

HORACE MANN EDUCATORS CORP /DE/

Form 10-K

February 28, 2008

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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, 2007

OR

.. **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 1-10890

HORACE MANN EDUCATORS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of

incorporation or organization)

1 Horace Mann Plaza, Springfield, Illinois 62715-0001

(Address of principal executive offices, including Zip Code)

Registrant's Telephone Number, Including Area Code: 217-789-2500

Securities Registered Pursuant to Section 12(b) of the Act:

37-0911756
(I.R.S. Employer

Identification No.)

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Title of each class	Name of each exchange on which registered
Common Stock, par value \$0.001 per share	New York Stock Exchange
Securities registered pursuant to Section 12(g) of the Act: None	

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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 the registrant's filer status, as such terms are defined in Rule 12b-2 of the Act.

Large accelerated filer Accelerated filer Non-accelerated filer

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

The aggregate market value of the registrant's Common Stock held by non-affiliates of the registrant based on the closing price of the registrant's Common Stock on the New York Stock Exchange and the shares outstanding on June 30, 2007, was \$919.2 million.

As of February 19, 2008, 40,633,237 shares of the registrant's Common Stock, par value \$0.001 per share, were outstanding, net of 20,241,747 shares of treasury stock.

DOCUMENTS INCORPORATED BY REFERENCE

Certain portions of the registrant's Proxy Statement for the 2008 Annual Meeting of Shareholders are incorporated by reference into Part II Item 5 and Part III Items 10, 11, 12, 13 and 14 of Form 10-K as specified in those Items and will be filed with the Securities and Exchange Commission within 120 days after December 31, 2007.

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HORACE MANN EDUCATORS CORPORATION

FORM 10-K

YEAR ENDED DECEMBER 31, 2007

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PART I

ITEM 1. Business
Forward-looking Information

It is important to note that the Company's actual results could differ materially from those projected in forward-looking statements. Additional information concerning factors that could cause actual results to differ materially from those in the forward-looking statements is contained in Item 1A. Risk Factors and in Management's Discussion and Analysis of Financial Condition and Results of Operations Forward-looking Information .

Overview and Available Information

Horace Mann Educators Corporation (HMEC ; and together with its subsidiaries, the Company or Horace Mann) is an insurance holding company incorporated in Delaware. Through its subsidiaries, HMEC markets and underwrites personal lines of property and casualty (primarily private passenger automobile and homeowners) insurance, retirement annuities (primarily tax-qualified products) and life insurance in the United States of America (U.S.). HMEC's principal insurance subsidiaries are Horace Mann Life Insurance Company (HMLIC), Horace Mann Insurance Company (HMIC) and Teachers Insurance Company (TIC), and each of which is an Illinois corporation; Horace Mann Property & Casualty Insurance Company (HMPCIC), a California corporation; and Horace Mann Lloyds (HM Lloyds), an insurance company domiciled in Texas.

The Company markets its products primarily to K-12 educators and other employees of public schools and their families. The Company's nearly one million customers typically have moderate annual incomes, with many belonging to two-income households. Their financial planning tends to focus on retirement, security, savings and primary insurance needs. Management believes that Horace Mann is the largest national multiline insurance company focused on the nation's educators as its primary market.

The Company markets and services its products primarily through an exclusive sales force of full-time agents employed by the Company and trained to sell multiline products. The Company's agents sell Horace Mann's products and limited additional third-party vendor products authorized by the Company. Many of the Company's agents are former educators or individuals with close ties to the educational community who utilize their contacts within, and knowledge of, the target market. Compensation for agents includes an incentive element based upon the profitability of the business they write. This exclusive agent sales force is supplemented by an independent agent distribution channel for the Company's annuity products.

The Company's insurance premiums written and contract deposits for the year ended December 31, 2007 were \$974.7 million and net income was \$82.8 million. The Company's total assets were \$6.3 billion at December 31, 2007. The property and casualty segment accounted for 55% of the Company's insurance premiums written and contract deposits for the year ended December 31, 2007; the annuity and life insurance segments together accounted for 45% of insurance premiums written and contract deposits for the year ended December 31, 2007 (35% and 10%, respectively).

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The Company is one of the largest participants in the 403(b) tax-qualified annuity market, measured by 403(b) net written premium on a statutory accounting basis. The Company's 403(b) tax-qualified annuities are annuities purchased voluntarily by individuals employed by public school systems or other tax-exempt organizations. The Company has approved 403(b) payroll reduction capabilities in over one-third of the 16,000 school districts in the U.S.

The Company's investment portfolio had an aggregate fair value of \$4.2 billion at December 31, 2007. Investments consist principally of investment grade, publicly traded fixed income securities.

The Company's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, and all amendments to those reports are available free of charge through the Investor Relations section of the Company's Internet Web site, www.horacemann.com, as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). The EDGAR filings of such reports are also available at the SEC's Web site, www.sec.gov.

Also available in the Investor Relations section of the Company's Web site are its corporate governance principles, code of conduct and code of ethics as well as the charters of the Board's Audit Committee, Compensation Committee, Executive Committee, Investment and Finance Committee, and Nominating and Governance Committee.

Louis G. Lower II, Chief Executive Officer of HMEC, timely submitted the Annual Section 12(a) CEO Certification to the New York Stock Exchange (NYSE) on June 11, 2007 without any qualifications. The Company filed with the SEC, as exhibits to the Annual Report on Form 10-K for the year ended December 31, 2006, the CEO and CFO certifications required under Section 302 of the Sarbanes-Oxley Act.

History

The Company's business was founded in Springfield, Illinois in 1945 by two school teachers to sell automobile insurance to other teachers within the State of Illinois. The Company expanded its business to other states and broadened its product line to include life insurance in 1949, 403(b) tax-qualified retirement annuities in 1961 and homeowners insurance in 1965. In November 1991, HMEC completed an initial public offering of its common stock (the IPO). The common stock is traded on the New York Stock Exchange under the symbol HMN.

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The following consolidated statement of operations and balance sheet data have been derived from the consolidated financial statements of the Company, which have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). The consolidated financial statements of the Company for each of the years in the five-year period ended December 31, 2007 have been audited by KPMG LLP, an independent registered public accounting firm. The following selected historical consolidated financial data should be read in conjunction with the consolidated financial statements of HMEC and its subsidiaries and Management's Discussion and Analysis of Financial Condition and Results of Operations .

	2007	Year Ended December 31,			2003
		2006	2005	2004	
	(Dollars in millions, except per share data)				
Statement of Operations Data:					
Insurance premiums and contract charges earned	\$ 654.3	\$ 653.9	\$ 664.9	\$ 674.7	\$ 643.5
Net investment income	223.8	209.0	194.6	191.4	184.7
Realized investment gains (losses)	(3.4)	10.9	9.8	12.2	25.5
Total revenues	887.0	885.8	880.2	883.2	855.8
Amortization of intangible assets (1)	5.4	6.1	5.1	6.0	5.0
Interest expense	14.1	13.1	8.9	6.8	6.3
Income before income taxes	117.1	140.3	94.0	69.7	19.2
Net income (2)	82.8	98.7	77.3	56.3	19.0
Ratio of earnings to fixed charges (3)	1.8x	2.0x	1.8x	1.6x	1.2x
Per Share Data (4):					
Net income per share:					
Basic	\$ 1.92	\$ 2.29	\$ 1.80	\$ 1.32	\$ 0.44
Diluted	\$ 1.86	\$ 2.19	\$ 1.67	\$ 1.25	\$ 0.44
Shares of Common Stock (in millions):					
Weighted average - basic	43.1	43.0	42.9	42.8	42.7
Weighted average - diluted	44.6	45.8	47.9	47.3	42.9
Ending outstanding	42.2	43.1	43.0	42.8	42.7
Cash dividends per share	\$ 0.42	\$ 0.42	\$ 0.42	\$ 0.42	\$ 0.42
Book value per share	\$ 16.41	\$ 15.25	\$ 13.51	\$ 13.45	\$ 12.42
Balance Sheet Data, at Year End:					
Total investments	\$ 4,180.3	\$ 4,302.2	\$ 3,996.5	\$ 3,657.2	\$ 3,385.7
Total assets	6,259.3	6,329.7	5,840.6	5,371.9	4,953.2
Total policy liabilities	3,383.3	3,301.4	3,172.1	3,010.6	2,787.0
Short-term debt				25.0	25.0
Long-term debt	199.5	232.0	190.9	144.7	144.7
Total shareholders' equity	693.3	657.1	580.6	576.2	530.5
Segment Information (5):					
Insurance premiums written and contract deposits					
Property and casualty	\$ 535.2	\$ 539.8	\$ 546.9	\$ 562.3	\$ 546.5
Annuity	337.1	325.7	320.1	327.0	296.6
Life	102.4	103.9	105.6	109.1	112.4
Total	974.7	969.4	972.6	998.4	955.5
Net income (loss)					
Property and casualty	\$ 61.2	\$ 74.3	\$ 45.0	\$ 27.6	\$ (17.8)
Annuity	17.6	13.2	15.1	12.6	14.4
Life	17.3	14.5	13.4	14.8	13.4
Corporate and other (2) (6)	(13.3)	(3.3)	3.8	1.3	9.0
Total	82.8	98.7	77.3	56.3	19.0

(1) Amortization of intangible assets is comprised of amortization of acquired value of insurance in force and is the result of purchase accounting adjustments related to the 1989 acquisition of the Company.

- (2) In 2005, the Company's federal income tax expense reflected a reduction of \$9.1 million from the closing of tax years 1996 through 2001 with favorable resolution of the contingent tax liabilities related to those prior tax years.
- (3) For the purpose of determining the ratio of earnings to fixed charges, earnings consist of income before income taxes and fixed charges, and fixed charges consist of interest expense (including amortization of debt issuance cost) and interest credited to policyholders on interest-sensitive contracts.
- (4) Basic earnings per share is computed based on the weighted average number of shares outstanding. Diluted earnings per share is computed based on the weighted average number of shares and common stock equivalents outstanding. The Company's common stock equivalents relate to outstanding common stock options, Director Stock Plan units, Employee Stock Plan units and restricted stock units. The Company's Senior Convertible Notes, which were issued in May 2002, are considered potentially dilutive securities and are included in the calculation of diluted earnings per share, to the extent dilutive, per Emerging Issues Task Force (EITF) issue 04-8, The Effect of Contingently Convertible Instruments on Diluted Earnings per Share. In May 2007, the Company redeemed all remaining Senior Convertible Notes.
- (5) Information regarding assets by segment at December 31, 2007, 2006 and 2005 is contained in Notes to Consolidated Financial Statements Note 13 Segment Information listed on page F-1 of this report.
- (6) The corporate and other segment primarily includes interest expense on debt and the impact of realized investment gains and losses, debt retirement costs and gains and certain public company expenses.

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Corporate Strategy and Marketing

The Horace Mann Value Proposition

The Horace Mann Value Proposition articulates the Company's overarching strategy and business purpose: Provide lifelong financial well-being for educators and their families through personalized service, advice, and a full range of tailored insurance and financial products.

Target Market

Management believes that Horace Mann is the largest national multiline insurance company focused on the nation's educators as its primary market. The Company's target market consists primarily of K-12 educators and other employees of public schools and their families located throughout the U.S. The U.S. Department of Education estimates that there are approximately 3.6 million elementary and secondary teachers in public and private schools in the U.S. The Company also markets its products to other education-related customers, including school administrators, education support personnel, private school teachers, community college personnel and customer referrals.

Exclusive Agency Force

A cornerstone of the Company's marketing strategy is its exclusive sales force of full-time employee agents trained to sell multiline products. As of December 31, 2007, the Company employed 790 full-time agents, approximately 75% of which are licensed by the Financial Industry Regulatory Authority (FINRA), formerly the National Association of Securities Dealers, Inc. (NASD), to sell variable annuities and variable universal life policies. Many of the Company's agents were previously teachers, other members of the education profession or persons with close ties to the educational community. The Company's exclusive agents are under contract to market only the Company's products and limited additional third-party vendor products authorized by the Company. Collectively, the Company's principal insurance subsidiaries are licensed to write business in 49 states and the District of Columbia.

In 2006, the Company began the transition from a single-person agent operation to its new Agency Business Model (ABM), with agents in outside offices with support personnel and licensed producers, designed to remove current capacity constraints and increase productivity. The first Agency Business School session was conducted in October 2006, beginning the formal roll-out of this model. From October 2006 through December 31, 2007, 196 of the agents at December 31, 2007 and all field sales management completed this training. At the time of this Annual Report on Form 10-K, management anticipates conducting additional schools in 2008 and beyond for those agents who meet the Company's qualifications and demonstrate they are able to successfully migrate into the ABM model. On an ongoing basis, the Company will also provide follow-up training and support to those agents who have completed the school, to further embed repeatable processes and fully maximize the potential of ABM. Property and casualty initiatives to support that transition and drive business growth include expanding to more states the Company's Educator Segmentation Model—a more precise approach to pricing automobile business—and its Product Management Organization focusing on localized approaches to pricing, underwriting and marketing. The Company is also developing a new property and casualty policy administration system with an automated point-of-sale front end. Annuity and life initiatives to support the transition to ABM include the roll out of a new lineup of Horace Mann manufactured and branded products, as described in Annuity Segment and Life Segment.

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In 2001, to complement and extend the reach of the Company's agency force and to more fully utilize its approved payroll deduction slots in school systems across the country which are assigned to Horace Mann, the Company began building a network of independent agents to distribute the Company's 403(b) tax-qualified annuity products. In addition to serving educators in areas where the Company does not have exclusive agents, the independent agents complement the annuity capabilities of the Company's agents in under-penetrated areas. At December 31, 2007, there were 903 independent agents approved to market the Company's annuity products throughout the U.S. During 2007, collected contract deposits from this distribution channel were approximately \$43 million.

Geographic Composition of Business

The Company's business is geographically diversified. For the year ended December 31, 2007, based on direct insurance premiums and contract deposits for all product lines, the top five states and their portion of total direct insurance premiums and contract deposits were Illinois, 7.9%; Florida, 7.2%; North Carolina, 6.6%; California, 6.5%; and Minnesota, 5.3%.

HMEC's property and casualty subsidiaries write business in 48 states and the District of Columbia. The following table sets forth the Company's top ten property and casualty states based on total direct premiums in 2007:

Property and Casualty Segment Top Ten States

(Dollars in millions)

<u>State</u>	Property and Casualty Segment	
	Direct Premiums (1)	Percent of Total
Florida	\$ 56.3	10.1%
California	48.2	8.6
North Carolina	38.8	7.0
Minnesota	37.4	6.7
Texas	29.7	5.3
Louisiana	26.9	4.8
Pennsylvania	24.3	4.3
South Carolina	24.3	4.3
Georgia	17.8	3.2
Maine	17.4	3.1
Total of top ten states	321.1	57.4
All other areas	238.2	42.6
Total direct premiums	\$ 559.3	100.0%

(1) Defined as earned premiums before reinsurance and is determined under statutory accounting principles.

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HMEC's principal life insurance subsidiary writes business in 48 states and the District of Columbia. The following table sets forth the Company's top ten combined life and annuity states based on total direct premiums and contract deposits in 2007:

Combined Life and Annuity Segments Top Ten States

(Dollars in millions)

State	Direct Premiums and Contract Deposits (1)	Percent of Total
Illinois	\$ 67.1	15.1%
Virginia	28.9	6.5
North Carolina	27.2	6.1
South Carolina	20.6	4.6
Tennessee	18.2	4.1
Texas	17.8	4.0
California	17.1	3.8
Indiana	16.2	3.6
Florida	15.8	3.5
Minnesota	15.4	3.5
Total of top ten states	244.3	54.8