excess of retention.

In the case of credit life business, we use reinsurance primarily as a means to provide producers of credit-related insurance products the opportunity to participate in the underwriting risk through offshore producer-owned reinsurance companies. The reinsurance treaties entered into by the Credit Insurance Division are normally written on a 100% coinsurance basis with benefit limits of \$100,000 on credit life.

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Our individual life reinsurance is primarily placed with highly rated companies, and we monitor the financial condition of those companies on a routine basis. For 2009, the companies where we have placed material amounts of reinsurance for the Life segment are shown in the table below (in thousands, except percentages):

Reinsurer	A.M. Best Rating	Ceded Premiums	Percentage of Total Gross Premium
Swiss Re Life and Health of America	A	\$ 22,476	6.3%
Transamerica Life Insurance Company	A	10,728	3.0%
Munich	A+	10,782	3.0%
General Re Life Corporation	A++	8,175	2.3%
Revios/SCOR	A-	6,560	1.9%
Canada Life Reinsurance	A+	5,000	1.4%
Other Reinsurers with no single company greater than 1% of the total		7,323	2.1%
<b>Total life reinsurance ceded</b>		<b>\$ 71,044</b>	<b>20.0%</b>

**Policy in-force information**

The following tables summarize changes in the Life segments in-force amounts and policy counts (in thousands, except percentages):

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
<b>Life insurance in-force:</b>							
Traditional life	\$ 45,229,407	\$ 45,007,657	\$ 44,538,506	\$ 221,750	0.5	\$ 469,151	1.1
Interest sensitive life	24,218,843	24,863,199	24,144,561	(644,356)	(2.6)	718,638	3.0
<b>Total life insurance in-force</b>	<b>\$ 69,448,250</b>	<b>\$ 69,870,856</b>	<b>\$ 68,683,067</b>	<b>\$ (422,606)</b>	<b>(0.6)</b>	<b>\$ 1,187,789</b>	<b>1.7</b>

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
<b>Number of policies:</b>							
Traditional life	2,347,423	2,451,748	2,606,012	(104,325)	(4.3)	(154,264)	(5.9)
Interest sensitive life	174,738	175,553	176,628	(815)	(0.5)	(1,075)	(0.6)
<b>Total number of policies</b>	<b>2,522,161</b>	<b>2,627,301</b>	<b>2,782,640</b>	<b>(105,140)</b>	<b>(4.0)</b>	<b>(155,339)</b>	<b>(5.6)</b>

The decreasing trend in our policy count is attributable to new business activity being comprised of fewer, but larger face-value policies. However, we experienced higher levels of traditional life in-force, due to the larger face values on

those policies. The changes in the Life segment are relatively normal to our business.

**Table of Contents****Annuity****Comparison of Years Ended December 31, 2009, 2008 and 2007**

We develop, sell and support a variety of immediate and deferred annuities, including fixed, equity-indexed and variable products. We sell these products through independent agents, brokers, financial institutions, and multiple line and employee agents. Segment financial results for the periods indicated were as follows (in thousands, except percentages):

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
<b>Revenues:</b>							
Premiums	\$ 220,284	\$ 116,248	\$ 222,748	\$ 104,036	89.5	\$ (106,500)	(47.8)
Other policy revenues	14,756	19,915	24,486	(5,159)	(25.9)	(4,571)	(18.7)
Net investment income	449,035	374,023	364,607	75,012	20.1	9,416	2.6
Other income	(3,870)	(5,718)	345	1,848	(32.3)	(6,063)	(1,757.4)
<b>Total revenues</b>	<b>680,205</b>	<b>504,468</b>	<b>612,186</b>	<b>175,737</b>	<b>34.8</b>	<b>(107,718)</b>	<b>(17.6)</b>
<b>Benefits, losses and expenses:</b>							
Policy benefits	249,709	142,867	249,878	106,842	74.8	(107,011)	(42.8)
Interest credited to policy account balances	311,580	237,612	232,605	73,968	31.1	5,007	2.2
Commissions	107,053	79,213	58,635	27,840	35.1	20,578	35.1
Other operating costs and expenses	59,254	45,491	35,030	13,763	30.3	10,461	29.9
Change in deferred policy acquisition costs	(62,013)	(20,690)	(911)	(41,323)	199.7	(19,779)	2,171.1
<b>Total benefits, losses and expenses</b>	<b>665,583</b>	<b>484,493</b>	<b>575,237</b>	<b>181,090</b>	<b>37.4</b>	<b>(90,744)</b>	<b>(15.8)</b>
<b>Income (loss) before other items and federal income taxes</b>	<b>\$ 14,622</b>	<b>\$ 19,975</b>	<b>\$ 36,949</b>	<b>\$ (5,353)</b>	<b>(26.8)</b>	<b>\$ (16,974)</b>	<b>(45.9)</b>

Income from continuing operations decreased for the year ended December 31, 2009 compared to 2008 and during 2008 compared to 2007. A number of factors contributed to pressure on earnings, including compressed earned investment spreads, decreased annuity surrender charge revenue and certain non-recurring expenses. The expense increases are primarily due to consultant fees related to our initial SEC registration and implementation costs associated with Sarbanes-Oxley compliance. In addition, 2008 expenses increased due to lawsuit settlements. Interest spreads in 2009 were decreased from 2008 levels as a result of yields decreasing on a relatively large cash position, which slightly increased from 2008. We experienced similar events with our interest spread during 2008 compared to 2007, as our cash position had built up, as a result of the very large inflow of funds into fixed deferred annuities just as

rates on short-term invested assets were starting to fall. The decreases in cash yield continues a trend first observed in 2008, but the decrease in 2009 was much more substantial than in 2008.

Surrender charge revenue decreased in 2009 compared to 2008 as a result of lower surrender volume. Also, our products with defined market value adjustment formulas, applicable to surrenders in the first ten years, had larger reductions to 2009 surrender charges due to positive market value adjustments. Surrender charge revenue also decreased in 2008 compared to 2007, despite the fact that total withdrawals increased from 2007 to 2008. This was a result of a shift in the proportion of surrenders that incurred surrender charges versus surrenders that did not incur charges. There was a larger number of policyholders who took advantage of an option provided under certain contracts that permits a withdrawal without penalty during a thirty-day window following the end of a guaranteed interest period. We expect to continue to see policyholders reaching their guarantee period surrender window and electing to surrender without penalty. As a result of the higher level of surrender activity on fixed deferred annuities in 2008 compared to 2007, DAC amortization expense increased, further contributing to the decrease in earnings.

**Table of Contents****Premiums**

Annuity premium and deposit amounts received during the last three years are shown in the table below (in thousands, except percentages):

	Years Ended December 31,			Change Over Prior Years			
	2009	2008	2007	2009		2008	
				amount	percentage	amount	percentage
Fixed deferred annuity	\$ 1,715,871	\$ 1,573,237	\$ 789,012	\$ 142,634	9.1	\$ 784,225	99.4
Equity indexed deferred annuity	239,664	85,334	90,327	154,330	180.9	(4,993)	(5.5)
Single premium immediate annuity	227,937	121,952	227,617	105,985	86.9	(105,665)	(46.4)
Variable deferred annuity	99,429	103,233	119,507	(3,804)	(3.7)	(16,274)	(13.6)
<b>Total</b>	<b>2,282,901</b>	<b>1,883,756</b>	<b>1,226,463</b>	<b>399,145</b>	<b>21.2</b>	<b>657,293</b>	<b>53.6</b>
Less: policy deposits	(2,062,617)	(1,767,508)	(1,003,715)	(295,109)	16.7	(763,793)	76.1
<b>Total earned premiums</b>	<b>\$ 220,284</b>	<b>\$ 116,248</b>	<b>\$ 222,748</b>	<b>\$ 104,036</b>	<b>89.5</b>	<b>\$ (106,500)</b>	<b>(47.8)</b>

Amounts received on single premium immediate annuities are classified as premiums and are taken immediately into income. Amounts received from deferred annuity policyholders and equity-indexed annuity policyholders are classified as deposits and are not immediately taken into income. Interest earned on the policyholder's deposits is classified as income. Fees assessed against variable annuity policyholder funds are reported as income.

Fixed deferred annuity receipts for the year ended December 31, 2009 increased compared to 2008. The increase in sales of our fixed annuity products is a result of lower rates on competing products such as CDs and money market funds. We can also attribute a portion of the increase to the economic environment. Equity-indexed deferred annuity sales also increased for the year ended December 31, 2009 compared to 2008. The increase in those sales was a result of investors accepting some risk in the pursuit of potentially higher returns. Equity-indexed annuities allow policyholders with greater risk tolerance to participate in equity returns while also having downside protection resulting from the guaranteed minimum returns defined in the product.

Fixed deferred annuity receipts increased in 2008 compared to 2007. The increase in premiums was the result of the economic circumstances leading investors to seek safer, less volatile investment avenues. Equity-indexed annuity premiums for the year ended December 31, 2008 compared to 2007 were relatively flat.

Single premium immediate annuities increased in 2009 compared to 2008. The increase in sales is a direct result of consumers' search for a more stable retirement income. We believe this upward trend will continue as more investors nearing retirement will change asset distribution strategies. Premiums from single premium immediate annuities decreased for the year ended December 31, 2008 compared to 2007. In 2007, premium income had increased by \$49.8 million from a small group of very large policies sold.

The competitiveness of rates on all our annuity products can change very quickly and premium income will reflect changes in our position relative to the financial marketplace. Cash flows from these products, therefore, can be somewhat volatile from period to period.

Variable annuity products are a relatively small portion of our annuity portfolio. Variable deferred annuity premiums and deposits decreased for the year ended December 31, 2009 compared to 2008 and during 2008 compared to 2007.



These decreases are primarily attributable to our decision to not offer income guarantees on our variable annuity business.

**Table of Contents****Other Policy Revenues**

Other policy revenues include surrender charges, variable annuity management and expense fees, other expense charges, and charges for riders on deferred annuities. Other policy revenues decreased for the year ended December 31, 2009 compared to 2008. We also experienced a decrease during 2008 compared to 2007. The decreases in other policy revenues are primarily a result of the decline in total collected surrender charges. The decrease in surrender charges in 2009 compared to 2008 resulted from lower surrenders. Also, in 2009 we had larger surrender charge reductions resulting from positive market value adjustments on contracts with defined market value adjustment formulas. In 2008, we had lower surrender charges compared to 2007, despite the fact that surrender volumes increased from 2007 to 2008. This was due to a change in the mix of surrenders between policyholders who incurred surrender charges and those where policyholders utilized their optional penalty-free withdrawal provisions. The annualized surrender rates on deferred annuities, which represent all withdrawals both full and partial, were 11.5%, 14.6% and 12.3% of account balances for 2009, 2008 and 2007, respectively.

**Net Investment Income**

Net investment income, which is a key component of the profitability of the Annuity segment increased for the year ended December 31, 2009 compared to 2008 and during 2008 compared to 2007. The increases were largely due to an increase in the asset base, brought about by an increase in the volume of in-force fixed deferred annuity account balances. In 2009, our fixed deferred annuity account values rose by \$1.2 billion to \$8.2 billion compared to an increase of \$707.9 million in 2008 and \$89.0 million in 2007. Also contributing to the increases in net investment income was the positive change in realized and unrealized gains on call option derivative. Call option derivative gains increased \$29.8 million to \$5.4 million during 2009. The increase in investment income in 2008 was partially offset by the \$24.3 million negative market value adjustment on these call option derivatives. Note that the call option gains and losses are largely offset by related reserve adjustments on the embedded derivative in the associated equity-indexed annuity contracts. These embedded derivatives are reported as liabilities on the consolidated statement of financial position and are recorded and measured at fair value.

Realized and unrealized gains or losses on the derivative hedge portfolio are recognized in earnings as investment income. Equity-indexed annuities include a fixed host annuity contract and an embedded equity derivative. The gain or loss on the embedded option is recognized in earnings as interest credited to policyholders.

The following table details the gain or loss on derivatives related to equity-indexed annuities (in thousands, except percentages):

	Years Ended December 31,			Change Over Prior Years	
	2009	2008	2007	2009	2008
Derivative gain/(loss) included in net investment income	\$ 5,380	\$ (24,400)	\$ (141)	\$ 29,780	\$ (24,259)
Embedded derivative gain/(loss) included in interest credited	\$ (8,138)	\$ 23,184	\$ 434	\$ (31,322)	\$ 22,750

For a number of years, earnings in the Annuity segment have been pressured by a long-term trend of lower average yield rates on the bonds and mortgage loans supporting the reserves. Offsetting the effect of lower yield rates, crediting rates on interest sensitive products have been decreased accordingly where permitted by policy terms. Since approximately 90% of the Annuity segment is interest sensitive, offsetting credited rate adjustments are usually possible subject to minimum interest rate guarantees that may apply. All contracts also have minimum floor interest rate guarantees, and we have reconfigured the product portfolio to lower those guarantees in response to the current low interest rate environment.