AMERICAN NATIONAL INSURANCE CO /TX/
Form 10-K
March 08, 2013
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended December 31, 2012

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 incorporation or organization)	**(I.R.S. Employer Identification No.)**
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 x 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 x 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. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

Indicate by check mark 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. ¨

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:

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

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

The aggregate market value on June 30, 2012 (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 $516.9 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, 2013, there were 26,898,717 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 registrant s Definitive Proxy Statement to be filed within 120 days of the close of the registrant s fiscal year in conjunction with the registrant s annual meeting of shareholders.

AMERICAN NATIONAL INSURANCE COMPANY

TABLE OF CONTENTS

PART I	
ITEM 1. BUSINESS	3
ITEM 1A. RISK FACTORS	11
ITEM 1B. UNRESOLVED STAFF COMMENTS	20
ITEM 2. PROPERTIES	20
ITEM 3. LEGAL PROCEEDINGS	21
ITEM 4. MINE SAFETY DISCLOSURES	21
PART II	
ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES	21
ITEM 6. SELECTED FINANCIAL DATA	23
ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	23
ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	59
ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA	62
ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE	104
ITEM 9A. CONTROLS AND PROCEDURES	104
ITEM 9B. OTHER INFORMATION	105
PART III	
ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE	105
ITEM 11. EXECUTIVE COMPENSATION	105
ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS	105
ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE	105
ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES	105
PART IV	
ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES	106
INDEX TO EXHIBITS	106
SIGNATURES	108

Table of Contents

PART I

ITEM 1. BUSINESS

Company Overview

American National Insurance Company has more than 100 years of experience. We have maintained our corporate headquarters in Galveston, Texas since our founding in 1905. Our core businesses are life insurance, annuities and property and casualty insurance. We also offer pension services and limited health insurance. We provide personalized service to approximately six million policyholders throughout the United States, the District of Columbia, Puerto Rico, Guam, and American Samoa.

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

Business Strategy

Our vision is 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 corporate culture. We have an unwavering commitment to serve our agents, policyholders, and shareholders 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 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.

Business Segments

Our family of companies includes six life insurance companies, eight property and casualty insurance companies, and numerous non-insurance subsidiaries. Our business segments are:

Life Segment We provide the following products under our Life segment:

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, and 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.

Term Life. Term life products provide 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.

Universal Life. Universal life products provide insurance coverage through a contract that gives the policyholder flexibility in premium payments and coverage amounts. Universal life products may allow the insured, within certain limits, 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 interest rate sensitive, and we determine the interest crediting rates, subject to specified minimums.

Equity-indexed universal life products have the same features as the universal life products, but also allow policyholders to earn additional return through interest credited tied to the performance of a particular stock index, such as the S&P 500.

Table of Contents

Variable Universal Life. Variable universal life products provide insurance coverage on the same basis as universal life, except that the policyholder bears the investment risk because the value of the policyholder s account balance varies with the investment experience of the securities held in the separate accounts selected by the policyholder.

Credit Life Insurance. Credit life insurance products are sold in connection with a loan or other credit account. Credit life insurance products are designed to pay off the borrower s remaining debt to the lender on a loan or credit account if the borrower dies during the coverage period.

Annuity Segment We provide the following products under our Annuity segment:

Deferred Annuity. A deferred annuity is an asset accumulation product. Deposits are received as a single payment, in the case of a single premium deferred annuity, or as multiple payments, in the case of a flexible premium deferred annuity. Deposits are credited with interest at our determined rates subject to policy minimums. For certain limited periods of time, usually from one to ten years, interest rates are guaranteed not to change. Deferred annuities usually have surrender charges that begin at issue and grade off over time and may have market value adjustments that can have a positive or negative effect on any surrender value.

An equity-indexed deferred annuity is credited with interest at minimum rates established by state insurance law. Any additional interest credited is typically tied to the performance of a particular stock market index.

Single Premium Immediate Annuity (SPIA). A SPIA is purchased with one premium payment, providing guaranteed periodic (usually monthly or annual) income payments to the annuitant for a specified period, such as for the remainder of the annuitant s life. Return of the original deposit may not be guaranteed, depending on the terms of the annuity contract.

Variable Annuity. In a variable annuity the policyholder bears the investment risk because the value of the policyholder s account balance varies with the investment experience of the securities held in the separate accounts selected by the policyholder.

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

Medicare Supplement. Medicare Supplement insurance is a type of private health insurance designed to supplement or pay the costs of certain medical services not covered by Medicare.

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

Medical Expense. Medical expense insurance covers most health expenses including hospitalization, surgery and outpatient services (excluding dental and vision costs). We discontinued new sales of this coverage in June 2010; however renewals continues to affect our operating results.

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

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

Aggregate Stop-Loss. Aggregate stop-loss coverage reimburses the employer once the group s total paid claims reach a 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 coverage period.

Table of Contents

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

Personal Lines. Personal lines include insurance policies issued to individuals for personal auto, homeowners and other personal exposures. Personal auto insurance covers specific risks involved in owning and operating an automobile. Homeowner insurance provides coverage that protects the insured s property against loss from perils. Other personal insurance provides coverage for property such as boats, motorcycles and recreational vehicles.

Commercial Lines. Agribusiness insurance comprises the majority of our commercial lines. This includes property and casualty coverage tailored for a farm, ranch, vineyard or other agricultural business, contractors, and business within the rural and suburban markets. Commercial auto insurance is typically issued in conjunction with the sale of our agribusiness insurance and covers specific risks involved in owning and operating vehicles. Other commercial insurance is also sold along with our agribusiness policy and encompasses property, liability and workers compensation coverages.

Credit-Related Property Insurance Products. We primarily offer the following credit insurance products:

Collateral or *Creditor Protection Insurance* (CPI). CPI provides insurance against loss, expense to recover, or damage to personal property (typically automobiles) pledged as collateral resulting from fire, burglary, collision, or other loss occurrence that would either impair a creditor s interest or adversely affect the value of the collateral. The coverage is purchased according to the terms of the credit obligation when the borrower fails to provide the required insurance. The cost of the insurance is charged to the borrower.

Guaranteed Auto Protection or *Guaranteed Asset Protection* (GAP). GAP insures the excess of the outstanding indebtedness over the primary property insurance benefits that may occur when there is a total loss to or an unrecovered theft of the collateral. GAP can be written on a variety of assets that are used as collateral to secure credit; however, it is most commonly written on automobiles.

Corporate and Other Segment Our Corporate and Other segment encompasses primarily our invested assets not used to support insurance activities. It also includes our non-insurance subsidiaries, such as investment advisory services.

Marketing Channels

Product distribution is managed to satisfy specific markets in such a way that channel conflict across our five marketing channels is minimized and key brand identities are maintained. Whenever possible, products are cross-sold to maximize product offerings and return on investment in products and distribution. Our marketing channels are:

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

IMG also markets to individuals who favor purchasing insurance directly from insurance companies. Direct Marketing offers life insurance to middle-income customers through multiple channels including direct mail, internet and call centers.

Career Sales and Service Division (CSSD) The Career Sales and Service Division offers life insurance, annuities, and limited benefit health insurance products through exclusive employee agents primarily to the middle-income market. The Division s business model is structured to distribute new products as well as provide door-to-door collections and personalized service to the customer via agents located throughout the United States. CSSD has evolved its operations to more of a non-traditional home service model by offering a wider variety of products and alternative payment options to meet the changing needs of the customer. The Career Sales and Service Division s roots can be traced back to The Company s founding in 1905.

Table of Contents

Multiple-line offers life insurance, annuities, and property and casualty insurance primarily through dedicated agents. Multiple-line is committed to remain a 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 individuals, families, and small business owners at all income levels.

Health Division through independent agents and managing general underwriters, primarily serves the needs of middle-income seniors and individuals preparing for retirement. The Health 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. Health Division is responsible for the administration of health insurance products sold by other marketing channels.

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 calculated to meet our future obligations on our outstanding policies. We compute the amounts for policyholder liabilities in accordance with generally accepted accounting principles (GAAP) and the standards of practice of the American Academy of Actuaries.

We establish 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 premiums and claims payable) and for unearned revenue (the unamortized portion of front-end loads charged). We also establish liabilities for unpaid claims and claim adjustment expenses, including those that have been incurred but not yet reported. In addition, we establish liabilities for minimum death benefit guarantees relating to certain annuity contracts, secondary guarantees relating to certain life policies and fair value reserves for living benefits embedded derivative guarantees.

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 future policy benefits determined using GAAP.

Additional information regarding our policyholder liabilities may be found in Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates *Reserves* section.

Risk Management

A conservative operating philosophy was a founding principle for our Company which is supported by our focus on sustainable and profitable growth. We manage risks throughout the Company by employing controls in our insurance and investment 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 have a formal risk management program on an enterprise-wide basis to coordinate risk management efforts and ensure alignment between our risk-taking activities and our strategic objectives. This risk management program includes a corporate risk officer who chairs a Management Risk Committee to ensure consistent application of the enterprise risk management process across all business segments. The Audit Committee of the Board of Directors also reviews the Company s risk assessment and risk management policies. Finally, we make use of several senior management committees to support the discussion and enforcement of risk controls in our management of the Company.

Table of Contents

Our insurance products are designed to offer a balance of features desired by the marketplace with provisions that mitigate our risk exposures to allow prudent management across our insurance portfolio. We employ underwriting standards to ensure proper rates are 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.

One of our significant risks is the management of the linkage between the timing of settlement and the amount of obligations related to our insurance and annuity contracts and the cash flows and valuations of the invested assets backing those obligations, a process commonly referred to as asset-liability management (ALM). This risk is most present in our Life and Annuity segments. Our ALM Committee regularly monitors the level of risk in the interaction of our assets and liabilities and helps shape courses of action intended to attain our desired risk-return profile. Investment allocations and duration targets also limit the risk exposure in our annuity products by limiting the credited rate to a range supported by these investments. Some of the additional tools which help shape investment decisions include deterministic and stochastic interest rate scenario analyses using a licensed, third party economic scenario generator and detailed insurance ALM models. These models also use experience analyses related to surrenders and death claims.

We also manage risk by using reinsurance to limit our exposure on any one insurance contract or any single event or series of events. Our reinsurance program addresses some of our individual risks with exposures above certain amounts as well as our exposure to catastrophes including hurricanes, tornadoes, wind and hail events, earthquakes, fires following earthquakes, winter storms, and wildfires. We purchase reinsurance from many providers and we are not dependent on any single reinsurer. We believe that our reinsurers are reputable and financially secure, and we regularly review the financial strength ratings of our reinsurers to ensure they meet established thresholds. Reinsurance does not remove our liability to pay our policyholders, and we remain liable to our policyholders for the risks we insure. In our Property and Casualty operations, the purchase of catastrophic and other reinsurance is an important risk management tool. Further, the use of catastrophic event models is an important element of our reinsurance program. These models assist us in the management of our exposure concentrations. In addition to reinsurance protection, we have managed our exposure to catastrophic risk by limiting personal homeowners business in coastal areas, implementing hurricane, wind and hail deductible requirements where appropriate, and not renewing coverage in over exposed regions with respect to hurricane or wind and earthquake risk.

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, and general business and economic conditions, including market rates of interest and inflation. Profitability is affected to the extent actual experience deviates from our pricing assumptions.

Collections for certain annuity and life products are not recognized as revenues, but are added to policyholder account balances. 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 policyholders.

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, requiring frequent rate increases, most of which are subject to approval by state regulatory agencies.

Competition

We compete principally on 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 a large number of domestic and foreign insurance companies, many of which offer one or more similar products. In addition, for our products that include a savings or investment component, our competition includes domestic and foreign securities firms, investment advisors, mutual funds, banks and other financial institutions.

Table of Contents

Several competing insurance carriers are larger than us and 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 our financial strength ratings. Rather than focusing our advertising efforts nationally, we support advertising in the local markets where our agents live and work.

Ratings

Insurer financial strength ratings are current independent opinions of rating agencies regarding the capacity of an insurance company to meet the obligations of its insurance policies and contracts in accordance with their terms. The ratings 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 as a guarantee of an insurer s current or future ability to meet contractual obligations. Each agency s rating should be evaluated independently of any other rating. Ratings may be changed, suspended, or withdrawn at any time.

Our insurer financial strength rating 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) [(1)]

Standard & Poor s (S&P): A (Strong) [(2)]

(1) A.M. Best s rating of A is the third highest of thirteen ratings and represents companies excellent ability to meet their ongoing insurance obligations. A.M. Best s active company rating scale consists of thirteen ratings ranging from A++ (Superior) to D (poor).
(2) S&P s rating of A is in the strong category and represents companies strong capacity to meet financial commitments, but somewhat susceptible to adverse economic conditions and changes in circumstances. A is the sixth highest of twenty active company ratings. Ranging from AAA (Extremely Strong) to CC (Extremely Weak) and uses plus (+) or Minus (-) modifiers show the relative standing within the AA to CCC categories.

Regulation Applicable to Our Business

Our insurance operations are subject to extensive regulation, primarily at the state level. The methods, extent and substance of such regulations vary by state but generally have their source in statutes that establish standards and requirements for conducting the business of insurance and that delegate broad regulatory authority to a state regulatory agency. In many cases, the regulatory models for state laws and regulations emanate from the National Association of Insurance Commissioners (NAIC). 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, policy benefits, price setting, accounting practices, the payment of dividends, the nature and amount of investments, underwriting practices, reserve requirements, marketing and advertising practices, privacy, policy forms, reinsurance reserve requirements, mergers and acquisitions, capital adequacy, transactions with affiliates, participation in shared markets and guaranty associations, claims practices and the remittance of unclaimed property.

State insurance departments monitor compliance with regulations through periodic reporting procedures and examinations. At any given time, financial, market conduct or other examinations of our insurance companies may be occurring.

The U.S. federal government has not historically regulated the insurance industry. The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), enacted in July 2010, however, expands the federal presence in insurance oversight. Dodd-Frank s requirements include streamlining the state-based regulation of reinsurance and non-admitted insurance. Dodd-Frank also establishes a new Federal Insurance Office within the U.S. Department of the Treasury, which is authorized to, among other things, gather data and information to monitor aspects of the insurance industry, identify issues in the regulation of insurers about insurance matters, and preempt state insurance measures under certain circumstances. It is possible that additional federal regulation of the insurance industry may occur in the future.

Table of Contents

The Patient Protection and Affordable Care Act of 2010 (the Health Act) makes significant changes to the regulation of health insurance and may affect us in various ways. We have business that could be affected by the Health Act however, the impact should be minimal based on the changes thus far indicated by the U.S. Department of Health and Human Services. We have moved diligently to comply with the Health Act and minimize any exposure to fines and taxes. While final regulations have not been released, the company expects the impact to be minimal to earnings, if any. We cannot predict the effect that the Health Act, or any regulatory pronouncement made thereunder, will have on our results of operations or financial condition.

Regulatory matters having the most significant effects on our insurance operations and financial reporting are described further below:

Limitations on Dividends by Insurance Subsidiaries. Dividends received from our insurance subsidiaries represent one source of cash for us. Our insurance subsidiaries ability 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 subject to regulation in the jurisdictions where our insurance companies do business. Our insurance companies are organized under the insurance codes of Texas, Missouri, New York, Louisiana, and California. Generally, these insurance codes require advance notice to, or in some cases approval by, the state insurance regulators prior to certain transactions between insurance companies and other entities within the holding company system. Such requirements may deter or delay certain transactions considered desirable by management. The NAIC recently approved revisions to its Model Holding Company System Regulatory Act that, when enacted by the legislatures of the states in which our insurance companies are domiciled, may increase reporting requirements with respect to transactions within the holding company system.

Price Regulation. Nearly all states have insurance laws requiring 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 these must be approved prior to use. The objectives of these pricing laws vary but generally 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 applicable regulator that its pricing or proposed pricing meets the requirements of the pricing laws. In those states that significantly restrict an insurer s underwriting ability, 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 price setting ability, an insurer can manage its risk of loss by being more selective in the type of business it offers. When a state has significant underwriting and pricing restrictions, it becomes more difficult for an insurer to maintain its profitability. These kinds of restrictions can impact our ability to market products to residents of such states.

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

Guaranty Associations and Involuntary Markets. 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. As a condition of maintaining our licenses to write 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 not been material to our results of operations.

Table of Contents

Investment Regulation. Our insurance companies are subject to regulations that require investment portfolio diversification and limit the amount of investment in certain asset categories. Failure to comply with these rules leads to the treatment of non-conforming investments as non-admitted assets for measuring statutory surplus. In some instances, these rules may require divestiture of non-conforming investments.

Exiting Geographic Markets, Canceling and Non-Renewing Policies. Most states regulate an insurer s ability to exit a market by limiting the 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 an approved plan. These regulations could restrict our ability to exit unprofitable markets.

Statutory Accounting. Our quarterly and annual financial reports to the state insurance regulators utilize statutory accounting principles as defined in the Accounting Practices and Procedures Manual of the NAIC, which are different from GAAP. While not a substitute for any GAAP measure of performance, statutory data frequently is used by industry analysts and other recognized reporting sources to facilitate comparisons of the performance of insurance companies. Statutory accounting principles, in keeping with the intent to assure the protection of policyholders, are generally based on a solvency concept, while GAAP used for public reporting to stockholders is based on a going-concern concept.

Insurance Reserves. State insurance laws require that property and casualty and life insurers annually analyze the adequacy of reserves. Our appointed actuaries must submit an opinion that reserves are adequate for policy claims-paying obligations and related expenses.

Risk-Based Capital Requirements. The NAIC has developed a formula for analyzing insurance companies called risk-based capital (RBC). The RBC formula is intended to establish minimum capital thresholds that vary with the size and mix of a company s business and assets. It is designed to identify companies with capital levels that may require regulatory attention. At December 31, 2012, the Company and each insurance subsidiary was more than adequately capitalized and exceeded the RBC minimum requirements.

Securities Regulation. 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 in 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. The U.S. 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 when warranted take corrective action.

In addition, our periodic reports and proxy statements to stockholders are subject to the requirements of the Securities Exchange Act of 1934, as amended, and corresponding rules of the SEC, and our corporate governance processes are subject to regulation by the SEC and the NASDAQ stock market. Our registered wholesale broker-dealer and registered investment adviser subsidiaries are subject to regulation and supervision by the SEC, FINRA and, in some cases, state securities administrators.

Privacy Regulation. U.S. federal laws, such as the Gramm-Leach-Bliley Act, and the laws of some states regulate disclosures of certain customer information and require us to protect the security and confidentiality of such information. Such laws also require us to notify customers about our policies and practices relating to the collection, protection and disclosure of confidential customer information. Furthermore, state and federal laws, such as the federal Health Insurance Portability and Accountability Act regulate our use, protection and disclosure of certain personal health 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 us, 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.

Other types of regulation that could affect us include insurable interest laws, employee benefit plan laws, antitrust laws, federal anti-money laundering and anti-terrorism laws, and employment and labor laws. In some cases, severe penalties may be imposed for breach of these laws.

Significant risks presented to our business by extensive regulation are discussed in Item 1A, Risk Factors section.

Employees

As of December 31, 2012, we had approximately 3,075 employees, of which approximately 739 are employed in our Galveston, Texas corporate headquarters. We consider our employee relations to be good.

Available Information

The Company files periodic and current reports, proxy statements and other information with the SEC. Such reports, proxy statements and other information may be obtained by visiting the Public Reference Room of the SEC at 100 F Street, N.E., Washington D.C. 20549 or by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an internet website (www.sec.gov) that contains reports, proxy statements, and other information regarding issuers that file electronically with the SEC.

Our press releases, financial information and reports filed with the SEC (for example, our Annual Report on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K and any amendments to those Forms) are available online at www.anico.com. The reference to our Internet website does not constitute the incorporation by reference of information contained at such website into this report. Copies of any documents on our website are available without charge, and reports filed with or furnished to the SEC will be available as soon as reasonably practicable after they are filed with or furnished to the SEC.

ITEM 1A. RISK FACTORS

The most significant risks and uncertainties that we face are described below. Any of these risks and uncertainties, individually or in the aggregate, could materially and adversely impair our business, financial condition or results of operations.

Economic Risk Factors

We face difficult conditions in the economy, which may not improve in the near future. Our results of operations are materially affected by economic conditions in the U.S. and elsewhere. Factors such as consumer spending, business investment, energy costs, geopolitical issues, the volatility and strength of the capital markets, inflation, the continuing threat of terrorism, ongoing military actions, concerns over tax and fiscal policy and downgrades in the sovereign debt of the U.S. and other countries all affect the business and economic environment, financial markets and, ultimately, the profitability of our business. Similarly, uncertainty associated with the absence of long-term government policy related to these or similar factors may have an adverse effect on consumers and businesses confidence, which ultimately may negatively impact our business.

In an economic downturn with higher unemployment and lower family income, lower consumer confidence and spending, increased defaults on mortgages, student and other consumer loans, and lower corporate earnings and business investment, the demand for our products could be adversely affected. For example, difficult credit conditions may adversely affect purchases of credit-related insurance products. In addition, our policyholders may choose to defer or stop paying insurance premiums, resulting in higher lapses or surrenders of policies. In particular, our distribution channels that serve middle-income markets face competition from alternative uses of the customer s disposable income.

Interest rates could remain persistently low, or significant changes in interest rates could occur. 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 we earn on investment and what we must pay under our contracts. Persistently low (or lower) interest rates, such as we are currently experiencing, compound this spread compression. Our ability to manage our investment margin 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 maturing or prepaid or sold bonds may be reinvested at lower yields, reducing investment margin. Lower product rates in such an environment can offset decreases in investment yield; however, these changes may be timed differently and could be limited by market conditions and regulatory or contractual minimum rate guarantees. Furthermore, decreases in the rates offered on products could make those products less attractive, leading to lower sales and increased 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, increasing rates on other insurance or investment products offered to our customers by competitors can lead to higher surrenders at a time when fixed maturity investment asset values are lower. 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.

While we use ALM processes to mitigate the effect on our spread of rising or falling interest rates, no assurance can be given that changes in interest rates will not affect our spreads. Additionally, our ALM incorporates 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 ALM may be negatively affected whenever actual results differ from these assumptions.

Operational Risk Factors

Our actual experience could differ from our estimates and assumptions regarding risk, the fair value and future performance of our investments, and the realization of deferred tax assets. 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 our operating expenses. Our profitability substantially depends on our actual experience being consistent with these assumptions. If we fail to appropriately price our insured risks, or if our claims experience is more severe than our underlying assumptions, our profit margins and financial condition could be negatively affected. Conversely, significantly overpriced risks could negatively impact new business growth and retention of existing business.

Similarly, our loss reserves are an estimate of amounts needed to pay and administer incurred claims and, as such, are inherently uncertain; they do not and cannot represent an exact measure of liability. Inflationary scenarios, especially scenarios outside of historical norms or regulatory changes that affect the assumptions underlying our estimates can cause variability in our loss estimates. For example, 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 health policies. Likewise, increases in costs for auto parts and repair services, construction costs, and commodities result in higher loss costs for property damage claims. Accordingly, our loss reserves for past periods could prove to be inadequate to cover our actual losses and related expenses. Changes in these estimates, both increases and decreases, are included in our results of operations during the period in which the changes are made.

With respect to our investments, the determination of the amount of allowances and impairments varies by investment type and is based upon our periodic evaluation and assessment of known and inherent risks associated with the respective asset class. Management updates its evaluations regularly and reflects changes in allowances and impairments in operations as evaluations are revised. Historical trends may not be indicative of future impairments or allowances. See Note 2, Summary of Significant Accounting Policies and Practices, of the Notes to the Consolidated Financial Statements for further description of our evaluation of impairments.

Deferred tax assets and liabilities are attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets are future tax deductions. The realization of the deferred tax assets is dependent upon the generation of sufficient future taxable income, including capital gains. If future events differ from our current forecasts and it is determined that the deferred tax assets cannot be realized, a deferred tax valuation allowance must be established, with a corresponding charge to net income.

Our risk management policies and procedures may leave us exposed to unidentified or unanticipated risk. Our performance is highly dependent on our ability to manage operational, financial, legal, and regulatory risks that arise from our day-to-day business activities, many of which are very complex. 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. In addition, we could experience unforeseen risks, or risks of a magnitude greater than expected, including those arising from failures in processes, procedures or systems implemented by us or a failure on the part of employees or third parties upon whom we rely in this regard.

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. 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 Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, for additional details.

Interest rate fluctuations and other events may require us to accelerate the amortization of deferred policy acquisition costs (DAC). When interest rates rise, life and annuity surrenders and withdrawals may increase as policyholders seek to buy products with higher or perceived higher returns, requiring us to accelerate the amortization of DAC. To the extent such amortization exceeds any surrender or other charges earned as income upon surrender and withdrawal, our results of operations could be negatively affected.

DAC for both insurance and investment products is reviewed for recoverability, which involves significant management judgment in estimating the future profitability of current business. Typically, estimated lower levels of profitability accelerate DAC amortization, and higher levels of profitability have the opposite effect. 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 Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates, and Part II, Item 8, Financial Statements and Supplementary Date Note 2, Summary of Significant Accounting Policies and Practices, and Note 10, Deferred Policy Acquisition Costs, of the Notes to the Consolidated Financial Statements for additional information.

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 rely on the availability, reliability, and security of our information-processing infrastructure, system platforms, and business applications to store, process, retrieve, and evaluate customer and company information. In certain lines of our business, our information technology and telecommunication systems interface with and rely upon third-party services. These business lines are highly dependent on our ability to access these external services to perform necessary business functions, such as acquiring new business, managing existing business, paying claims, and ensuring timely and accurate financial reporting. Systems failures or extended outages and our not being able to react quickly to such events could compromise our ability to perform critical functions on a timely basis. Therefore, we have implemented various strategies and ongoing processes in an effort to ensure our ability to support, expand and continually update our infrastructure and systems to keep up with business requirements and changes whether regulatory, internal or market driven. If these systems were inaccessible for an extended period of time due to natural or man-made disasters, or if they fail to function as designed, the resulting disruptions may impede or interrupt our business operations. To mitigate these risks we have business continuity and recovery plans to help ensure continued operations should an event occur. We cannot be certain that such plans will address every event or could be implemented successfully under all circumstances.

We receive and transmit confidential data with and among customers, agents, financial institutions and selected third party vendors and service providers in the normal course of business. Despite our implementation of secure transmission techniques, internal data security measures, monitoring tools and best practices, our systems are vulnerable to security threats and breach attempts from both external and internal sources. Any such breach could result in access, viewing, misappropriation, altering or deleting information in our systems, including personal customer information, customer financial information and our proprietary business information. We rely on several layers of data protection technologies and designs to provide security and authentication capabilities to protect this information. We have invested significant time and resources to prevent and mitigate data security risks; however, we cannot be certain that our efforts will be effective considering increasingly advanced persistent threat techniques and complexity, and the evolving sophistication of cyber-attacks. Any significant disruption or security breach resulting in misappropriation of our proprietary information or customers personal data could cause significant damage to our business operations and reputation. In addition, it could result in substantial costs and consequences, including repairing systems, increased security costs, customer notifications, lost revenues, litigation, regulatory action, and reputational damage.

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, annuity, 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 a negative effect on our results of operations and our reputation, if such problems or discrepancies are replicated through multiple policies.

Investment and Financial Markets Risk Factors

Fluctuations in the markets for fixed maturity securities, equity securities, and commercial real estate could adversely affect the valuation of our investment portfolio and our net investment income. Investment returns are an important part of our overall profitability. Our investment portfolio is subject to market risks, such as interest rate risk, market volatility, and deterioration in the credit of companies or governmental entities in which we have invested. In the event of extreme market events we could incur significant losses. Significant volatility in the markets can cause changes in interest rates, declines in equity prices, and the strengthening or weakening of foreign currencies against the U.S. dollar, which individually or in aggregate could have a material adverse effect on our results of operations, financial condition, liquidity or cash flows.

When interest rates rise, the value of our investment portfolio may decline due to decreases in the fair value of our fixed maturity securities. Generally, we expect to hold our fixed maturity investments to maturity, including those 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 investee 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 a lower rate. The decline in market rates could reduce our investment income as new funds are invested at lower yields.

The concentration of our investment portfolios in any particular industry, group of related industries, or geographic sector could adversely affect us. 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. In addition, many companies have capitalized on the current low interest rates and issued bonds or incurred other debt above historic norms that may reduce below historic norms the amount of new debt coming to the market in 2013 and beyond. This imbalance may make it more difficult to maintain a well-diversified portfolio, which may increase our credit risk.

Table of Contents

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. Our mortgage loan investments are principally collateralized by commercial properties. A significant increase in interest rates may also make it more difficult for commercial property owners to refinance existing mortgages as they are scheduled to mature, making repayment of balloon payments to us more difficult. A significant increase in the default rate of our mortgage loan investments could have a material adverse effect on us.

Some of our investments are relatively illiquid. Our investments in privately placed securities, mortgage loans, and real estate, including real estate joint ventures and other limited partnership interests, are relatively illiquid. If we require significant amounts of cash in excess of ordinary course cash requirements on a short notice it may be difficult or not possible to monetize these investments in an orderly manner, and we may be forced to sell them for less than we otherwise would have been able to realize.

A decline in equity markets or an increase in volatility in the equity markets may adversely affect sales and/or yields of our investment products, as well as the funding status of our sponsored pension plans. Significant downturns and volatility in the equity markets could adversely affect the profitability of our investment products, which may have a material adverse effect on us in multiple ways. First, market downturns and volatility may cause some of our existing customers to withdraw cash values or reduce investments in such products that have returns linked to the performance of the equity market, in turn reducing the fee revenues generated from these 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. 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 these products.

Third, we provide certain guarantees within some of our products that protect policyholders against significant downturns in the equity markets. These guarantees may be more costly than expected in volatile or declining equity market conditions, which could cause us to increase our liabilities for future policy benefits, negatively affecting our net income.

Lastly, our estimates of liabilities and expenses for pension and other postretirement benefits incorporate assumptions regarding the rate used to discount our estimated future liability, the long-term rate of return on plan assets and the employee work force. Declines in the discount rate or the rate of return on plan assets both of which are influenced by potential investment returns could increase our required cash contributions or pension-related expenses in future periods.

Catastrophic Event Risk Factors

We may incur significant losses resulting from catastrophic events. Our property and casualty operations are exposed to catastrophes caused by natural events, such as hurricanes, tornadoes, wildfires, droughts, earthquakes, snow, hail and windstorms, and manmade events, such as terrorism, riots, hazardous material releases, or utility outages. Our life and health insurance operations are 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.

We cannot accurately predict the likelihood, timing or severity of catastrophe events, or the number and type of catastrophe events that will affect us. As a result, our operating 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 operating results will not be materially adversely affected by our exposure to catastrophe losses.

The extent of our losses in connection with catastrophic events is a function of the severity of the event and the amount of policyholder exposure in the affected area. Where we have geographic concentrations of policyholders, a single catastrophe (such as an earthquake) or a destructive weather event, may have a significant impact on our financial condition and results of operations. In addition, 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 our loss experience. In addition, state regulators responsible for insurance regulation have the ability to impose claim settlement practices or suspend rules we may have expected to mitigate our losses. Actions such as these may negatively impact our ability to manage claims or cause us to incur additional costs.

Table of Contents

Some scientists believe that in recent years, climate change has added to the unpredictability, severity and frequency of natural disasters. To the extent climate change increases the frequency and severity of such weather events, we may face increased claims. In response to this belief, a number of legal and regulatory measures as well as social initiatives have been introduced in an effort to reduce greenhouse gas and other carbon emissions, which may be chief contributors to global climate change. We cannot predict how legal, regulatory and social responses to concerns about global climate change will impact our business.

The occurrence of events that are unanticipated in our business continuity and disaster recovery planning could impair our ability to conduct business effectively. Our corporate headquarters is located in Galveston, Texas, on the coast of the Gulf of Mexico and in the past has been impacted by a hurricane. We have expanded our operations in League City, Texas and established a remote processing center in San Antonio, Texas. These locations are designed to support our operations and service our policyholders in the event of a hurricane or other natural disaster affecting Galveston. 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. There is no assurance, however, our off-site disaster recovery systems and business continuity plans for these locations will prove successful. The severity, timing, duration or extent of an event may be unanticipated by our planning, and the event could have an adverse impact on our ability to conduct business, 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.

Marketplace Risk Factors

Our future results are dependent in part on our ability to successfully operate in insurance and annuity industries that are highly competitive. Product development and 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.

In particular, our Medicare Supplement business is subject to intense price competition, 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 what we estimate to be very small profit margins or to underprice new sales in order to gain market share. We have elected not to underprice new sales, which we believe has negatively affected sales and could continue to do so if we do not match these industry practices.

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. 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.

We may be unable to attract and retain sales representatives and third-party independent agents for our 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, reputation, stable ownership, support services, compensation, product features and pricing. We may be unable to compete with insurers that adopt more aggressive pricing or compensation, that offer a broader array of products, that offer policies similar to ours at lower prices or as part of a package of products, or that have extensive promotional and advertising campaigns. If we are unsuccessful in attracting and retaining sales representatives and agents, sales of individual insurance and annuity products could be materially adversely affected.

Table of Contents

Our Medicare Supplement business could be negatively affected by alternative healthcare providers or changes to the Medicare program. 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.

In addition, because of increasing medical cost inflation and concerns about the U.S. fiscal policy and the solvency of the Medicare program, Congress could make changes or cuts to the Medicare program in the future. The nature and timing of these changes and cuts cannot be predicted and could adversely impact our Medicare Supplement business.

Litigation and Regulation Risk Factors

Litigation and regulatory investigations may result in significant financial losses and harm our reputation. 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, agent misconduct, product design, product disclosure, product administration, fees charged, denial or delay of benefits, product suitability, claim and refund practices, and breaches of duties to customers. Plaintiffs in such 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 have a material adverse effect on us. Even when we are successful in the defense of such actions, we could incur significant defense costs, including attorneys fees, other direct litigation costs and substantial amounts of management time that otherwise would be devoted to our business. Note 19, Commitments and Contingencies, of the Notes to the Consolidated Financial Statements contains a discussion of certain pending and ongoing litigation.

In addition, the insurance industry is the focus of increased regulatory scrutiny as various state and federal government agencies, including state attorneys general and comptrollers, conduct inquiries and investigations into the products and practices of the financial services industries. These lines of inquiry and investigation are broad and unpredictable and may raise issues not yet identified, as well as focusing on issues such as sales and marketing practices, suitability, pricing and fees, product disclosure, and unclaimed property policies and processes. Such investigations could result in new legal actions against us and industry-wide regulations that could adversely affect us.

We are subject to extensive regulation, and potential further restrictive regulation may increase our operating costs and limit our growth. Our insurance companies are subject to extensive insurance laws and regulations, most of which are designed to protect the interests of policyholders rather than the Company or its stockholders. Such regulation varies, but typically has its source in state statutes that delegate regulatory and supervisory powers to a state insurance official. This regulation and supervision affects nearly every aspect of our insurance business.

We are also subject to additional laws and regulations administered and enforced by a number of different governmental authorities, including state securities administrators, the SEC, the Internal Revenue Service (IRS), FINRA, the U.S. Department of Justice, the U.S. Department of Labor, 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 or enforcement authority s interpretation of a legal issue may not result in compliance with another regulator or enforcement authority s interpretation of the same issue.

Table of Contents

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 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 our profitability.

The regulatory environment could have other significant effects on 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 developments or actions against us could have material adverse financial effects, cause significant harm to our reputation, or harm our business prospects.

The laws and regulations applicable to us are complex and subject to change. Compliance with these laws and regulations is time consuming and personnel-intensive. Changes in these laws and regulations may materially increase our direct and indirect compliance and other expenses of doing business. In addition, with respect to our property and casualty and health business, state departments of insurance regulate and approve underwriting practices and rate changes. Obtaining timely rate increases is of great importance when necessary to match rate to risk. Any delay in such regulatory approvals could adversely affect our profitability.

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 changes may include modifications to long established business practice or the interpretation of how policy contract provisions may be applied, which may adversely affect us by extending coverage beyond our underwriting intent or increasing the type, number, or size of claims. For example, the National Conference of Insurance Legislators has adopted the Model Unclaimed Life Insurance Benefits Act, which would impose new requirements on insurers to periodically compare their life insurance and annuity contracts and retained asset accounts against the U.S. Social Security Administration s Death Master File, investigate any potential matches, determine whether benefits are payable, and attempt to locate beneficiaries. Some states have adopted legislation similar to such model act, and more states could do so. It is possible that this activity may result in additional payments to beneficiaries, additional escheatment of funds deemed abandoned under state laws, administrative penalties, interest, and changes to our procedures for the identification and escheatment of abandoned property. Given the legal and regulatory uncertainty in this area, it is also possible that we and other life insurers could be subject to claims, regulatory actions and litigation resulting in payments or costs that could have a material adverse effect on us. We have already modified our claims process in our life segment to comport with emerging trends. See the discussion of Benefits losses and expenses in the life segment discussion of the Management Discussion and Analysis (MD&A) below.

In addition to state regulatory changes, the enactment of Dodd-Frank provides for enhanced federal regulation of the financial services industry through multiple initiatives. Certain provisions of Dodd-Frank are or may become applicable to us, our competitors, or certain entities with which we do business. For example, Dodd-Frank includes a new framework for the regulation of over-the-counter derivatives markets, which will require the clearing of certain types of derivatives currently traded over-the-counter, which could potentially impose additional costs and regulation on us and expose us to the risk of a default by a clearinghouse with respect to our cleared derivative transactions. While some studies and rulemaking required under Dodd-Frank have been completed, there still remains significant uncertainty regarding the full impact of Dodd-Frank on us. We cannot predict with certainty the requirements or specific applicability of all regulations ultimately adopted under Dodd-Frank, nor can we predict with certainty how such regulations will affect our business or the financial markets generally.

For further discussions of the kinds of regulation applicable to us, see Item 1, Business, Regulation Applicable to Our Business section.

Changes in tax laws could decrease sales and profitability of certain products and increase our tax cost. Under current U.S. 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 some of our products a competitive advantage over non-insurance products. The U.S. Congress from time to time may consider legislation that would reduce or eliminate this favorable policyholder tax treatment.

The U.S. 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 to some of our products, making them less competitive. Such proposals, if adopted, could have a material adverse effect on our ability to sell such products and could result in the surrender of some existing contracts and policies. In addition, changes in the U.S. federal and state estate tax laws could negatively affect the demand for the types of life insurance used in estate planning.

Table of Contents

Changes to the tax laws, administrative rulings or court decisions affecting U.S. corporations or the insurance industry could increase our effective tax rate and lower our net income. In addition, uncertainty regarding the tax structure in the future may also cause some current or future purchasers to delay or indefinitely postpone the purchase of products we offer. We cannot predict whether any tax legislation will be enacted or whether any legislation would have a material adverse effect on our financial condition and results of operations.

New accounting rules or changes to existing accounting rules could negatively impact our business. We are required to comply with GAAP. A number of organizations are instrumental in the development and interpretation of GAAP, such as the SEC, the Financial Accounting Standards Board, and the American Institute of Certified Public Accountants. 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.

We also must 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 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. For example, the NAIC is currently considering various initiatives to modernize financial and solvency regulations. We cannot predict whether or in what form, potential changes will be enacted or what impact any such changes may have on our product mix, product profitability, reserve and capital requirements, financial condition or results of operations.

See Note 3, Recently Issued Accounting Pronouncements, of the Notes to Consolidated Financial Statements for a detailed discussion regarding the impact of the recently issued accounting pronouncements and the future adoption of new accounting standards on the Company.

Reinsurance and Counterparty Risk Factors

Reinsurance may not be available, affordable or adequate to protect us against losses. As part of our risk management strategy, we purchase reinsurance for certain risks that we underwrite. Market conditions and geo-political events beyond our control, including the continued threat of terrorism, influence the availability and cost of reinsurance for new business. Moreover, in certain circumstances, the price of existing reinsurance contracts may also increase.

Recently, access to reinsurance has become more costly for us as well as the insurance industry in general. We may be forced to incur additional expenses for reinsurance, or we 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. A decrease in the amount of reinsurance, however, will increase our risk of loss.

The counterparties to our reinsurance arrangements or to the derivative instruments we use to hedge our business risks could default or fail to perform. We use reinsurance to mitigate our risks in various circumstances. Reinsurance does not relieve us of our direct liability to our policyholders, even when the reinsurer is liable to us. Our reinsurers may not pay the reinsurance recoverables owed to us or they may not pay these balances on a timely basis.

We enter into derivative contracts, including options, with a number of counterparties to hedge various business risks. If our counterparties fail or refuse to honor their obligations, our economic 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 us. In addition, our estimates and assumptions regarding our use of any derivative instrument may fail to correspond to our actual long-term exposure with respect to identified risks. Moreover, we may fail to identify the nature or magnitude of risks to which we are exposed.

Table of Contents

Other Risk Factors

Our financial strength ratings could be downgraded. Financial strength ratings various Nationally Recognized Statistical Rating Organizations (NRSROs) publish as their opinion regarding an insurance company s creditworthiness and ability to meet policyholder and contractholder obligations are important to maintaining public confidence in our products, our ability to market our products, and our competitive position. We cannot predict what actions rating agencies may take, or what actions we may take in response to the actions of rating agencies. As with other companies in the financial services industry, our ratings could be downgraded at any time and without any notices by any NRSRO. For example, in 2010 and 2011, we experienced downgrades in our counterparty credit and financial strength ratings.

A downgrade or an announced potential downgrade of 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 and annuity products;
- adversely affecting our relationships with our sales force and independent sales intermediaries;
- materially increasing the number or amount of policy surrenders and withdrawals;
- requiring us to reduce prices to remain competitive;
- increasing our possible borrowing cost;
- adversely affecting our ability to obtain reinsurance at reasonable prices; and
- adversely affecting our relationships with credit counterparties.

It is likely that the NRSROs will continue to apply a high level of scrutiny to financial institutions, including us and our competitors in the insurance industry, and may adjust upward the capital and other requirements employed in the NRSRO models for maintenance of certain ratings levels.

We are controlled by a small number of stockholders. As of December 31, 2012, the Moody Foundation, a charitable trust controlled by Robert L. Moody, Sr. and two of his children, beneficially owned 6,157,822 shares of our common stock. In addition to these shares and as of such date, Moody National Bank, of which Robert L. Moody, Sr. is chairman and chief executive officer, in its capacity as trustee or agent of various accounts had the power to vote an additional 12,097,507 shares of our common stock. These two stockholders have the power to vote approximately 68.0% of our common stock. As a result, these two stockholders, subject to applicable legal and regulatory requirements, have the ability to exercise a controlling influence over all matters affecting us, including the composition of our Board of Directors, and through the Board of Directors any determination with respect to our business direction and policies, and any other matters submitted for stockholder approval.

This concentration of voting power could deter a change of control or other business combination that might otherwise be beneficial or preferable to other stockholders. It 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.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We own and occupy approximately 420,000 square feet at our corporate headquarters located in Galveston, Texas. We also own the following properties that are materially important to our operations:

We own and occupy four buildings in League City, Texas, totaling approximately 346,000 square feet. Our Life, Health, and Corporate and Other business segments use approximately 60% of such space.

Our Property and Casualty segment conducts substantial operations in Springfield, Missouri, and in Glenmont, New York. The Springfield facility is approximately 232,000 square feet, of which we occupy approximately 80%, and the Glenmont facility is approximately 140,000 square feet, all of which is occupied by us.

We own a building in San Antonio, Texas, which is approximately 100,000 square feet. We use approximately 75% of this facility for customer service and business operations.

20

Table of Contents

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 Note 19, Commitments and Contingencies, in the Notes to the Consolidated Financial Statements.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable

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 and the quarterly dividends declared per share.

	Stock Price Per Share		Dividend
	High	Low	Per Share
2012			
Fourth quarter	$ 74.34	$ 63.68	$ 0.77
Third quarter	72.64	68.14	0.77
Second quarter	72.79	66.58	0.77
First quarter	78.08	70.28	0.77
			$ 3.08
2011			
Fourth quarter	$ 75.04	$ 66.11	$ 0.77
Third quarter	80.52	65.71	0.77
Second quarter	81.13	74.50	0.77
First quarter	89.25	75.17	0.77
			$ 3.08

We expect to continue to pay regular cash dividends, although there is no assurance as to future dividends because they depend on future earnings, capital requirements and financial conditions. The payment of dividends is subject to restrictions described in Note 16, Stockholders Equity and Noncontrolling Interest, of the Notes to the Consolidated Financial Statements and as discussed in Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Capital Resources.

On December 31, 2012, our closing stock price was $68.29 per share. As of December 31, 2012, there were approximately 865 holders of record of our issued and outstanding shares of common stock.

21

Table of Contents

Securities Authorized for Issuance under Equity Compensation Plans

The following table provides information regarding our common stock that is authorized for issuance under American National s 1999 Stock and Incentive Plan as of December 31, 2012:

Equity Compensation Plan Information

	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Plan category			
Equity compensation plans			
Approved by security holders		$ 111.31	2,103,166
Not approved by security holders			
Total		$ 111.31	2,103,166

Performance Graph

The following graph compares the performance of the cumulative total stockholder return for the Company s stockholders for the last five 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, 2007 over the periods shown.

Value at each year-end of a $100 initial investment made on December 31, 2007:

	12/31/07	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12
American National	$ 100.00	$ 63.61	$ 103.66	$ 78.20	$ 70.34	$ 69.06
NASDAQ Total	100.00	61.17	87.93	104.13	104.69	123.85
NASDAQ Insurance	100.00	92.63	96.74	108.93	113.45	133.04

This performance graph shall not be deemed to be incorporated by reference into our SEC 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)	**Years ended December 31,**				
	2012	**2011[1]**	**2010[1]**	**2009[1]**	**2008[1]**
Total premiums and other revenues	$ 2,987	$ 3,023	$ 3,073	$ 2,941	$ 2,507
Income (loss) from continuing operations attributable to American National Insurance Company and Subsidiaries	192	192	144	12	(176)
Income (loss) from discontinued operations, net of tax			(1)	(1)	20
Net income (loss)	192	192	143	11	(156)
Net income (loss) attributable to American National Insurance Company and Subsidiaries	191	191	144	16	(154)
Per common share					
Income (loss) from continuing operations:					
basic	7.15	7.18	5.48	0.41	(5.88)
diluted	7.11	7.14	5.46	0.41	(5.88)
Income (loss) from discontinued operations:					
basic			(0.05)	(0.05)	0.73
diluted			(0.05)	(0.05)	0.73
Net income (loss) attributable to American National Insurance Company and Subsidiaries:					
basic	7.15	7.18	5.43	0.36	(5.15)
diluted	7.11	7.14	5.41	0.36	(5.15)
Cash dividends per share	3.08	3.08	3.08	3.08	3.08

	Years ended December 31,				
	2012	**2011[1]**	**2010[1]**	**2009[1]**	**2008[1]**
Total assets	$ 23,107	$ 22,490	$ 21,416	$ 20,118	$ 18,358
Total American National Insurance Company and Subsidiaries stockholders equity	3,828	3,637	3,614	3,441	3,116
Total stockholder s equity	3,839	3,650	3,618	3,453	3,124

[1] Amounts were adjusted to reflect the effect of the retrospective adoption of a new accounting standard on deferred policy acquisition costs.

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

Management s discussion and analysis (MD&A) of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included herein.

Forward-Looking Statements

Certain statements made in this report include forward-looking statements, within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may be identified by words such as expects, 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 changes and uncertainties, which are, in many instances, beyond our control and have been made based upon our assumptions, 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 as anticipated. It is not 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.

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, including without limitations risks, uncertainties and other factors discussed in Item 1A, Risk Factors and elsewhere in this report.

Table of Contents

Overview

We are a diversified insurance and financial services company, offering a broad spectrum of insurance products. Chartered in 1905, we are headquartered in Galveston, Texas. We operate in all 50 states, the District of Columbia, Guam, American Samoa and Puerto Rico.

Segments

The insurance segments do not directly own assets. Rather, assets are allocated to support the liabilities and surplus of each segment. The mix of assets allocated to each of the insurance segments is managed to support the characteristics of the insurance liabilities including cash flows and pricing assumptions, and is considered sufficient to support each segment s business activities. We have utilized this methodology consistently over all periods presented.

The Corporate and Other business segment acts as the owner of all of the invested assets of the Company. The investment income from the invested assets is allocated to the insurance segments in accordance with the assets allocated to each insurance segment. Earnings of the Corporate and Other business segment are derived from our non-insurance businesses as well as earnings from those invested assets not allocated to the insurance segments. All realized investment gains and losses, which includes other than temporary impairments (OTTI), are recorded in this segment.

Outlook

This report contains many forward-looking statements, particularly relating to our future financial performance. Actual results are likely to differ materially from those forecasts, depending on the outcome of various factors.

Our business has been and 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 to impact our overall business. Second, we discuss certain segment-specific trends we believe may impact individual segments or specific products within these segments.

General Trends

Challenging Financial and Economic Environment: We believe that as expectations for global economic growth remain uncertain, 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 have a material adverse effect on our business, financial condition and results of operations. However, we believe those risks are somewhat mitigated by our financial strength, active enterprise risk management and disciplined underwriting for our products. Our diverse product mix across insurance segments is a strength that we expect will help us adapt to current economic times and give us the ability to serve the changing needs of our customers. For example, fluctuations in the stock market during recent years 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. Additionally, 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.

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 amounts we earn on the investments that support these obligations. We have an ALM Committee that actively manages the profitability of our in-force insurance and annuity contracts. We believe we were an early adopter of lower guaranteed minimum crediting rates on new fixed annuity contracts, which has afforded us the flexibility to respond to the unusually low interest rates in recent years . Additionally, we have 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 profitability of these products, although sales volume has and could further diminish as a result. Additionally, we maintain 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. Rapidly rising interest rates, however, could result in reduced persistency of our spread-based products, as contract holders shift assets into higher yielding investments. We believe our ability to react quickly to the changing marketplace will help us manage this risk.

Low interest rates are also challenging for property and casualty companies. Investment income is generally a substantial element in earning an acceptable return on capital. Lower interest rates resulting in lower investment income require us to achieve better underwriting results. We have taken pricing actions to help mitigate the adverse impact of low interest rates on our property and casualty business.

Importance of Operating Efficiencies: The challenging economic environment creates a further need for operating cost reductions and efficiencies. We 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. We anticipate continually improving our use of technology to enhance our policyholders and agents experience and increase efficiency of our employees.

Changing Regulatory Environment: The insurance industry is regulated at the state level and some life and annuity products and services are subject to U.S. federal regulation. We are regularly subjected to additional or changing regulation that requires us to update systems, change product structure or increase the amount of reporting. These changes may increase the capital requirements for us and the industry, increase operating costs, change our operating practices and change our ability to provide products with pricing attractive to the marketplace.

Life and Annuity

Life insurance continues to be our mainstay segment, as it has been 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 agents.

Effective management of invested assets and associated liabilities involving crediting rates and, where applicable, financial hedging instruments (which are utilized as economic hedges of equity-indexed life and annuity products), are important to the success of our life and annuity segments. Asset disintermediation , the risk of large outflows of cash at times when it is disadvantageous to us to dispose of invested assets, is a risk associated with this segment.

Demographics: We believe a key driver shaping the actions of the life insurance industry is the rising income protection, wealth accumulation, and insurance needs of retiring Baby Boomers (those born between 1946 and 1964). According to the US Census Bureau Brief entitled Age and Sex Composition: 2010 , the median age of the population, increased from 35.3 years in 2000 to 37.2 years in 2010. The aging of the Baby Boom population is a major contributor to the increase, along with stable birth rates and improving mortality. While the total population grew at a rate of 9.7% over the 10-year period from 2000 to 2010, the increase in the number aged 45 to 64 years and those 65 years and over grew at rates of 31.5% and 15.1%, respectively. 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 increasing need for savings tools and income protection. We believe our overall financial strength and broad distribution channels position us to respond with a variety of products to individuals approaching retirement age who seek information to plan for and manage their retirement needs. We believe our products that offer guaranteed income flows for life, including single premium immediate annuities, are well positioned to serve this market.

Competitive Pressures: The life insurance industry remains highly competitive. Product development and 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 we possess sufficient scale, financial strength and flexibility to effectively compete in this market.

Table of Contents

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 also a growing competition from other financial service firms. Insurers continue to evaluate their distribution channels and the way they deliver products to consumers. We have never provided guaranteed living benefits as a part of our variable annuity products. We believe these products were not adequately priced relative to the risk profile of the product. While this may have impeded our ability to sell variable annuities in the short term, we believe this strategy has given us an advantage in terms of profitability over the long term.

We believe we will continue to be competitive in the life and annuity markets through our broad line of products, diverse distribution channels, and consistent high level of customer service. We modify our products to meet customer needs and to expand our reach where we believe we can obtain profitable growth. Some highlights of recent activities include:

- Sales of traditional life insurance products increased in 2012 primarily resulting from a new portfolio of term products. 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.

- Sales of equity-indexed universal life insurance products through each of our life distribution channels increased in 2012.

- New accelerated underwriting processes were implemented to more efficiently serve middle income customers purchases of life insurance.

Health

The Patient Protection and Affordable Care Act, and a reconciliation measure, the Health Care and Education Reconciliation Act of 2010 (collectively, the Healthcare Acts), were signed into law in 2010. The Healthcare Acts mandate broad changes in the delivery of health care benefits that impact our current business model, including its relationship with current and future customers, producers and health care providers, products, services, processes and technology. As a result of the Healthcare Acts, management decided to discontinue the sale of individual medical expense insurance plans in 2010.

The Healthcare Acts have generated new opportunities in the limited benefit and supplemental product markets. During 2011, we began building a portfolio of products to be sold in the worksite market as well as to individuals. In 2012, we began establishing new distribution channels and sales strategies and are experiencing an increase in sales of our new worksite products.

We expect our Managing General Underwriter line (MGU), which provides a significant contribution to Health profits, to continue to grow during 2012. Most of the income associated with this line is fee income included in *Other income* of the Health segment s operating results; we retain only 10% of the MGU premium.

Property and Casualty

Our operating results continue to be significantly impacted by a high level of catastrophe losses in the Midwest and Northeast. We are adjusting our pricing models to incorporate the increased probability of severe weather losses and monitoring our geographic exposures on an ongoing basis to address the volatility on our portfolio of risks.

U.S. Property/Casualty Review and Preview published by A.M. Best on February 4, 2013 noted that the U.S. property and casualty insurance industry has continued to experience above average catastrophe losses. While Sandy was certainly the most significant U.S. catastrophe of 2012, it was not the only weather event to cause losses. Through the first six months of 2012, in fact, the industry s weather-related losses were significantly above industry s average. Tornadoes, wildfires, hailstorms, Tropical Storms Beryl and Debby, and an outbreak of severe storms that caused damage from the Midwest to the mid-Atlantic, brought total industry losses through June 30 to more than $13 billion, an unusually high mid-year industry total. Hurricane Isaac the only storm to make U.S. landfall classified as a hurricane in 2012 cause an estimated $2 billion in total economic damage. Without Sandy, expected to be the second costliest catastrophe on record, at $25 billion, the United States would have experienced an average catastrophe year, with approximately 4 points of industry losses attributable to catastrophe events.

Table of Contents

Also noted in the report, the personal lines segment has faced many challenges over the past few years and has been impacted by frequent and severe weather-related events. This property line volatility has been offset by general stable results on the automobile line. Although loss cost pressures, particularly regarding medical inflation, continue to influence results, overall automobile performance within the industry has been generally adequate. The industry s commercial-lines segment is still grappling with competitive market conditions, less favorable reserve development, sluggish economic growth and depressed investment yields.

Demand for P&C credit-related insurance products continues to increase. Credit markets have improved from the previous recessionary years, which resulted in increasing sales in the auto dealer market and, in turn, demand for our GAP products. We continue to update credit-related insurance product offerings and pricing to meet changing market needs, as well as adding new agents to expand market share in the credit-related insurance market. We are reviewing and implementing procedures to enhance customer service and, at the same time, looking for efficiencies to reduce administrative costs.

Competition: Also noted in the A.M. Best publication referenced above is that the property and casualty insurers are facing a continued competitive pricing environment. Despite the challenging pricing environment, we expect to identify profitable opportunities through our strong distribution channels, expanding geographic coverage, marketing efforts, new product development and pricing sophistication.

Critical Accounting Estimates

The preparation of financial statements in accordance with GAAP requires us to make estimates and assumptions that often involve a significant degree of judgment, in particular, expectations of current and future mortality, morbidity, persistency, claims and claim 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 as reported are appropriate, based upon the facts available upon compilation of the consolidated financial statements.

Management reviews the estimates and assumptions used in the preparation of our financial statements on an ongoing basis. If management determines that modifications in estimates and assumptions are appropriate given current facts and circumstances, our financial position and results of operations as reported in the consolidated financial statements could change significantly.

A description of these critical accounting estimates is presented below. Also, see the Notes to the Consolidated Financial Statements for additional information.

Reserves

Life and Annuity Reserves

Life Reserving Methodology   Establishing an adequate liability for amounts payable under life insurance policies requires the use of assumptions. (Principal assumptions used in the establishment of liabilities for future policy benefits are mortality, policy lapse rates, investment return, inflation, expenses and other contingent events as appropriate to the respective product type). Reserves for incurred but not reported (IBNR) claims on life policies are also established using historical claims information. Liabilities for interest-sensitive and variable universal life insurance policies 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.

Annuity Reserving Methodology   We establish liabilities for amounts payable under annuity contracts, including fixed payout and deferred annuities. Liabilities for payout annuities with more than insignificant amounts of mortality risk are calculated in accordance with the applicable accounting guidance 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 annuity reserves are calculated using standard industry mortality tables specified for statutory reporting. 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.

Table of Contents

Liabilities for deferred annuities are established equivalent to the account value held on behalf of the policyholder. Additional reserves for guaranteed minimum death benefits are determined as needed in accordance with the applicable accounting guidance. 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.

Key Assumptions

Implicit in the actuarial methodologies are the following assumptions, which reflect our best estimates and may impact our life and annuity reserves:

- Lapse rates will remain reasonably consistent with our expectations;
- Mortality rates will remain reasonably consistent within standard industry mortality table ranges;
- Interest spreads will remain reasonably consistent with our expectations.

Recoverability At least annually, we test the adequacy of the net benefit reserves (policy benefit reserves less DAC) established for life insurance and annuity products. This testing is referred to as Loss Recognition for traditional products and Unlocking for interest-sensitive products. The assumptions used to perform the tests are our current best estimate assumptions as to policyholder mortality, persistency, 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 interest-sensitive business, best-estimate assumptions are updated to reflect 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 profitability. In particular, changes in estimates of the future invested asset return assumption have a large effect on the degree of reserve adequacy and DAC recoverability.

Health Reserves

Overview We establish future policy benefit reserves in order to match income and benefit expenses by accounting period. Policy and contract claim reserves are established in order to associate future benefit payments, both known and unknown, with the period in which they were incurred. As of year-end 2012, the total Health net reserves were $154.6 million versus $164.3 million at year-end 2011. The following methods are employed to establish the Health reserves:

Completion Factor Approach This method assumes that the historical lag pattern will be an accurate representation of unpaid claim payments. An estimate of the unpaid claims is calculated by subtracting period-to-date paid claims from an estimate of the ultimate complete payment for all incurred claims in the period. Completion factors are calculated which complete the current period-to-date payment totals for each incurred month to estimate the ultimate expected payout.

Tabular Claims Reserves This method is used to calculate the reserves for disability income and long-term care blocks of business. These reserves rely on published valuation continuance tables created using industry experience regarding assumptions of continued morbidity and subsequent recovery. The tabular reserves are calculated by applying these continuance tables, along with appropriate company experience adjustments, to the stream of contractual benefit payments. These expected benefit payments are discounted at the required interest rate.

Table of Contents

Future Policy Benefits Liabilities for future policy benefits 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.

Premium Deficiency Reserves Deficiency reserves are established when the expected future claim payments and expenses 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 established premium deficiency reserves for portions of the major medical business and the long-term care business that are in run-off. 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 Claims and Claim Adjustment Expense (CAE) Property and Casualty reserves are established to provide for the estimated cost of paying claims under insurance policies written. These reserves include estimates for both case and IBNR reserves. Included in these reserves are estimates of the expenses associated with settling claims, also known as CAE. The two major categories of CAE are defense and cost containment expense, and adjusting and other expense. The details of property and casualty claims and CAE reserves are shown in the following table (in thousands):

	December 31, 2012			December 31, 2011		
	Gross	Ceded	Net	Gross	Ceded	Net
Case	$ 471,998	$ 43,676	$ 428,322	$ 470,519	$ 37,673	$ 432,846
IBNR	412,839	8,508	404,331	440,473	15,479	424,994
Total	**$ 884,837**	**$ 52,184**	**$ 832,653**	**$ 910,992**	**$ 53,152**	**$ 857,840**

Case Reserves Reserves for reported losses are established on either a judgment or a formula basis, depending on the timing and type of the loss. The formula reserve is a fixed amount for each claim of a given type based on historical paid loss data for similar claims with provisions for trend changes, such as those caused by inflation. Judgment reserve amounts generally replace initial formula reserves and are set on a per case basis based on facts and circumstances of each case and the expectation of damages. We regularly monitor the adequacy of 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 claims reserves. Loss and premium data is aggregated by exposure class and by accident year. IBNR reserves are calculated by projecting ultimate losses on each class of business and subtracting paid losses and case reserves. Our overall reserve practice provides for ongoing claims evaluation and adjustment based on the development of related data and other relevant information pertaining to claims. Adjustments in aggregate reserves, if any, are included in the results of operations of the period during which such adjustments are made.

We believe our actuaries conservatively reflect the potential uncertainty generated by volatility in our loss development profiles when selecting loss development factor patterns for each line of business. See Results of Operations and Related Information by Segment Property and Casualty, Prior Period Reserve Development section of the MD&A for additional information.

The evaluation process to establish the claims and CAE reserves involves the collaboration of underwriting, claims and internal actuarial departments. The process also includes consultation with independent actuarial firms on a regular basis. Work performed by independent actuarial firms is an important part of our process of gaining reassurance that the claims and CAE reserves determined by our internal actuarial department sufficiently meet all obligations arising from all claims incurred as of year-end. Additionally, the independent actuarial firms complete the Statements of Actuarial Opinion at each year-end, certifying that the recorded claims and CAE reserves appear reasonable.

Table of Contents

Premium Deficiency Reserve Deficiency reserves are established when the expected claims payments and a maintenance component for a product line is in excess of the expected premiums for that product line. The determination of a deficiency reserve takes into consideration the current profitability of a product line using anticipated claims, claims expense, and policy maintenance costs. The assumptions and methods used to determine the deficiency reserves are reviewed periodically for reasonableness and the reserve amount is monitored against emerging losses. There were no reserves of this type at December 31, 2012.

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

Initial Expected Loss Ratio 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 and the 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 a selected ratio of prior calendar years paid expense to paid loss to project ultimate loss adjustment expenses for adjusting and other expense. 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 that 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 blended result 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 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 are the following assumptions, which may impact our property and casualty reserves:

- Stability of future inflation rates and consistency with historical inflation norms;
- 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 laws that would significantly affect future payouts.
- No significant change in the overall level of case reserve adequacy from period to period

The loss ratio selections and loss development profiles are developed primarily 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 our loss reserves at December 31, 2012 are adequate. New information, legislation, events or circumstances, unknown at the original valuation date, however, may result in future development to our ultimate losses significantly greater or less than the recorded reserves at December 31, 2012.

For non-credit lines of business, future inflation rates could vary from our assumption of relatively stable rates. Unexpected changes in future inflation rates could impact our financial position and liquidity, and thus we chose to measure the sensitivity of our reserve levels to unexpected changes in inflation.

The impacts of a future 1.6% decrease and 2.4% increase over the implied inflation rate in our year-end gross loss reserve balance are as follows (amounts in thousands):

	December 31, 2012 Future Inflation	
Cumulative Increase (Decrease) in Reserves	**1.6% Decrease**	**2.4% Increase**
Personal		
Auto	$ (7,503)	$ 12,053
Homeowner	(1,263)	2,613

Commercial		
Agribusiness	(8,508)	16,422
Auto	(2,075)	4,830

The analysis of our credit insurance line of business quantifies the estimated impact on gross loss reserves of a reasonably likely scenario of varying the ratio applied to the earned premium to determine the IBNR reserves at December 31, 2012. 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 in gross reserves across all accident years combined of approximately $6.9 million.

It is not appropriate to aggregate the impacts shown in our sensitivity analysis, as our lines of business are not directly correlated. The variations are not meant to be a best-case or worst-case scenario, and it is possible that future variations will be more or less than the amounts in our sensitivity analysis. 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 our sensitivity analysis an actual reserve range.

Table of Contents

Reserving by Class of Business

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

Short-tail business The emergence of paid losses and case reserves for short-tail business is credible and likely indicator of ultimate losses; therefore, more reliance is placed on the Loss or Expense Development methods. Large catastrophe and weather-related events are analyzed separately using information available to our claims staff, loss development profiles from similar events and our own historical experience.

Long-tail business The emergence of paid losses and case reserves for long-tail business is less credible in early periods and, accordingly, may not be indicative of ultimate losses. Therefore, 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 previously discussed.

Claim adjustment expenses We estimate adjusting and other expenses 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.

Deferred Policy Acquisition Costs

We had a total DAC asset of approximately $1.25 billion and $1.32 billion at December 31, 2012 and 2011, respectively. Effective January 1, 2012, we retrospectively adopted new accounting guidance and implemented a new DAC capitalization policy. See Note 3, Recently Issued Accounting Pronouncements, of the Notes to the Consolidated Financial Statements for a detailed discussion regarding the impact of this pronouncement on us.

We believe that the estimates used in our DAC calculations provide a representative example of how variations in assumptions and estimates would affect our business. 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 for the year ended December 31, 2012 (in thousands):

	Increase/(decrease) in DAC
Increase in future investment margins of 25 basis points	$ 35,858
Decrease in future investment margins of 25 basis points	(40,486)
Decrease in future life mortality by 1%	3,299
Increase in future life mortality by 1%	(3,398)

Reinsurance

We manage our underwriting risk exposures by reinsuring portions of our insurance risks. 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 monitor the financial condition of those companies and believe we currently have no significant credit risk related to those counterparties.

Some of our reinsurance contracts contain clauses that allow us to terminate the participation with reinsurers whose ratings are downgraded. Information used in our risk assessment is comprised of industry ratings, recent news and reports, and a limited review of financial statements. We also may require letters of credit, trust agreements, or cash advances from reinsurers not licensed in our state of domicile to fund their share of outstanding claims and CAE. Final assessment is based on the judgment of senior management.

Other-Than-Temporary Impairment

Our accounting policy requires that a decline in the fair value of investment securities below their cost basis be evaluated on an ongoing basis to determine if the decline is other-than-temporary. A number of assumptions and estimates inherent in evaluating impairments are used to determine if they are other-than-temporary, which include 1) our ability and intent to hold the investment securities 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 cost basis; 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.

Valuation of Financial Instruments

The fair value of available-for-sale securities (equity and fixed maturity securities) is determined by management using one of the three primary sources of information: the quoted prices in active markets; third-party pricing services; or independent broker quotations. Estimated fair value of securities based on quoted prices in active markets are readily and regularly available; therefore, valuation of these securities generally does not involve management judgment.

For securities priced using third-party pricing services, fair value measurements are determined using the third-party pricing services proprietary pricing applications. The typical inputs used by the models are relevant market information, benchmark curves, benchmark pricing of like securities, sector groupings and matrix pricing. Any securities remaining unpriced after utilizing the first two pricing methods are submitted to the independent brokers for prices. We have analyzed the third-party pricing services and independent brokers valuation methodologies and related inputs, and have evaluated the various types of securities in our investment portfolio to determine an appropriate fair value hierarchy level based upon trading activity and the observability of market inputs. Management does complete certain tests throughout the year and at year-end to determine that prices provided by our pricing services are reasonable.

We utilize equity options to hedge equity-indexed universal life and deferred annuity benefits. Equity-indexed universal life and deferred annuity include a fixed host contracts and an embedded equity derivative. The embedded derivative portion of the contracts represent benefits in excess of fixed guarantees, and the host is associated with fixed guarantees. At issue, the value of the host contract equals the premium paid less the fair value of the embedded derivative. The initial host contract value is accreted to the fixed guaranteed value at end of the contract indexing term. The fair value of the embedded derivative is recalculated at each reporting period using the current contract values and option pricing assumptions. Interest credited is generally comprised of interest accruals to fixed deferred annuity account balances. In addition to the accrual of interest on the host contracts, the gain or loss on the embedded equity derivative is also recognized as interest credited for equity-indexed universal life and deferred annuities. Embedded derivative gains and losses can cause material fluctuations in interest credited from one period to the next.

Pension and Postretirement Benefit Plans

Our pension and postretirement benefit obligations and related costs covering our employees are calculated using actuarial concepts in accordance with the relevant accounting guidance. The discount rate and the expected return on plan assets are important elements of expense and/or liability measurements. Each year, these key assumptions are reevaluated to determine whether they reflect the best estimates for the current period. Changes in the methodology used to determine the best estimates are made when facts or circumstances change, for example, a general decline or rise in interest rates that have not yet been reflected in the rates implicit in the current prices of annuity contracts. Other assumptions involve demographic factors such as retirement age, mortality, turnover and rate of compensation increases. The expected long-term rate of return on plan assets is determined using the building-block method.

Table of Contents

Litigation Contingencies

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 condition. 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 statements.

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. Our income tax liability includes the liability for unrecognized tax benefits, interest and penalties, that 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.

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. 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.

Management s best estimate of future events and their impact is included in our 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 (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 U.S. federal statutory tax rate of 35%. The U.S. Department of the Treasury and the IRS have indicated that they 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.

Table of Contents

Consolidated Results of Operations

The following sets forth the consolidated results of operations (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Premiums and other revenues					
Premiums	$ 1,704,173	$ 1,748,612	$ 1,877,908	$ (44,439)	$ (129,296)
Other policy revenues	198,401	189,494	185,805	8,907	3,689
Net investment income	985,398	968,165	911,915	17,233	56,250
Realized investments gains (losses), net	68,208	90,866	74,062	(22,658)	16,804
Other income	30,880	25,890	23,491	4,990	2,399
Total premiums and other revenues	**2,987,060**	**3,023,027**	**3,073,181**	**(35,967)**	**(50,154)**
Benefits, losses and expenses					
Policyholder benefits	496,622	480,063	500,125	16,559	(20,062)
Claims incurred	949,106	1,032,497	1,108,290	(83,391)	(75,793)
Interest credited to policyholder s account balances	416,015	405,083	393,119	10,932	11,964
Commissions for acquiring and servicing policies	364,911	430,310	446,463	(65,399)	(16,153)
Other operating expenses	455,746	461,906	462,212	(6,160)	(306)
Change in deferred policy acquisition costs [1]	32,915	(38,262)	(40,119)	71,177	1,857
Total benefits and expenses	**2,715,315**	**2,771,597**	**2,870,090**	**(56,282)**	**(98,493)**
Income (loss) before other items and federal income taxes	**$ 271,745**	**$ 251,430**	**$ 203,091**	**$ 20,315**	**$ 48,339**

(1) A negative amount of net change indicates more expense was deferred than amortized and represents a decrease to expenses in the periods indicated.

Consolidated earnings increased during 2012 compared to 2011 primarily as a result of

- improved earnings in our annuity segment, and
- improved earnings in our property and casualty segment;
- partially offset by decreases in realized investment gains.

Consolidated earnings increased during 2011 compared to 2010 primarily as a result of

- improved Property and Casualty segment results, and
- an increase in net investment income primarily due to an increase in invested assets,

partially offset by a decrease in Life segment results.

In the Consolidated Results of Operations above and in the segment discussions that follow, certain amounts in the prior year have been reclassified to conform to the current year presentation. Additionally, certain prior year amounts were adjusted to reflect the effect of the retrospective adoption of a new accounting standard relating to DAC, which impacted reported income before other items and federal income taxes by a decrease of $2.3 million and an increase of $0.5 million during 2011 and 2010, respectively.

Table of Contents

Results of Operations and Related Information by Segment

Life

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

	Years ended December 31,			Change over prior year	
	2012	**2011**	**2010**	**2012**	**2011**
Premiums and other revenues					
Premiums	$ 281,621	$ 277,724	$ 282,160	$ 3,897	$ (4,436)
Other policy revenues	185,536	174,406	170,729	11,130	3,677
Net investment income	235,712	238,275	234,905	(2,563)	3,370
Other income	2,871	3,301	3,547	(430)	(246)
Total premiums and other revenues	**705,740**	**693,706**	**691,341**	**12,034**	**2,365**
Benefits, losses and expenses					
Policyholder benefits	340,003	344,328	294,177	(4,325)	50,151
Interest credited to policyholder s account balances	58,158	60,494	59,149	(2,336)	1,345
Commissions for acquiring and servicing policies	97,455	88,300	91,165	9,155	(2,865)
Other operating expenses	183,040	173,188	178,278	9,852	(5,090)
Change in deferred policy acquisition costs [(1)]	(7,167)	(2,115)	(1,460)	(5,052)	(655)
Total benefits and expenses	**671,489**	**664,195**	**621,309**	**7,294**	**42,886**
Income before other items and federal income taxes	**$ 34,251**	**$ 29,511**	**$ 70,032**	**$ 4,740**	**$ (40,521)**

(1) A negative amount of net change indicates more expense was deferred than amortized and represents a decrease to expenses in the periods indicated.

Earnings increased in 2012 compared to 2011 primarily due to an increase in other policy revenues, partially offset by an increase in other operating expenses.

In 2011, earnings decreased compared to 2010 as a result of an increase in policyholder benefits. This increase includes a $26.6 million increase in claims not yet reported and a $4.9 million increase in claims incurred or paid, both due to a modification of our claim settlement procedures.

Premiums and other revenues

Revenues from traditional life insurance products include scheduled premium payments from policyholders on whole life and term life products. The change in these premiums is impacted primarily by policy persistency and new sales during the period. Premiums increased during 2012 compared to 2011 primarily due to improved persistency and new sales. The decrease in 2011 compared to 2010 was primarily driven by higher reinsurance premiums due to increasing policy face values, and a decrease in the credit-related life products as a result of lower sales.

Other policy revenues include mortality charges, earned policy service fees and surrender charges on interest-sensitive life insurance policies. These charges increased during 2012 and 2011 compared to each preceding year primarily due to higher policy service fees on a growing block of life policies. This increase reflects the continued growth in interest-sensitive life business.

Table of Contents

Benefits, losses and expenses

Benefits decreased slightly during 2012 compared to 2011, and increased in 2011 compared to 2010, primarily as the result of an increase in the estimate of claims incurred but not reported. During 2011, there was an emerging shift of view regarding claim processes from the long-standing practice that a claim must be filed by a beneficiary to a view that an insurer should actively seek possible beneficiaries by monitoring information of a policyholder s death. This type of information might be ascertainable using the U.S. Social Security Death Master File (SSA Master File). We modified our claims settlement procedures in the fourth quarter of 2011 to apply this perspective on a nationwide basis. This led to an increase in our policy benefits of $22.1 million and $31.5 million during 2012 and 2011, respectively.

Commissions increased during 2012 compared to 2011 primarily due to increased sales. The decrease during 2011 compared to 2010 primarily resulted from the decrease in premiums of traditional products.

Other operating costs and expenses increased during 2012 compared to 2011, and decreased for 2011 compared to 2010, as a result of 2011 benefitting from a reduction of an accrual for litigation contingencies in addition to an increase in allocated costs to this segment during 2012.

The following table presents the components of the change in DAC (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Acquisition cost capitalized	$ 80,877	$ 76,890	$ 81,069	$ 3,987	$ (4,179)
Amortization of DAC	(73,710)	(74,775)	(79,609)	1,065	4,834
Change in DAC [(1)]	**$ 7,167**	**$ 2,115**	**$ 1,460**	**$ 5,052**	**$ 655**

(1) A positive amount of net change indicates more expense was deferred than amortized and represents a decrease to expenses in the periods indicated.

Acquisition costs capitalized increased during 2012 compared to 2011 primarily as a result of an increase in commissions from higher premiums. Acquisition costs capitalized decreased during 2011 compared to 2010 primarily as a result of the decrease in premiums. The decrease in the amortization of DAC during 2011 compared to 2010 was the result of an improved persistency.

Policy in-force information

The following table summarizes changes in the Life segment s in-force amounts (in thousands):

		December 31,		Change over prior year	
	2012	2011	2010	2012	2011
Life insurance in-force					
Traditional life	$ 48,856,459	$ 46,484,826	$ 45,919,219	$ 2,371,633	$ 565,607
Interest-sensitive life	24,132,101	23,671,800	23,879,283	460,301	(207,483)
Total life insurance in-force	**$ 72,988,560**	**$ 70,156,626**	**$ 69,798,502**	**$ 2,831,934**	**$ 358,124**

37

Table of Contents

The following table summarizes changes in the Life segment s number of policies in-force:

	December 31,			Change Over Prior Year	
	2012	2011	2010	2012	2011
Number of policies in-force					
Traditional life	2,122,666	2,204,187	2,274,144	(81,521)	(69,957)
Interest-sensitive life	185,729	178,595	176,160	7,134	2,435
Total number of policies	**2,308,395**	**2,382,782**	**2,450,304**	**(74,387)**	**(67,522)**

There was an increase in total life insurance in-force in 2012 compared to 2011, and 2011 compared to 2010. The increases of in-force amounts in our traditional life products is believed to be the result of consumers seeking contract guarantees due to the uncertain economic environment in recent years. During 2011, this increase was partially offset by a decrease in our interest-sensitive life policies as the result of lower prevailing interest rates. The decrease in our policy count during 2012 and 2011 is attributable to surrenders and lapses, as well as new business activity generally being comprised of fewer but larger face-value policies.

Reinsurance

The table below summarizes reinsurance reserves and premium amounts assumed and ceded (in thousands):

	Reserves December 31,			Premiums Years ended December 31,		
	2012	2011	2010	2012	2011	2010
Reinsurance assumed	$ 1,564	$ 4,318	$ 9,827	$ 2,189	$ 2,974	$ 5,716
Reinsurance ceded	(189,335)	(188,812)	(173,097)	(93,066)	(92,208)	(90,459)
Total	**$ (187,771)**	**$ (184,494)**	**$ (163,270)**	**$ (90,877)**	**$ (89,234)**	**$ (84,743)**

We use reinsurance to mitigate excessive risk to the Life segment. During 2012 our retention limits were $2,350,000 for issue ages 65 and under, and $1,550,000 for issue ages 66 and older for traditional and universal life, unchanged from 2011, as compared to a single limit of $1,550,000 during 2010. Accidental death and premium waiver benefits are mostly retained on new business. Increases in reserves and premium amounts ceded primarily reflect increased use of reinsurance in conjunction with treaties related to universal life products. Decreases in assumed reserves and premium were primarily due to the cancellation of our reinsurance agreement with two credit life reinsurers. Those blocks of business are now in run-off, and the new business retained is currently written by us on a direct basis.

Consistent with our corporate risk management strategy we periodically adjust our reinsurance program and retention limits as market conditions warrant. While, in the past, we have 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 100% in excess of retention. Current traditionally marketed term products are reinsured on a modified excess retention basis, in which we reinsure mortality risk on a yearly renewable term basis, ceding 50% quota share of face amounts in excess of $250,000 up to our retention and then 100% in excess of retention. Current direct marketed products are coinsured on a 60% basis, up to our retention, and then 100% in excess of retention.

Reinsurance is used in the credit life business primarily to provide producers of credit-related insurance products the opportunity to participate in the underwriting risk through offshore producer-owned captive reinsurance companies. A majority of the treaties entered into by our Credit Insurance Division are written on a 100% coinsurance basis with benefit limits of $100,000 on credit life. We have entered into funds withheld reinsurance treaties, which are ceded to the reinsurer on a written basis.

Table of Contents

For 2012, the companies to whom we have ceded reinsurance for the Life segment are shown below (in thousands, except percentages):

Reinsurer	A.M. Best Rating[(1)]	Ceded Premium	Percentage of Gross Premium
Swiss Re Life and Health of America	A+	$ 24,258	6.5%
SCOR Global Life Americas Reinsurance Company	A	17,964	4.8
Munich American Reassurance Company	A+	12,952	3.5
Reinsurance Group of America	A-	7,748	2.1
Canada Life Assurance	A+	6,759	1.8
General Re Life Corporation	A ++	4,729	1.3
Other Reinsurers with no single company greater than 5% of the total ceded premium		18,656	5.0
Total life reinsurance ceded		**$ 93,066**	**25.0%**

(1) A.M. Best rating as of the most current information available February 14, 2013.

Annuity

Annuity segment financial results for the periods indicated were as follows (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Premiums and other revenues					
Premiums	$ 116,393	$ 94,753	$ 174,193	$ 21,640	$ (79,440)
Other policy revenues	12,865	15,088	15,076	(2,223)	12
Net investment income	603,349	577,707	535,581	25,642	42,126
Other income	196	250	607	(54)	(357)
Total premiums and other revenues	**732,803**	**687,798**	**725,457**	**45,005**	**(37,659)**
Benefits, losses and expenses					
Policyholder benefits	156,619	135,735	205,948	20,884	(70,213)
Interest credited to policyholder s account balances	357,857	344,589	333,970	13,268	10,619
Commissions for acquiring and servicing policies	54,785	94,851	95,701	(40,066)	(850)
Other operating expenses	45,317	72,201	71,202	(26,884)	999
Change in deferred policy acquisition costs [(1)]	21,724	(29,354)	(44,127)	51,078	14,773
Total benefits and expenses	**636,302**	**618,022**	**662,694**	**18,280**	**(44,672)**
Income before other items and federal income taxes	**$ 96,501**	**$ 69,776**	**$ 62,763**	**$ 26,725**	**$ 7,013**

(1) A negative amount of net change indicates more expense was deferred than amortized and represents a decrease to expenses in the periods indicated.

Earnings increased in 2012 compared to 2011 primarily due to a decrease in other operating expenses. In addition, the increase in net investment income outpaced the related increase in interest credited to policyholders account balances. Other operating expenses were higher during 2011 primarily as a result of the settlement of litigation in 2011 for $12.0 million.

Earnings increased in 2011 compared to 2010 primarily as the result of the growth in net investment income outpacing the growth in interest credited. Additionally, the above-referenced litigation settlement impacted other operating expenses during 2011.

During 2012, we discontinued marketing annuities through one of our third-party marketing organizations. Termination of this relationship is not expected to have an significant impact on our annuity volume or our ability to generate annuity sales, and is not expected to materially impact earnings. The total business written by this organization represented 13.3% of total annuity premium and deposits during 2012 and 8.6% of account values at December 31, 2012, and was primarily comprised of fixed deferred annuities.

Table of Contents

Premiums and other revenues

Annuity premium and deposit amounts received are shown below (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Fixed deferred annuity	$ 568,716	$ 1,470,159	$ 1,045,429	$ (901,443)	$ 424,730
Single premium immediate annuity	200,921	159,824	177,688	41,097	(17,864)
Equity-indexed deferred annuity	127,357	142,526	340,920	(15,169)	(198,394)
Variable deferred annuity	104,432	99,224	90,188	5,208	9,036
Total premium and deposits	**1,001,426**	**1,871,733**	**1,654,225**	**(870,307)**	**217,508**
Less: Policy deposits	885,033	1,776,980	1,480,032	(891,947)	296,948
Total earned premiums	**$ 116,393**	**$ 94,753**	**$ 174,193**	**$ 21,640**	**$ (79,440)**

We monitor account values and changes in those values as a key indicator of performance in our Annuity segment. Changes in account values are mainly the result of net inflows, surrenders, policy fees, interest credited and market value changes. Shown below are the changes in account values (in thousands):

	Years ended December 31,		
	2012	2011	2010
Fixed deferred and equity-indexed annuity			
Account value, beginning of period	$ 9,824,416	$ 9,006,692	$ 8,151,365
Net inflows	518,074	1,349,874	1,180,826
Surrenders	(879,886)	(863,590)	(652,519)
Fees	(8,219)	(10,146)	(10,080)
Interest credited	348,812	341,586	337,100
Account value, end of period	**$ 9,803,197**	**$ 9,824,416**	**$ 9,006,692**
Single premium immediate annuity			
Reserve, beginning of period	$ 978,722	$ 903,126	$ 820,295
Net inflows	52,957	32,167	42,502
Interest and mortality	43,959	43,429	40,329
Reserve, end of period	**$ 1,075,638**	**$ 978,722**	**$ 903,126**
Variable deferred annuity			
Account value, beginning of period	$ 380,129	$ 415,757	$ 400,624
Net inflows	99,432	88,044	86,528
Surrenders	(102,058)	(112,221)	(114,320)
Fees	(4,742)	(4,786)	(4,795)
Change in market value and other	44,884	(6,665)	47,720
Account value, end of period	**$ 417,645**	**$ 380,129**	**$ 415,757**

Fixed deferred annuity net inflows decreased significantly during 2012 compared to 2011. The volume of net inflows is highly sensitive to the interest rate credited on new annuity sales. We managed these products to lower sales during 2012, to mitigate risks associated with investing in the persistently low interest rate environment. Net inflows increased significantly during 2011 compared to 2010, primarily as a result of our marketing efforts to expand distribution through new accounts.

An equity-indexed annuity allows a policyholder to participate in equity returns while also having certain downside protection from the guaranteed minimum returns defined in the product. Net inflows for this product decreased during 2012 compared to 2011, and during 2011 compared to 2010. These decreases were primarily attributed to lower indexed crediting terms resulting from lower fixed investment yields.

Table of Contents

Single premium immediate annuity (SPIA) net inflows increased during 2012 compared to 2011, driven primarily by the changing investment priorities of potential customers entering the market for guaranteed monthly payouts on a portion of their retirement dollars. Net inflows decreased during 2011 compared to 2010 primarily as a result of lower investment yields, restraining demand for this product in anticipation of increased income payments in the future.

Variable deferred annuity products remain relatively unchanged for all years presented. These products have no living benefits. Our total direct exposure on the guaranteed minimum death benefits associated with these products were $2.4 million and $3.9 million as of December 31, 2012 and 2011, respectively. After reinsurance, the net exposure was $0.6 million and $1.3 million, as of December 31, 2012 and 2011, respectively. All such guaranteed minimum death benefit reinsurance is with reinsurers rated A or higher by A.M. Best.

Net investment income increased during 2012 compared to 2011, and 2011 compared to 2010. The 2012 increase was primarily as a result of a $21.7 million increase in realized gains from marking our option portfolio to fair value, in addition to a 4.5% increase in the assets attributable to annuity account balances during 2012. The increase during 2011 was primarily the result of a 9.2% increase in the assets attributable to annuity account balances, partially offset by a $14.7 million decrease in realized gains from our option portfolio.

Benefits, losses and expenses

Policyholder benefits consist of annuity payments and reserve increases for SPIA contracts. Benefits are highly correlated to the sales volume of SPIA contacts and increased for 2012 compared to 2011, and decreased for 2011 compared to 2010, due to the changes in SPIA premium during the period.

Commissions decreased for 2012 compared to 2011 primarily due to reduced fixed deferred annuity production as well as decreases in commission rates on certain annuities. Commissions were essentially flat in 2011 compared to 2010.

Other operating expenses decreased during 2012 compared to 2011 primarily as a result of an accrual during 2011 related to the settlement of certain litigation, as well as a decrease in allocated costs to this segment during 2012. Additionally, a decrease in producer compensation linked to annuity production further reduced other operating expenses. Other operating expenses were unchanged during 2011 compared to 2010.

The change in DAC represents acquisition costs capitalized less the amortization of existing DAC, which is calculated in proportion to gross profits. The following shows the components of the change in DAC (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Acquisition cost capitalized	$ 68,799	$ 116,206	$ 115,813	$ (47,407)	$ 393
Amortization of DAC	(90,523)	(86,852)	(71,686)	(3,671)	(15,166)
Change in DAC [1]	**$ (21,724)**	**$ 29,354**	**$ 44,127**	**$ (51,078)**	**$ (14,773)**

(1) A positive amount of net change indicates more expense was deferred than amortized and is a decrease to expense in the periods indicated. The decrease in acquisition costs capitalized during 2012 compared to 2011 was the result of lower commissions incurred with the decrease in fixed deferred annuity production. The increase in the amortization of DAC during 2011 as compared to 2010 was primarily as a result of surrender activity.

An important measure of the Annuity segment is amortization of DAC as a percentage of gross profits. The amortization of DAC as a percentage of gross profits for the years ended December 31, 2012, 2011, and 2010 was 41.5%, 41.9%, and 38.6%, respectively. The decrease in the ratio during 2012 was primarily driven by improvement in persistency which we attribute to fewer surrenders as contract holders believed the rates on existing contracts were at least as good or better than rates on new contracts being offered by our competition. The increase in the ratio during 2011 compared to 2010 was the result of a decline in persistency during the year.

41

Options and Derivatives

Shown below is the analysis of the impact to net investment income of the option return, along with the impact to interest credited of the equity-indexed annuity embedded derivative (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Net investment income					
Without option return	$ 584,418	$ 580,501	$ 523,670	$ 3,917	$ 56,831
Option return	18,931	(2,794)	11,911	21,725	(14,705)
Interest credited to policy account balances					
Without embedded derivative	344,526	352,410	327,366	(7,884)	25,044
Equity-indexed annuity embedded derivative	13,331	(7,821)	6,604	21,152	(14,425)

Net investment income without option return increased during 2012 and 2011, primarily due to increases in aggregate annuity account values. Interest credited to policyholders account balances without equity-indexed return decreased during 2012 due to a decrease in crediting rates, and increased during 2011 due to increases in aggregate annuity account values.

The option return, as well as the related equity-indexed annuity embedded derivative return, increased during 2012 compared to 2011, and decreased during 2011 compared to 2010, as a result of the change in the S&P 500 Index during the respective periods. These option returns correlate to the 13.4%, 0.0%, and 12.8% return of the S&P 500 Index during 2012, 2011, and 2010, respectively.

Health

Health segment results for the periods indicated were as follows (in thousands):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Premiums and other revenues					
Premiums	$ 223,773	$ 231,793	$ 263,294	$ (8,020)	$ (31,501)
Net investment income	11,789	13,413	15,492	(1,624)	(2,079)
Other income	15,548	13,356	10,384	2,192	2,972
Total premiums and other revenues	**251,110**	**258,562**	**289,170**	**(7,452)**	**(30,608)**
Benefits, losses and expenses					
Claims incurred	155,825	159,289	184,554	(3,464)	(25,265)
Commissions for acquiring and servicing policies	26,383	25,808	35,263	575	(9,455)
Other operating expenses	44,966	47,160	49,627	(2,194)	(2,467)
Change in deferred policy acquisition costs [(1)]	5,890	9,172	4,930	(3,282)	4,242
Total benefits and expenses	**233,064**	**241,429**	**274,374**	**(8,365)**	**(32,945)**
Income before other items and federal income taxes	**$ 18,046**	**$ 17,133**	**$ 14,796**	**$ 913**	**$ 2,337**

(1) A negative amount of net change indicates more expense was deferred than amortized and represents a decrease to expenses in the periods indicated.

Earnings increased 5.3% for 2012 compared to 2011. Earnings increased for 2011 as compared to 2010 driven primarily by an increase in other income comprised of fee income associated with high sales by a new MGU, in addition to a decrease in the benefit ratio.

Premiums and other revenues

Health earned premiums for the periods indicated are as follows (in thousands, except percentages):

	Years ended December 31,					
	2012		**2011**		**2010**	
	dollars	percentage	dollars	percentage	dollars	percentage
Medicare Supplement	$ 96,808	43.3%	$ 100,924	43.6%	$ 117,132	44.5%
Medical expense	37,414	16.7	47,323	20.4	67,050	25.5
Group health	40,130	17.9	33,906	14.6	29,343	11.1
Credit accident and health	16,686	7.5	19,897	8.6	21,553	8.2
MGU	17,103	7.6	13,681	5.9	11,173	4.2
All other	15,632	7.0	16,062	6.9	17,043	6.5
Total	**$ 223,773**	**100.0%**	**$ 231,793**	**100.0%**	**$ 263,294**	**100.0%**

Earned premiums decreased during 2012 compared 2011, primarily resulting from the run-off of our closed medical expense block of insurance plans, which will continue decreasing. In addition, Medicare Supplement premiums declined due to policy lapses outpacing new sales along with a lower average premium per policy on those new sales. These decreases were partially offset by increases in revenues of our group and MGU lines.

The Health segment s earned premiums decreased during the year ended December 31, 2011 as compared to 2010 primarily due to the discontinuation of sales of our medical expense insurance plans effective June 30, 2010. In-force policies continue to lapse and this produced the reduction in premiums. Due to the competitive nature of the market, sales of our Medicare Supplement product also decreased. Additionally, our credit accident and health premiums decreased primarily due to a decrease in new business related to short-term financing.

Our in-force certificates or policies as of the dates indicated are as follows:

	December 31,					
	2012		**2011**		**2010**	
	number	percentage	number	percentage	number	percentage
Medicare Supplement	41,562	6.7%	42,760	6.8%	48,584	7.7%
Medical expense	5,745	0.9	7,962	1.3	11,057	1.8
Group	19,868	3.2	20,122	3.2	20,893	3.3
Credit accident and health	253,710	40.7	271,700	43.3	294,702	46.6
MGU	197,050	31.6	147,251	23.5	103,666	16.4
All other	105,499	16.9	137,596	21.9	152,917	24.2
Total	**623,434**	**100.0%**	**627,391**	**100.0%**	**631,819**	**100.0%**

Our total in-force policies decreased during 2012 compared to 2011, and in 2011 compared to 2010. Increases in the MGU line were more than offset by decreases in the credit accident and health and other lines. The MGU line increased due to increased production by existing MGU s, and the addition of new MGUs. The all other line is mostly composed of closed blocks of business, and has few new sales. The MGU and Group in-force policies include a block of 100% reinsured certificates, which is a rapidly growing block of business. The increases in these 100% reinsured certificates will not translate into corresponding increases in premiums.

Benefits, losses and expenses

Claims incurred were relatively unchanged during 2012, and decreased during 2011 compared to 2010 primarily as the result of a decline in sales of our medical expense insurance plans and Medicare Supplement products. The decline in claims incurred was consistent with lower premiums and lower commissions. Additionally, the medical expense benefit ratio, measured as the ratio of claims and other benefits to premiums, increased to 69.6% in 2012, from 68.7% in 2011, but decreased from 70.1% in 2010. The 2011 decrease in the benefit ratio compared

to 2010 was driven primarily by a significant decrease in claims.

Table of Contents

Commissions were relatively unchanged during 2012, and decreased during 2011 compared to 2010, as a result of lower sales.

Other operating expenses decreased slightly during 2012 compared to 2011, and 2011 compared to 2010 as a result of managing expenses down as the aggregate health block of business decreased.

Change in Deferred Policy Acquisition Costs

The following table presents the components of the change in DAC (in thousands):

	Years ended December 31,			Change over prior year	
	2012	**2011**	**2010**	**2012**	**2011**
Acquisition cost capitalized	$ 11,018	$ 11,815	$ 17,994	$ (797)	$ (6,179)
Amortization of DAC	(16,908)	(20,987)	(22,924)	4,079	1,937
Change in DAC [(1)]	**$ (5,890)**	**$ (9,172)**	**$ (4,930)**	**$ 3,282**	**$ (4,242)**

(1) A negative amount of net change indicates less expense was deferred than amortized and represents an increase to expenses in the periods indicated.

Acquisition cost capitalized decreased during 2012 compared to 2011 primarily due to the decreases in amortization outpacing costs capitalized due to the aggregate decrease in the health block of business. Acquisition cost capitalized decreased during 2011 compared to 2010 primarily resulting from the decrease in sales and resulting decrease in commissions.

Reinsurance

For the medical expense business, we use reinsurance on an excess of loss basis. Our retention limit is $500,000 per claim on these types of policies. We cede or retrocede the majority of the risk associated with our stop loss and other catastrophic health reinsurance programs. We maintain reinsurance on a quota share basis for our long-term care and disability income business.

Reinsurance is also used in the credit accident and health business. In certain cases, particularly in the auto retail market, we may also reinsure the policy written through offshore producer-owned captive reinsurers to allow the dealer to participate in the performance of these credit accident and health contracts. A majority of the treaties entered into by our Credit Insurance Division are written on a 100% coinsurance basis with benefit limits of $1,000 per month.

For 2012, the companies to which we have ceded reinsurance for the Health segment are shown below (in thousands, except percentages):

Reinsurer	**A.M. Best Rating[(1)]**	**Ceded Premium**	**Percentage of Gross Premium**
Harbour Life & Reinsurance Co Ltd.	NR	$ 59,358	14.1%
Maiden Re	A-	30,997	7.4
Munich Reinsurance America	A+	27,764	6.6
American First Insurance Company	NR	20,582	4.9
Other reinsurers with no single company greater than 5.0% of the total ceded premium		59,058	14.0
Total health reinsurance ceded		**$ 197,759**	**47.0%**

(1) A.M.Best rating as of the most current information available February 14, 2013.

Table of Contents

Property and Casualty

Property and Casualty results for the periods indicated were as follows (in thousands, except percentages):

	Years ended December 31,			Change over prior year	
	2012	**2011**	**2010**	**2012**	**2011**
Premiums and other revenues					
Net premiums written	$ 1,047,211	$ 1,137,445	$ 1,154,415	$ (90,234)	$ (16,970)
Net premiums earned	$ 1,082,386	$ 1,144,342	$ 1,158,261	$ (61,956)	$ (13,919)
Net investment income	69,604	72,071	72,620	(2,467)	(549)
Other income	6,360	6,003	5,778	357	225
Total premiums and other revenues	**1,158,350**	**1,222,416**	**1,236,659**	**(64,066)**	**(14,243)**
Benefits, losses and expenses					
Claims incurred	793,281	873,208	923,736	(79,927)	(50,528)
Commissions for acquiring and servicing policies	186,288	221,351	224,334	(35,063)	(2,983)
Other operating expenses	120,888	124,336	124,410	(3,448)	(74)
Change in deferred policy acquisition costs (1)	12,468	(15,965)	538	28,433	(16,503)
Total benefits and expenses	**1,112,925**	**1,202,930**	**1,273,018**	**(90,005)**	**(70,088)**
Income (loss) before other items and federal income taxes	**$ 45,425**	**$ 19,486**	**$ (36,359)**	**$ 25,939**	**$ 55,845**
Loss ratio	73.3%	76.3%	79.8%	(3.0)	(3.5)
Underwriting expense ratio	29.5	28.8	30.2	0.7	(1.4)
Combined ratio	**102.8%**	**105.1%**	**110.0%**	**(2.3)**	**(4.9)**
Impact of catastrophe events on combined ratio	9.3	11.4	10.8	(2.1)	0.5
Combined ratio without impact of catastrophe events	**93.5%**	**93.7%**	**99.2%**	**(0.2)**	**(5.4)**
Gross catastrophe losses	$ 135,625	$ 217,851	$ 141,685	$ (82,226)	$ 76,166
Net catastrophe losses	94,025	120,628	123,239	(26,603)	(2,611)

(1) A negative amount of net change indicates more expense was deferred than amortized and represents a decrease to expenses in the periods indicated.

Property and Casualty results improved during 2012 compared to 2011 primarily due to continued actions to address price adequacy, underwriting and additional risk mitigation actions resulting in a significant decrease in claims incurred, partially offset by a decrease in premiums. Commissions also declined primarily due to a shift from commission to non-commission products in our credit insurance division. Earnings improved during 2011 compared to 2010 primarily due to improvements in pricing adequacy, changes to our reinsurance programs which provided for an increase in recoveries on catastrophe losses in excess of additional reinsurance premium paid, and to a lesser extent rigorous management of our expenses.

Premiums and other revenues

Net premiums written and earned decreased during 2012 compared to 2011 resulting from a decline of policies in-force due to attrition and risk mitigation actions in our Personal lines, in addition to product alterations in our Credit Insurance Division. Net premiums written and earned

decreased during 2011 compared to 2010 primarily due to an increase in catastrophe reinsurance reinstatement premiums and decreased premiums across the personal lines of business due to a decline in policies in-force, partially offset by increased premium per exposure. Our catastrophe reinsurance reinstatement premium increased by $9.0 million over the same period in 2010 as the result of higher catastrophe reinsurance recoveries in 2011 compared to 2010.

Benefits, losses and expenses

Claims incurred decreased during 2012 compared to 2011 as a result of a decrease in catastrophe losses and a decline in non-catastrophe losses due primarily to reduced exposure in high catastrophe areas. The lower catastrophe losses, together with improved rate adequacy and improved claims frequency, caused the decrease in the loss ratio. Claims incurred decreased during 2011 compared to 2010 as a result of a decline in losses in all lines except agribusiness and other personal lines.

Table of Contents

Gross catastrophes for the year ended December 31, 2012 were $135.6 million, compared to $217.9 million for the same period in 2011. We experienced a significant decrease in catastrophe losses due primarily to a decrease in frequency of catastrophes in 2012 as compared to 2011, as well as the severity of the catastrophe events in 2011. In 2012 there were 26 catastrophe events compared to 31 in 2011 and 33 in 2010. Hurricane Sandy accounted for $46.6 million in gross catastrophe losses and $11.1 million in net catastrophe losses in 2012. 2011 catastrophe activity included a record number of tornados, including two events which impacted primarily Alabama in late April 2011 and Joplin, Missouri in May 2011.

The combined ratio, excluding net catastrophe impact, remained relatively flat during 2012 compared to 2011 and improved during 2011 compared to 2010. This was driven by an improvement in rate adequacy. Inherent to our fundamental risk management practices, we continue to evaluate and manage our aggregate catastrophe risk exposure with risk selection and reinsurance coverage.

Commissions decreased during 2012 compared to 2011 primarily due to a shift from commission to non-commission products in our Credit Insurance Division. Commissions remained flat during 2011 compared to 2010.

The change in DAC during 2012 increased total expenses compared to 2011. The higher amortization is attributable to Credit business written in prior years being earned while recently introduced products with lower revenue and without commissions are a larger portion of the current Credit business. The decrease during 2011 compared to 2010 is attributable to a shift in our credit-related property products from shorter duration products to longer duration products. We regularly review the recoverability of DAC, and if the actual emergence of future profitability were to be substantially lower than estimated, we would accelerate DAC amortization to account for any recoverability issues or premium deficiency. We have not historically experienced these issues with our DAC balances.

Products

Our Property and Casualty segment consists of: (i) Personal, which we market primarily to individuals, represent 63.1% of net premiums written, (ii) Commercial, which focus primarily on agricultural and other commercial markets, represent 29.3% of net premiums written, and (iii) Credit-related property insurance products, which are marketed to and through financial institutions and retailers represent 7.6% of net premiums written.

Personal Products

Personal Products results for the periods indicated were as follows (in thousands, except percentages):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Net premiums written					
Auto	$ 416,611	$ 444,454	$ 468,100	$ (27,843)	$ (23,646)
Homeowner	208,131	213,513	217,785	(5,382)	(4,272)
Other Personal	36,212	35,691	38,875	521	(3,184)
Total net premiums written	**660,954**	**693,658**	**724,760**	**(32,704)**	**(31,102)**
Net premiums earned					
Auto	423,265	463,171	470,535	(39,906)	(7,364)
Homeowner	207,048	217,619	216,849	(10,571)	770
Other Personal	35,738	36,173	39,298	(435)	(3,125)
Total net premiums earned	**$ 666,051**	**$ 716,963**	**$ 726,682**	**$ (50,912)**	**$ (9,719)**
Loss ratio					
Auto	77.9%	75.7%	78.0%	2.2	(2.3)
Homeowner	94.5	102.1	104.1	(7.6)	(2.0)
Other Personal	56.2	67.8	61.6	(11.6)	6.2
Personal line loss ratio	**81.9%**	**83.3%**	**84.9%**	(1.4)	(1.6)
Combined Ratio					
Auto	99.4%	96.6%	102.3%	2.8	(5.7)
Homeowner	119.0	125.7	129.6	(6.7)	(3.9)
Other Personal	76.6	89.6	68.7	(13.0)	20.9
Personal line combined ratio	**104.3%**	**105.0%**	**108.6%**	(0.7)	(3.6)

Personal Automobile: Net premiums written and earned decreased in our personal automobile line during 2012 compared to 2011 primarily due to a decline in policies in-force resulting from a combination of the decreases in homeowner policies in-force, which decreased cross-sell opportunities. Net premiums written and earned decreased during 2011 compared to 2010, due to a decline in policies in-force resulting from a competitive marketplace and lower new business sales. The loss and combined ratios increased slightly during 2012 compared to 2011 consistent with our expectations. The loss and combined ratios decreased during 2011 compared to 2010 due to improved rate adequacy as well as an increase in commissions in 2010 that was not incurred in 2011.

The combined industry ratios per A.M. Best s U.S. Property/Casualty-Review and Preview for 2012 (estimated), 2011 and 2010 are 99.6%, 101.9 and 101.0%, respectively.

Homeowners: Net premiums written and earned decreased during 2012 compared to 2011 primarily due to fewer policies in-force. The decrease in homeowner policies in-force was primarily driven by improved rate adequacy and our catastrophe risk mitigation actions, which are tailored to the local market conditions in the states where we write policies. Net premiums written decreased during 2011 compared to 2010 attributable to increased catastrophe reinsurance reinstatement premiums as a result of higher catastrophe reinsurance losses ceded and a decline in policies in-force. Net premiums earned remained relatively flat during 2011 compared to 2010.

The loss and combined ratios decreased during 2012 and 2011 compared to the prior years primarily due to improved catastrophe experience and improved rate adequacy. The loss and combined ratios improved slightly during the year ended December 31, 2011 compared to 2010 primarily due to improved rate adequacy. The combined ratios for the industry per A.M. Best for 2012 (estimated), 2011 and 2010 were 118.0%, 122.2% and 106.7%, respectively.

Other Personal: These products include watercraft, rental-owner and umbrella coverages for individuals seeking to protect their personal property and liability not covered within their homeowner and auto policies. Net premiums written and earned remained substantially unchanged during 2012 compared to 2011, and decreased during 2011 compared to 2010 due to a decline in policies in-force. Premiums for these products

generally trend with the homeowners and personal automobile lines as policies are typically sold in conjunction with one another.

Table of Contents

Commercial Products

Commercial Products results for the periods indicated were as follows (in thousands, except percentages):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Net premiums written					
Other Commercial	$ 130,103	$ 126,013	$ 123,605	$ 4,090	$ 2,408
Agribusiness	98,026	98,152	103,937	(126)	(5,785)
Auto	78,450	82,266	80,109	(3,816)	2,157
Total net premiums written	**306,579**	**306,431**	**307,651**	**148**	**(1,220)**
Net premiums earned					
Other Commercial	122,174	121,420	120,365	754	1,055
Agribusiness	104,098	102,946	106,678	1,152	(3,732)
Auto	79,478	84,201	80,948	(4,723)	3,253
Total net premiums earned	**$ 305,750**	**$ 308,567**	**$ 307,991**	**$ (2,817)**	**$ 576**
Loss ratio					
Other Commercial	66.4%	66.2%	82.9%	0.2	(16.7)
Agribusiness	92.3	118.2	108.3	(25.9)	9.9
Auto	64.6	60.8	72.9	3.8	(12.1)
Commercial line loss ratio	**74.7%**	**82.1%**	**89.1%**	(7.4)	(7.0)
Combined ratio					
Other Commercial	93.9%	94.4%	112.1%	(0.5)	(17.7)
Agribusiness	127.8	155.0	145.2	(27.2)	9.8
Auto	86.8	83.0	97.2	3.8	(14.2)
Commercial line combined ratio	**103.6%**	**111.5%**	**119.6%**	(7.9)	(8.1)

Other Commercial: Net premiums written and earned increased during 2012 and 2011 compared to prior years primarily as a result of an increase in workers compensation premiums due to rate increases and premium assumed from involuntary pools. Net written and earned premiums increased through 2011 compared to 2010 primarily as a result of rate increases in the workers compensation product. The loss and combined ratios during 2012 remained substantially unchanged compared to 2011. The loss and combined ratios decreased during 2011 compared to 2010 as a result of lower claim severity in the workers compensation product.

Agribusiness Product: Our agribusiness product allows policyholders to customize and cover their agriculture exposure via a package policy which includes coverage for residences and household contents, farm buildings and building contents, personal and commercial liability and personal property. Net premiums written were substantially unchanged in 2012 as compared to 2011, and net premiums earned increased during 2012 as compared to 2011, primarily as a result of a decrease in reinsurance reinstatement premiums. Net premiums written and earned decreased during 2011 compared to the same period in 2010 primarily as a result of a decrease in policies in-force as the result of non-renewing certain policies in unprofitable segments and catastrophe reinsurance reinstatement premiums that were not incurred in 2010.

The loss and combined ratios decreased significantly during 2012, primarily as the result of a reduction in net catastrophe losses. These ratios increased during 2011 compared to 2010 primarily as the result of increases in catastrophe losses and the frequency and severity of non-catastrophe losses. The frequency and severity of storms and weather related events continue to cause variability in this line of business.

Commercial Automobile: Net premiums written and earned decreased during 2012 compared to 2011 primarily as a result of lower new business writings in our small commercial business as well as selective underwriting intended to improve risk selection. Net premiums written and earned increased during 2011 compared to 2010 primarily as the result of a vehicle reclassification adjustment that resulted in refunds to policyholders in 2010 that did not occur in 2011. The increase was offset by a reduction in polices in-force from our primary lines and improved selective underwriting.

This product line experienced relatively unchanged losses during 2012 compared to 2011, and a decrease in losses during 2011 compared to 2010 due to a decrease in the frequency and severity of claims, which resulted in an improvement in the loss and combined ratios during the period. The combined industry ratios per A.M. Best for 2012 (estimated), 2011, and 2010 were 107.1%, 104.6% and 98.0%, respectively.

Table of Contents

Credit Products

Credit-related property products for the periods indicated were as follows (in thousands, except percentages):

	Years ended December 31,			Change over prior year	
	2012	2011	2010	2012	2011
Net premiums written	$ 79,678	$ 137,356	$ 122,004	$ (57,678)	$ 15,352
Net premiums earned	110,585	118,812	123,588	(8,227)	(4,776)
Loss ratio	17.6%	19.1%	26.2%	(1.5)	(7.1)
Combined ratio	88.0%	88.5%	96.1%	(0.5)	(7.6)

Credit-related property insurance products are offered on automobiles, furniture and appliances in connection with the financing of those items. These policies pay an amount if the insured property is lost or damaged and is not directly related to an event affecting the consumer s ability to pay the debt. The primary distribution channel for credit-related property insurance is general agents who market to sellers of covered products and financial institutions.

Net premiums written and earned decreased during 2012 compared to 2011. The primary driver for the decrease in premiums is a shift from Guaranteed Auto Protection (GAP) Insurance to GAP Waiver, a lower premium debt protection product. Net premiums written increased during 2011 compared to 2010. This increase was primarily driven by the reduction of reinsurance placed with producer-owned reinsurance companies. Net premiums earned decreased during 2011 due to our credit business continuing to shift from the shorter duration collateral protection products, to the longer duration GAP products.

The loss ratios remained substantially unchanged during 2012 compared to 2011. The decrease in the loss ratio during 2011 compared to 2010 was attributable to an overall decline in claims incurred as a result of lower frequency and severity of claims. Specifically, the GAP line of business experienced a positive trend in claims incurred as the result of used automobile market values rebounding from the recent financial crisis.

The combined ratios remained substantially unchanged during 2012 compared to 2011. The combined ratios decrease during 2011 compared to 2010 primarily as a result of the decrease in the loss ratio, which was partially offset by higher underwriting expenses from rising commission expenses as a result of the change in our product mix.

Reinsurance

We reinsure a portion of the risks that we underwrite to manage our loss exposure and protect capital resources. In return for a premium, reinsurers assume a portion of the claims incurred.

In addition to our reinsurance coverage, we are partially protected by the Terrorism Risk Insurance Act of 2002, which was modified and extended through December 31, 2014 by the Terrorism Risk Insurance Program Reauthorization Act of 2007.

Table of Contents

We retain the first $1.0 million of loss per risk, which will remain the same for 2013. Our catastrophe reinsurance retention covering all our property and casualty companies in total has been $40.0 million in recent years and will remain the same in 2013. The following table summarizes the Company s catastrophe reinsurance coverage effective January 1, 2013 to December 31, 2013.

Layer of Loss	Catastrophe Reinsurance Coverage in Force
Less than $10 million	100% of loss retained except for certain losses covered by the *Catastrophe Aggregate* cover described below
$10 million $40 million	95% of earthquake losses outside of California 95% of multiple peril losses in Northeast and mid Atlantic states 90% of multiple peril losses in Texas, Oklahoma, and Arkansas 90% of multiple peril losses in coastal states from Louisiana to Virginia 95% of multiple peril losses in states outside the Northeast excluding hurricane losses in coastal states (covered by previous two covers)
$40 million $500 million	95% of multiple peril losses covered by *Corporate Program* (all perils). The Corporate Program covers all non-credit property and casualty business, subject to certain limits, and is not specific to the Company or any of its subsidiaries, or any state or region.

All per event covers above include one automatic reinstatement and were placed at 97.5% in 2012. The automatic reinstatement requires us to pay additional reinsurance premium for any losses into each reinsurance layer. The reinstatement premium is prorated by the percentage of actual loss to the coverage.

We also purchase a *Catastrophe Aggregate* reinsurance cover that provides for $30 million of limit excess of $90 million of aggregated catastrophe losses. Qualifying losses include amounts of retained losses below the $10 million retention of the catastrophe program. This cover has been fully placed (100% of limit) for 2013 compared to 50.6% in 2012. The Catastrophe Aggregate does not include a reinstatement. The protection provided by the full placement of this program in 2013 has made it possible to reduce placements on the other catastrophe layers while staying within overall risk appetite thresholds.

We use multiple reinsurers with each reinsurer absorbing part of the overall risk ceded. The primary reinsurers in the 2013 programs and the coverage each provides are shown in the following table:

Reinsurer	A.M. Best Rating[1]	Percent of Risk Covered: Non Catastrophe	Percent of Risk Covered: Catastrophe
Lloyd s Syndicates	A+	39.1%	52.7%
Tokio Millennium Re Ltd.	AA-	0.0%	5.8%
Swiss Re	AA-	5.6%	5.0%
Catlin Insurance Company Limited, Bermuda	A	5.2%	3.9%
Sompo Japan Insurance Inc., Japan	A+	0.0%	3.8%
Other Reinsurers with no single company with greater than a 5% share		50.1%	28.8%

Total Reinsurance Coverage	**100.0**	**100.0%**

(1) A.M.Best rating as of the most current information available February 14, 2013.

Our credit-related property insurance products do not employ reinsurance to manage catastrophe loss exposure, and their reinsurers for risks other than catastrophes are not deemed significant to our business.

Prior Period Reserve Development

The loss development table included herein shows the development of our claims and CAE reserves. The table does not present individual accident or policy year development data.

Table of Contents

The top line shows our original reserves, net of reinsurance recoverable, for each of the indicated years. The table then shows the cumulative net paid claims and CAE as of successive years. The table below also shows the re-estimated amount of previously recorded reserves based on experience as of the end of each succeeding year. The cumulative deficiency or redundancy represents the aggregate change in the estimates over all prior years. Conditions and trends that affected development of liabilities in the past may not occur in the future. Accordingly, it is inappropriate to anticipate future redundancies or deficiencies based on historical experience.

Loss Development Table

Property and Casualty Claims and Claim Adjustment Expense Liability Development-Net of Reinsurance

Years Ended December 31,

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Liability for unpaid claims and claim adjustment expenses, net of reinsurance (includes loss reserves, IBNR, allocated and unalloc expense)	$ 490,215	$ 590,365	$ 678,379	$ 796,267	$ 801,953	$ 809,500	$ 847,860	$ 856,658	$ 887,008	$ 857,840	$ 832,653
Cumulative paid claims and claim expenses											
One year later	233,074	256,386	274,810	366,007	296,620	318,944	345,346	308,113	331,196	329,102	
Two years later	338,459	377,139	405,748	506,463	453,042	477,958	495,277	467,402	501,444		
Three years later	399,651	445,702	479,410	590,643	544,100	569,031	593,384	565,819			
Four years later	429,408	479,524	518,972	640,003	593,126	625,925	651,781				
Five years later	443,161	498,349	541,627	664,588	623,884	655,613					
Six years later	452,256	509,521	552,136	682,171	638,513						
Seven years later	457,972	513,968	563,113	688,866							
Eight years later	460,785	518,251	567,260								
Nine years later	463,303	519,781									
Ten years later	464,068										
Liabilites re-estimated											
One year later	488,595	564,287	638,910	770,238	711,880	766,882	798,587	776,808	818,937	810,263	
Two years later	488,455	564,485	617,374	737,341	713,339	733,361	770,900	753,152	809,757		
Three years later	490,717	553,163	596,242	739,825	680,900	727,675	766,994	751,538			
Four years later	482,799	538,459	596,754	714,995	682,460	727,733	770,441				
Five years later	476,615	542,429	585,370	717,474	685,471	735,407					
Six years later	478,201	534,287	585,914	720,931	694,268						
Seven years later	472,502	534,477	589,384	726,479							
Eight years later	473,754	535,429	593,294								
Nine years later	474,451	537,875									
Ten years later	476,612										
Deficiency(redundancy), net of reinsurance	(13,603)	(52,490)	(85,085)	(69,788)	(107,685)	(74,093)	(77,419)	(105,120)	(77,251)	(47,577)	

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Net reserve, as initially estimated	$ 490,215	$ 590,365	$ 678,379	$ 796,267	$ 801,953	$ 809,500	$ 847,860	$ 856,658	$ 887,008	$ 857,840	$ 832,653
Reinsurance and other recoverables as initially estimated	59,806	52,908	67,698	65,186	62,115	55,951	89,410	46,778	40,552	53,152	52,184
Gross reserve as initially estimated	**550,021**	**643,273**	**746,077**	**861,453**	**864,068**	**865,451**	**937,270**	**903,436**	**927,560**	**910,992**	**884,837**

Net re-estimated reserve	**476,612**	**537,875**	**593,294**	**726,479**	**694,268**	**735,407**	**770,441**	**751,538**	**809,757**	**810,263**
Re-estimated and other reinsurance recoverables	83,607	86,657	87,813	500,423	100,340	82,239	117,503	50,696	43,873	48,982
Gross re-estimated reserve	**560,219**	**624,532**	**681,107**	**1,226,902**	**794,608**	**817,646**	**887,944**	**802,234**	**853,630**	**859,245**
Deficiency(redundancy), gross of reinsurance	**$ 10,198**	**$ (18,741)**	**$ (64,970)**	**$ 365,449**	**$ (69,460)**	**$ (47,805)**	**$ (49,326)**	**$ (101,202)**	**$ (73,930)**	**$ (51,747)**

While we believe that our claims reserves at December 31, 2012 are adequate, new information, events or circumstances, unknown at the original valuation date, may lead to future developments in our ultimate losses in amounts significantly greater or less than the reserves currently provided. The actual final cost of settling both claims outstanding at December 31, 2012 and claims expected to arise from unexpired periods of risk is uncertain. There are many other factors that would cause our losses to increase or decrease, which include but are not limited to: changes in claim severity; changes in the expected level of reported claims; judicial action changing the scope or liability of coverage; changes in the regulatory, social and economic environment; and unexpected changes in loss inflation. The deficiency or redundancy for different reporting dates is cumulative and should not be added together.

We participate in the National Flood Insurance Program as administered by the Federal Emergency Management Agency. For the year ended December 31, 2005, the $365.4 million deficiency gross of reinsurance was primarily the result of our participation in this program. As these losses are 100% reimbursed by the Federal government they do not impact our net reserve calculations or our net loss development patterns. The National Flood Insurance Program had paid losses of $390.0 million for the year ended December 31, 2005 because of the 2005 hurricanes, specifically Hurricane Katrina. Since reserves are not set up for the National Flood Insurance Program, any payments made subsequent to year-end will appear as adverse development on a gross basis. If the flood losses were removed from the gross data, the $365.4 million deficiency would have been a $24.6 million redundancy, gross of reinsurance.

Table of Contents

For 2012, the net favorable prior year claims and CAE development was $47.6 million, compared to approximately $68.1 million of net favorable prior year development in 2011, as a result of better than expected paid and incurred loss emergence across several lines of business.

The current year loss ratio is a blend of the current accident year loss ratio and the impact of favorable or adverse development on prior accident years during the current calendar year. Excluding the 4.4 point impact of favorable prior year loss development for accident years 2011 and prior, the 2012 loss ratio would have been 77.7%. Excluding the 6.8 point impact of favorable prior year loss development for accident years 2010 and prior, the 2011 loss ratio would have been 83.1%.

Net favorable reserve development during 2012 and 2011 was primarily driven by personal and commercial auto and commercial liability lines. Net and gross reserve calculations have shown favorable development as a result of loss emergence compared to what was implied by the loss development patterns used in the original estimation of losses. For additional information regarding claims and CAE, refer to Note 12, Liability for Unpaid Claims and Claim Adjustment Expenses, of the Notes to the Consolidated Financial Statements.

Corporate and Other

Corporate and Other segment financial results for the periods indicated were as follows (in thousands):

	Years ended December 31,			Change over prior year	
	2012	**2011**	**2010**	**2012**	**2011**
Premiums and other revenues					
Net investment income	$ 64,944	$ 66,699	$ 53,317	$ (1,755)	$ 13,382
Realized investments gains, net	68,208	90,866	74,062	(22,658)	16,804
Other Income	5,905	2,980	3,175	2,925	(195)
Total premiums and other revenues	**139,057**	**160,545**	**130,554**	**(21,488)**	**29,991**
Benefits, losses and expenses					
Other operating expenses	61,535	45,021	38,695	16,514	6,326
Total benefits, losses and expenses	**61,535**	**45,021**	**38,695**	**16,514**	**6,326**
Income before other items and federal income taxes	**$ 77,522**	**$ 115,524**	**$ 91,859**	**$ (38,002)**	**$ 23,665**

Earnings during 2012 decreased substantially due to the lower realized gains, primarily as a result of other-than-temporary impairments related to bond and equity investments of $22.5 million during 2012. Other operating costs increased during 2012 as a result of an increase in expenses for share-based compensation under the stock and incentive plan as well as an increase in allocated costs to this segment during 2012.

Earnings during 2011 increased compared to 2010 primarily due to the increase in realized gains from investments as a result of improved financial markets. The 2011 increase was also driven by the increase in net investment income as a result of our growing portfolio of bonds and mortgage loans.

The Corporate and Other business segment recorded other-than-temporary impairments of $22.5 million, $9.5 million and $5.7 million in 2012, 2011 and 2010, respectively, which are included in Realized investments gains, net.

Table of Contents

Discontinued Operations

On December 31, 2010, we sold our wholly-owned broker-dealer subsidiary, Securities Management & Research, Inc. (SM&R) and recorded a $1.0 million loss. The results of operations for this subsidiary are presented as income (loss) from discontinued operations in our consolidated statements of operations for all periods presented. SM&R had previously been a component of the Corporate and Other business segment. See Note 21, Discontinued Operations, of the Notes to the Consolidated Financial Statements for additional details.

Investments

We manage our investment portfolio to optimize the rate of return commensurate with sound and prudent asset selection and to maintain a well-diversified portfolio. Our investment operations are regulated by various regulatory authorities, primarily the state insurance departments where we or our insurance subsidiaries are domiciled. Investment activities, including the setting of investment policies and defining acceptable risk levels, are subject to review and approval by our Board of Directors, which is assisted by our Finance Committee and Management Risk Committee.

Our insurance and annuity products are primarily supported by investment-grade bonds, and to a lesser extent collateralized mortgage obligations and commercial mortgage loans. We purchase fixed maturity securities and designate them as either held-to-maturity or available-for-sale considering our estimated future cash flow needs. We also monitor the composition of our fixed maturity securities classified as held-to-maturity and available-for-sale and adjust the mix within the portfolio as investments mature or new investments are purchased.

We invest in commercial mortgage loans when the yield and credit risk compare favorably with fixed maturity securities. Individual residential mortgage loans have not been part of our investment portfolio, and we do not anticipate investing in them in the future. Therefore, we have no direct exposure to sub-prime or Alt A mortgage loans in the mortgage loan portfolio. We invest in real estate and equity securities based on a risk and reward analysis where we believe there are opportunities for enhanced returns.

Composition of Invested Assets

The following summarizes the carrying values of our invested assets (other than investments in unconsolidated affiliates) by asset class (in thousands, except percentages):

	December 31, 2012		**December 31, 2011**	
	Amount	Percent	Amount	Percent
Bonds held-to-maturity, at amortized cost	$ 9,009,282	46.8	$ 9,251,972	49.0
Bonds available-for-sale, at fair value	4,665,576	24.3	4,381,607	23.2
Equity securities, at fair value	1,075,439	5.6	1,006,080	5.3
Mortgage loans on real estate, net of allowance	3,143,011	16.2	2,925,482	15.5
Policy loans	395,333	2.1	393,195	2.1
Investment real estate, net of accumulated depreciation	511,233	2.7	470,222	2.5
Short-term investments	313,086	1.6	345,330	1.8
Other invested assets	125,104	0.7	109,514	0.6
Total investments	**$ 19,238,064**	**100.0**	**$ 18,883,402**	**100.0**

The increase in our total investments at December 31, 2012 as compared to 2011 was primarily a res