INDEPENDENCE HOLDING CO
Form 10-Q
November 09, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

[X]

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

For the quarterly period ended **September 30, 2010.**

[ ]

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

58-1407235

(State or other jurisdiction of incorporation or organization)

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

96 CUMMINGS POINT ROAD, STAMFORD, CONNECTICUT **06902**

(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 [X] 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 [X]

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 [X]

Class	Outstanding at November 9, 2010
Common stock, $ 1.00 par value	**15,232,865 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)

	September 30, 2010	December 31, 2009
	(Unaudited)	
ASSETS:		

Investments:	
Short-term investments	
$	53
$	52
Securities purchased under agreements to resell	
	34,060

42,708

Fixed maturities,
available-for-sale

803,239

689,863

Equity securities,
available-for-sale

53,858

60,815

Other investments

36,233

37,643

Total investments

927,443

831,081

Cash and cash equivalents

9,617

7,394

Due from securities brokers	
17,629	
5,579	
Investment in American Independence Corp. ("AMIC")	
-	
19,234	
Deferred acquisition costs	
38,647	
44,244	

Due and unpaid premiums	47,873	48,731
Due from reinsurers	166,360	184,583
Premium and claim funds	44,307	43,663

Notes and other receivables	18,092	13,528
Goodwill	51,713	48,859
Other assets	59,399	57,580

TOTAL ASSETS

$

1,381,080

$

1,304,476

LIABILITIES AND EQUITY:

LIABILITIES:		
Insurance reserves-health	$ 184,374	$ 184,146
Insurance reserves-life and annuity	274,272	270,987

Funds on deposit	408,054	408,298
Unearned premiums	8,869	13,217
Policy claims-health	18,558	18,655
Policy claims-life		

11,364

11,392

Other policyholders' funds

19,456

20,517

Due to securities brokers

30,679

8,187

Due to reinsurers

34,619

45,516

Accounts payable, accruals and other liabilities

73,210

71,362

Liabilities related to discontinued operations

910

1,546

Debt

7,500

9,000

Junior subordinated debt securities

38,146

38,146

TOTAL LIABILITIES

1,110,011

1,100,969

EQUITY:

IHC STOCKHOLDERS' EQUITY:

Preferred stock (none issued)

-

-

Common stock $1.00 par value, 20,000,000 shares authorized;

15,472,000 and 15,459,720 shares issued;

15,232,865 and 15,426,965 shares outstanding

15,472

15,460

Paid-in capital

100,901

100,447

Accumulated other comprehensive income (loss)

10,095

(7,104)

Treasury stock, at cost 239,155 and 32,755 shares	
	(1,917)
	(326)
Retained earnings	
	116,234
	94,490
TOTAL IHC STOCKHOLDERS EQUITY	

240,785

202,967

NONCONTROLLING INTERESTS IN SUBSIDIARIES

30,284

540

TOTAL EQUITY

	271,069
	203,507
TOTAL LIABILITIES AND EQUITY	
$	1,381,080
$	1,304,476

See the accompanying Notes to Condensed Consolidated Financial Statements.

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data) (Unaudited)

Three Months Ended

Nine Months Ended

September 30,

September 30,

2010

2009

2010

2009

REVENUES:

Premiums earned:

Health

$

74,071

$

62,527

$

211,735

$

197,452

Life and annuity

9,188

9,215

27,022

27,804

Net investment income

11,136

11,303

30,638

33,450

Fee income

8,102

6,614

25,343

22,943

Net realized investment gains

4,030

553

6,013

3,480

Other-than-temporary impairment losses

(132)

-

(2,797)

(271)

Equity income from AMIC

-

76

280

1,004

Gain on bargain purchase of AMIC

-

-

27,830

-

Other income

1,480

2,224

4,592

5,428

107,875

92,512

330,656

291,290

EXPENSES:

Insurance benefits, claims and reserves:	
Health	
	48,494
	45,636
	145,309
	137,876
Life and annuity	

12,826

9,831

37,518

34,210

Selling, general and administrative expenses

37,182

33,250

105,007

104,719

Amortization of deferred acquisitions costs

1,678

1,001

4,716

3,351

Interest expense on debt

499

701

1,447

2,232

100,679

90,419

293,997

282,388

Income from continuing operations

before income taxes

7,196

2,093

36,659

8,902

Income taxes

2,145

212

12,913

1,709

Income from continuing operations

5,051

1,881

23,746

7,193

Discontinued operations:

Income (loss) from discontinued operations, net of tax

(21)

49

(203)

(305)

Net income

5,030

1,930

23,543

6,888

(Income) loss from noncontrolling interests in subsidiaries	
	(610)
	(5)
	(1,391)
	15

NET INCOME ATTRIBUTABLE TO IHC	$ 4,420	$ 1,925	$ 22,152	$ 6,903

Basic income per common share:

Income from continuing operations	$	.29	$	.12	$	1.46	$	.47
Loss from discontinued operations		-		-				

(.01)

(.02)

Basic income per common share

$

.29

$

.12

$

1.45

$

.45

WEIGHTED AVERAGE SHARES OUTSTANDING

15,233

15,423

15,279

15,417

Diluted income per common share:

Income from continuing operations	$ .29	$ .12	$ 1.46	$ .47
Loss from discontinued operations	-	-	(.01)	(.02)
Diluted income per common share	$			

.29

$

.12

$

1.45

$

.45

WEIGHTED AVERAGE DILUTED SHARES OUTSTANDING

15,233

15,429

15,282

15,420

See the accompanying Notes to Condensed Consolidated Financial Statements.

INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Unaudited)

NINE MONTHS ENDED SEPTEMBER 30, 2010 (In thousands)

ACCUMULATED

NON-

OTHER

TREASURY

TOTAL IHC

CONTROLLING

COMMON

PAID-IN

COMPREHENSIVE

STOCK,

RETAINED

STOCKHOLDERS'

INTERESTS IN

TOTAL

STOCK

CAPITAL

INCOME (LOSS)

AT COST

EARNINGS

EQUITY

SUBSIDIARIES

EQUITY

BALANCE AT

DECEMBER 31, 2009

$

15,460

$

100,447

$

(7,104)

$

(326)

$

94,490

$

202,967

$

540

$

203,507

Net income

22,152

22,152

1,391

23,543

Net change in
unrealized

gains (losses)

17,199

17,199

-

17,199

Total comprehensive

income

39,351

1,391

40,742

Repurchase of common stock

(1,591)

(1,591)

-

(1,591)

Acquisition of MedWatch

-

480

480

Acquisition of HBA

-

480

480

Acquisition of American

Independence Corp.

(4)

(4)

26,960

26,956

Common Stock
dividend

($0.025 Per share)

(381)

(381)

-

(381)

Share-based compensation

expenses and related

tax benefits

12

417

429

-

429

Other capital transactions

41

(27)

14

433

447

BALANCE AT

SEPTEMBER 30, 2010
$
15,472
$
100,901
$
10,095
$
(1,917)
$
116,234
$
240,785
$
30,284
$
271,069

See the accompanying Notes to Condensed Consolidated Financial Statements.

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INDEPENDENCE HOLDING COMPANY AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands) (Unaudited)

	Nine Months Ended September 30,	
	2010	**2009**
CASH FLOWS PROVIDED BY (USED BY) OPERATING ACTIVITIES:		
Net income	$	

23,543

$

6,888

Adjustments to reconcile net income to net change in cash from

operating activities:

Gain on bargain purchase of AMIC

(27,830)

		-
Loss from discontinued operations	203	305
Amortization of deferred acquisition costs	4,716	3,351
Net realized investment gains	(6,013)	(3,480)

Other-than-temporary impairment losses	
2,797	
271	
Equity income from AMIC and other equity method investments	
(927)	
(1,696)	
Depreciation and amortization	
3,609	
4,028	
Share-based compensation expenses	

574

404

Deferred tax expense

14,730

1,811

Other

1,408

414

Changes in assets and liabilities:

Net purchases of trading securities	(1,355)
	-
Change in insurance liabilities	(27,244)
	(18,879)
Additions to deferred acquisition costs, net	(4,952)
	(1,368)
Change in net amounts due from and to reinsurers	

15,934

(40,777)

Change in premium and claim funds

3,702

13,255

Change in income tax liability

(3,175)

(40)

Change in due and unpaid premiums

10,655

3,040

Change in other assets

79

3,504

Change in other liabilities

(9,732)

(955)

Net change in cash from operating activities of continuing operations

722

(29,924)

Net change in cash from operating activities of discontinued operations

(975)

(2,120)

Net change in cash from operating activities

(253)

(32,044)

CASH FLOWS PROVIDED BY (USED BY) INVESTING ACTIVITIES:

Change in net amount due from and to securities brokers	
	10,093
	16,601
Net sales of securities under resale and repurchase agreements	
	9,951
	37,155
Sales of equity securities	
	49,295

13,672

Purchases of equity securities

(37,719)

-

Sales of fixed maturities

535,848

342,316

Maturities and other repayments of fixed maturities

96,178

87,641

Purchases of fixed maturities	(657,028)	(462,797)
Additional investments in other investments, net of distributions	2,070	(331)
Cash acquired in acquisition of AMIC, net of cash paid	4,562	-

Cash paid in acquisitions of companies, net of cash acquired	(3,469)
	(775)
Cash paid in acquisition of policy blocks	(2,791)
	-
Change in notes and other receivables	844
	1,803
Other	

(1,581)

(1,540)

Net change in cash from investing activities

6,253

33,745

CASH FLOWS PROVIDED BY (USED BY) FINANCING ACTIVITIES:

Proceeds from issuance of common stock	
	-
	1
Repayment of long-term debt	
	(1,500)
	(1,000)
Repurchases of common stock	
	(1,591)
	-
Excess tax expense from expired stock options and vesting	

of restricted stock	
	(22)
	(422)
Proceeds of investment-type insurance contracts	
	118
	1,176
Dividends paid	
	(767)
	(772)
Other capital transactions	
	(15)

-

Net change in cash from financing activities

(3,777)

(1,017)

Net change in cash and cash equivalents

2,223

684

Cash and cash equivalents, beginning of year

7,394

7,767

Cash and cash equivalents, end of period

$

9,617

$

8,451

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.

Significant Accounting Policies and Practices

(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 wholly owned insurance companies, Standard Security Life Insurance Company of New York ("Standard Security Life") and Madison National Life Insurance Company, Inc. ("Madison National Life"); (ii) its majority owned insurance company, Independence American Insurance Company (Independence American); and (iii) its marketing and administrative companies, including IHC Administrative Services, Inc., managing general underwriters ("MGUs") in which it owns a significant voting interest, IHC Health Solutions, Inc. (IHC Health Solutions), and Actuarial Management Corporation (AMC). These companies are sometimes collectively referred to as the "Insurance Group," and IHC and its subsidiaries (including the Insurance Group) are sometimes collectively referred to as the "Company." IHC also owns a 50.1% interest in American Independence Corp. (AMIC).

Geneve Corporation, a diversified financial holding company, and its affiliated entities held approximately 54% of IHC's outstanding common stock at September 30, 2010.

(B)

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; (ii) the disclosure of contingent assets and liabilities at the date of the financial statements; and (iii) 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.

IHC acquired a controlling interest in AMIC on March 5, 2010. Prior to obtaining control, IHC recorded its investment in AMIC using the equity method. IHC recorded changes in its investment in AMIC in the Equity income from AMIC line in the Condensed Consolidated Statements of Operations. Upon achieving control, on March 5, 2010, AMIC s income and expense amounts became consolidated with IHC s results. The Condensed Consolidated Balance Sheet at September 30, 2010 includes the consolidated balance sheet of AMIC.

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 nine months ended September 30, 2010 are not necessarily indicative of the results to be anticipated for the entire year.

(C)

Recent Accounting Pronouncements

Recently Adopted Accounting Standards

In January 2010, the Financial Accounting Standards Board (FASB) issued standards requiring new disclosures regarding (i) transfers in and out of Level 1 and Level 2 fair value measurements and (ii) activity in Level 3 fair value measurements. This guidance also clarifies existing disclosures regarding (i) the level of asset and liability disaggregation and (ii) fair value measurement inputs and valuation techniques. The guidance is effective for interim and annual periods beginning after December 15, 2009, except for the requirement to provide Level 3 activity of purchases, sales, issuances, and settlements on a gross basis, which will be effective for fiscal years beginning after December 15, 2010; early adoption is permitted. The adoption of this guidance, effective January 1, 2010, did not have a material effect on the Company's consolidated financial statements.

In September 2009, the FASB issued standards which among other things, amends former guidance on the consolidation of variable interest entities. The standards (i) require an entity to perform an analysis to determine whether an entity's variable interest or interests give it a controlling financial interest in a variable interest entity; (ii) require ongoing reassessments of whether an entity is the primary beneficiary of a variable interest entity and eliminate the quantitative approach previously required for determining the primary beneficiary of a variable interest entity; (iii) amend previous guidance for determining whether an entity is a variable interest entity; and (iv) require enhanced disclosure that will provide users of financial statements with more transparent information about an entity's involvement in a variable interest entity. In December 2009, these standards were added to the Accounting Standards Codification (Codification). The adoption of this guidance, effective January 1, 2010, did not have a material effect on the Company's consolidated financial statements.

In September 2009, the FASB issued standards to revise previous authoritative guidance related to accounting for transfers of financial assets, and will require more disclosures about transfers of financial assets, including securitization transactions, and where entities have continuing exposure to the risks related to transferred financial assets. In December 2009, these standards were added to the Codification. Among other things, the guidance eliminates the concept of a "qualifying special-purpose entity", changes the requirements for derecognizing financial assets and enhances information reported to users of financial statements by providing greater transparency about transfers of financial assets and an entity's continuing involvement in transferred financial assets. The guidance was effective for the first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter with earlier application prohibited. The recognition and measurement provisions shall be applied to transfers that occur on or after the effective date. The adoption of this guidance, effective January 1, 2010, did not have a material effect on the Company's consolidated financial statements.

Recently Issued Accounting Standards Not Yet Adopted

In April 2010, the FASB issued guidance on the accounting effect, if any, that arises from the different signing dates between the Health Care and Education Reconciliation Act of 2010, which is a reconciliation bill that amends the Patient Protection and Affordable Care Act. This guidance is applicable for registrants with a period end that falls between the signing dates for which the timing difference could have an accounting impact. The adoption of this guidance is not expected to have a material effect on the Company's consolidated financial statements.

In October 2010, the FASB issued guidance that specifies the accounting treatment for the costs incurred by insurance entities when acquiring new and renewal insurance contracts. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011 and should be applied prospectively upon adoption. The Company is currently evaluating the potential impact the amendments in this update will have on its consolidated financial statements.

(D)

Reclassifications

Certain amounts in prior years' Condensed Consolidated Financial Statements and Notes thereto have been reclassified to conform to the 2010 presentation.

(E)

Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before the financial statements are issued or are available to be issued. The Company has evaluated all such events occurring subsequent to the balance sheet date herein of September 30, 2010. The effects of all subsequent events that provided additional evidence about conditions that existed at the date of the balance sheet, including estimates, if any, have been recognized in the accompanying Condensed Consolidated Balance Sheet and Condensed Consolidated Statements of Operations as of and for the three-month and nine-month periods ended September 30, 2010. The Company did not recognize subsequent events that provided evidence about conditions that arose after the balance sheet date.

Note 2.

American Independence Corp.

AMIC is an insurance holding company engaged in the insurance and reinsurance business. AMIC does business with the Insurance Group, including reinsurance treaties under which, in 2009, Standard Security Life and Madison National Life ceded to Independence American an average of 23% of their medical stop-loss business, 9% of a majority of their fully insured health business and 20% of their New York Statutory Disability business.

In March 2010, IHC acquired a controlling interest in AMIC as a result of the purchase of AMIC common stock in the open market. The principal reasons for acquiring control were: (i) the low market price of the AMIC stock; (ii) the improved financial presentation for IHC resulting from the consolidation of financial reporting; and (iii) a closer relationship that will create greater long-term value for both companies. The acquisition furthers IHC's goal of creating efficiencies by integrating the back office operations of our MGUs and marketing companies. Share purchases of 27,668 shares, or $141,000, through March 5, 2010 (the "Acquisition Date"), totaling 0.33% of voting equity interest, brought the total of AMIC shares owned by the Company to more than 50% of AMIC's outstanding common stock and as a result, IHC has included AMIC s consolidated assets and liabilities and results of operations subsequent to the Acquisition Date in its condensed consolidated financial results as of and for the period ended September 30, 2010. At December 31, 2009, IHC owned 49.7% of AMIC's outstanding common stock which was purchased in various transactions from 2002 through 2008 and accounted for its investment in AMIC under the equity method. In the fourth quarter of 2009, under the equity method of accounting, due to the length of time, and the magnitude of the amount by which the quoted market price of AMIC had been below IHC s carrying value, the Company recorded an other-than-temporary impairment loss of $29,198,000 on its investment in AMIC. At December 31, 2009, the carrying value of IHC's investment in AMIC was $19,234,000.

In determining the bargain purchase gain with regard to the acquisition of the controlling interest in AMIC, IHC first recognized a gain of $2,201,000 as a result of remeasuring its equity interest in AMIC to its fair value of $22,013,000 immediately before the acquisition based on the closing market price of AMIC's common stock. Then, upon the acquisition of a controlling interest on March 5, 2010, the Company consolidated the net assets of AMIC. Accordingly, the Company determined the fair value of the identifiable assets acquired and liabilities assumed from AMIC on the Acquisition Date. The fair value of the net assets acquired exceeded the sum of: (i) the fair value of the consideration paid; (ii) the fair value of IHC s equity investment prior to the acquisition; and (iii) the fair value of the noncontrolling interests in AMIC, resulting in a bargain purchase gain of $25,629,000. The total gain, amounting to $27,830,000, pre-tax, is included in gain on bargain purchase of AMIC on the Company s Condensed Consolidated Statement of Operations. This gain is a result of the quoted market price of AMIC being significantly less than the fair value of the net assets of AMIC. This disparity is due to the low trading volume in AMIC shares, and a discount on the shares traded due to a lack of control by minority shareholders. The fair value of the noncontrolling interests in AMIC was based on the closing market price of AMIC s common stock on the Acquisition Date.

In connection with the acquisition, the Company recorded $12,200,000 of intangible assets. Of this amount, $1,700,000 represents the fair value of agent and marketing contracts and relationships, $1,000,000 represents the fair value of a domain name, and $2,000,000 represents the fair value of customer lists and all are amortizable over the life of the respective intangible asset. The remaining $7,500,000 represents non-amortizable intangible assets consisting of the fair value of insurance licenses with indefinite lives. As the AMIC acquisition was accounted for as a bargain purchase, the Company did not record goodwill in connection with the transaction.

The following table presents the identifiable assets acquired and liabilities assumed in the acquisition of AMIC on the Acquisition Date based on their respective fair values (in thousands).

Investments	$	58,418
Cash and cash equivalents		4,761
Identifiable intangible assets		

12,200

Deferred tax assets, net

10,654

Other assets

31,127

Total identifiable assets

117,160

Insurance liabilities

	27,671
Other liabilities	19,023
Total liabilities	46,694
Net identifiable assets acquired	70,466

Purchase consideration	(71)
Fair value of equity investment prior to the acquisition	(22,013)
Noncontrolling interests in AMIC	(22,065)
Elimination of the fair value adjustment related to AMIC s	

investment in Majestic

(688)

Gain on bargain purchase

25,629

Gain on fair value of equity investment prior to the acquisition

2,201

Total gain on bargain purchase of AMIC, pretax	27,830
Deferred income taxes	11,097
Total gain on bargain purchase of AMIC, after tax	

$
16,733

For the three-months ended September 30, 2010, the Company s Condensed Consolidated Statement of Operations includes revenues and net income of $21,803,000 and $1,000,000, respectively, from AMIC.

For the period from the Acquisition Date to September 30, 2010, the Company s Condensed Consolidated Statement of Operations includes revenues and net income of $53,207,000 and $2,253,000, respectively, from AMIC.

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The unaudited pro forma revenues and operating results had the acquisition occurred as of the beginning of each period are presented below. The unaudited pro forma information presented is not indicative of the results of operations in future periods, nor does it necessarily reflect the results of operations that would have resulted had the acquisition been completed as of the beginning of the applicable periods presented.

	Three Months Ended
	Nine Months Ended
	September 30,
	September 30,
	2010
	2009
	2010

2009

(in thousands)

Revenues

$

107,875

$

117,283

$

316,426

$

365,239

Net income

$

5,030

$

2,437

$

7,323

$

8,933

Pro forma adjustments to revenues principally reflect the elimination of intercompany fee income, the elimination of the Company s equity income related to AMIC and, in 2010, the elimination of the gain resulting from the bargain purchase. Pro forma adjustments to net income principally reflect the elimination of the Company s equity income related to AMIC and, in 2010, the elimination of the gain resulting from the bargain purchase.

Subsequent to the Acquisition Date, IHC purchased an additional 9,537 shares of AMIC common stock for a total consideration of $58,000 through September 30, 2010.

During the period from January 1, 2010 to the Acquisition Date (the Stub Period) IHC recorded $280,000 of equity income from its investment in AMIC. During the three months and nine months ended September 30, 2009, IHC recorded $76,000 and $1,004,000, respectively, of equity income from its investments in AMIC. These amounts represent IHC's proportionate share of income based on its ownership interests during those periods. AMIC paid no dividends on its common stock during the Stub Period in 2010 or the three-month and nine-month periods ended September 30, 2009.

The following disclosures summarize the effects of certain transactions between IHC and its subsidiaries with AMIC during the Stub Period and other periods prior to the Acquisition Date. Subsequent to the Acquisition Date, the effects of these transactions are eliminated in consolidation. IHC and its subsidiaries recorded income of $208,000 during the Stub Period in 2010 and $327,000 and $833,000, respectively, for the three months and nine months ended September 30, 2009 from service agreements with AMIC and its subsidiaries. These are reimbursements to IHC and its subsidiaries, at agreed upon rates including an overhead factor, for management services provided by IHC and its subsidiaries, including accounting, legal, compliance, underwriting and claims. The Company ceded premiums to AMIC of $5,867,000 during the Stub Period in 2010 and $10,994,000 and $34,728,000, respectively, for the three months and nine months ended September 30, 2009. Benefits to policyholders on business ceded to AMIC were $3,020,000 during the Stub Period in 2010 and $8,461,000 and $23,115,000, respectively, for the three months and nine months ended September 30, 2009. Additionally, AMIC subsidiaries market, underwrite and provide administrative services (including premium collection, medical management and claims adjudication) for a substantial portion of the Medical Stop-Loss business written by the insurance subsidiaries of IHC. IHC recorded gross premiums of $8,452,000 during the Stub Period in 2010 and $15,422,000 and $48,271,000, respectively, for the three months and nine months ended September 30, 2009 and IHC recorded net commission expense of $326,000 during the Stub Period in 2010 and $624,000 and $2,032,000, respectively, for the three months and nine months ended September 30, 2009 for these services. The Company also contracts for several types of insurance coverage (e.g. directors and officers and professional liability coverage) jointly with AMIC. The cost of this coverage is allocated between the Company and AMIC according to the type of risk, and IHC s portion is recorded in Selling, General and Administrative Expenses.

Included in the Company s Condensed Consolidated Balance Sheet at December 31, 2009 are the following balances arising from transactions in the normal course of business with AMIC and its subsidiaries: Due from reinsurers $15,453,000; Other assets $2,632,000; and Other liabilities of $480,000.

Note 3.

Income Per Common Share

Income per share calculations are based on income from continuing operations attributable to the common shareholders of IHC for the three months and nine months ended September 30, 2010 and 2009, as shown below (in thousands):

Three Months Ended
Nine Months Ended
September 30,
September 30,
2010
2009

	2010	2009		
Income from continuing operations	$ 5,051	$ 1,881	$ 23,746	$ 7,193

(Income) loss from noncontrolling interests

in subsidiaries

(610)

(5)

(1,391)

15

Income from continuing operations

attributable to IHC shareholders, net of tax

4,441

1,876

22,355

7,208

Income (loss) from discontinued operations, net of tax

(21)

49

(203)

(305)

Net income attributable to IHC shareholders	$	4,420	$	1,925	$	22,152	$	6,903

Included in the diluted income per share calculations for the three months and nine months ended September 30, 2010 are zero and 3,000 of incremental shares, respectively, from the assumed exercise of dilutive stock options and the assumed vesting of dilutive restricted stock computed using the treasury stock method. Included in the diluted income per share calculations for the three months and nine months ended September 30, 2009 are 6,000 and 3,000 of incremental shares from assumed exercise of options and vesting of restricted stock using the treasury stock method.

Note 4.

Investments

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:

September 30, 2010
GROSS
GROSS
AMORTIZED
UNREALIZED
UNREALIZED

FAIR

COST

GAINS

LOSSES

VALUE

(In thousands)

FIXED MATURITIES

AVAILABLE-FOR-SALE:

Corporate securities	$	280,360	$	8,093	$	(587)	$	287,866
CMOs- residential [1]		69,936		6,395		(3,334)		72,997

CMOs - commercial

1,447

-

(625)

822

U.S. Government obligations

14,261

701

-

14,962

Agency MBS - residential [2]

10,680

213

-

10,893

GSEs (3)

53,977

1,153

(175)

54,955

States and political subdivisions

355,818

6,920

(1,994)

360,744

Total fixed maturities	$	786,479	$	23,475	$	(6,715)	$	803,239

EQUITY SECURITIES

AVAILABLE-FOR-SALE:

Common stocks

$

8,060

$

	398
	$
	(103)
	$
	8,355
Preferred stock - perpetuals	
	33,405
	1,411
	(454)
	34,362
Preferred stock - with maturities	
	9,790
	1,351
	-
	11,141

Total equity securities	$	51,255	$	3,160	$	(557)	$	53,858

December 31, 2009

GROSS

GROSS

AMORTIZED

UNREALIZED

UNREALIZED

FAIR

COST

GAINS

LOSSES

VALUE

(In thousands)

FIXED MATURITIES

AVAILABLE-FOR-SALE:

Corporate securities

$

207,554

$

332

$

(7,357)

$

200,529

CMOs - residential [1]

78,889

3,620

(8,582)

73,927

CMOs - commercial

868

-

(402)

466

U.S. Government obligations

6,319

44

-

6,363

Agency MBS - residential [2]

40,156

182

-

40,338

GSEs [3]

15,398

-

(251)

15,147

States and political subdivisions

358,012

3,170

(8,089)

353,093

Total fixed maturities	$	707,196	$	7,348	$	(24,681)	$	689,863

EQUITY SECURITIES

AVAILABLE-FOR-SALE:

Common stocks

$

3,790

$

151

$

(69)

$

3,872

Preferred stock - perpetuals

32,434

3,509

(215)

35,728

Preferred stock - with maturities

20,996

747

(528)

21,215

Total equity securities	$	57,220	$	4,407	$	(812)	$	60,815

(1)

Collateralized mortgage obligations (CMOs).

(2)

Mortgage-backed securities (MBS).

(3)

Government-sponsored enterprises (GSEs) which are the Federal Home Loan Mortgage Corporation, Federal National Mortgage Association and Federal Home Loan Banks. GSEs are private enterprises established and chartered by the Federal Government.

The cost basis of certain preferred stocks with maturities at September 30, 2010 and December 31, 2009 includes an adjustment of $1,763,000 and $2,394,000, respectively, related to other-than-temporary impairment losses recorded in accumulated other comprehensive income in prior periods.

Government-sponsored enterprise securities consist of Federal National Mortgage Association mortgage-backed securities and other fixed maturity securities issued by the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association.

The amortized cost and fair value of fixed maturities at September 30, 2010, by contractual maturity, are shown below. 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. The average life of mortgage-backed securities is affected by prepayments on the underlying loans and, therefore, is materially shorter than the original stated maturity.

% OF

AMORTIZED

FAIR

TOTAL FAIR

COST

VALUE

VALUE

(In thousands)

Due after one year through five years	$ 167,842	$ 172,049	21.4%
Due after five years through ten years	139,925	143,659	17.9%
Due after ten years	343,986		

349,271

43.5%

651,753

664,979

82.8%

CMO and MBS

15 year

97,607

100,818

12.5%

20 year

10,399

10,351

1.3%

30 year

26,720

27,091

3.4%

$

786,479

$

803,239

100.0%

The following tables summarize, for all securities in an unrealized loss position at September 30, 2010 and December 31, 2009, respectively, the aggregate fair value and gross unrealized loss by length of time those securities that have continuously been in an unrealized loss position:

Less than 12 Months
12 Months or Longer
Total

Fair

Unrealized

Fair

Unrealized

Fair

Unrealized

September 30, 2010

Value

Losses

Value

Losses

Value

Losses

(In thousands)

Corporate securities

$

16,887

$

219

$

10,511

$

368

$

27,398

$

587

CMOs - residential

3,187

533

24,285

2,801

27,472

3,334

CMO's - commercial

329

250

493

375

822

625

GSEs

27,703

162

1,447

13

29,150

175

States and political

subdivisions

92,502

1,689

7,570

305

100,072

1,994

Total fixed maturities

140,608

2,853

44,306

3,862

184,914

6,715

Common stocks

2,148

103

-

-

2,148

103

Preferred stocks-perpetual

15,071

454

-

-

15,071

454

Total temporarily

impaired securities

$

157,827

$

3,410

$

44,306

$

3,862

$

202,133

$

7,272

15

Less than 12 Months

12 Months or Longer

Total

Fair

Unrealized

Fair

Unrealized

Fair

Unrealized

December 31, 2009

Value

Losses

Value

Losses

Value

Losses

(In thousands)

Corporate securities	
$	122,122
$	2,287
$	66,652
$	5,070

$

188,774

$

7,357

CMOs - residential

7,937

990

35,757

7,592

43,694

8,582

CMOs - commercial

-

-

466

402

466

402

GSEs

9,901

186

5,246

65

15,147

251

States and political

subdivisions

132,180

4,459

52,196

3,630

184,376

8,089

Total fixed maturities

272,140

7,922

160,317

16,759

432,457

24,681

Common stocks

1,861

69

-

-

1,861

69

Preferred stocks-perpetual

416

8

8,060

207

8,476

215

Preferred stocks-
with

maturities
-
-
8,692
528
8,692
528

Total temporarily impaired securities
$
274,417
$
7,999

$

177,069

$

17,494

$

451,486

$

25,493

At September 30, 2010 and December 31, 2009, a total of 39 and 75 fixed maturities, respectively, and 12 and 13 equity securities, respectively, were in a continuous unrealized loss position for less than 12 months. At September 30, 2010 and December 31, 2009 a total of 24 and 56 fixed maturities, respectively, had continuous unrealized losses for 12 months or longer. At December 31, 2009, a total of 5 equity securities had continuous unrealized losses for 12 months or longer.

Substantially all of the unrealized losses on fixed maturities at September 30, 2010 and December 31, 2009 relate to investment grade securities and are attributable to changes in market interest rates and general disruptions in the credit market subsequent to purchase. The unrealized loss on corporate securities and state and political subdivisions are due to wider spreads. Spreads have widened as investors shifted funds to US Treasuries in response to the current market turmoil. Because the Company does not intend to sell, nor is it more likely than not that the Company will have to sell such investments before recovery of their amortized cost bases, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2010.

At September 30, 2010, the Company had $29,174,000 invested in whole loan CMOs backed by Alt-A mortgages. Of this amount, 43.4% were in CMOs that originated in 2005 or earlier and 56.6% were in CMOs that originated in 2006. The unrealized losses on all other CMO s relate to prime rate CMO s and are primarily attributed to general disruptions in the credit market subsequent to purchase.

Other-Than-Temporary Impairment Evaluations

The Company reviews its investment securities regularly and determines whether other-than- temporary impairments have occurred. If the Company intends to sell a debt security, or it is more likely than not that it would be required to sell a debt security before the recovery of its amortized cost basis, the entire difference between the security's amortized cost basis and its fair value at the balance sheet date would be recognized by a charge to total other-than-temporary impairment losses in the Consolidated Statement of Operations. For fixed maturities, if a decline in fair value is judged by management to be other-than-temporary, and the Company does not intend to sell the security and it is not more likely than not that it will be required to sell the security prior to recovery of the security s amortized cost, the impairment is bifurcated into (a) the amount of the total impairment related to the credit loss, and (b) the amount of the total impairment related to all other factors. The amount of the other-than-temporary impairment related to the credit loss is recognized by a charge to total other-than-temporary impairment losses in the Consolidated Statements of Operations, establishing a new cost basis for the security. The amount of the other-than-temporary impairment related to all other factors is recognized in other comprehensive income in the Consolidated Balance Sheets. The factors considered by management in its regular review include, but are not limited to: the length of time and extent to which the fair value has been less than cost; the financial condition and near-term prospects of the issuer; adverse changes in ratings announced by one or more rating agencies; subordinated credit support; whether the issuer of a debt security has remained current on principal and interest payments; current expected cash flows; whether the decline in fair value appears to be issuer specific or, alternatively, a reflection of general market or industry conditions (including, in the case of fixed maturities, the effect of changes in market interest rates); and the Company's intent to sell, or be required to sell, the debt security before the anticipated recovery of its remaining amortized cost basis.

In assessing corporate debt securities for other-than-temporary impairment, the Company evaluates the ability of the issuer to meet its debt obligations and the value of the company or specific collateral securing the debt position. For transactions where loan level data is not available, the model uses a proxy based on the collateral characteristics. Assumptions about loss severity and defaults used in the model are primarily based on actual losses experienced and defaults in the collateral pool. Prepayment speeds, both actual and estimated, are also considered. The cash flows generated by the collateral securing these securities are then determined with these default, loss severity and prepayment assumptions. These collateral cash flows are then utilized, along with consideration for the issue s position in the overall structure, to determine the cash flows associated with the mortgage-backed security held by the Company. In addition, the Company evaluates other asset-backed securities for other-than-temporary impairment by examining similar characteristics referenced above for mortgage-backed securities. The Company evaluates U.S. Treasury securities and obligations of U.S. Government corporations, U.S. Government agencies, and obligations of states and political subdivisions for other-than-temporary impairment by examining similar characteristics referenced above for corporate debt securities.

To the extent that the present value of the cash flows generated by a debt security is less than the amortized cost, a credit loss exists, and an other-than-temporary impairment is recognized through earnings. It is reasonably possible that further declines in estimated fair values of such investments, or changes in assumptions or estimates of anticipated recoveries and/or cash flows, may cause further other-than-temporary impairments in the near term, which could be significant.

Equity securities may experience other-than-temporary impairment in the future based on the prospects for full recovery in value in a reasonable period of time and the Company s ability and intent to hold the security to recovery. If a decline in fair value is judged by management to be other-than-temporary or management does not have the intent or ability to hold a security, a loss is recognized by a charge to total other-than-temporary impairment losses in the Consolidated Statements of Operations. For the purpose of other-than-temporary impairment evaluations, preferred stocks are treated in a manner similar to debt securities. Declines in the creditworthiness of the issuer of debt securities with both debt and equity-like features requires the use of the equity model in analyzing the security for other-than-temporary impairment.

Subsequent increases and decreases, if not an other-than-temporary impairment, in the fair value of available-for-sale securities that were previously impaired, are included in other comprehensive income in the Condensed Consolidated Balance Sheet.

Based on management s review of the portfolio, which considered these factors, the Company recorded the following losses for other-than-temporary impairments in the Condensed Consolidated Statements of Operations for the three months and nine months ended September 30, 2010 and 2009 (in thousands):

	Three Months Ended
	Nine Months Ended
	September 30,
	September 30,
	2010
	2009
	2010
	2009

Other-than-temporary
impairments:

Fixed maturities

$

132

$

-

$

2,797

$

-

Preferred stocks

-

-

-

271

$

132

$

-

$

2,797

$

271

Other-than-temporary impairments of $132,000 and $2,797,000, respectively, were recorded on fixed maturities during the three months and nine months ended September 30, 2010. Of these amounts, for the three months and nine months ended September 30, 2010, $132,000 and $2,065,000, respectively, are credit losses resulting from expected cash flows of debt securities less than the debt securities amortized cost, and $732,000 was the result of the Company s intent to sell certain municipal debt securities prior to the recovery of their amortized cost bases. No losses for other-than-temporary impairments were recognized in other comprehensive income for the three months or nine months ended September 30, 2010.

Cumulative credit losses for other-than-temporary impairments recorded on securities for which a portion of an other-than-temporary impairment was recognized in other comprehensive income were as follows (in thousands):

Balance at beginning of year

$

2,394

Securities sold

(631)

Balance at September 30, 2010	$ 1,763

Further deterioration in credit quality of the companies backing the securities, further deterioration in the condition of the financial services industry, a continuation of the current imbalance in liquidity that exists in the marketplace, a continuation or worsening of the current economic recession, or additional declines in real estate values may further affect the fair value of these securities and increase the potential that certain unrealized losses be designated as other-than-temporary in future periods and the Company may incur additional write-downs.

Note 5.

Net Realized Investment Gains

Net realized investment gains for the three months and nine months ended September 30, 2010 and 2009 are as follows (in thousands):

Three Months Ended

Nine Months Ended

September 30,

September 30,

2010

2009

2010

	2009
Net realized investment gains (losses):	
Fixed maturities	$ 5,104

$

553

$

6,847

$

3,492

Common stocks

(210)

-

(58)

-

Preferred stocks

490

-

516

(12)

5,384

553

7,305

3,480

Sales of trading securities

(1,355)

-

(1,355)

-

Other

1

-

63

-

Net realized investment gains

$

4,030

$

553

$

6,013

$

3,480

For the three months and nine months ended September 30, 2010, the Company realized gross gains of $6,220,000 and $11,400,000, respectively, and realized gross losses of $836,000 and $4,095,000, respectively, on sales of available-for-sale securities. For the three months and nine months ended September 30, 2009, the Company realized gross gains of $1,093,000 and $5,922,000, respectively, and gross losses of $540,000 and $2,442,000, respectively, on sales of available-for-sale securities. As of September 30, 2010 and December 31, 2009, the Company did not hold any trading securities.

Note 6.

Derivative Instruments

In connection with its previously outstanding line of credit, a subsidiary of IHC entered into an interest rate swap with the commercial bank lender, for a notional amount equal to the debt principal amount, under which the Company received a variable rate equal to the rate on the debt and paid a fixed rate (6.65%) in order to manage the risk in overall changes in cash flows attributable to forecasted interest payments. There was no hedge ineffectiveness on this interest rate swap which was accounted for as a cash flow hedge and, in August 2009, the interest rate swap expired.

For the nine months ended September 30, 2009, the Company recorded $156,000 of gains on the effective portion of the interest rate swap in accumulated other comprehensive loss on the accompanying Condensed Consolidated Balance Sheets, net of related taxes of $104,000.

Note 7.

Fair Value Disclosures of Financial Instruments

For all financial and non-financial assets and liabilities accounted for at fair value on a recurring basis, the Company utilizes valuation techniques based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market expectations. These two types of inputs create the following fair value hierarchy:

Level 1 - Quoted prices for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 - Instruments where significant value drivers are unobservable.

The following section describes the valuation methodologies we use to measure different assets at fair value.

Investments in fixed maturities and equity securities:

Available-for-sale securities included in Level 1 are equities with quoted market prices. Level 2 is primarily comprised of our portfolio of government securities, agency mortgage-backed securities, corporate fixed income securities, collateralized mortgage obligations, municipals, GSEs and certain preferred stocks that were priced with observable market inputs. Level 3 securities consist of CMO securities, primarily Alt-A mortgages. For these securities, we use industry-standard pricing methodologies, including discounted cash flow models, whose inputs are based on management s assumptions and available market information. Further we retain independent pricing vendors to assist in valuing certain instruments.

The following tables present our financial assets and liabilities measured at fair value on a recurring basis, at September 30, 2010 and December 31, 2009, respectively (in thousands):

	September 30, 2010
	Level 1

Level 2

Level 3

Total

FINANCIAL ASSETS:

Fixed maturities available-for-sale:

Corporate securities

$

-

$

287,866

$

-

$

287,866

CMOs - residential

-

30,235

42,762

72,997

CMOs - commercial

-

-

822

822

US Government obligations

-

14,962

-

14,962

Agency MBS - residential

-

10,893

-

10,893

GSEs

-

54,955

-

54,955

States and political subdivisions

-

360,744

-

360,744

Total fixed maturities

-

759,655

43,584

803,239

Equity securities available-for-sale:

Common stocks

8,355

-

-

8,355

Preferred stocks - perpetual

34,362

-

-

34,362

Preferred stocks - with maturities

11,141

-

-

11,141

Total equity securities

53,858

-

-

53,858

Total
$
53,858
$
759,655
$
43,584
$
857,097

December 31, 2009

Level 1

Level 2

Level 3

Total

FINANCIAL ASSETS:

Fixed maturities available-for-sale:

Corporate securities

$

-

$

200,529

$

-

$

200,529

CMOs - residential

-

34,885

39,042

73,927

CMOs - commercial	
	-
	-
	466
	466
US Government obligations	
	-
	6,363
	-
	6,363
Agency MBS - residential	

	-
	40,338
	-
	40,338
GSEs	
	-
	15,147
	-
	15,147
States and political subdivisions	
	-

353,093

-

353,093

Total fixed maturities

-

650,355

39,508

689,863

Equity securities available-for-sale:

Common stocks

3,872

-

-

3,872

Preferred stocks - perpetual

	35,728
	-
	-
	35,728
Preferred stocks - with maturities	
	19,015
	2,200
	-
	21,215
Total equity securities	
	58,615

2,200

-

60,815

Total

$

58,615

$

652,555

$

39,508

$

750,678

It is the Company s policy to recognize transfers of assets and liabilities between levels of the fair value hierarchy at the end of a reporting period. For the nine months ending September 30, 2010, there were no transfers of assets and liabilities between Level 1 and Level 2 of the fair value hierarchy. No securities were transferred out of Level 2 and into the Level 3 category as a result of limited or inactive markets during the first nine months of 2010. All transfers into the Level 3 category during 2010 were the result of the AMIC acquisition. The Company does not transfer out of Level 3 and into Level 2 until such time as observable inputs become available and reliable or the range of available independent prices narrow. No securities were sold or transferred out of the Level 3 category in 2010. For the nine months ending September 30, 2010, the Company did not include in earnings any realized investment gains or losses related to sales of securities categorized as Level 3 securities. The changes in the carrying value of Level 3 assets and liabilities for the nine months ended September 30, 2010 are summarized as follows (in thousands):

	September 30, 2010
	CMOs

	Residential	Commercial	Total
Beginning balance	$ 39,042	$ 466	$ 39,508

Transfers into Level 3:

Acquisition of AMIC

1,831

305

2,136

Gains (losses) included in earnings:

Other-than-temporary impairments

(2,065)

-

(2,065)

Net unrealized gains (losses) included in accumulated other comprehensive loss

7,500

50

7,550

Repayments and amortization of fixed maturities

(3,546)

1

(3,545)

Balance at end of period	$ 42,762	$ 822	$ 43,584

The following methods and assumptions were used to estimate the fair value of financial instruments not disclosed elsewhere in the Notes to Condensed Consolidated Financial Statements:

(A)

Policy Loans

The fair value of policy loans is estimated by projecting aggregate loan cash flows to the end of the expected lifetime period of the life insurance business at the average policy loan rates, and discounting them at a current market interest rate.

(B)

Funds on Deposit

The Company has two types of funds on deposit. The first type is credited with a current market interest rate, resulting in a fair value which approximates the carrying amount. The second type carries fixed interest rates which are higher than current market interest rates. The fair value of these deposits was estimated by discounting the payments using current market interest rates. The Company's universal life policies are also credited with current market interest rates, resulting in a fair value which approximates the carrying amount.

(C)

Debt

The fair value of debt with variable interest rates approximates its carrying amount. The fair value of fixed rate debt is estimated by discounting the cash flows using current market interest rates.

The estimated fair values of financial instruments not disclosed elsewhere in the Notes to Condensed Consolidated Financial Statements are as follows:

September 30, 2010

December 31, 2009

Carrying

Fair

Carrying

Fair

Amount

Value

Amount

Value

(In thousands)

FINANCIAL ASSETS:

Policy loans

$

23,168

$

26,647

$

23,833

$

27,422

FINANCIAL

LIABILITIES:

Funds on deposit

$

408,054

$

405,626

$

408,298

$

410,485

Debt and junior

subordinated
debt

securities

45,646

45,646

47,146

47,146

Note 8.

Goodwill and Other Intangible Assets

The change in the carrying amount of goodwill and other intangible assets (included in other assets in the Condensed Consolidated Balance Sheets) for the first nine months of 2010 is as follows (in thousands):

	Other Intangible Assets
	Total

Other

Definitive

Indefinite

Intangible

Goodwill

Lives

Lives

Assets

Balance at December 31, 2009

$

48,859

$

7,785

$

477

$

8,262

Acquisitions:

AMIC

-

4,700

7,500

12,200

Alliance
Underwriters

1,459

1,100

-

1,100

MedWatch

581

340

20

360

HBA

814

200

-

200

Capitalized
software
development

-

177

-

177

Amortization expense

-

(1,697)

-

(1,697)

Balance at September 30,

2010	$ 51,713
	$ 12,605
	$ 7,997
	$ 20,602

In connection with the acquisition of a controlling interest in AMIC discussed in Note 2, the Company recorded $12,200,000 of intangible assets. Of this amount, $1,700,000 represents the fair value of agent and marketing contracts and relationships, which is being amortized over a weighted average period of 7.6 years, $1,000,000 represents the fair value of a domain name being amortized over a 10 year period, and $2,000,000 represents the fair value of customer lists, which are being amortized over a period of 5.0 years. The remaining $7,500,000 represents non-amortizable intangible assets consisting of the fair value of insurance licenses with indefinite lives. The AMIC acquisition was accounted for as a bargain purchase and accordingly, the Company did not record goodwill in connection with the transaction.

In January 2010, the Company acquired the assets of a managing general underwriter, Alliance Underwriters, LLC (AU) for a $2,500,000 purchase price. The Company recorded goodwill of $1,459,000 and other intangible assets of $1,100,000, for the fair value of customer relationships, which is being amortized over a weighted average period of

8.0 years. AU is a managing general underwriter that controls approximately $30 million of employer medical stop-loss business.

In January 2010, IHC Health Holdings Corp., a wholly owned subsidiary of the Company (IHC Health Holdings), acquired a 51% interest in the stock of MedWatch, LLC (MedWatch) for a $500,000 purchase price. The Company recorded goodwill of $581,000 and other intangible assets of $360,000, primarily for the fair value of customer relationships, which is being amortized over a weighted average period of 11.6 years. MedWatch provides utilization review and medical management services to fully insured and self-funded health plans.

In January 2010, IHC Health Holdings acquired a 51% interest in the stock of Hospital Bill Analysis, LLC (HBA), a hospital bill review company, for a $500,000 purchase price. The Company recorded goodwill of $814,000 and other intangible assets of $200,000, primarily for the fair value of customer relationships, which is being amortized over a weighted average period of 11.0 years.

Note 9.

Discontinued Operations

The Company sold its credit life and disability segment by entering into a 100% coinsurance agreement with an unaffiliated insurer effective December 31, 2007. Unearned premium reserves of this block and the corresponding amount in due from reinsurers of $6,237,000 and $8,847,000 are included in the Condensed Consolidated Balance Sheets at September 30, 2010 and December 31, 2009, respectively.

The Company recorded losses from discontinued operations representing expenses and changes in claims and reserves related to the insurance liabilities (currently in run-off status) for claims incurred prior to the sale on December 31, 2007 as follows (in thousands):

	Three Months Ended
	Nine Months Ended
	September 30,
	September 30,

	2010	**2009**	**2010**	**2009**
Pretax loss from discontinued operations	$ (32)	$ 76	$ (312)	$

(469)

Tax benefits allocated to discontinued operations

11

27

109

(164)

Loss from discontinued operations, net
$ (21)
$ 49
$ (203)
$ (305)

Changes in the liabilities related to discontinued operations for the nine months ended September 30, 2010 were as follows (in thousands):

Claims

Accrued

Termination

Liability

Expenses

Benefits

Total

Balance at beginning of year	
	$
	1,522
	$
	-
	$
	24
	$
	1,546

Loss from discontinued operations:

Changes in claims and reserves

related to block in run-off

283

-

-

283

Expenses incurred related to block in run-off

-

29

-

29

312

Payments of expenses accrued to administer

the business sold

-

(29)

(24)

(53)

Claim payments related to block in run-off
(895)
-
-
(895)

Balance at September 30, 2010
$
910
$
-
$
-
$
910

The Company believes that the net liabilities of discontinued operations at September 30, 2010 adequately estimate the remaining costs associated with the credit life and disability discontinued operations.

Note 10.

Share-Based Compensation

IHC and AMIC each have share-based compensation plans. The following is a summary of the activity pertaining to each of these plans. AMIC disclosures reflect the activity subsequent to the Acquisition Date.

A)

IHC Share-Based Compensation Plans

Total share-based compensation was $208,000 and $63,000 for the three months ended September 30, 2010 and 2009, respectively and $530,000 and $404,000 for the nine months ended September 30, 2010 and 2009, respectively. Related tax benefits of $83,000 and $25,000 were recognized for the three months ended September 30, 2010 and 2009, respectively and $211,000 and $161,000 for the nine months ended September 30, 2010 and 2009, respectively.

Under the terms of IHC s stock-based compensation plans, option exercise prices are more than or equal to the quoted market price of the shares at the date of grant; option terms range from five to ten years; and vesting periods are three years for employee options. The Company may also grant shares of restricted stock, share appreciation rights (SARs) and share-based performance awards. Restricted shares are valued at the quoted market price of the shares at the date of grant and have a three year vesting period. Exercise prices of SARs are more than or equal to the quoted market price of IHC shares at the date of the grant and have three year vesting periods. At September 30, 2010, there were 726,589 shares available for future stock-based compensation grants under the IHC stock incentive plans.

Stock Options

IHC s stock option activity for the nine months ended September 30, 2010 is as follows:

	Shares	Weighted-Average
	Under Option	

Exercise Price

December 31, 2009

312,170

$

14.62

Granted

461,800

10.00

Expired

(6,490)

20.07

September 30, 2010

767,480

11.79

The following table summarizes information regarding IHC s outstanding and exercisable options as of September 30, 2010:

	Outstanding	Exercisable
Number of options	767,480	239,010
Weighted average exercise price per share	$ 11.79	$

15.48

Aggregate intrinsic value for all options

$

-

$

-

Weighted average contractual term remaining

3.3 years

1.7 years

The fair value of an option award is estimated on the date of grant using the Black-Scholes option valuation model. The weighted average grant-date fair-value of options granted during the nine months ended September 30, 2010 was $1.57 per share. No options were granted during the nine months ended September 30, 2009. The assumptions set forth in the table below were used to value the stock options granted during the nine-month period ended September 30, 2010:

Weighted-average risk-free interest rate

2.3%

Annual dividend rate per share

$

.05

Weighted-average volatility factor of the Company's common stock

45.0%

Weighted-average expected term of options

4.5 years

Compensation expense of $120,000 and $75,000 was recognized in the three months ended September 30, 2010 and 2009, respectively, and $374,000 and $281,000 in the nine months ended September 30, 2010 and 2009, respectively, for the portion of the grant-date fair value of stock options vesting during that period.

No options were exercised during the three months and nine months ended September 30, 2010 or 2009.

As of September 30, 2010, the total unrecognized compensation expense related to non-vested stock options was $655,000 which is expected to be recognized over the remaining requisite weighted-average service period of 1.7 years.

Restricted Stock

IHC issued 2,250 shares of restricted stock during both the nine months ended September 30, 2010 and 2009. The total fair value of IHC s restricted stock that vested during the first nine months of 2010 and 2009 was $23,000 and $70,000, respectively. Restricted stock expense was $5,000 and $12,000 for the three months ended September 30, 2010 and 2009, respectively, and was $24,000 and $92,000 for the nine months ended September 30, 2010 and 2009, respectively.

The following table summarizes restricted stock activity for the nine months ended September 30, 2010:

No. of

Weighted-Average

Non-vested

Grant-Date

Shares

Fair Value

December 31, 2009

5,380

$

12.43

Granted

2,250

$

7.01

Vested

(3,130)

$

15.19

September 30, 2010

4,500

$

7.80

As of September 30, 2010, the total unrecognized compensation expense related to IHC s non-vested restricted stock awards was $29,000 which is expected to be recognized over the remaining requisite weighted-average service period of 2.0 years.

SARs and Share-Based Performance Awards

The fair value of SARs is calculated using the Black-Scholes valuation model at the grant date and each subsequent reporting period until settlement. Compensation cost is based on the proportionate amount of the requisite service that has been rendered to date. Once fully vested, changes in fair value of the SARs continue to be recognized as compensation expense in the period of the change until settlement. No SARs were exercised in the nine months ended September 30, 2010 or 2009. Other liability-classified awards include share-based performance awards. Compensation costs for these plans are recognized and accrued as performance conditions are met, based on the current share price.

The intrinsic value of all of IHC s share-based liabilities paid in the nine months ended September 30, 2010 and 2009 was $54,000 and $35,000, respectively. Included in Other Liabilities on the Company s Condensed Consolidated Balance Sheets at September 30, 2010 and December 31, 2009 are liabilities of $136,000 and $58,000, respectively, pertaining to IHC s SARs and share-based performance awards.

B)

AMIC Share-Based Compensation Plans

Total AMIC share-based compensation expense was $18,000 and $44,000, respectively, for the three months ended September 30, 2010 and the period between the Acquisition Date and September 30, 2010. Related tax benefits of $8,000 and $18,000, respectively, were recognized for the three months ended September 30, 2010 and the period between the Acquisition Date and September 30, 2010.

Under the terms of the AMIC s stock-based compensation plan, option exercise prices are equal to the quoted market price of the shares at the date of grant; option terms are ten years; and vesting periods range from three to four years. AMIC may also grant shares of restricted stock, stock appreciation rights and share-based performance awards. Restricted shares are valued at the quoted market price of the shares at the date of grant, and have a three year vesting period. At September 30, 2010, there were 6,537,222 shares available for future stock-based compensation grants under the AMIC stock incentive plan.

Stock Options

The following table summarizes information regarding AMIC s outstanding and exercisable options for the period between the Acquisition Date and September 30, 2010:

	Shares	Weighted-Average
	Under Option	Exercise Price
March 5, 2010		

355,900

$

10.00

Granted

13,334

4.60

Exercised

10,000

4.50

September 30, 2010

359,234

9.95

The following table summarizes information regarding AMIC s outstanding and exercisable options as of September 30, 2010:

	Outstanding	Exercisable
Number of options	359,234	338,705
Weighted average exercise price per share	$ 9.95	$ 10.20
Aggregate intrinsic value for all options	$ 11,439	$

10,639

Weighted average contractual term remaining

3.6 years

3.3 years

The fair value of an option award is estimated on the date of grant using the Black-Scholes option valuation model. The weighted average grant-date fair-value of options granted during the period between the Acquisition Date and September 30, 2010 was $2.79 per share. The assumptions set forth in the table below were used to value the stock options granted during the period between the Acquisition Date and September 30, 2010:

Weighted-average risk-free interest rate	3.69%
Annual dividend rate per share	$ -
Weighted-average volatility factor of the Company's common stock	

	45.0%
Weighted-average expected term of options	5 years

Compensation expense of $14,000 and $33,000 was recognized for the three months ended September 30, 2010 and the period between the Acquisition Date and September 30, 2010, respectively, for the portion of the grant-date fair value of AMIC s stock options vesting during those periods.

AMIC received cash proceeds of $45,000 upon the exercise of 10,000 options with an intrinsic value of $1,000 during the period between the Acquisition Date and September 30, 2010.

As of September 30, 2010, the total unrecognized compensation expense related to AMIC s non-vested options was $64,000 which will be recognized over the remaining requisite service periods.

Restricted Stock

AMIC issued 12,000 restricted stock awards in the second quarter of 2008, with a weighted average grant-date fair value of $6.92 per share. No restricted stock awards were issued in 2010. The total fair value of AMIC s restricted stock that vested during the period between the Acquisition Date and September 30, 2010 was $13,000. Restricted stock expense was $4,000 and $11,000 for the three months ended September 30, 2010 and the period between the Acquisition Date and September 30, 2010, respectively.

The following table summarizes AMIC s restricted stock activity for the period between the Acquisition Date and September 30, 2010:

	No. of
	Weighted-Average
	Non-vested
	Grant-Date
	Shares
	Fair Value

March 5, 2010

6,333

$

6.92

Vested

(2,500)

$

6.92

Forfeited

(1,333)

$

6.92

	September 30, 2010
	2,500
	$
	6.92

As of September 30, 2010, there was approximately $12,000 of total unrecognized compensation expense related to AMIC s non-vested restricted stock which will be recognized over the remaining requisite service periods.

Note 11.

Debt

On August 22, 2010, the Company made a $1,500,000 principal debt repayment in accordance with the terms of its amortizing term note.

Note 12.

Income Taxes

The provision for income taxes shown in the Condensed Consolidated Statements of Operations was computed based on the Company's actual results which approximate the effective tax rate expected to be applicable for the balance of the current fiscal year in accordance with consolidated life/non-life group income tax regulations. Such regulations adopt a subgroup method in determining consolidated taxable income, whereby taxable income is determined separately for the life insurance company group and the non-life insurance company group.

The deferred income tax expense allocated to stockholders' equity (principally for net unrealized gains on investment securities) for the nine months ended September 30, 2010 was $9,626,000, representing the decrease in the related net deferred tax liability to $5,658,000 at September 30, 2010 from a tax asset of $3,968,000 at December 31, 2009.

At September 30, 2010, AMIC, had net operating loss carryforwards of approximately $273,400,000 for federal income tax purposes which expire between 2019 and 2029. The federal deferred tax asset relative to AMIC included in other assets on IHC s Condensed Consolidated Balance Sheet at September 30, 2010 was $10,165,000, net of a valuation allowance of $86,400,000. AMIC continues to file its own separate income tax return and is not included in the consolidated tax return of IHC.

Note 13.

Supplemental Disclosures of Cash Flow Information

Tax payments, net of tax refunds, were $467,000 during the nine months ended September 30, 2010. Tax refunds, net of tax payments, were $335,000 during the nine months ended September 30, 2009

Cash payments for interest were $1,431,000 and $2,380,000 during the nine months ended September 30, 2010 and 2009, respectively.

Note 14.

Comprehensive Income

The components of comprehensive income (loss) include: (i) net income or loss reported in the Condensed Consolidated Statements of Operations; (ii) the after-tax net unrealized gains and losses on investment securities available for sale, including the subsequent increases and decreases in fair value of available-for-sale securities previously impaired; and (iii) the non-credit related component of other-than-temporary impairments of fixed maturities, net of tax.

Comprehensive income for the three months and nine months ended September 30, 2010 and 2009 is summarized as follows (in thousands):

	Three Months Ended
	Nine Months Ended

	September 30,		**September 30,**	
	2010	**2009**	**2010**	**2009**
Net income	$ 5,030	$ 1,930		

$

23,543

$

6,888

Unrealized gains arising

during the period, net of income taxes

8,268

23,907

17,199

52,223

Comprehensive income
13,298
25,837
40,742
59,111
Comprehensive (income) losses attributable to

noncontrolling interest

(610)

(5)

(1,391)

15

Comprehensive income attributable to IHC

$

12,688

$
25,832
$
39,351
$
59,126

Unrealized gains arising during the three months and nine months ended September 30, 2010 include the reclassification to earnings of $410,000 of the non-credit related component of previously recorded other-than-temporary impairments on securities that were sold during the period, net of $221,000 tax. No losses for other-than-temporary impairments of fixed maturities were recognized in other comprehensive income during the three months or nine months ended September 30, 2010.

Note 15.

Segment Reporting

The Insurance Group principally engages in the life and health insurance business. Information by business segment for the three months and nine months ended September 30, 2010 and 2009 is presented below (in thousands):

	Three Months Ended
	Nine Months Ended
	September 30,
	September 30,
	2010
	2009
	2010
	2009

Revenues:

Medical Stop-Loss (A)

$

34,187

$

31,222

$

99,533

$

103,536

Fully Insured Health (B)

37,629

28,184

105,981

87,695

Group disability, life, annuities and DBL (C)

16,626

16,720

50,416

49,578

Individual life, annuities and other

15,858

15,379

44,027

46,164

Corporate

(323)

454

27,483

1,108

103,977

91,959

327,440

288,081

Net realized investment gains

4,030

553

6,013

3,480

Other-than-temporary impairment losses, net

(132)

-

(2,797)

(271)

$

107,875

$

92,512

$

330,656

$

291,290

Income from Continuing Operations

Before Income Taxes:

Medical Stop-Loss (A)	$	955	$	772	$	3,407	$	3,548
Fully Insured Health (B) (D)		888		(3,016)				

1,967

(3,766)

Group disability, life, annuities and DBL [C]

3,704

1,701

5,018

5,082

Individual life, annuities and other

754

3,248

1,648

5,049

Corporate

(2,504)

(464)

22,850

(1,988)

3,797

2,241

34,890

7,925

Net realized investment gains

4,030

553

6,013

3,480

Other-than-temporary impairment losses,

net

(132)

-

(2,797)

(271)

Interest expense

(499)

(701)

(1,447)

(2,232)

$

7,196

$

2,093

$

36,659

$

8,902

(A)

The amount includes equity income from AMIC (prior to its acquisition) of $40,000 for the three months ended September 30, 2009, and $14,000 and $693,000 for the nine months ended September 30, 2010 and 2009, respectively.

(B)

The amount includes equity income from AMIC (prior to its acquisition) of $25,000 for the three months ended September 30, 2009 and $244,000 and $211,000 for nine months ended September 30, 2010 and 2009, respectively.

(C)

The amount includes equity income from AMIC (prior to its acquisition) of $11,000 for the three months ended September 30, 2009, and $22,000 and $100,000 for nine months ended September 30, 2010 and 2009, respectively.

(D)

The Fully Insured Health segment includes amortization of intangible assets recorded as a result of purchase accounting for the recent acquisitions. Total amortization expense was $611,000 and $619,000 for the three months ended September 30, 2010 and 2009, respectively, and $1,771,000 and $1,846,000 for the nine months ended September 30, 2010 and 2009, respectively. Amortization expense for the other segments is insignificant.

30

ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL

CONDITION AND RESULTS OF OPERATIONS

The following discussion of the financial condition and results of operations of Independence Holding Company ("IHC") and its subsidiaries (collectively, the "Company") should be read in conjunction with, and is qualified in its entirety by reference to, the Consolidated Financial Statements of the Company and the related Notes thereto appearing in our annual report on Form 10-K for the fiscal year ended December 31, 2009, as filed with the Securities and Exchange Commission, and our unaudited Condensed Consolidated Financial Statements and related Notes thereto appearing elsewhere in this quarterly report.

Overview

Independence Holding Company, a Delaware corporation ("IHC"), is a holding company principally engaged in the life and health insurance business through: (i) its wholly owned insurance companies, Standard Security Life Insurance Company of New York ("Standard Security Life") and Madison National Life Insurance Company, Inc. ("Madison National Life"); (ii) its majority owned insurance company, Independence American Insurance Company (Independence American); and (iii) its marketing and administrative companies, including IHC Administrative Services, Inc., managing general underwriters ("MGUs") in which it owns a significant voting interest, IHC Health Solutions, Inc. (IHC Health Solutions), and Actuarial Management Corporation (AMC). These companies are sometimes collectively referred to as the "Insurance Group," and IHC and its subsidiaries (including the Insurance Group) are sometimes collectively referred to as the "Company." IHC also owns a 50.1% interest in American Independence Corp. (AMIC).

While management considers a wide range of factors in its strategic planning and decision-making, underwriting profit is consistently emphasized as the primary goal in all decisions as to whether or not to increase our retention in a core line, expand into new products, acquire an entity or a block of business, or otherwise change our business model. Management's assessment of trends in healthcare and morbidity, with respect to medical stop-loss, fully insured medical, disability and New York State short-term statutory disability benefit product ("DBL"); mortality rates with respect to life insurance; and changes in market conditions in general play a significant role in determining the rates charged, deductibles and attachment points quoted, and the percentage of business retained. IHC also seeks transactions that permit it to leverage its vertically integrated organizational structure by generating fee income from production and administrative operating companies as well as risk income for its carriers and profit commissions. Management has always focused on managing the costs of its operations and providing its insureds with the best cost containment tools available.

The following is a summary of key performance information and events:

The results of operations for the three months and nine months ended September 30, 2010 and 2009 are summarized as follows (in thousands):

Three Months Ended
Nine Months Ended
September 30,
September 30,
2010
2009
2010
2009

Revenues	$ 107,875	$ 92,512	$ 330,656	$ 291,290
Expenses	100,679	90,419	293,997	282,388

Income from continuing operations

before income taxes

7,196

2,093

36,659

8,902

Income taxes

2,145

212

12,913

1,709

Income from continuing operations

5,051

1,881

23,746

7,193

Discontinued operations:

Income (loss) from discontinued operations

(21)

49

(203)

(305)

Net income

5,030

1,930

23,543

6,888

(Income) loss
from
noncontrolling
interests

in subsidiaries

(610)

(5)

(1,391)

15

Net income attributable to IHC

$

4,420

$

1,925

$

22,152

$

6,903

.

Income from continuing operations increased $3.2 million to $5.1 million for the three months ended September 30, 2010 from $1.9 million for the three months ended September 30, 2009. Income from continuing operations increased $16.5 million to $23.7 million for the nine months ended September 30, 2010 from $7.2 million for the nine months ended September 30, 2009 primarily due to the $16.8 million after-tax gain on the bargain purchase of AMIC (see Note 2 of Notes to Condensed Consolidated Financial Statements);

.

Consolidated investment yields (on an annualized basis) of 4.9% and 4.6%, respectively, for the three months and nine months ended September 30, 2010 compared to 5.4% and 5.2% for the respective periods in 2009;

.

Revenues of $107.9 million and $330.7 million for the three months and nine months ended September 30, 2010, respectively, representing increases of 16.6% and 13.5% over the respective three-month and nine-month periods in 2009; and

.

Book value of $15.81 per common share, representing a 20.1% increase from December 31, 2009, primarily reflecting net income (including the gain on bargain purchase) and net unrealized gains on securities for the nine months ended September 30, 2010.

32

The following is a summary of key performance information by segment:

.

The Medical Stop-Loss segment reported income from continuing operations before taxes of $1.0 million and $.8 million for the three months ended September 30, 2010 and 2009, respectively, and reported income from continuing operations of $3.4 million and $3.5 million for the nine months ended September 30, 2010 and 2009, respectively. The increase in the quarterly results is primarily attributable to the consolidation of AMIC results in addition to business produced by a managing general underwriter acquired in 2010 for which there are no comparable amounts in 2009. For the nine months ended September 30, 2010, the aforementioned increases were offset by the cancellation of underperforming managing general underwriters and market conditions;

o

Premiums earned increased $.9 million for three months ended September 30, 2010 and decreased $8.6 million for the nine months ended September 30, 2010 when compared to the same periods in 2009. Excluding $9.6 million and $23.3 million of earned premiums related to the consolidation of AMIC s results for the three months and nine months ended September 30, 2010, respectively, premiums earned decreased $8.7 million and $31.9 million, respectively, due to reduced production volume for the reasons stated above;

o

Combined ratios for the three months and nine months ended September 30, 2010 include reported stop-loss combined ratios from AMIC of 98.3% and 100.4%, respectively, as adjusted for purchase accounting;

o

Underwriting experience for the Medical Stop-Loss segment, as indicated by its GAAP combined ratios, are as follows for the periods indicated (in thousands):

Three Months Ended
Nine Months Ended
September 30,
September 30,
2010
2009
2010
2009

Premiums Earned

$

30,730

$

29,832

$

90,526

$

99,121

Insurance Benefits, Claims & Reserves

22,081

22,321

65,355

71,684

Expenses

8,700

7,523

24,109

26,455

Loss Ratio(A)

71.9%

74.8%

72.2%

72.3%

Expense Ratio [B]	Combined Ratio [C]
28.3%	100.2%
25.2%	100.0%
26.6%	98.8%
26.7%	99.0%

(A)

Loss ratio represents insurance benefits, claims and reserves divided by premiums earned.

(B)

Expense ratio represents net commissions (including profit commissions), administrative fees, premium taxes and other underwriting expenses divided by premiums earned.

(C)

Combined ratio is equal to the sum of the loss ratio and the expenses ratio.

.

The Fully Insured Health segment reported $.9 million of income from continuing operations before taxes for the three months ended September 30, 2010 compared to losses before taxes of $3.0 million for the three months ended September 30, 2009. For the nine months ended September 30, 2010, the Fully Insured Health segment reported $2.0 million of income from continuing operations before tax as compared to losses of $3.8 million for the same period in 2009;

o

Fee and other income decreased $.6 million and $3.2 million for the three months and nine months ended September 30, 2010, respectively, as compared to the same periods in 2009.

Excluding AMIC fee and other income of $.3 million and $1.0 million, respectively, fee and other income decreased by $.9 million and $4.2 million, respectively, primarily due to a decrease in non-IHC carrier business administered by IHC Administrative Services and reduced profit commissions from the comparable 2009 period. The Company also experienced a decrease in general expenses due to its lower volume of business;

o

Premiums earned increased $9.8 million and $21.0 million for the three months and nine months ended September 30, 2010, respectively, over the comparable periods in 2009. Excluding AMIC premiums of $7.4 million and $18.1 million during these respective periods, earned premiums increased $2.4 million for the three months ended September 30, 2010 and increased $2.9 million for the nine months ended September 30, 2010 compared to the prior year;

o

Underwriting experience for the Fully Insured segment, as indicated by its GAAP combined ratios, for the three months and nine months ended September 30, 2010 and 2009 is as follows (in thousands):

Three Months Ended
Nine Months Ended

	September 30,
	September 30,
	2010
	2009
	2010
	2009
Premiums Earned	
	$
	30,920

$

21,109

$

84,428

$

63,362

Insurance
Benefits,
Claims &
Reserves

21,004

16,225

57,371

44,802

Expenses

9,168

6,038

24,506

19,120

Loss Ratio	
	67.9%
	76.9%
	68.0%
	70.7%
Expense Ratio	
	29.7%
	28.6%
	29.0%

30.2%

Combined Ratio

97.6%

105.5%

97.0%

100.9%

o

The underwriting expense ratio decreased primarily as a result of a decrease in profit commission and other general expenses in 2010;

.

Income before taxes from the Group disability, life, annuities and DBL segment increased $2.0 million for the three months ended September 30, 2010 and remained flat for the nine months ended September 30, 2010 compared to the same periods in 2009. The LTD line experienced higher profitablilty in both the three months and nine months ended September 30, 2010, which, on a year to date basis, was offset by higher death claims experienced by group term life lines in the first quarter of 2010.

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Income before taxes from the Individual life, annuities and other segment decreased $2.4 million and $3.4 million for the three months and nine months ended September 30, 2010, respectively, compared to the same periods in 2009 primarily as a result of the commutation of reserves in the third quarter of 2009 and decreased investment income in 2010;

.

Income before taxes from the Corporate segment decreased $2.0 million for the three months ended September 30, 2010 compared to 2009 due to lower partnership income in 2010 and higher expenses; and increased $24.9 million for the nine months ended September 30, 2010 over 2009 primarily due to the inclusion of a $27.8 million gain as a result of the March 2010 acquisition of a controlling interest in AMIC;

.

Net realized investment gains were $4.0 million and $6.0 million for the three months and nine months ended September 30, 2010, respectively, compared to $.6 million and $3.5 million for the comparable periods in 2009. Other-than-temporary impairment losses for the three months and nine months ended September 30, 2010 were $.1 million and $2.8 million, respectively, compared to $.3 million for the nine months ended September 30, 2009. No other-than-temporary impairment losses were recorded in the three months ended September 30, 2009, and;

.

Premiums by principal product for the three months and nine months ended September 30, 2010 and 2009 are as follows (in thousands):

	Three Months Ended
	Nine Months Ended
	September 30,
	September 30,

Gross Direct and Assumed Earned Premiums:	**2010**	**2009**	**2010**	**2009**
Medical Stop-Loss	$ 40,440	$		

47,920

$

122,040

$

156,367

Fully Insured Health

52,139

47,538

155,685

142,970

Group disability, life, annuities and DBL

25,744

26,845

78,588

78,328

Individual, life, annuities and other

8,655

7,403

24,395

22,960

$

126,978

$

129,706

$

380,708

$

400,625

Three Months Ended

Nine Months Ended

September 30,

September 30,

Net Premiums Earned:

2010

2009

2010

2009

Medical Stop-Loss	$ 30,730	$ 29,832	$ 90,526	$ 99,121
Fully Insured Health	30,920	21,109	84,428	63,362
Group disability, life, annuities and DBL	14,127	14,178	42,723	41,993
Individual, life, annuities and other				

7,482

6,623

21,080

20,780

$

83,259

$

71,742

$

238,757

$

225,256

CRITICAL ACCOUNTING POLICIES

The accounting and reporting policies of the Company conform to U.S. generally accepted accounting principles ("GAAP"). The preparation of the Condensed Consolidated Financial Statements in conformity with GAAP requires the Company's management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. A summary of the Company's significant accounting policies and practices is provided in Note 1 of the Notes to the Consolidated Financial Statements included in Item 8 of the Annual Report on Form 10-K for the fiscal year ended December 31, 2009. Management has identified the accounting policies related to *Insurance Premium Revenue Recognition and Policy Charges, Insurance Reserves, Deferred Acquisition Costs, Investments, Goodwill and Other Intangible Assets, and Deferred Income Taxes* as those that, due to the judgments, estimates and assumptions inherent in those policies, are critical to an understanding of the Company's Consolidated Financial Statements and this Management's Discussion and Analysis. A full discussion of these policies is included under the heading, Critical Accounting Policies in Item 7 of the Annual Report on Form 10-K for the fiscal year ended December 31, 2009. During the nine months ended September 30, 2010, there were no additions to or changes in the critical accounting policies disclosed in the 2009 Form 10-K except for the recently adopted accounting standards discussed in Note 1(C) of the Notes to Condensed Consolidated Financial Statements.

Results of Operations for the Three Months Ended September 30, 2010 Compared to the Three Months Ended September 30, 2009

Income from continuing operations was $5.1 million for the three months ended September 30, 2010, an increase of $3.2 million compared to $1.9 million for the three months ended September 30, 2009. The Company's income from continuing operations before taxes increased $5.1 million to $7.2 million for the three months ended September 30, 2010 from $2.1 million for the three months ended September 30, 2009. Information by business segment for the three months ended September 30, 2010 and 2009 is as follows:

Equity

Benefits,

Amortization

Selling,

Net

Income

Fee and

Claims

of Deferred

General

Premiums

Investment

From

Other

and

Acquisition

And

September 30, 2010

Earned

Income

AMIC

Income

Reserves

Costs

Administrative

Total
(In thousands)
Medical Stop-Loss
$
30,730
1,407
-
2,050

22,081

-

11,151

$

955

Fully Insured Health

30,920

384

-

6,325

21,004

7

15,730

888

Group disability,