NATIONAL WESTERN LIFE INSURANCE CO
Form 10-Q
November 10, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

# FORM 10-Q

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

For the Quarterly Period Ended September 30, 2008

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

For the transition period from __________ to __________

Commission File Number: 2-17039

NATIONAL WESTERN LIFE INSURANCE COMPANY
(Exact name of Registrant as specified in its charter)

| | |
|---|---|
| COLORADO<br>(State of Incorporation) | 84-0467208<br>(I.R.S. Employer Identification Number) |
| 850 EAST ANDERSON LANE<br>AUSTIN, TEXAS 78752-1602<br>(Address of Principal Executive Offices) | (512) 836-1010<br>(Telephone Number) |

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

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

As of November 6, 2008, the number of shares of Registrant's common stock outstanding was: Class A – 3,425,966 and Class B - 200,000.

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)

| ASSETS | | (Unaudited) September 30, 2008 | December 31, 2007 |
|---|---|---|---|
| Investments: | | | |
| Securities held to maturity, at amortized cost | $ | 3,850,139 | 3,778,603 |
| Securities available for sale, at fair value | | 1,793,722 | 1,900,714 |
| Mortgage loans, net of allowance for possible losses | | | |
| ($3,571 and $3,567) | | 87,789 | 99,033 |
| Policy loans | | 80,937 | 83,772 |
| Derivatives, index options | | 6,095 | 25,907 |
| Other long-term investments | | 23,523 | 16,562 |
| Total investments | | 5,842,205 | 5,904,591 |
| Cash and short-term investments | | 34,851 | 45,206 |
| Deferred policy acquisition costs | | 688,973 | 664,805 |
| Deferred sales inducements | | 117,177 | 104,029 |
| Accrued investment income | | 67,503 | 65,034 |
| Federal income tax receivable | | 5,184 | 10,010 |
| Other assets | | 44,975 | 41,651 |
| | $ | 6,800,868 | 6,835,326 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

| LIABILITIES AND STOCKHOLDERS' EQUITY | | (Unaudited) September 30, 2008 | December 31, 2007 |
|---|---|---|---|
| LIABILITIES: | | | |
| Future policy benefits: | | | |
| Traditional life and annuity contracts | $ | 137,978 | 138,672 |
| Universal life and annuity contracts | | 5,419,282 | 5,441,871 |
| Other policyholder liabilities | | 129,078 | 120,400 |
| Federal income tax liability: | | | |
| Current | | - | - |
| Deferred | | 36,428 | 61,720 |
| Other liabilities | | 81,833 | 60,978 |
| Total liabilities | | 5,804,599 | 5,823,641 |
| COMMITMENTS AND CONTINGENCIES (Notes 5 and 9) | | | |
| STOCKHOLDERS' EQUITY: | | | |
| Common stock: | | | |
| Class A - $1 par value; 7,500,000 shares authorized; 3,425,966 and 3,422,324 issued and outstanding in 2008 and 2007 | | 3,426 | 3,422 |
| Class B - $1 par value; 200,000 shares authorized, issued, and outstanding in 2008 and 2007 | | 200 | 200 |
| Additional paid-in capital | | 36,680 | 36,236 |
| Accumulated other comprehensive loss | | (44,448) | (7,065) |
| Retained earnings | | 1,000,411 | 978,892 |
| Total stockholders' equity | | 996,269 | 1,011,685 |
| | $ | 6,800,868 | 6,835,326 |

Note: The condensed consolidated balance sheet at December 31, 2007, has been derived from the audited consolidated financial statements as of that date.

See accompanying notes to condensed consolidated financial statements.

4

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
For the Three Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands, except per share amounts)

| | | 2008 | 2007 |
|---|---|---|---|
| Premiums and other revenue: | | | |
| Life and annuity premiums | $ | 4,057 | 4,755 |
| Universal life and annuity contract revenues | | 32,885 | 30,025 |
| Net investment income | | 69,582 | 75,075 |
| Other income | | 3,056 | 3,786 |
| Net investment losses | | (21,620) | (1,505) |
| Total premiums and other revenue | | 87,960 | 112,136 |
| Benefits and expenses: | | | |
| Life and other policy benefits | | 10,794 | 11,337 |
| Amortization of deferred policy acquisition costs | | 37,188 | 25,238 |
| Universal life and annuity contract interest | | 38,339 | 38,219 |
| Other operating expenses | | 17,905 | 12,871 |
| Total benefits and expenses | | 104,226 | 87,665 |
| Earnings (loss) before Federal income taxes | | (16,266) | 24,471 |
| Provision (benefit) for Federal income taxes: | | | |
| Current | | 3,488 | (2,836) |
| Deferred | | (9,954) | 11,685 |
| Total Federal income taxes | | (6,466) | 8,849 |
| Net earnings (loss) | $ | (9,800) | 15,622 |
| Basic Earnings (Loss) Per Share: | | | |
| Class A | $ | (2.78) | 4.44 |
| Class B | $ | (1.39) | 2.22 |
| Diluted Earnings (Loss) Per Share: | | | |
| Class A | $ | (2.78) | 4.38 |
| Class B | $ | (1.39) | 2.22 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
For the Nine Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands, except per share amounts)

| | | 2008 | 2007 |
|---|---|---|---|
| Premiums and other revenue: | | | |
| Life and annuity premiums | $ | 12,575 | 14,074 |
| Universal life and annuity contract revenues | | 98,696 | 87,474 |
| Net investment income | | 201,290 | 260,033 |
| Other income | | 9,348 | 10,461 |
| Net investment gains (losses) | | (21,931) | 2,901 |
| Total premiums and other revenue | | 299,978 | 374,943 |
| Benefits and expenses: | | | |
| Life and other policy benefits | | 28,905 | 32,748 |
| Amortization of deferred policy acquisition costs | | 93,699 | 74,660 |
| Universal life and annuity contract interest | | 98,511 | 143,037 |
| Other operating expenses | | 45,962 | 43,354 |
| Total benefits and expenses | | 267,077 | 293,799 |
| Earnings before Federal income taxes | | 32,901 | 81,144 |
| Provision (benefit) for Federal income taxes: | | | |
| Current | | 15,307 | 6,551 |
| Deferred | | (5,194) | 18,448 |
| Total Federal income taxes | | 10,113 | 24,999 |
| Net earnings | $ | 22,788 | 56,145 |
| Basic Earnings Per Share: | | | |
| Class A | $ | 6.47 | 15.94 |
| Class B | $ | 3.23 | 7.97 |
| Diluted Earnings Per Share: | | | |
| Class A | $ | 6.42 | 15.74 |
| Class B | $ | 3.23 | 7.97 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the Three Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands)

| | | 2008 | 2007 |
|---|---|---|---|
| Net earnings (loss) | $ | (9,800) | 15,622 |
| Other comprehensive income (loss), net of effects of deferred costs and taxes: | | | |
| Unrealized losses on securities: | | | |
| Net unrealized holding gains (losses) arising during period | | (34,258) | 4,860 |
| Reclassification adjustment for net losses included in net earnings | | 11,707 | 16 |
| Amortization of net unrealized gains related to transferred securities | | 11 | 25 |
| Net unrealized gains (losses) on securities | | (22,540) | 4,901 |
| Foreign currency translation adjustments | | (8) | 47 |
| Benefit plans: | | | |
| Amortization of net prior service cost and net loss | | 342 | 308 |
| Other comprehensive income (loss) | | (22,206) | 5,256 |
| Comprehensive income (loss) | $ | (32,006) | 20,878 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the Nine Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands)

| | | 2008 | 2007 |
|---|---|---|---|
| Net earnings | $ | 22,788 | 56,145 |
| Other comprehensive income (loss), net of effects of deferred costs and taxes: | | | |
| Unrealized losses on securities: | | | |
| Net unrealized holding losses arising during period | | (49,353) | (3,745) |
| Reclassification adjustment for net losses (gains) included in net earnings | | 11,097 | (2,848) |
| Amortization of net unrealized gains (losses) related to transferred securities | | (3) | 79 |
| Net unrealized losses on securities | | (38,259) | (6,514) |
| Foreign currency translation adjustments | | (150) | (139) |
| Benefit plans: | | | |
| Amortization of net prior service cost and net loss | | 1,026 | 926 |
| Other comprehensive loss | | (37,383) | (5,727) |
| Comprehensive income (loss) | $ | (14,595) | 50,418 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
For the Nine Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands)

| | | 2008 | 2007 |
|---|---|---|---|
| Common stock: | | | |
| Balance at beginning of year | $ | 3,622 | 3,621 |
| Shares exercised under stock option plan | | 4 | 1 |
| Balance at end of period | | 3,626 | 3,622 |
| Additional paid-in capital: | | | |
| Balance at beginning of year | | 36,236 | 36,110 |
| Shares exercised under the stock option plan | | 444 | 126 |
| Balance at end of period | | 36,680 | 36,236 |
| Accumulated other comprehensive loss: | | | |
| Unrealized gains (losses) on securities: | | | |
| Balance at beginning of year | | 1,184 | 3,148 |
| Change in unrealized losses during period | | (38,259) | (6,514) |
| Balance at end of period | | (37,075) | (3,366) |
| Foreign currency translation adjustments: | | | |
| Balance at beginning of year | | 3,078 | 3,122 |
| Change in translation adjustments during period | | (150) | (139) |
| Balance at end of period | | 2,928 | 2,983 |
| Benefit plan liability adjustment: | | | |
| Balance at beginning of year | | (11,327) | (10,001) |
| Amortization of net prior service cost and net gain | | 1,026 | 926 |
| Balance at end of period | | (10,301) | (9,075) |
| Accumulated other comprehensive loss at end of period | | (44,448) | (9,458) |
| Retained earnings: | | | |
| Balance at beginning of year | | 978,892 | 896,984 |
| Cumulative effect of change in accounting principle, net of tax | | - | (2,195) |
| Net earnings | | 22,788 | 56,145 |
| Stockholder dividends | | (1,269) | (1,268) |

| | | | |
|---|---|---|---|
| Balance at end of period | | 1,000,411 | 949,666 |
| Total stockholders' equity | $ | 996,269 | 980,066 |

See accompanying notes to condensed consolidated financial statements.

9

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Nine Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands)

| | | 2008 | 2007 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Net earnings | $ | 22,788 | 56,145 |
| Adjustments to reconcile net earnings to net cash from operating activities: | | | |
| Universal life and annuity contract interest | | 98,511 | 143,037 |
| Surrender charges and other policy revenues | | (30,324) | (26,776) |
| Net investment losses (gains) | | 21,931 | (2,901) |
| Accrual and amortization of investment income | | (3,715) | (3,829) |
| Depreciation and amortization | | 786 | 746 |
| Decrease in value of derivatives | | 52,824 | 26,393 |
| Decrease (increase) in deferred policy acquisition and sales inducement costs | | 14,508 | (9,730) |
| (Increase) decrease in accrued investment income | | (2,496) | 924 |
| Decrease in other assets | | 991 | 582 |
| (Decrease) increase in liabilities for future policy benefits | | (694) | 338 |
| Increase in other policyholder liabilities | | 8,678 | 4,893 |
| (Decrease) increase in Federal income tax liability | | (368) | 6,861 |
| Increase (decrease) in other liabilities | | 11,116 | (5,924) |
| Other | | 844 | 167 |
| Net cash provided by operating activities | | 195,380 | 190,926 |
| Cash flows from investing activities: | | | |
| Proceeds from sales of: | | | |
| Securities held to maturity | | - | 5,175 |
| Securities available for sale | | 1,522 | 28,418 |
| Other investments | | 5,382 | 33,255 |
| Proceeds from maturities and redemptions of: | | | |
| Securities held to maturity | | 417,933 | 106,023 |
| Securities available for sale | | 190,284 | 268,999 |
| Other investments | | - | - |
| Purchases of: | | | |
| Securities held to maturity | | (493,363) | (256,014) |
| Securities available for sale | | (190,039) | (284,742) |
| Other investments | | (47,195) | (35,619) |
| Principal payments on mortgage loans | | 12,308 | 21,623 |
| Cost of mortgage loans acquired | | (6,046) | (18,480) |

| | | |
|---|---|---|
| Decrease in policy loans | 2,835 | 2,309 |
| Other | (4,316) | (6,624) |
| Net cash used in investing activities | (110,695) | (135,677) |

(Continued on next page)

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS, CONTINUED
For the Nine Months Ended September 30, 2008 and 2007
(Unaudited)
(In thousands)

| | | 2008 | | | 2007 |
|---|---|---|---|---|---|
| Cash flows from financing activities: | | | | | |
| Deposits to account balances for universal life and annuity contracts | $ | 346,119 | | | 380,708 |
| Return of account balances on universal life and annuity contracts | | (441,195) | | | (444,877) |
| Issuance of common stock under stock option plan | | 448 | | | 127 |
| Net cash used in financing activities | | (94,628) | | | (64,042) |
| Effect of foreign exchange | | (412) | | | (72) |
| Net decrease in cash and short-term investments | | (10,355) | | | (8,865) |
| Cash and short-term investments at beginning of period | | 45,206 | | | 49,901 |
| Cash and short-term investments at end of period | $ | 34,851 | | | 41,036 |

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

| | | | |
|---|---|---|---|
| Cash paid during the period for: | | | |
| Interest | $ | 30 | 30 |
| Income taxes | | 10,481 | 19,155 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

NATIONAL WESTERN LIFE INSURANCE COMPANY AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

## (1) CONSOLIDATION AND BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for annual financial statements. In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments necessary to present fairly the financial position of National Western Life Insurance Company and its subsidiaries (the Company) as of September 30, 2008, and the results of their operations and their cash flows for the three months and nine months ended September 30, 2008 and 2007. The results of operations for the three months and nine months ended September 30, 2008 and 2007 are not necessarily indicative of the results to be expected for the full year. For further information, refer to the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007 accessible free of charge through the Company's internet site at www.nationalwesternlife.com or the Securities and Exchange Commission (“SEC”) internet site at www.sec.gov.

The accompanying condensed consolidated financial statements include the accounts of National Western Life Insurance Company and its wholly-owned subsidiaries ("Company"), The Westcap Corporation, NWL Investments, Inc., NWL Services, Inc., NWL Financial, Inc., NWL Mortgage I Corp, NWL Mortgage, Ltd. and Regent Care San Marcos Holdings, LLC. All significant intercorporate transactions and accounts have been eliminated in consolidation.

## (2) CHANGES IN ACCOUNTING PRINCIPLES

In September 2005, the AICPA issued Statement of Position 05-1, Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts ("SOP 05-1") which was effective for internal replacements occurring in fiscal years beginning after December 15, 2006. SOP 05-1 provides guidance on accounting by insurance enterprises for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in FASB No. 97. SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverages that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. The Company had an impact related to the adoption of SOP 05-1 for contracts which annuitized and for reinstatements of contracts. The unamortized deferred acquisition costs and deferred sales inducement assets have to be written-off at the time of annuitization and can not be continued related to reinstatements. SOP 05-1 resulted in changes in assumptions relative to estimated gross profits which affected unamortized deferred acquisition costs, unearned revenue liabilities, and deferred sales inducement balances as of the beginning of 2007. The effect of this SOP on beginning retained earnings as of January 1, 2007 was a decrease of $2.2 million, net of tax, as detailed below.

| | | Amounts (In thousands) |
|---|---|---|
| Write-off of deferred acquisition cost | $ | 3,321 |
| Adjustment to deferred annuity revenue | | 56 |
| | | 3,377 |

| | | |
|---|---|---|
| Federal income tax | | (1,182) |
| Cumulative effect of change in accounting for internal replacements and investment contracts | $ | 2,195 |

12

Table of Contents

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The Company adopted SFAS 157 effective January 1, 2008, and the adoption did not have an impact on the Company's consolidated financial statements. See Note 11 for additional disclosures concerning fair value measurement.

In February 2008, the FASB issued FSP FAS 157-2, Effective Date of FASB Statement No. 157. This FSP delays the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis, to fiscal years and interim periods beginning after November 15, 2008.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. The Company adopted SFAS 159 effective January 1, 2008, and the adoption did not have an impact on the consolidated financial statements as no items were elected for measurement at fair value upon initial adoption.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements. SFAS 160 establishes accounting and reporting standards for entities that have equity investments that are not attributable directly to the parent, called noncontrolling interests or minority interests. Specifically, SFAS 160 states where and how to report noncontrolling interests in the consolidated statements of financial position and operations, how to account for changes in noncontrolling interests and provides disclosure requirements. The provisions of SFAS 160 are effective beginning January 1, 2009. The Company is currently evaluating the impact that the adoption of this statement will have on the consolidated financial position, results of operations and disclosures.

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations. SFAS 141(R) establishes how an entity accounts for the identifiable assets acquired, liabilities assumed, and any noncontrolling interests acquired, how to account for goodwill acquired and what disclosures are required as part of a business combination. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The adoption of SFAS 141(R) is not expected to have a material impact on the Company's consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133. This statement requires enhanced disclosures regarding an entity's derivative and hedging activity to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The adoption of SFAS No. 161 is not expected to have a material impact on the Company's consolidated financial statements.

In April 2008, the FASB issued FSP No. FAS 142-3, Determination of the Useful Life of Intangible Assets. FSP FAS 142-3 amends the factors to be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS 142. The provisions of FSP FAS 142-3 are to be applied prospectively to intangible assets acquired after January 1, 2009 although the disclosure provisions are required for all intangible assets as of or subsequent to January 1, 2009. The adoption of FSP FAS 142-3 is not expected to impact the Company's consolidated financial condition and results of operations.

In May 2008, the FASB issued SFAS No. 163, Accounting for Financial Guarantee Insurance Contracts—an interpretation of FASB Statement No. 60 ("SFAS 163"). The scope of SFAS 163 is limited to financial guarantee insurance (and reinsurance) contracts issued by enterprises that are included within the scope of SFAS No. 60, "Accounting and Reporting by Insurance Enterprises" ("SFAS 60") and that are not accounted for as derivative instruments. SFAS 163 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and all interim periods within those fiscal years. The Company does not have financial guarantee insurance products, and, accordingly does not expect the adoption of SFAS 163 to have an effect on the Company's consolidated financial condition and results of operations.

Table of Contents

In September 2008, the FASB issued FSP No. FAS 133-1 and FIN 45-4, Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45; and Clarification of the Effective Date of FASB Statement No. 161. This FSP amends SFAS 133 to require disclosures by entities that assume credit risk through the sale of credit derivatives including credit derivatives embedded in a hybrid instrument to enable users of financial statements to assess the potential effect on its financial position, financial performance, and cash flows from these credit derivatives. This FSP also amends FASB Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, to require additional disclosure about the current status of the payment/performance risk of a guarantee. FSP FAS 133-1 and FIN 45-4 are effective for financial statements issued for fiscal years and interim periods ending after November 15, 2008. The Company does not expect the adoption of FSP FAS 133-1 and FIN 45-4 to have an effect on the Company's consolidated financial condition and results of operations.

In October 2008, the FASB issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. This FSP clarifies the application of SFAS 157 in a market that is not active and illustrates key considerations including the use of an entity's own assumptions about future cash flows and appropriately risk-adjusted discount rates, appropriate risk adjustments for nonperformance and liquidity risks, and the reliance that an entity should place on quotes that do not reflect the result of market transactions. This FSP was preceded by a press release that was jointly issued by the Office of the Chief Accountant of the SEC and the FASB staff on September 30, 2008 which provided immediate clarification on fair value accounting based on the measurement guidance of SFAS 157. The FSP was effective upon issuance and did not have a material impact on the Company's consolidated financial statements. See Note 11 for disclosures regarding the Company's fair value measurements.

(3) STOCKHOLDERS' EQUITY

The Company is restricted by state insurance laws as to dividend amounts which may be paid to stockholders without prior approval from the Colorado Division of Insurance. The Company paid no cash dividends on common stock during the nine months ended September 30, 2008 and 2007. However, the Company declared a cash dividend on August 22, 2008 payable November 28, 2008 to stockholders on record as of October 31, 2008. The dividends declared were $0.36 per common share to Class A stockholders and $0.18 per common share to Class B stockholders. The dividend payment was approved by the Colorado Division of Insurance. A dividend in the same amounts per share on Class A and Class B shares was declared in August and paid in November of 2007.

Table of Contents

(4) EARNINGS PER SHARE

Basic earnings per share of common stock are computed by dividing net income (loss) by the weighted-average basic common shares outstanding during the period. Diluted earnings per share assumes the issuance of common shares applicable to stock options in the denominator.

| | Three Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2008 | | 2007 | |
| | Class A | Class B | Class A | Class B |
| | (In thousands except per share amounts) | | | |
| Numerator for Basic and Diluted Earnings Per Share: | | | | |
| Net income (loss) | $ (9,800) | | 15,622 | |
| Dividends – Class A shares | (1,233) | | (1,232) | |
| Dividends – Class B shares | (36) | | (36) | |
| Undistributed income (loss) | $ (11,069) | | 14,354 | |
| Allocation of net income (loss): | | | | |
| Dividends | $ 1,233 | 36 | 1,232 | 36 |
| Allocation of undistributed income (loss) | (10,755) | (314) | 13,946 | 408 |
| Net income (loss) | $ (9,522) | (278) | 15,178 | 444 |
| Denominator: | | | | |
| Basic earnings per share - weighted-average shares | 3,426 | 200 | 3,422 | 200 |
| Effect of dilutive stock options | - | - | 42 | - |
| Diluted earnings per share - adjusted weighted-average shares for assumed Conversions | 3,426 | 200 | 3,464 | 200 |
| Basic Earnings (Loss) Per Share | $ (2.78) | (1.39) | 4.44 | 2.22 |
| Diluted Earnings (Loss) Per Share | $ (2.78) | (1.39) | 4.38 | 2.22 |

Table of Contents

| | Nine Months Ended September 30, 2008 Class A | 2008 Class B | 2007 Class A | 2007 Class B |
|---|---|---|---|---|
| | (In thousands except per share amounts) | | | |
| Numerator for Basic and Diluted Earnings Per Share: | | | | |
| Net income | $ 22,788 | | 56,145 | |
| Dividends – Class A shares | (1,233) | | (1,232) | |
| Dividends – Class B shares | (36) | | (36) | |
| Undistributed income | $ 21,519 | | 54,877 | |
| Allocation of net income: | | | | |
| Dividends | $ 1,233 | 36 | 1,232 | 36 |
| Allocation of undistributed income | 20,909 | 610 | 53,319 | 1,558 |
| Net income | $ 22,142 | 646 | 54,551 | 1,594 |
| Denominator: | | | | |
| Basic earnings per share - weighted-average shares | 3,425 | 200 | 3,422 | 200 |
| Effect of dilutive stock options | 26 | - | 45 | - |
| Diluted earnings per share - adjusted weighted-average shares for assumed conversions | 3,451 | 200 | 3,467 | 200 |
| Basic Earnings Per Share | $ 6.47 | 3.23 | 15.94 | 7.97 |
| Diluted Earnings Per Share | $ 6.42 | 3.23 | 15.74 | 7.97 |

(5) PENSION AND OTHER POSTRETIREMENT PLANS

(A) Defined Benefit Pension Plans

The Company sponsors a qualified defined benefit pension plan covering substantially all employees. The plan provides benefits based on the participants' years of service and compensation. The Company makes annual contributions to the plan that comply with the minimum funding provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"). On October 19, 2007, the Company’s Board of Directors approved an amendment to freeze the Pension Plan as of December 31, 2007. The freeze ceased future benefit accruals to all participants and closed the Plan to any new participants. In addition, all participants became immediately 100% vested in their accrued benefits as of that date. Using estimated assumptions, the cumulative estimated minimum required contribution for the next five years is $2.1 million at which time the Plan is expected to be fully funded. Future pension expense is projected to be minimal.

16

Table of Contents

The following summarizes the components of net periodic benefit cost.

| | Three Months Ended September 30, 2008 | 2007 | Nine Months Ended September 30, 2008 | 2007 |
|---|---|---|---|---|
| | (In thousands) | | | |
| Service cost | $ - | 180 | - | 540 |
| Interest cost | 259 | 272 | 777 | 815 |
| Expected return on plan assets | (285) | (275) | (855) | (825) |
| Amortization of prior service cost | 1 | 1 | 3 | 3 |
| Amortization of net loss | 60 | 80 | 182 | 240 |
| Net periodic benefit cost | $ 35 | 258 | 107 | 773 |

The Company has contributed $1.1 million to the plan in 2008. No further contributions are expected in 2008.

The Company also sponsors a non-qualified defined benefit plan primarily for senior officers. The plan provides benefits based on the participants' years of service and compensation. The pension obligations and administrative responsibilities of the plan are maintained by a pension administration firm, which is a subsidiary of American National Insurance Company ("ANICO"). ANICO has guaranteed the payment of pension obligations under the plan. However, the Company has a contingent liability with respect to the pension plan should these entities be unable to meet their obligations under the existing agreements. Also, the Company has a contingent liability with respect to the plan in the event that a plan participant continues employment with the Company beyond age seventy, the aggregate average annual participant salary increases exceed 10% per year, or any additional employees become eligible to participate in the plan. If any of these conditions are met, the Company would be responsible for any additional pension obligations resulting from these items. Amendments were made to the plan to allow an additional employee to participate and to change the benefit formula for the Chairman of the Company. As previously mentioned, these additional obligations are a liability to the Company. Effective December 31, 2004, this plan was frozen with respect to the continued accrual of benefits of the Chairman and the President of the Company in order to comply with law changes under the American Jobs Creation Act of 2004 ("Act").

Effective July 1, 2005, the Company established a second non-qualified defined benefit plan for the benefit of the Chairman of the Company. This plan is intended to provide for post-2004 benefit accruals that mirror and supplement the pre-2005 benefit accruals under the previously discussed non-qualified plan, while complying with the requirements of the Act.

Effective November 1, 2005, the Company established a third non-qualified defined benefit plan for the benefit of the President of the Company. This plan is intended to provide for post-2004 benefit accruals that supplement the pre-2005 benefit accruals under the first non-qualified plan as previously discussed, while complying with the requirements of the Act.

The following summarizes the components of net periodic benefit costs for these non-qualified plans.

| Three Months Ended September 30, 2008 | 2007 | Nine Months Ended September 30, 2008 |
|---|---|---|