

INDEPENDENCE HOLDING CO
Form 10-Q
August 08, 2014

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

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the quarterly period ended **June 30, 2014**.

Transition Report under Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the transition period from: _____ to _____

Commission File Number: **0-10306**

INDEPENDENCE HOLDING COMPANY

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

58-1407235

(I.R.S. Employer Identification No.)

96 CUMMINGS POINT ROAD, STAMFORD, CONNECTICUT

06902

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(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: **(203) 358-8000**

NOT APPLICABLE

Former name, former address and former fiscal year, if changed since last report.

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

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

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

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 No

Class
Common stock, \$ 1.00 par value

Outstanding at August 1, 2014
17,417,586 Shares

INDEPENDENCE HOLDING COMPANY

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Copies of the Company's SEC filings can be found on its website at www.ihcgroup.com.

Forward-Looking Statements

This report on Form 10-Q contains certain “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which are intended to be covered by the safe harbors created by those laws. We have based our forward-looking statements on our current expectations and projections about future events. Our forward-looking statements include information about possible or assumed future results of our operations. All statements, other than statements of historical facts, included or incorporated by reference in this report that address activities, events or developments that we expect or anticipate may occur in the future, including such things as the growth of our business and operations, our business strategy, competitive strengths, goals, plans, future capital expenditures and references to future successes may be considered forward-looking statements. Also, when we use words such as anticipate, believe, estimate, expect, intend, probably or similar expressions, we are making forward-looking statements.

Numerous risks and uncertainties may impact the matters addressed by our forward-looking statements, any of which could negatively and materially affect our future financial results and performance. We describe some of these risks and uncertainties in greater detail in Item 1A, Risk Factors, of IHC’s annual report on Form 10-K as filed with Securities and Exchange Commission.

Although we believe that the assumptions underlying our forward-looking statements are reasonable, any of these assumptions, and, therefore, also the forward-looking statements based on these assumptions, could themselves prove to be inaccurate. In light of the significant uncertainties inherent in the forward-looking statements that are included in this report, our inclusion of this information is not a representation by us or any other person that our objectives and plans will be achieved. Our forward-looking statements speak only as of the date made, and we will not update these forward-looking statements unless the securities laws require us to do so. In light of these risks, uncertainties and assumptions, any forward-looking event discussed in this report may not occur.

PART I - FINANCIAL INFORMATION**Item 1.****Financial Statements**

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	June 30, 2014	December 31, 2013
	(Unaudited)	
ASSETS:		
Investments:		
Short-term investments	\$ 50	\$ 50
Securities purchased under agreements to resell	19,260	22,594
Trading securities	11,600	7,125
Fixed maturities, available-for-sale	571,727	542,287
Equity securities, available-for-sale	12,962	11,803
Other investments	25,599	25,123
Total investments	641,198	608,982
Cash and cash equivalents	26,631	24,229
Deferred acquisition costs	30,106	29,777
Due and unpaid premiums	59,282	59,435
Due from reinsurers	331,649	380,229
Premium and claim funds	39,235	37,353
Goodwill	50,318	50,318
Other assets	60,446	78,712
TOTAL ASSETS	\$ 1,238,865	\$ 1,269,035
LIABILITIES AND STOCKHOLDERS EQUITY:		
LIABILITIES:		
Policy benefits and claims	\$ 233,992	\$ 237,754
Future policy benefits	283,036	287,449
Funds on deposit	234,863	274,826
Unearned premiums	12,639	12,423
Other policyholders' funds	22,629	25,129
Due to reinsurers	37,833	37,113
Accounts payable, accruals and other liabilities	77,681	71,889
Debt	6,000	6,000
Junior subordinated debt securities	38,146	38,146
TOTAL LIABILITIES	946,819	990,729

STOCKHOLDERS' EQUITY:

IHC STOCKHOLDERS' EQUITY:

Preferred stock (none issued)	-	-
Common stock \$1.00 par value, 23,000,000 shares authorized;		
18,528,683 and 18,523,733 shares issued;		
17,451,262 and		
17,660,390 shares outstanding	18,529	18,524
Paid-in capital	126,899	126,239
Accumulated other comprehensive loss	(1,519)	(10,472)
Treasury stock, at cost; 1,077,421 and 863,343 shares	(11,039)	(8,169)
Retained earnings	149,555	142,669
TOTAL IHC STOCKHOLDERS' EQUITY	282,425	268,791
NONCONTROLLING INTERESTS IN SUBSIDIARIES	9,621	9,515
TOTAL EQUITY	292,046	278,306
TOTAL LIABILITIES AND EQUITY	\$ 1,238,865	\$ 1,269,035

See the accompanying Notes to Condensed Consolidated Financial Statements.

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
(In thousands, except per share data)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2014	2013	2014	2013
REVENUES:				
Premiums earned	\$ 121,135	\$ 125,465	\$ 244,405	\$ 242,833
Net investment income	5,434	7,002	11,235	15,003
Fee income	3,861	6,039	13,200	12,581
Other income	1,070	1,659	2,181	3,011
Net realized investment gains	4,519	11,735	6,070	16,354
	136,019	151,900	277,091	289,782
EXPENSES:				
Insurance benefits, claims and reserves	83,263	89,276	168,572	174,736
Selling, general and administrative expenses	44,947	44,862	93,082	87,742
Amortization of deferred acquisitions costs	1,189	10,948	2,471	12,388
Interest expense on debt	337	490	818	977
	129,736	145,576	264,943	275,843
Income before income taxes	6,283	6,324	12,148	13,939
Income taxes	2,403	2,166	4,263	4,741
Net income	3,880	4,158	7,885	9,198
Less: Income from noncontrolling interests in subsidiaries	(32)	(467)	(336)	(806)
	\$ 3,848	\$ 3,691	\$ 7,549	\$ 8,392
NET INCOME ATTRIBUTABLE TO IHC				
Basic income per common share	\$.22	\$.21	\$.43	\$.47
WEIGHTED AVERAGE SHARES OUTSTANDING	17,485	17,753	17,553	17,836
Diluted income per common share	\$.22	\$.21	\$.43	\$.47
WEIGHTED AVERAGE DILUTED SHARES OUTSTANDING	17,657	17,805	17,709	17,922

See the accompanying Notes to Condensed Consolidated Financial Statements.

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)
(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Net income	\$ 3,880	\$ 4,158	\$ 7,885	\$ 9,198
Other comprehensive income (loss):				
Available-for-sale securities:				
Unrealized gains (losses) on available-for-sale securities, pre-tax	5,003	(25,889)	13,020	(27,996)
Tax expense (benefit) on unrealized gains (losses) on available-for-sale securities	1,499	(8,325)	3,877	(8,905)
Unrealized gains (losses) on available-for-sale securities, net of taxes	3,504	(17,564)	9,143	(19,091)
Cash flow hedge:				
Unrealized gains on cash flow hedge, pre-tax	21	22	38	45
Tax expense on unrealized gains on cash flow hedge	8	9	15	18
Unrealized gains on cash flow hedge, net of taxes	13	13	23	27
Other comprehensive income (loss), net of tax	3,517	(17,551)	9,166	(19,064)
COMPREHENSIVE INCOME (LOSS), NET OF TAX	7,397	(13,393)	17,051	(9,866)
Comprehensive income, net of tax, attributable to noncontrolling interests:				
Income from noncontrolling interests in subsidiaries	(32)	(467)	(336)	(806)
Other comprehensive (income) loss, net of tax, attributable to noncontrolling interests:				
Unrealized (gain) loss on available-for-sale securities, net of tax	(82)	465	(213)	556
Other comprehensive (income) loss, net of tax, attributable to noncontrolling interests	(82)	465	(213)	556
COMPREHENSIVE INCOME, NET OF TAX, ATTRIBUTABLE TO NONCONTROLLING INTERESTS	(114)	(2)	(549)	(250)

**COMPREHENSIVE INCOME (LOSS), NET OF
TAX,**

ATTRIBUTABLE TO IHC	\$ 7,283	\$ (13,395)	\$ 16,502	\$ (10,116)
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See the accompanying Notes to Condensed Consolidated Financial Statements.

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Unaudited)
SIX MONTHS ENDED JUNE 30, 2014 (In thousands)

	COMMON STOCK	PAID-IN CAPITAL	ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)	TREASURY STOCK, AT COST	RETAINED EARNINGS	TOTAL IHC STOCKHOLDERS' EQUITY	NON- CONTROLLING INTERESTS SUBSIDIARIES
BALANCE AT DECEMBER 31, 2013	18,524\$	126,239\$	(10,472)\$	(8,169)\$	142,669 \$	268,791 \$	
Net income					7,549	7,549	
Other comprehensive income, net of tax			8,953			8,953	
Repurchases of common stock				(2,870)		(2,870)	
Common stock dividend (\$0.035 per share)					(613)	(613)	
Share-based compensation expenses and related tax benefits	5	580				585	
Distributions to noncontrolling interests							-
Other capital transactions		80			(50)	30	
BALANCE AT							

JUNE \$	18,529\$	126,899\$	(1,519)\$	(11,039)\$	149,555 \$	282,425 \$
30, 2014						

See the accompanying Notes to Condensed Consolidated Financial Statements.

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(In thousands)

	Six Months Ended June 30,	
	2014	2013
CASH FLOWS PROVIDED BY (USED BY) OPERATING ACTIVITIES:		
Net income	\$ 7,885	\$ 9,198
Adjustments to reconcile net income to net change in cash from operating activities:		
Amortization of deferred acquisition costs	2,471	12,388
Net realized investment gains	(6,070)	(16,354)
Equity income from equity method investments	(741)	(1,160)
Depreciation and amortization	2,013	2,342
Share-based compensation expenses	683	508
Deferred tax expense	1,885	6,025
Other	2,411	2,623
Changes in assets and liabilities:		
Net purchases of trading securities	(3,603)	(428)
Change in insurance liabilities	(48,149)	47,468
Additions to deferred acquisition costs	(2,974)	(3,082)
Change in amounts due from reinsurers	48,580	(216,968)
Change in premium and claim funds	(1,882)	4,072
Change in current income tax liability	4,702	(782)
Change in due and unpaid premiums	153	(23,716)
Change in other assets	6,310	1,188
Change in other liabilities	(6,303)	(3,284)
Net change in cash from operating activities	7,371	(179,962)
CASH FLOWS PROVIDED BY (USED BY) INVESTING ACTIVITIES:		
Net sales of securities under resale and repurchase agreements	3,334	23,368
Sales of equity securities	288	10,029
Purchases of equity securities	(998)	-
Sales of fixed maturities	222,627	460,981
Maturities and other repayments of fixed maturities	28,007	32,970
Purchases of fixed maturities	(254,891)	(368,514)
Other investing activities	2,082	23,169
Net change in cash from investing activities	449	182,003
CASH FLOWS PROVIDED BY (USED BY) FINANCING ACTIVITIES:		
Repurchases of common stock	(2,810)	(2,898)

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Cash paid in acquisitions of noncontrolling interests	-	(1,199)
Withdrawals of investment-type insurance contracts	(1,555)	(1,570)
Dividends paid	(620)	(624)
Other financing activities	(433)	(718)
Net change in cash from financing activities	(5,418)	(7,009)
Net change in cash and cash equivalents	2,402	(4,968)
Cash and cash equivalents, beginning of year	24,229	23,945
Cash and cash equivalents, end of period	\$ 26,631	\$ 18,977

See the accompanying Notes to Condensed Consolidated Financial Statements.

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INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note 1.

Organization, Consolidation, Basis of Presentation and Accounting Policies

(A)

Business and Organization

Independence Holding Company, a Delaware corporation (IHC), is a holding company principally engaged in the life and health insurance business through: (i) its insurance companies, Standard Security Life Insurance Company of New York ("Standard Security Life"), Madison National Life Insurance Company, Inc. ("Madison National Life"), Independence American Insurance Company (Independence American); and (ii) its marketing and administrative companies, including IHC Risk Solutions, LLC, IHC Health Solutions, Inc., IHC Specialty Benefits Inc. and IHC Carrier Solutions, Inc. IHC also owns a significant equity interest in a managing general underwriter (MGU) that writes medical stop-loss. Standard Security Life, Madison National Life and Independence American are sometimes collectively referred to as the Insurance Group . IHC and its subsidiaries (including the Insurance Group) are sometimes collectively referred to as the "Company", or IHC , or are implicit in the terms we , us and our .

Geneve Corporation, a diversified financial holding company, and its affiliated entities, held 52.4% of IHC's outstanding common stock at June 30, 2014.

(B)

Consolidation

American Independence Corp.

The Company owned approximately 90% of the outstanding common stock of American Independence Corp. ("AMIC") at both June 30, 2014 and December 31, 2013. AMIC is an insurance holding company engaged in the insurance and reinsurance business.

(C)

Basis of Presentation

The Condensed Consolidated Financial Statements have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP") for interim financial statements and with the instructions to Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The Condensed Consolidated Financial Statements include the accounts of IHC and its consolidated subsidiaries. All significant intercompany transactions have been eliminated in consolidation. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect: (i) the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements; and (ii) the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. IHC's annual report on Form 10-K as filed with the Securities and Exchange Commission should be read in conjunction with the accompanying Condensed Consolidated Financial Statements.

In the opinion of management, all adjustments (consisting only of normal recurring accruals) that are necessary for a fair presentation of the consolidated financial position and results of operations for the interim periods have been included. The condensed consolidated results of operations for the three months and six months ended June 30, 2014 are not necessarily indicative of the results to be anticipated for the entire year.

(D)

Reclassifications

Certain amounts in prior year's Condensed Consolidated Financial Statements and Notes thereto have been reclassified to conform to the 2014 presentation.

(E)

Recent Accounting Pronouncements

Recently Adopted Accounting Standards

In July 2013, the Financial Accounting Standards Board (FASB), issued guidance for the presentation of unrecognized tax benefits to better reflect the manner in which an entity would settle, at the reporting date, any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. The adoption of this guidance, effective January 1, 2014, did not have an effect on the Company's consolidated financial statements.

In July 2011, the FASB issued guidance specifying that the liability for the fees paid to the Federal Government by health insurers as a result of recent healthcare reform legislation should be estimated and recorded in full once the entity provides qualifying health insurance in the applicable calendar year in which the fee is payable with a corresponding deferred cost that is amortized to expense using a straight-line method of allocation unless another method better allocates the fee over the calendar year that it is payable. The amendments in this Update became effective January 1, 2014 and in accordance with the provisions, IHC recorded the estimated gross liability for the mandated fees payable to the Federal Government of \$1,500,000 and the corresponding deferred cost in the first quarter of 2014. The amounts were recorded in accounts payable, accruals and other liabilities and in other assets, respectively, on the Condensed Consolidated Balance Sheet. The deferred asset will be amortized ratably over the calendar year to selling, general and administrative expense in the Condensed Consolidated Statement of Income. Upon final assessment, the Company increased its gross liability for the mandated fees payable to the Federal Government to \$1,816,000 as of June 30, 2014.

Recently Issued Accounting Standards Not Yet Adopted

In June 2014, the FASB issued explicit guidance for entities that grant their employees share-based payments in which the terms of the award include a performance target that affects vesting and could be achieved after the requisite service period. This guidance is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015. Earlier adoption is permitted. The guidance may be applied either prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. The adoption of this guidance is not expected to have a material effect on the Company's consolidated financial statements.

In May 2014, the FASB issued revenue recognition guidance for entities that either enter into contracts with customers to transfer goods or services or enter into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards such as insurance contracts or lease contracts. The amendment provides specific steps that an entity should apply in order to achieve its main objective which is recognizing revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. For public entities, this guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, and requires one of two specified retrospective methods of application. Early application is prohibited. Management has not yet determined the impact that the adoption of this guidance will have on the Company's consolidated financial statements.

In April 2014, the FASB issued guidance: (i) improving the definition of discontinued operations by limiting the reporting of discontinued operations to disposals of components that represent strategic shifts that have (or will have) a major effect on an entity's operations and financial results; and (ii) requiring expanded disclosures for discontinued operations. Public entities are required to apply this guidance to: (i) all disposals (or classifications as held for sale) of components of the entity that occur within annual periods beginning on or after December 15, 2014, and interim periods within those years; and (ii) to all businesses that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within those years. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in previously issued financial statements. The adoption of this guidance is not expected to have a material effect on the Company's consolidated financial statements.

Note 2.

Income Per Common Share

Diluted earnings per share was computed using the treasury stock method and includes incremental common shares, primarily from the dilutive effect of share-based payment awards, amounting to 172,000 and 156,000 shares for the three months and six months ended June 30, 2014, respectively, and 52,000 and 86,000 shares for the three months and six months ended June 30, 2013, respectively.

Note 3.

Investment Securities

The cost (amortized cost with respect to certain fixed maturities), gross unrealized gains, gross unrealized losses and fair value of investment securities are as follows for the periods indicated (in thousands):

	June 30, 2014					
	AMORTIZED COST		GROSS UNREALIZED GAINS		GROSS UNREALIZED LOSSES	FAIR VALUE
FIXED MATURITIES						
AVAILABLE-FOR-SALE:						
Corporate securities	\$ 210,454	\$	1,467	\$	(3,279)	\$ 208,642
CMOs - residential ⁽¹⁾	3,325		28		(6)	3,347
CMOs - commercial	975		-		(69)	906
U.S. Government obligations	25,356		135		-	25,491
Agency MBS - residential ⁽²⁾	72		4		-	76
GSEs ⁽³⁾	19,926		5		(259)	19,672
States and political subdivisions	250,549		3,157		(3,042)	250,664
Foreign government obligations	60,059		268		(1,596)	58,731
Redeemable preferred stocks	4,036		162		-	4,198
Total fixed maturities	\$ 574,752	\$	5,226	\$	(8,251)	\$ 571,727
EQUITY SECURITIES						
AVAILABLE-FOR-SALE:						
Common stocks	\$ 8,222	\$	702	\$	(76)	\$ 8,848
Nonredeemable preferred stocks	4,004		110		-	4,114
Total equity securities	\$ 12,226	\$	812	\$	(76)	\$ 12,962

	December 31, 2013			
	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
FIXED MATURITIES				
AVAILABLE-FOR-SALE:				
Corporate securities	\$ 215,412	\$ 1,315	\$ (7,467)	\$ 209,260
CMOs - residential ⁽¹⁾	2,457	8	(8)	2,457
CMOs - commercial	975	-	(382)	593
U.S. Government obligations	15,596	271	(6)	15,861
Agency MBS - residential ⁽²⁾	79	4	-	83
GSEs ⁽³⁾	28,484	4	(340)	28,148
States and political subdivisions	256,645	2,435	(9,377)	249,703
Foreign government obligations	34,437	20	(2,107)	32,350
Redeemable preferred stocks	4,036	74	(278)	3,832
Total fixed maturities	\$ 558,121	\$ 4,131	\$ (19,965)	\$ 542,287
EQUITY SECURITIES				
AVAILABLE-FOR-SALE:				
Common stocks	\$ 7,517	\$ 328	\$ (70)	\$ 7,775
Nonredeemable preferred stocks	4,004	58	(34)	4,028
Total equity securities	\$ 11,521	\$ 386	\$ (104)	\$ 11,803

(1)

Collateralized mortgage obligations (CMOs).

(2)

Mortgage-backed securities (MBS).

(3)

Government-sponsored enterprises (GSEs) are private enterprises established and chartered by the Federal Government or its various insurance and lease programs which carry the full faith and credit obligation of the U.S. Government.

The amortized cost and fair value of fixed maturities available-for-sale at June 30, 2014, by contractual maturity, are shown below (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. CMOs and MBSs are shown

separately, as they are not due at a single maturity.

	AMORTIZED COST	FAIR VALUE
Due in one year or less	\$ 16,386	\$ 16,220
Due after one year through five years	79,181	78,983
Due after five years through ten years	208,270	206,892
Due after ten years	247,646	246,655
CMOs and MBSs	23,269	22,977
	\$ 574,752	\$ 571,727

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The following tables summarize, for all available-for-sale securities in an unrealized loss position, the aggregate fair value and gross unrealized loss by length of time those securities that have continuously been in an unrealized loss position for the periods indicated (in thousands):

June 30, 2014

Less than 12 Months		12 Months or Longer		Total	
Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses