KANSAS CITY LIFE INSURANCE CO
Form 10-Q
April 27, 2012
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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 March 31, 2012 or

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

For the transition period from__________to__________

Commission File Number 2-40764

KANSAS CITY LIFE INSURANCE COMPANY

(Exact name of registrant as specified in its charter)

Missouri	44-0308260
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3520 Broadway, Kansas City, Missouri	64111-2565
(Address of principal executive offices)	(Zip Code)

816-753-7000

Registrant s telephone number, including area code

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 x 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨ 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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Common Stock, $1.25 par	11,309,477 shares
Class	Outstanding March 31, 2012

KANSAS CITY LIFE INSURANCE COMPANY

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Part I. Financial Information

Item 1. Financial Statements

Amounts in thousands, except share data, or as otherwise noted

Kansas City Life Insurance Company

Consolidated Balance Sheets

	March 31 2012 (Unaudited)	December 31 2011
ASSETS		
Investments:		
Fixed maturity securities available for sale, at fair value	$ 2,770,777	$ 2,682,142
Equity securities available for sale, at fair value	37,245	36,689
Mortgage loans	573,702	601,923
Real estate	98,595	127,962
Policy loans	79,574	80,375
Short-term investments	54,293	49,316
Other investments	3,113	3,364
Total investments	3,617,299	3,581,771
Cash	5,172	10,436
Accrued investment income	38,981	34,705
Deferred acquisition costs	179,987	181,564
Reinsurance receivables	191,214	189,885
Property and equipment	22,419	22,671
Other assets	60,576	60,601
Separate account assets	341,250	316,609
Total assets	$ 4,456,898	$ 4,398,242
LIABILITIES		
Future policy benefits	$ 880,071	$ 879,015
Policyholder account balances	2,105,428	2,089,452
Policy and contract claims	33,836	36,511
Other policyholder funds	151,005	152,125
Other liabilities	217,661	213,825
Separate account liabilities	341,250	316,609
Total liabilities	3,729,251	3,687,537
STOCKHOLDERS EQUITY		
Common stock, par value $1.25 per share		
Authorized 36,000,000 shares, issued 18,496,680 shares	23,121	23,121
Additional paid in capital	41,106	41,101
Retained earnings	797,305	780,918
Accumulated other comprehensive income	30,636	30,086
Treasury stock, at cost (2012 - 7,187,203 shares; 2011 - 7,187,315 shares)	(164,521)	(164,521)

Total stockholders equity	727,647	710,705
Total liabilities and stockholders equity	$ 4,456,898	$ 4,398,242

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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Kansas City Life Insurance Company

Consolidated Statements of Comprehensive Income

	Quarter Ended March 31	
	2012	2011
	(Unaudited)	
REVENUES		
Insurance revenues:		
Premiums, net	$ 32,704	$ 33,625
Contract charges	25,133	26,234
Total insurance revenues	57,837	59,859
Investment revenues:		
Net investment income	44,209	45,391
Net realized investment gains, excluding impairment losses	15,837	1,012
Net impairment losses recognized in earnings:		
Total other-than-temporary impairment losses	(268)	(269)
Portion of impairment losses recognized in other comprehensive income	108	58
Net impairment losses recognized in earnings	(160)	(211)
Total investment revenues	59,886	46,192
Other revenues	2,185	2,408
Total revenues	119,908	108,459
BENEFITS AND EXPENSES		
Policyholder benefits	38,470	45,274
Interest credited to policyholder account balances	20,558	20,481
Amortization of deferred acquisition costs	7,901	9,584
Operating expenses	23,962	25,865
Total benefits and expenses	90,891	101,204
Income before income tax expense	29,017	7,255
Income tax expense	9,576	2,464
NET INCOME	$ 19,441	$ 4,791
Comprehensive income, net of taxes:		
Change in net unrealized gains on securities available for sale	$ 2,092	$ (625)
Change in future policy benefits	(1,467)	720
Change in policyholder account balances	(75)	7
Other comprehensive income	550	102
COMPREHENSIVE INCOME	$ 19,991	$ 4,893

Basic and diluted earnings per share:		
Net income	$ 1.72	$ 0.42

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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Kansas City Life Insurance Company

Consolidated Statement of Stockholders Equity

	Quarter Ended March 31, 2012 (Unaudited)
COMMON STOCK, beginning and end of period	$ 23,121
ADDITIONAL PAID IN CAPITAL	
Beginning of period	41,101
Excess of proceeds over cost of treasury stock sold	5
End of period	41,106
RETAINED EARNINGS	
Beginning of period	780,918
Net income	19,441
Stockholder dividends of $0.27 per share	(3,054)
End of period	797,305
ACCUMULATED OTHER COMPREHENSIVE INCOME, net of taxes	
Beginning of period	30,086
Other comprehensive income	550
End of period	30,636
TREASURY STOCK, at cost	
Beginning of period	(164,521)
Cost of 103 shares acquired	(3)
Cost of 215 shares sold	3
End of period	(164,521)
TOTAL STOCKHOLDERS EQUITY	$ 727,647

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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Kansas City Life Insurance Company

Consolidated Statements of Cash Flows

	Quarter Ended March 31	
	2012	2011
	(Unaudited)	
OPERATING ACTIVITIES		
Net income	$ 19,441	$ 4,791
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Amortization of investment premium and discount	995	939
Depreciation	828	645
Acquisition costs capitalized	(9,652)	(8,743)
Amortization of deferred acquisition costs	7,901	9,584
Realized investment gains	(15,677)	(801)
Changes in assets and liabilities:		
Reinsurance receivables	(1,329)	(2,220)
Future policy benefits	(1,200)	(2,962)
Policyholder account balances	(1,714)	(6,381)
Income taxes payable and deferred	5,976	1,577
Other, net	(9,304)	3,992
Net cash provided (used)	(3,735)	421
INVESTING ACTIVITIES		
Purchases of investments:		
Fixed maturity securities	(128,592)	(78,118)
Equity securities	(705)	(1,030)
Mortgage loans	(11,292)	(15,472)
Real estate	(2,656)	(2,900)
Policy loans	(3,460)	(3,450)
Sales of investments:		
Fixed maturity securities	6,250	10,143
Equity securities	150	201
Real estate	47,328	-
Net purchases of short-term investments	(4,977)	(7,517)
Maturities, calls, and principal paydowns of investments:		
Fixed maturity securities	40,036	64,114
Mortgage loans	38,954	19,864
Policy loans	4,261	4,822
Net disposition (acquisition) of property and equipment	(72)	40
Net cash used	(14,775)	(9,303)

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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Kansas City Life Insurance Company

Consolidated Statements of Cash Flows (Continued)

	Quarter Ended March 31	
	2012	2011
	(Unaudited)	
FINANCING ACTIVITIES		
Deposits on policyholder account balances	$ 61,463	$ 57,464
Withdrawals from policyholder account balances	(43,661)	(47,888)
Net transfers from separate accounts	1,358	871
Change in other deposits	(2,865)	921
Cash dividends to stockholders	(3,054)	(3,096)
Net disposition of treasury stock	5	7
Net cash provided	13,246	8,279
Decrease in cash	(5,264)	(603)
Cash at beginning of year	10,436	5,445
Cash at end of period	$ 5,172	$ 4,842
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	$ -	$ -
Income taxes	3,000	2,000

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited)

1. Nature of Operations and Significant Accounting Policies

Basis of Presentation

The unaudited interim consolidated financial statements and the accompanying notes to these unaudited interim consolidated financial statements of Kansas City Life Insurance Company include the accounts of the consolidated entity (the Company), which primarily consists of three life insurance companies. Kansas City Life Insurance Company (Kansas City Life) is the parent company. Sunset Life Insurance Company of America (Sunset Life) and Old American Insurance Company (Old American) are wholly-owned subsidiaries.

The unaudited interim consolidated financial statements have been prepared on the basis of U.S. generally accepted accounting principles (GAAP) for interim financial reporting and with the instructions to Form 10-Q and Regulations S-K, S-X, and other applicable regulations. Accordingly, they do not include all of the disclosures required by GAAP for complete financial statements. As such, these unaudited interim consolidated financial statements should be read in conjunction with the Company s 2011 Form 10-K as filed with the Securities and Exchange Commission. Management believes that the disclosures are adequate to make the information presented not misleading, and all normal and recurring adjustments necessary to present fairly the financial position at March 31, 2012 and the results of operations for all periods presented have been made. The results of operations for any interim period are not necessarily indicative of the Company s operating results for a full year. Significant intercompany transactions have been eliminated in consolidation and certain immaterial reclassifications have been made to prior period results to conform with the current period s presentation.

The preparation of the unaudited interim consolidated financial statements requires management of the Company to make estimates and assumptions relating to the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the unaudited interim consolidated financial statements, and the reported amounts of revenue and expenses during the period. These estimates are inherently subject to change and actual results could differ from these estimates.

Immaterial Correction of Errors

During the first quarter of 2012, the Company identified an error related to the amortization period for unrecognized actuarial gains and losses for its pension plan of $2.0 million before applicable income taxes and an after-tax impact of $1.3 million to net income and stockholders equity, which had been previously recorded during 2011. Management has evaluated this error both quantitatively and qualitatively, concluding that the error is not material to the consolidated financial statements. Please refer to Note 11 Pensions and Other Postretirement Benefits for additional information.

During 2011, the Company identified errors related to the classification of amounts reported in the Consolidated Statement of Cash Flows. The Company has revised the Consolidated Statement of Cash Flows for the period ended March 31, 2011. The changes resulted in an increase of $1.9 million to cash flows from operating activities and a decrease of the same amount to cash flows from financing activities. This change did not impact net income, the balance sheet, or stockholders equity for the period. Management has evaluated this error both quantitatively and qualitatively, concluding that this correction is not material to the consolidated financial statements.

Significant Accounting Policies

No significant updates or changes to these policies occurred during the quarter ended March 31, 2012.

For a full discussion of these significant accounting policies, please refer to the Company s 2011 Form 10-K.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

2. New Accounting Pronouncements

For a full discussion of new accounting pronouncements and other regulatory activity and their impact on the Company, please refer to the Company s 2011 Form 10-K.

Accounting Pronouncements Adopted During 2012

In October 2010, the FASB issued guidance that modifies the types of costs incurred by insurance entities that can be capitalized when issuing or renewing insurance contracts. The guidance defines allowable deferred acquisition costs as incremental or directly related to the successful acquisition of new or renewal contracts. In addition, certain costs related directly to acquisition activities performed by the insurer, such as underwriting and policy issuance, are also deferrable. This guidance also defines the considerations for the deferral of direct-response advertising costs. This guidance became effective for interim and annual periods beginning after December 15, 2011, with either prospective or retrospective application permitted. The Company adopted this new guidance prospectively on January 1, 2012. Please refer to Note 7 Change in Accounting Principle for additional information.

In April 2011, the FASB issued new guidance concerning repurchase agreements. This guidance amends previously provided guidance as to when an entity may or may not recognize a sale upon the transfer of financial assets subject to repurchase agreements. That determination was previously based upon whether the entity has maintained effective control over the transferred financial assets. One of the relevant considerations for assessing effective control is the transferor s ability to repurchase or redeem financial assets before maturity. This update removes the assessment of effective control. The update became effective for interim or annual periods beginning on or after December 15, 2011. The Company adopted this new guidance on January 1, 2012 with no material impact to the consolidated financial statements.

In May 2011, the FASB issued new guidance concerning fair value measurements and disclosure. The new guidance is the result of joint efforts by the FASB and the International Accounting Standards Board (IASB) to develop a single, converged fair value framework on how to measure fair value and the necessary disclosures concerning fair value measurements. The guidance became effective for interim and annual periods beginning after December 15, 2011. The Company adopted this new guidance on January 1, 2012 with no material impact to the consolidated financial statements.

In June 2011, the FASB issued new guidance regarding the manner in which entities present comprehensive income in the financial statements. This guidance removes the previous presentation options and provides that entities must report comprehensive income in either a continuous statement of comprehensive income or two separate but consecutive statements. This guidance also includes the requirement for reclassification adjustments for items that are reclassified from other comprehensive income to net income to be presented on the face of the financial statements. This guidance does not change the items that must be reported in other comprehensive income nor does it require any disclosures in addition to those previously required. In December 2011, the FASB deferred the effective date for amendments to the presentation of reclassification adjustments. The guidance became effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company adopted this new guidance on January 1, 2012 with no material impact to the consolidated financial statements.

All other new accounting standards and updates of existing standards issued through the date of this filing were considered by management and did not relate to accounting policies and procedures pertinent to the Company at this time.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

3. Investments

Fixed Maturity and Equity Securities Available for Sale

Securities by Asset Class

The following table provides amortized cost and fair value of securities by asset class at March 31, 2012.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. Government	$ 118,343	$ 11,886	$ 58	$ 130,171
Federal agencies [1]	22,206	3,075	1	25,280
Federal agency issued residential mortgage-backed securities [1]	103,397	9,756	-	113,153
Subtotal	243,946	24,717	59	268,604
Corporate obligations:				
Industrial	476,199	41,500	2,312	515,387
Energy	165,977	19,033	144	184,866
Communications and technology	195,564	17,497	209	212,852
Financial	313,231	18,598	2,483	329,346
Consumer	478,165	42,792	862	520,095
Public utilities	260,966	36,009	579	296,396
Subtotal	1,890,102	175,429	6,589	2,058,942
Corporate private-labeled residential mortgage-backed securities	163,020	2,425	9,238	156,207
Municipal securities	148,669	21,608	20	170,257
Other	109,840	3,846	8,768	104,918
Redeemable preferred stocks	11,735	337	223	11,849
Fixed maturity securities	2,567,312	228,362	24,897	2,770,777
Equity securities	35,504	1,890	149	37,245
Total	$ 2,602,816	$ 230,252	$ 25,046	$ 2,808,022

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table provides amortized cost and fair value of securities by asset class at December 31, 2011.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. Government	$ 120,593	$ 13,856	$ 12	$ 134,437
Federal agencies [1]	22,401	3,480	-	25,881
Federal agency issued residential mortgage-backed securities [1]	109,738	9,901	2	119,637
Subtotal	252,732	27,237	14	279,955
Corporate obligations:				
Industrial	444,030	43,710	860	486,880
Energy	152,580	19,131	-	171,711
Communications and technology	184,983	16,566	156	201,393
Financial	308,813	15,155	5,890	318,078
Consumer	452,962	43,788	263	496,487
Public utilities	259,609	38,094	1,366	296,337
Subtotal	1,802,977	176,444	8,535	1,970,886
Corporate private-labeled residential mortgage-backed securities	167,666	1,856	12,620	156,902
Municipal securities	150,267	18,316	61	168,522
Other	100,315	3,576	9,235	94,656
Redeemable preferred stocks	11,735	226	740	11,221
Fixed maturity securities	2,485,692	227,655	31,205	2,682,142
Equity securities	34,951	1,873	135	36,689
Total	$ 2,520,643	$ 229,528	$ 31,340	$ 2,718,831

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

Contractual Maturities

The following table provides the distribution of maturities for fixed maturity securities available for sale at March 31, 2012 and December 31, 2011. Expected maturities may differ from these contractual maturities since borrowers may have the right to call or prepay obligations.

	March 31, 2012		December 31, 2011	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 99,799	$ 101,794	$ 79,651	$ 81,212
Due after one year through five years	582,944	626,986	599,904	639,706
Due after five years through ten years	1,039,768	1,140,637	946,752	1,045,645

Due after ten years	484,594	528,887	486,126	532,927
Securities with variable principal payments	348,472	360,624	361,524	371,431
Redeemable preferred stocks	11,735	11,849	11,735	11,221
	$ 2,567,312	$ 2,770,777	$ 2,485,692	$ 2,682,142

Unrealized Losses on Investments

The Company reviews all security investments, with particular attention given to those having unrealized losses. Further, the Company specifically assesses all investments with greater than 10% declines in fair value below amortized cost and, in general, monitors all security investments as to ongoing risk. These risks are fundamentally evaluated through both a qualitative and quantitative analysis of the issuer. The Company also prepares a formal review document no less often than quarterly of all investments where fair value is less than 80% of amortized cost for six months or more and selected investments that have changed significantly from a previous period and that have a decline in fair value greater than 10% of amortized cost.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The Company has a policy and process in place to identify securities that could potentially have an impairment that is other-than-temporary (OTTI). This process involves monitoring market events and other items that could impact issuers. The Company considers relevant facts and circumstances in evaluating whether the impairment of a security is other-than-temporary. Relevant facts and circumstances considered are described in the Valuation of Investments section of Note 1 Nature of Operations and Significant Accounting Policies of the Company s 2011 Form 10-K.

To the extent the Company determines that a fixed maturity security is deemed to be other-than-temporarily impaired, the portion of the impairment that is deemed to be due to credit is charged to the Consolidated Statements of Comprehensive Income and the cost basis of the underlying investment is reduced. The portion of such impairment that is determined to be non-credit-related is deducted from net realized loss in the Consolidated Statements of Comprehensive Income and is reflected in other comprehensive income and accumulated other comprehensive income.

There are a number of significant risks and uncertainties inherent in the process of monitoring impairments, determining if an impairment is other-than-temporary and determining the portion of an other-than-temporary impairment that is due to credit. These risks and uncertainties are described in the Valuation of Investments section of Note 1 of the Company s 2011 Form 10-K.

Once a security is determined to have met certain of the criteria for consideration as being other-than-temporarily impaired, further information is gathered and evaluated pertaining to the particular security. If the security is an unsecured obligation, the additional research is a top-down approach with particular emphasis on the likelihood of the issuer to meet the contractual terms of the obligation. If the security is secured by an asset or guaranteed by another party, the value of the underlying secured asset or the financial ability of the third-party guarantor is evaluated as a secondary source of repayment. Such research is based upon a top-down approach, narrowing to the specific estimates of value and cash flow of the underlying secured asset or guarantor. If the security is a collateralized obligation, such as a mortgage-backed or other asset-backed instrument, research is also conducted to obtain and analyze the performance of the collateral relative to expectations at the time of acquisition and with regard to projections for the future. Such analyses are based upon historical results, trends, comparisons to collateral performance of similar securities, and analyses performed by third parties. This information is used to develop projected cash flows that are compared to the amortized cost of the security.

If a determination is made that an unsecured security, secured security, or security with a guaranty of payment by a third-party is other-than-temporarily impaired, an estimate is developed of the portion of such impairment that is due to credit. The estimate of the portion of impairment due to credit is based upon a comparison of ratings and maturity horizon for the security and relative historical default probabilities from one or more nationally recognized rating organizations. When appropriate for any given security, sector or period in the business cycle, the historical default probability is adjusted to reflect periods or situations of distress by adding to the default probability increments of standard deviations from mean historical results. The credit impairment analysis is supplemented by estimates of potential recovery values for the specific security, including the potential impact of the value of any secured assets, in the event of default. This information is used to determine the Company s best estimate, derived from probability-weighted cash flows.

The evaluation of loan-backed and similar asset-backed securities, particularly including residential mortgage-backed securities, with significant indications of potential other-than-temporary impairment requires considerable use of estimates and judgment. Specifically, the Company performs discounted cash flow projections on these securities to evaluate whether the value of the investment is expected to be fully realized. Projections of expected future cash flows are based upon considerations of the performance of the actual underlying assets, including historical delinquencies, defaults, severity of losses incurred, and prepayments, along with the Company s estimates of future results for these factors. The Company s estimates of future results are based upon actual historical performance of the underlying assets relative to historical, current and expected general economic conditions, specific conditions related to the underlying assets, industry data, and other factors that are believed to be relevant. If the present value of the projected expected future cash flows is determined to be below the Company s carrying value, the Company recognizes an other-than-temporary impairment on the portion of the carrying value that exceeds the projected expected future cash flows. To the extent that the loan-backed or other asset-backed securities were high quality investments at the time of acquisition, and they remain high quality investments and do not otherwise demonstrate characteristics of impairment, the Company performs other initial evaluations to determine whether other-than-temporary cash flow evaluations need to be performed.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The discounted future cash flow calculation typically becomes the primary determinant of whether any portion and to what extent an unrealized loss is due to credit on loan-backed and similar asset-backed securities with significant indications of potential other-than-temporary impairment. Such indications typically include below investment grade ratings and significant unrealized losses for an extended period of time, among other factors. The Company identified 17 non-U.S. Agency mortgage-backed securities that had such indications at March 31, 2012 and December 31, 2011. Discounted future cash flow analysis was performed for each of these securities to determine if any portion of the impairment was due to credit and deemed to be other-than-temporary. The discount rate used in calculating the present value of future cash flows was the investment yield at the time of purchase for each security. The initial default rates were assumed to remain constant over a 24-month time frame and grade down thereafter, reflecting the general perspective of a more stabilized residential housing environment in the future.

For loan-backed and similar asset-backed securities, the determination of any amount of impairment that is due to credit is based upon the present value of projected future cash flows being less than the amortized cost of the security. This amount is recognized as a realized loss in the Company s Consolidated Statements of Comprehensive Income and the carrying value of the security is written down by the same amount. The portion of an impairment that is determined not to be due to credit is recorded as a component of accumulated other comprehensive income in the Consolidated Balance Sheets.

As part of the required accounting for unrealized gains and losses, the Company also adjusts the deferred acquisition costs (DAC) and value of business acquired (VOBA) assets to recognize the adjustment to those assets as if the unrealized gains and losses from securities classified as available for sale actually had been realized.

The following table provides information regarding fixed maturity and equity security investments available for sale with unrealized losses by length of time at March 31, 2012.

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government	$ 3,798	$ 47	$ 907	$ 11	$ 4,705	$ 58
Federal agency issued residential mortgage-backed securities [1]	-	-	294	1	294	1
Subtotal	3,798	47	1,201	12	4,999	59
Corporate obligations:						
Industrial	33,204	2,312	-	-	33,204	2,312
Energy	10,594	144	-	-	10,594	144
Communications and technology	13,048	209	-	-	13,048	209
Financial	18,230	183	17,873	2,300	36,103	2,483
Consumer	49,311	665	4,537	197	53,848	862
Public utilities	7,169	327	11,924	252	19,093	579
Subtotal	131,556	3,840	34,334	2,749	165,890	6,589
Corporate private-labeled residential mortgage-backed securities	12,866	1,779	59,115	7,459	71,981	9,238
Municipal securities	-	-	882	20	882	20
Other	3,125	1,054	45,671	7,714	48,796	8,768
Redeemable preferred stocks	622	3	3,461	220	4,083	223
Fixed maturity securities	151,967	6,723	144,664	18,174	296,631	24,897
Equity securities	67	106	1,041	43	1,108	149

Total	$ 152,034	$ 6,829	$ 145,705	$ 18,217	$ 297,739	$ 25,046

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table provides information regarding fixed maturity and equity security investments available for sale with unrealized losses by length of time at December 31, 2011.

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government	$ -	$ -	$ 959	$ 12	$ 959	$ 12
Federal agency issued residential mortgage-backed securities [1]	649	-	294	2	943	2
Subtotal	649	-	1,253	14	1,902	14
Corporate obligations:						
Industrial	25,455	860	-	-	25,455	860
Communications and technology	7,239	156	-	-	7,239	156
Financial	51,273	2,107	16,402	3,783	67,675	5,890
Consumer	11,765	119	3,689	144	15,454	263
Public utilities	4,710	344	11,152	1,022	15,862	1,366
Subtotal	100,442	3,586	31,243	4,949	131,685	8,535
Corporate private-labeled residential mortgage-backed securities	41,734	2,668	61,864	9,952	103,598	12,620
Municipal securities	-	-	3,909	61	3,909	61
Other	9,257	921	47,146	8,314	56,403	9,235
Redeemable preferred stocks	2,939	115	3,056	625	5,995	740
Fixed maturity securities	155,021	7,290	148,471	23,915	303,492	31,205
Equity securities	69	104	1,054	31	1,123	135
Total	$ 155,090	$ 7,394	$ 149,525	$ 23,946	$ 304,615	$ 31,340

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

In addition, the Company also considers as part of its monitoring and evaluation process the length of time the fair value of a security is below amortized cost. At March 31, 2012, the Company had 82 issues in its investment portfolio of fixed maturity and equity securities with unrealized losses. Included in this total, 46 security issues were below cost for less than one year; 7 security issues were below cost for one year or more and less than three years; and 29 security issues were below cost for three years or more. At December 31, 2011 the Company had 85 issues in its investment portfolio of fixed maturity and equity securities with unrealized losses. Included in this total, 46 security issues were below cost for less than one year; 10 security issues were below cost for one year or more and less than three years; and 29 security issues were below cost for three years or more.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table provides the distribution of maturities for fixed maturity securities available for sale with unrealized losses at March 31, 2012 and December 31, 2011. Expected maturities may differ from these contractual maturities since borrowers may have the right to call or prepay obligations.

	March 31, 2012		December 31, 2011	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fixed maturity security securities available for sale:				
Due in one year or less	$ 935	$ 20	$ 2,953	$ 48
Due after one year through five years	18,682	392	42,416	2,120
Due after five years through ten years	117,755	3,983	64,772	2,616
Due after ten years	82,899	11,038	82,816	13,060
Total	220,271	15,433	192,957	17,844
Securities with variable principal payments	72,277	9,241	104,540	12,621
Redeemable preferred stocks	4,083	223	5,995	740
Total	$ 296,631	$ 24,897	$ 303,492	$ 31,205

The following table provides a reconciliation of credit losses recognized in earnings on fixed maturity securities held by the Company for which a portion of the other-than-temporary loss was recognized in other comprehensive income for the quarter ended March 31, 2012.

Credit losses on securities held at beginning of year in accumulated other comprehensive income	$ 13,559
Additions for credit losses not previously recognized in other-than-temporary impairment	28
Additions for increases in the credit loss for which an other-than-temporary impairment was previously recognized when there was no intent to sell the security before recovery of its amortized cost basis	132
Reductions for securities sold during the period (realized)	-
Reductions for securities previously recognized in other comprehensive income because of intent to sell the security before recovery of its amortized cost basis	-
Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	(4)
Credit losses on securities held at the end of year in accumulated other comprehensive income	$ 13,715

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

Realized Gains (Losses)

The following table provides detail concerning realized investment gains and losses for the first quarters ended March 31, 2012 and 2011.

	Quarter Ended March 31	
	2012	2011
Gross gains resulting from:		
Sales of investment securities	$ 313	$ 311
Investment securities called and other	208	863
Sales of real estate	15,170	-
Total gross gains	15,691	1,174
Gross losses resulting from:		
Investment securities called and other	(53)	(54)
Mortgage loans	(165)	(3)
Total gross losses	(218)	(57)
Change in allowance for potential future losses on mortgage loans	364	-
Amortization of DAC and VOBA	-	(105)
Net realized investment gains, exluding impairment losses	15,837	1,012
Net impairment losses recognized in earnings:		
Total other-than-temporary impairment losses	(268)	(269)
Portion of loss recognized in other comprehensive income	108	58
Net impairment losses recognized in earnings	(160)	(211)
Net realized investment gains	$ 15,677	$ 801

Proceeds From Sales of Investment Securities

The table below provides information regarding sales of fixed maturity and equity securities, excluding maturities and calls, for the quarters ended March 31.

	2012	2011
Proceeds	$ 6,400	$ 10,143
Gross realized gains	313	311
Gross realized losses	-	-

Mortgage Loans

The Company invests on an ongoing basis in commercial mortgage loans that are secured by real estate. The Company had 16% of its invested assets in commercial mortgage loans at March 31, 2012, compared to 17% at December 31, 2011. In addition to the subject collateral underlying the mortgage, the Company typically requires some amount of recourse from borrowers as another potential source of repayment. The recourse requirement is determined as part of the underwriting requirements of each loan. The average loan to value ratio for the overall portfolio was 45% and 46% at March 31, 2012 and December 31, 2011, respectively, and is based upon the appraisal of value at the time the loan was originated or acquired.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table summarizes the amount of mortgage loans held by the Company at March 31, 2012 and December 31, 2011, segregated by year of origination. Purchased loans are shown in the year acquired by the Company, although the individual loans may have been initially originated in prior years.

	March 31 2012	% of Total	December 31 2011	% of Total
Prior to 2002	$ 24,382	4%	$ 28,437	5%
2003	39,632	7%	42,112	7%
2004	29,460	5%	29,966	5%
2005	53,229	9%	54,802	9%
2006	41,420	7%	42,676	7%
2007	34,964	6%	35,323	6%
2008	38,940	7%	44,285	7%
2009	48,872	8%	50,574	8%
2010	108,278	19%	133,684	22%
2011	141,592	25%	142,913	24%
2012	15,418	3%	-	-
	576,187	100%	604,772	100%
Allowance for potential future losses	(2,485)		(2,849)	
Total	$ 573,702		$ 601,923	

The following table identifies mortgage loans by geographic location at March 31, 2012 and December 31, 2011.

	March 31 2012	% of Total	December 31 2011	% of Total
Pacific	$ 135,033	23%	$ 138,529	23%
West north central	106,635	19%	130,481	22%
West south central	100,445	17%	98,036	16%
Mountain	81,144	14%	82,029	14%
South atlantic	61,567	11%	63,125	10%
Middle atlantic	41,851	7%	42,112	7%
East north central	30,682	5%	30,482	5%
East south central	18,830	4%	19,978	3%
	576,187	100%	604,772	100%
Allowance for potential future losses	(2,485)		(2,849)	
Total	$ 573,702		$ 601,923	

The following table identifies mortgage loans by property type at March 31, 2012 and December 31, 2011. The Other category consists of apartments and retail properties.

	March 31 2012	% Total	December 31 2011	% Total
Industrial	$ 242,222	42%	$ 251,839	42%
Office	236,417	41%	243,885	40%
Medical	42,572	7%	43,089	7%
Other	54,976	10%	65,959	11%
	576,187	100%	604,772	100%
Allowance for potential future losses	(2,485)		(2,849)	
Total	$ 573,702		$ 601,923	

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table identifies the concentration of mortgage loans by state greater than 5% at March 31, 2012 and December 31, 2011.

	March 31 2012	% of Total	December 31 2011	% of Total
California	$ 115,233	20%	$ 117,261	19%
Texas	87,289	15%	84,724	14%
Minnesota	63,932	11%	64,952	11%
Florida	35,093	6%	31,310	5%
All others	274,640	48%	306,525	51%
	576,187	100%	604,772	100%
Allowance for potential future losses	(2,485)		(2,849)	
Total	$ 573,702		$ 601,923	

The table below identifies the carrying amount of mortgage loans by maturity at March 31, 2012 and December 31, 2011.

	March 31 2012	% of Total	December 31 2011	% of Total
Due in one year or less	$ 6,188	1%	$ 2,356	-
Due after one year through five years	191,385	33%	153,822	25%
Due after five years through ten years	239,835	42%	255,615	42%
Due after ten years	138,779	24%	192,979	33%
	576,187	100%	604,772	100%
Allowance for potential future losses	(2,485)		(2,849)	
Total	$ 573,702		$ 601,923	

The Company may refinance commercial mortgage loans prior to contractual maturity as a means of originating new loans that meet the Company s underwriting and pricing parameters. The Company refinanced loans with outstanding balances of $4.7 million and $7.8 million during the first quarters of 2012 and 2011, respectively.

In the normal course of business, the Company commits to fund commercial mortgage loans generally up to 120 days in advance. These commitments generally have fixed expiration dates. A small percentage of commitments expire due to the borrower s failure to deliver the requirements of the commitment by the expiration date. In these cases, the Company retains the commitment fee. For additional information, please see Note 16-Commitments.

At March 31, 2012, the Company had a construction-to-permanent loan in the amount of $2.8 million, of which $2.5 million had been disbursed. At completion and fulfillment of occupancy requirements, the construction loan will convert to long-term, fixed rate permanent loans.

4. Fair Value Measurements

Under U.S. GAAP, fair value represents the price that would be received to sell an asset (exit price) or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is the Company s policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements.

Following is a description of valuation methodologies used for assets and liabilities recorded at fair value and for estimating fair value for financial instruments not recorded at fair value but for which fair value is disclosed.

Assets

Securities Available for Sale

Fixed maturity and equity securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon unadjusted quoted prices, if available, except as described in the subsequent paragraphs.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

Short-Term Financial Assets

Short-term financial assets include cash and other short-term assets. Other short-term assets are invested in institutional money market funds. These assets are categorized as Level 2 in the fair value hierarchy as the valuation is based upon the net asset value (NAV) of the fund.

Loans

The Company does not record loans at fair value. As such, valuation techniques discussed herein for loans are primarily for estimating fair value for purpose of disclosure.

Fair values of mortgage loans on real estate properties are calculated by discounting contractual cash flows, using discount rates based on current industry pricing or the Company s estimate of an appropriate risk-adjusted discount rate for loans of similar size, type, remaining maturity, likelihood of prepayment, and repricing characteristics. Mortgage loans are categorized as Level 3 in the fair value hierarchy.

The Company also has loans made to policyholders. These loans cannot exceed the cash surrender value of the policy. Carrying value of policy loans approximates fair value. Policy loans are categorized as Level 3 in the fair value hierarchy.

Separate Accounts

The separate account assets and liabilities, which are equal, are recorded at fair value based upon NAV. They are categorized as Level 2 in the fair value hierarchy, as the Company receives independent prices from external pricing sources to determine the fair value.

Liabilities

Investment-Type Liabilities Included in Policyholder Account Balances and Other Policyholder Funds

Fair values for liabilities under investment-type insurance contracts are based upon account value. The fair values of investment-type insurance contracts included with policyholder account balances for fixed deferred annuities are estimated to be their cash surrender values. The fair values of supplementary contracts without life contingencies are estimated to be the present value of payments using a market yield. The fair values of deposits with no stated maturity are estimated to be the amount payable on demand at the measurement date. These liabilities are categorized as Level 3 in the fair value hierarchy.

Guaranteed Minimum Withdrawal Benefits (GMWB)

The Company offers a GMWB rider that can be added to new or existing variable annuity contracts. The rider provides an enhanced withdrawal benefit that guarantees a stream of income payments to an owner or annuitant, regardless of the contract account value. Fair value for GMWB rider contracts is a Level 3 valuation, as it is based on models which utilize significant unobservable inputs. These models require actuarial and financial market assumptions, which reflect the assumptions market participants would use in pricing the contract, including adjustments for volatility, risk, and issuer non-performance.

Notes Payable

Fair values for short-term notes payable approximate carrying value. The carrying amount is a reasonable estimate of the fair value because of the relatively short time between the origination of the loan and its expected repayment.

Determination of Fair Value

The determination of the fair value of the Company s fixed maturity and equity securities is the responsibility of the Company s investment accounting group, which reports to the Principal Accounting Officer. This group manages and creates the policies and processes used to determine the fair value for these assets. This group employs third-party pricing services and obtains selected support from the Company s portfolio managers in order to achieve results for this multi-tiered process. All prices are reviewed by the investment accounting group. The financial reporting group, the Principal Accounting Officer, and the Chief Financial Officer also review the fair value methodologies and the fair values that are obtained each quarter. The results of those reviews are made known to the Company s internal Disclosure Committee and to the Company s Audit Committee. In addition, any significant policy or process changes made during the quarter are also discussed with the Company s Audit Committee.

The Company utilizes external independent third-party pricing services to determine the majority of its fair values on investment securities available for sale. At March 31, 2012, 96% of the carrying value of these investments was from external pricing services, 1% was from brokers, and 3% was derived from internal matrices and calculations. In the event that the primary pricing service does not provide a price, the Company utilizes the price provided by a second pricing service. The Company reviews prices received from service providers for unusual fluctuations but generally accepts the price identified from the primary pricing service. In the event that a price is not available from either third-party pricing service,

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

the Company pursues external pricing from brokers. Generally, the Company pursues and utilizes only one broker quote per security. In doing so, the Company solicits only brokers which have previously demonstrated knowledge and experience of the subject security. If a broker price is not available, the Company determines a fair value through various valuation techniques that may include discounted cash flows, spread-based models or similar techniques, depending upon the specific security to be priced. These techniques are primarily applied to private placement securities. The Company utilizes available market information, wherever possible, to identify inputs into the fair value determination, primarily including prices and spreads on comparable securities. In total, the Company internally determined the prices for 18 securities at March 31, 2012. These securities totaled 3% of the fair value of the Company s investment portfolio.

Each quarter, the Company performs an analysis on the prices received from third-party security pricing services and independent brokers to assess that the prices represent a reasonable estimate of the fair value. The Company corroborates and validates the primary pricing sources through a variety of procedures that include but are not limited to comparison to additional independent third-party pricing services or brokers, where possible; a review of third-party pricing service methodologies; back testing; and comparison of prices to actual trades for specific securities where observable data exists. In addition, the Company analyzes the primary third-party pricing service s methodologies and related inputs and also evaluates the various types of securities in its investment portfolio to determine an appropriate fair value hierarchy.

Fair value measurements for assets and liabilities where there exists limited or no observable market data are calculated using the Company s own estimates and are categorized as Level 3. These estimates are based on current interest rates, credit spreads, liquidity premium or discount, the economic and competitive environment, unique characteristics of the asset or liability, and other pertinent factors. Therefore, these estimates cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset or liability. Additionally, there may be inherent weaknesses in any valuation technique. Further, changes in the underlying assumptions used, including discount rates and estimates of future cash flows, could significantly affect the results of current or future values.

The Company s own estimates of fair value of fixed maturity and equity securities are derived in a number of ways, including but not limited to: 1) pricing provided by brokers, where the price indicates reliability as to value; 2) fair values of comparable securities, incorporating a spread adjustment for maturity differences, collateralization, credit quality, liquidity, and other items, if applicable; 3) discounted cash flow models and margin spreads; 4) bond yield curves; 5) observable market prices and exchange transaction information not provided by external pricing services; and 6) statement values provided to the Company by fund managers.

The determination of the value of the Company s liabilities that are reported at fair value in the financial statements is the responsibility of the Company s valuation actuary group, which reports to the Company s Senior Vice President and Actuary. This group manages and creates the policies and processes used to determine the fair value for these liabilities. This methodology uses internal assumptions and directed third-party inputs to derive a value including a risk-neutral option pricing model that incorporates a third-party-developed index that is consistent with the attributes of the product and provides for an approximate match of the volatility measure with the expected life of the underlying contracts. The fair value methodologies and the fair values are reviewed by the Senior Vice President and Actuary, the Principal Accounting Officer, and the Chief Financial Officer. The results of those reviews are made known to the Company s internal Disclosure Committee and to the Company s Audit Committee. In addition, any significant policy or process changes made during the quarter are also discussed with the Company s Audit Committee.

Fair Values Hierarchy

The Company categorizes its financial assets and liabilities measured at fair value in three levels, based on the inputs and assumptions used to determine the fair value. These levels are as follows:

Level 1 Valuations are based upon quoted prices for identical instruments traded in active markets.

Level 2 Valuations are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. Valuations are obtained from third-party pricing services or inputs that are observable or derived principally from or corroborated by observable market data.

Level 3 Valuations are generated from techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company s assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of discounted cash flow models, spread-based models, and similar techniques, using the best information available in the circumstances.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

Categories Reported at Fair Value

The following tables present categories reported at fair value on a recurring basis.

	March 31, 2012			
Assets:	Level 1	Level 2	Level 3	Total
U.S. Treasury securities and obligations of U.S. Government	$ 12,781	$ 114,005	$ 3,385	$ 130,171
Federal agencies [1]	-	25,280	-	25,280
Federal agency issued residential mortgage-backed securities [1]	-	113,153	-	113,153
Subtotal	12,781	252,438	3,385	268,604
Corporate obligations:				
Industrial	-	512,936	2,451	515,387
Energy	-	182,475	2,391	184,866
Communications and technology	-	212,852	-	212,852
Financial	-	317,554	11,792	329,346
Consumer	-	498,831	21,264	520,095
Public utilities	-	296,396	-	296,396
Subtotal	-	2,021,044	37,898	2,058,942
Corporate private-labeled residential mortgage-backed securities	-	156,207	-	156,207
Municipal securities	-	165,888	4,369	170,257
Other	-	104,918	-	104,918
Redeemable preferred stocks	11,849	-	-	11,849
Fixed maturity securities	24,630	2,700,495	45,652	2,770,777
Equity securities	2,297	33,855	1,093	37,245
Total	$ 26,927	$ 2,734,350	$ 46,745	$ 2,808,022
Percent of total	1%	97%	2%	100%
Liabilities:				
Other policyholder funds				
GMWB	$ -	$ -	$ (950)	$ (950)
Total	$ -	$ -	$ (950)	$ (950)

1 Federal agency securities are not backed by the full faith and credit of the U.S. Government.

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Notes to Consolidated Financial Statements (Unaudited) Continued

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
Assets:				
U.S. Treasury securities and obligations of U.S. Government	$ 12,876	$ 118,130	$ 3,431	$ 134,437
Federal agencies [1]	-	25,881	-	25,881
Federal agency issued residential mortgage-backed securities [1]	-	119,637	-	119,637
Subtotal	12,876	263,648	3,431	279,955
Corporate obligations:				
Industrial	-	486,380	500	486,880
Energy	-	169,342	2,369	171,711
Communications and technology	-	201,393	-	201,393
Financial	-	307,464	10,614	318,078
Consumer	-	474,553	21,934	496,487
Public utilities	-	296,337	-	296,337
Subtotal	-	1,935,469	35,417	1,970,886
Corporate private-labeled residential mortgage-backed securities	-	156,902	-	156,902
Municipal securities	-	163,611	4,911	168,522
Other	-	94,656	-	94,656
Redeemable preferred stocks	11,221	-	-	11,221
Fixed maturity securities	24,097	2,614,286	43,759	2,682,142
Equity securities	2,216	33,350	1,123	36,689
Total	$ 26,313	$ 2,647,636	$ 44,882	$ 2,718,831
Percent of total	1%	97%	2%	100%
Liabilities:				
Other policyholder funds				
GMWB	$ -	$ -	$ (187)	$ (187)
Total	$ -	$ -	$ (187)	$ (187)

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following tables present the fair value of fixed maturity and equity securities available for sale by pricing source and fair value hierarchy level.

	March 31, 2012			
	Level 1	Level 2	Level 3	Total
Fixed maturity securities available for sale:				
Priced from external pricing services	$ 24,630	$ 2,662,120	$ -	$ 2,686,750
Priced from independent broker quotations	-	38,375	-	38,375
Priced from internal matrices and calculations	-	-	45,652	45,652
Subtotal	24,630	2,700,495	45,652	2,770,777
Equity securities available for sale:				
Priced from external pricing services	2,297	7,245	-	9,542
Priced from independent broker quotations	-	-	-	-
Priced from internal matrices and calculations	-	26,610	1,093	27,703
Subtotal	2,297	33,855	1,093	37,245
Total	$ 26,927	$ 2,734,350	$ 46,745	$ 2,808,022
Percent of total	1%	97%	2%	100%

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
Fixed maturity securities available for sale:				
Priced from external pricing services	$ 24,097	$ 2,582,617	$ -	$ 2,606,714
Priced from independent broker quotations	-	31,669	-	31,669
Priced from internal matrices and calculations	-	-	43,759	43,759
Subtotal	24,097	2,614,286	43,759	2,682,142
Equity securities available for sale:				
Priced from external pricing services	2,216	7,444	-	9,660
Priced from independent broker quotations	-	-	-	-
Priced from internal matrices and calculations	-	25,906	1,123	27,029
Subtotal	2,216	33,350	1,123	36,689
Total	$ 26,313	$ 2,647,636	$ 44,882	$ 2,718,831
Percent of total	1%	97%	2%	100%

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Notes to Consolidated Financial Statements (Unaudited) Continued

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the first quarter ended March 31, 2012 and year ended December 31, 2011 are summarized below:

	Quarter Ended March 31, 2012			
	Assets			Liabilities
	Fixed maturity securities available for sale	Equity securities available for sale	Total	GMWB
Beginning balance	$ 43,759	$ 1,123	$ 44,882	$ (187)
Included in earnings	4	-	4	(688)
Included in other comprehensive income	(299)	(30)	(329)	-
Purchases, issuances, sales and other dispositions:				
Purchases	-	-	-	-
Issuances	-	-	-	55
Sales	-	-	-	-
Other dispositions	(1,626)	-	(1,626)	(130)
Transfers into Level 3	3,814	-	3,814	-
Transfers out of Level 3	-	-	-	-
Ending balance	$ 45,652	$ 1,093	$ 46,745	$ (950)
Net unrealized losses	$ (299)	$ (30)	$ (329)	

	Year Ended December 31, 2011			
	Assets			Liabilities
	Fixed maturity securities available for sale	Equity securities available for sale	Total	GMWB
Beginning balance	$ 55,801	$ 1,180	$ 56,981	$ (2,799)
Included in earnings	11	92	103	2,500
Included in other comprehensive income	1,385	51	1,436	-
Purchases, issuances, sales and other dispositions:				
Purchases	-	-	-	-
Issuances	-	-	-	163
Sales	-	-	-	-
Other dispositions	(2,977)	(200)	(3,177)	(51)
Transfers into Level 3	8,640	-	8,640	-
Transfers out of Level 3	(19,101)	-	(19,101)	-
Ending balance	$ 43,759	$ 1,123	$ 44,882	$ (187)
Net unrealized gains	$ 1,401	$ 105	$ 1,506	

The Company did not exclude any realized or unrealized gains or losses on items transferred into Level 3. Depending upon the availability of Level 1 or Level 2 pricing, specific securities may transfer into or out of Level 3. The Company did not have any transfers between Level 1 or Level 2 during the quarter ended March 31, 2012.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table presents quantitative information about Level 3 fair value measurements as of March 31, 2012.

	Fair Value	Valuation Technique	Unobservable Inputs	Range	Weighted Average
Fixed maturity securities	$ 45,652	Market comparable	Spread adjustment	46-376	180

The Company s primary category of Level 3 fair values is fixed maturity securities, totaling $45.7 million as of March 31, 2012. These assets are valued using comparable security valuations through the unobservable input of estimated discount spreads. Specifically, the Company reviews the values and discount spreads on similar securities for which such information is observable in the market. Estimates of increased discount spreads are then determined based upon the characteristics of the securities being evaluated. The Company estimates that an increased spread of 10 basis points on each of the Level 3 securities would reduce the reported fair value by $0.2 million, as of March 31, 2012.

Other assets and liabilities categorized as Level 3 for purposes of fair value determination are not material to the Company s financial statements, and the sensitivities of such valuations to unobservable inputs are also believed to not be material.

The table below is a summary of fair value estimates at March 31, 2012 and December 31, 2011 for financial instruments. The Company has not included assets and liabilities that are not financial instruments in this disclosure. The total of the fair value calculations presented do not represent, and should not be construed to represent, the underlying value of the Company.

	March 31, 2012		December 31, 2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Investments:				
Fixed maturity securities available for sale	$ 2,770,777	$ 2,770,777	$ 2,682,142	$ 2,682,142
Equity securities available for sale	37,245	37,245	36,689	36,689
Mortgage loans	573,702	615,458	601,923	642,905
Policy loans	79,574	79,574	80,375	80,375
Cash and short-term investments	59,465	59,465	59,752	59,752
Separate account assets	341,250	341,250	316,609	316,609
Liabilities:				
Individual and group annuities	1,101,097	1,079,562	1,082,324	1,062,407
Supplementary contracts without life contingencies	55,488	54,216	56,193	54,824
Separate account liabilities	341,250	341,250	316,609	316,609
Other policyholder funds - GMWB	(950)	(950)	(187)	(187)

5. Financing Receivables

The Company has financing receivables that have both a specific maturity date, either on demand or on a fixed or determinable date, and are recognized as an asset in the Company s balance sheet.

The table below identifies the Company s financing receivables by classification at March 31, 2012 and December 31, 2011.

	March 31 2012	December 31 2011
Receivables:		
Agent receivables, net (allowance $2,232; $2,226 2011)	$ 1,524	$ 1,708
Investment-related financing receivables:		
Mortgage loans, net (allowance $2,485; $2,849 2011)	573,702	601,923
Total financing receivables	$ 575,226	$ 603,631

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

Agent Receivables

The Company has agent receivables which are classified as financing receivables and which are reduced by an allowance for doubtful accounts. These trade receivables from agents are long-term in nature and are specifically assessed as to the collectability of each receivable. The Company s gross agent receivables totaled $3.7 million at March 31, 2012 and the Company maintained an allowance for doubtful accounts totaling $2.2 million. Gross agent receivables totaled $3.9 million with an allowance for doubtful accounts of $2.2 million at December 31, 2011. The Company identified additions to the allowance for doubtful accounts of $0.1 million in the first quarter of 2012, the result of expected defaults on selected agent receivables. Also, the allowance was reduced $0.1 million during the first quarter of 2012, largely due to write-offs of defaulted agent receivables and collections of agent receivables. The Company has two types of agent receivables included in this category as follows:

- Agent specific loans. At March 31, 2012, these loans totaled $1.0 million with an allowance for doubtful accounts of $0.2 million. At December 31, 2011, agent specific loans totaled $0.8 million with an allowance for doubtful accounts of $0.2 million.
- Various agent commission advances and other commission receivables. Gross agent receivables in this category totaled $2.7 million, with an allowance for doubtful accounts of $2.0 million at March 31, 2012. Gross agent receivables totaled $3.1 million and the allowance for doubtful accounts was $2.0 million at December 31, 2011.

Mortgage Loans

The Company considers its mortgage loan portfolio to be long-term financing receivables. Mortgage loans are stated at cost, net of allowance for potential future losses. Mortgage loan interest income is recognized on an accrual basis with any premium or discount amortized over the life of the loan. Prepayment and late fees are recorded on the date of collection. Loans in foreclosure, loans considered impaired or loans past due 90 days or more are placed on a non-accrual status.

If a mortgage loan is determined to be on non-accrual status, the Company does not accrue interest income. The loan is independently monitored and evaluated as to potential impairment or foreclosure. This evaluation includes assessing the probability of receiving future cash flows, along with consideration of many of the factors described below. If delinquent payments are made and the loan is brought current, then the Company returns the loan to active status and accrues income accordingly.

Generally, the Company considers its mortgage loans to be a portfolio segment. The Company considers its primary class to be property type. The Company primarily uses loan-to-value as its credit risk quality indicator but also monitors additional secondary risk factors, such as geographic distribution both on a regional and specific state basis. The mortgage loan portfolio segment is presented by property-type in a table in Note 3 Investments. In addition, geographic distributions for both regional and significant state concentrations are also presented in Note 3. These measures are also supplemented with various other analytics to provide additional information concerning mortgage loans and management s assessment of financing receivables.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The following table presents an aging schedule for delinquent payments for both principal and interest at March 31, 2012 and December 31, 2011, by property type.

		Amount of Payments Past Due			
	Book Value	30-59 Days	60-89 Days	> 90 Days	Total
March 31, 2012					
Industrial	$ -	$ -	$ -	$ -	$ -
Medical	-	-	-	-	-
Office	184	9	-	-	9
Other	-	-	-	-	-
Total	$ 184	$ 9	$ -	$ -	$ 9
December 31, 2011					
Industrial	$ -	$ -	$ -	$ -	$ -
Office	816	13	-	-	13
Medical	7,019	75	-	-	75
Other	-	-	-	-	-
Total	$ 7,835	$ 88	$ -	$ -	$ 88

At March 31, 2012, there was one mortgage loan that was 30 days past due. Subsequently, payment was received and this loan was brought current in April 2012.

The allowance for potential future losses on mortgage loans is maintained at a level believed by management to be adequate to absorb estimated credit losses. Management s periodic evaluation and assessment of the adequacy of the reserve is based on known and inherent risks in the portfolio, historical and industry data, current economic conditions, and other relevant factors. The Company assesses the amount it maintains in the mortgage loan allowance through an assessment of what the Company believes are relevant factors at both the macro-environmental level and specific loan basis. A loan is considered impaired if it is probable that contractual amounts due will not be collected. The Company s allowance for credit losses was $2.5 million at March 31, 2012 and $2.8 million at December 31, 2011. For information regarding management s periodic evaluation and assessment of mortgage loans and the allowance for potential future losses, please refer to Note 5 Financing Receivables in the Company s 2011 Form 10-K.

The following table details the activity of the allowance for potential future losses on mortgage loans at March 31, 2012 and December 31, 2011.

	March 31, 2012	December 31, 2011
Beginning of year	$ 2,849	$ 3,410
Additions	-	-
Deductions	(364)	(561)
End of period	$ 2,485	$ 2,849

The Company has had three mortgage loan defaults in the current and prior year. One loan was foreclosed in the first quarter of 2012 and an impairment of $0.2 million was recorded. One of the loan defaults in 2011 resulted in an impairment of $0.4 million, while the second loan default in 2011 did not result in an impairment based upon the fair value of the property being greater than the loan value. The Company had no troubled loans that were restructured or modified during 2012 or 2011.

6. Variable Interest Entities

The Company invests in certain affordable housing and real estate joint ventures which are considered to be variable interest entities (VIEs) and are included in Real Estate in the Consolidated Balance Sheets. The assets held in affordable housing real estate joint venture VIEs are primarily residential real estate properties that are restricted to provide affordable housing under federal or state programs for varying periods of time. The restrictions primarily apply to the rents that may be paid by tenants residing in the properties during the term of an agreement to remain in the affordable housing program. Investments in real estate joint ventures are equity interests in partnerships or limited liability corporations that may or may not participate in profits or residual value. In certain cases, the Company may issue fixed-rate senior mortgage loan investments secured by properties controlled by VIEs. These investments are classified as mortgage loans in the Consolidated Balance Sheets, and

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

the income received from such investments is recorded as investment income in the Consolidated Statements of Comprehensive Income. For additional information, please refer to Note 6 - Variable Interest Entities in the Company s 2011 Form 10-K.

The following table presents the carrying amount and maximum exposure to loss relating to VIEs for which the Company holds a variable interest, but is not the primary beneficiary, and which had not been consolidated at March 31, 2012 and December 31, 2011. The table includes investments in eight real estate joint ventures and 28 affordable housing real estate joint ventures at March 31, 2012 and investments in eleven real estate joint ventures and 28 affordable housing real estate joint ventures at December 31, 2011.

	March 31 2012		December 31 2011	
	Carrying Amount	Maximum Exposure to Loss	Carrying Amount	Maximum Exposure to Loss
Real estate joint ventures	$ 24,170	$ 24,170	$ 35,551	$ 35,551
Affordable housing real estate joint ventures	22,127	61,007	20,749	61,124
Total	$ 46,297	$ 85,177	$ 56,300	$ 96,675

The maximum exposure to loss relating to the real estate joint ventures and affordable housing real estate joint ventures, as shown in the table above, is equal to the carrying amounts plus any unfunded equity commitments, exposure to potential recapture of tax credits, guarantees of debt or other obligations of the VIE with recourse to the Company. Unfunded equity and loan commitments typically require financial or operating performance by other parties and have not yet become due or payable but which may become due in the future.

At March 31, 2012 and December 31, 2011, the Company had $4.3 million and $6.4 million, respectively, in fixed-rate senior mortgage loan commitments outstanding to the benefit of entities that are also real estate joint venture VIEs. The loan commitments are included in the discussion of commitments in the Notes to Consolidated Financial Statements (Unaudited) for both periods. The Company also has contingent commitments to fund additional equity contributions for operating support to certain real estate joint venture VIEs, which could result in additional exposure to loss. However, the Company is not able to quantify the amount of these contingent commitments.

In addition, the maximum exposure to loss on affordable housing joint ventures at March 31, 2012 and December 31, 2011 includes $12.5 million and $13.2 million, respectively, of losses which could be realized if the tax credits received by the VIEs were recaptured. Recapture events would cause the Company to reverse some or all of the benefit previously recognized by the Company or third parties to whom the tax credit interests were transferred. A recapture event can occur at any time during a 15-year required compliance period. The principal causes of recapture include financial default and non-compliance with affordable housing program requirements by the properties controlled by the VIE. The potential exposure due to recapture may be mitigated by guarantees from the managing member or managing partner in the VIE, insurance contracts, or changes in the residual value accruing to the Company s interests in the VIEs.

7. Change in Accounting Principle

The Company adopted Accounting Standards Update (ASU) No. 2010-26 *Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts* effective January 1, 2012. This guidance modifies the types of costs incurred by insurance entities that can be capitalized when issuing or renewing insurance contracts. The guidance defines allowable deferred acquisition costs as incremental or directly related to the successful acquisition of new or renewal contracts. In addition, certain costs related directly to acquisition activities performed by the insurer, such as underwriting and policy issuance, are also deferrable. This guidance also defines the considerations for the deferral of direct-response advertising costs.

Effective January 1, 2012, the Company prospectively adopted this guidance. Pursuant to this guidance, the Company evaluated the types of acquisition costs it capitalizes. The Company capitalizes agent compensation and benefits and other expenses that are directly related to the successful acquisition of contracts. The Company also capitalizes expenses directly related to activities performed by the Company, such as underwriting, policy issuance, and processing fees incurred in connection with successful contract acquisitions.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

Deferred acquisition costs are capitalized as incurred. These costs for life insurance products are generally deferred and amortized over the premium paying period. Policy acquisition costs that relate to interest sensitive and variable insurance products are deferred and amortized in relation to the estimated gross profits to be realized over the lives of the contracts. For interest sensitive and variable insurance products, estimated gross profits are composed of net interest income, net realized investment gains and losses, fees, surrender charges, expenses, and mortality gains and losses. At the issuance of policies, projections of estimated gross profits are made which are then replaced by actual gross profits over the lives of the policies. The Company considers the following assumptions to be of significance when projecting future estimated gross profits: mortality, interest rates and spreads, surrender and withdrawal rates and expense margins.

The amount of acquisition costs capitalized during the first quarter of 2012, the period of adoption, was $9.7 million. The amount of acquisition costs that would have been capitalized during the first quarter of 2012 if the Company s previous policy had been applied during that period would have been $8.7 million. Thus, the adoption of this guidance resulted in a $1.0 million increase in the amount of acquisition costs capitalized. In addition, the implementation of this guidance also impacted the amortization of DAC and benefit and contract reserve change on selected products. The net result of the adoption of ASU No. 2010-26 was a $0.7 million increase in pretax earnings in the first quarter of 2012.

8. Separate Accounts

The Company has a guaranteed minimum withdrawal benefit (GMWB) rider that can be added to new or existing variable annuity contracts. The rider provides an enhanced withdrawal benefit that guarantees a stream of income payments to an owner or annuitant, regardless of the contract account value. The value of variable annuity separate accounts with the GMWB rider was $94.2 million at March 31, 2012 (December 31, 2011 $86.6 million) and the guarantee liability was ($1.0) million at March 31, 2012 (December 31, 2011 ($0.2) million). The value of the GMWB rider is recorded at fair value. The change in this value is included in policyholder benefits in the Consolidated Statements of Comprehensive Income. The value of variable annuity separate accounts with the GMWB rider is recorded in separate account liabilities and the value of the rider is included in other policyholder funds in the Consolidated Balance Sheets. The determination of fair value of the GMWB liability requires models that use actuarial and financial market assumptions, which reflect the assumptions market participants would use in pricing the contract, including adjustments for risk and issuer non-performance.

Guarantees are offered under variable universal life and variable annuity contracts: a guaranteed minimum death benefit (GMDB) rider is available on certain variable universal life contracts, and GMDB are provided on all variable annuities. The GMDB rider for variable universal life and variable annuity contracts guarantees the death benefit for specified periods of time, regardless of investment performance, provided cumulative premium requirements are met. The total reserve held for the variable annuity GMDB at March 31, 2012 was $0.1 million (December 31, 2011 $0.2 million).

9. Notes Payable

The Company had no notes payable at March 31, 2012 or December 31, 2011.

As a member of the Federal Home Loan Bank of Des Moines (FHLB) with a capital investment of $4.8 million, the Company has the ability to borrow on a collateralized basis from the FHLB. The Company received dividends on the capital investment of less than $0.1 million in both the first quarter of 2012 and 2011.

The Company has unsecured revolving lines of credit of $60.0 million with two major commercial banks with no balances outstanding and which are at variable interest rates based upon short-term indices. These lines of credit will expire in June of 2012. The Company anticipates renewing these lines as they come due.

10. Income Taxes

The first quarter income tax expense was $9.6 million or 33% of income before tax for 2012, versus $2.5 million or 34% of income before tax for the prior year period.

The effective income tax rate in 2012 was less than the prevailing corporate federal income tax rate of 35% primarily due to permanent differences, including the dividends-received deduction, and tax benefits related to affordable housing investments.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

The effective income tax rate in 2011 was less than the prevailing corporate federal income tax rate of 35% primarily due to permanent differences, including the dividends-received deduction, which resulted in a tax benefit of approximately 2% of income before tax. Partially offsetting the benefit from the permanent differences was a tax expense of approximately 1% of income before tax related to affordable housing investments.

The Company did not have any uncertain tax positions at March 31, 2012.

At March 31, 2012, the Company had a $5.6 million current tax liability and a $69.1 million deferred tax liability compared to a $0.3 million current tax recoverable and a $68.8 million deferred tax liability at December 31, 2011.

11. Pensions and Other Postretirement Benefits

The following table provides the components of net periodic benefit cost for the first quarters ended March 31, 2012 and 2011:

	Pension Benefits Quarter Ended March 31		Other Benefits Quarter Ended March 31	
	2012	2011	2012	2011
Service cost	$ -	$ -	$ 199	$ 161
Interest cost	1,475	1,871	452	387
Expected return on plan assets	(2,225)	(2,342)	(8)	(9)
Amortization of:				
Unrecognized actuarial gain (loss)	(1,425)	896	70	4
Unrecognized prior service cost	-	-	(63)	(68)
Net periodic benefit cost	$ (2,175)	$ 425	$ 650	$ 475

During the first quarter of 2012, the Company identified an error related to the amortization period for unrecognized actuarial gains and losses for its pension plan. The Company determined that upon curtailment of the plan on January 1, 2011, the status of the plan participants should have changed from active to inactive. The amortization period was corrected from the average remaining service period of plan participants, approximately 10 years, to the average remaining life expectancy of plan participants, approximately 26 years. The Company has recognized approximately a $2.0 million pre-tax benefit related to the reversal of amortization recorded during 2011.

12. Share-Based Payment

The Company has a long-term incentive plan for senior management that provides a cash award to participants for the increase in the share price of the Company s common stock through units (phantom shares) assigned by the Board of Directors. The cash award is calculated over a three-year interval on a calendar year basis. At the conclusion of each three-year interval, participants will receive a cash award based on the increase in the share price during a defined measurement period, times the number of units. The increase in the share price will be determined based on the change in the share price from the beginning to the end of the three-year interval. Dividends are accrued and paid at the end of each three-year interval to the extent that they exceed negative stock price appreciation. Plan payments are contingent on the continued employment of the participant unless termination is due to a qualifying event such as death, disability or retirement. The Company does not make payments in shares, warrants or options.

No payments were made under this plan during quarters ended March 31, 2012 and 2011.

At each reporting period, an estimate of the share-based compensation expense is accrued, utilizing the share price at the period end. Accruals of share-based compensation as operating expense were $0.3 million and $0.1 million, net of tax, in the first quarters of 2012 and 2011, respectively.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

13. Comprehensive Income

Comprehensive income is comprised of net income and other comprehensive income. Other comprehensive income includes the unrealized investment gains or losses on securities available for sale (net of adjustments for realized investment gains or losses) net of adjustments to DAC, VOBA, future policy benefits, and policyholder account balances. In addition, other comprehensive income includes the change in the liability for benefit plan obligations. Other comprehensive income reflects these items net of tax.

The table below provides information about comprehensive income for the first quarters ended March 31, 2012 and 2011.

	Quarter Ended March 31, 2012		
	Before-Tax Amount	Tax (Expense) or Benefit	Net-of-Tax Amount
Net unrealized gains (losses) arising during the year			
Fixed maturity securities	$ 7,324	$ 2,563	$ 4,761
Equity securities	2	1	1
Less reclassification adjustments:			
Net realized investment gains (losses), excluding impairment losses	468	164	304
Other-than-temporary impairment losses recognized in earnings	(268)	(94)	(174)
Other-than-temporary impairment losses recognized in other comprehensive income	108	38	70
Net unrealized gains (losses) excluding impairment losses	7,018	2,456	4,562
Effect on DAC and VOBA	(3,800)	(1,330)	(2,470)
Future policy benefits	(2,256)	(789)	(1,467)
Policyholder account balances	(116)	(41)	(75)
Other comprehensive income	$ 846	$ 296	$ 550
Net income			19,441
Comprehensive income			$ 19,991

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

	Quarter Ended March 31, 2011		
	Before-Tax Amount	Tax (Expense) or Benefit	Net-of-Tax Amount
Net unrealized gains (losses) arising during the year			
Fixed maturity securities	$ (146)	$ (51)	$ (95)
Equity securities	28	10	18
Less reclassification adjustments:			
Net realized investment gains (losses), excluding impairment losses	1,120	392	728
Other-than-temporary impairment losses recognized in earnings	(269)	(94)	(175)
Other-than-temporary impairment losses recognized in other comprehensive income	58	20	38
Net unrealized gains (losses) excluding impairment losses	(1,027)	(359)	(668)
Effect on DAC and VOBA	67	24	43
Future policy benefits	1,107	387	720
Policyholder account balances	10	3	7
Other comprehensive income	$ 157	$ 55	$ 102
Net income			4,791
Comprehensive income			$ 4,893

The following table provides accumulated balances related to each component of accumulated other comprehensive income at March 31, 2012.

	Net Unrealized Gain (Loss) on Non-Impaired Securities	Net Unrealized Gain (Loss) on Impaired Securities	Benefit Plan Obligations	DAC/ VOBA Impact	Future Policy Benefits	Policyholder Account Balances	Tax Effect	Total
Beginning of year	$ 213,800	$ (15,612)	$ (78,451)	$ (56,971)	$ (15,903)	$ (578)	$ (16,199)	$ 30,086
Other comprehensive income	2,138	4,880	-	(3,800)	(2,256)	(116)	(296)	550
End of period	$ 215,938	$ (10,732)	$ (78,451)	$ (60,771)	$ (18,159)	$ (694)	$ (16,495)	$ 30,636

14. Earnings Per Share

Due to the Company s capital structure and the absence of other potentially dilutive securities, there is no difference between basic and diluted earnings per common share for any of the periods reported. The average number of shares outstanding for the quarters ended March 31, 2012 and 2011 was 11,309,395 and 11,467,208, respectively. The number of shares outstanding at March 31, 2012 and 2011 was 11,309,477 and 11,467,319, respectively.

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Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

15. Segment Information

The following schedule provides the financial performance of each of the three reportable operating segments of the Company.

		Individual Insurance	Group Insurance	Old American	Intercompany Eliminations[1]	Consolidated
Insurance revenues:						
First quarter:	2012	$ 28,569	$ 12,067	$ 17,300	$ (99)	$ 57,837
	2011	30,732	12,554	16,708	(135)	59,859
Net investment income:						
First quarter:	2012	$ 41,121	$ 128	$ 2,960	$ -	$ 44,209
	2011	42,113	145	3,133	-	45,391
Net income (loss):						
First quarter:	2012	$ 19,487	$ (335)	$ 289	$ -	$ 19,441
	2011	6,105	(400)	(914)	-	4,791

[1] Elimination entries to remove intercompany transactions for life and accident and health insurance that the Company purchases for its employees and agents were as follows: insurance revenues from the Group Insurance segment and operating expenses from the Individual Insurance segment to arrive at Consolidated Statements of Comprehensive Income.

16. Commitments

In the normal course of business, the Company has open purchase and sale commitments. At March 31, 2012, the Company had purchase commitments to fund mortgage loans and other investments of $13.5 million. Included in this total, the Company had commitments to originate mortgage loans of $8.9 million at March 31, 2012 with fixed interest rates ranging from 4.125% to 5.50%. At March 31, 2012, the Company also had commitments to fund one construction-to-permanent loan of $0.3 million that is subject to the borrower s performance.

17. Contingent Liabilities

The Company is occasionally involved in litigation, both as a defendant and as a plaintiff. The life insurance industry, including the Company and its subsidiaries, has been subject to an increase in litigation in recent years. Such litigation has been pursued on behalf of purported classes of insurance purchasers, often questioning the conduct of insurers in the marketing of their products. In addition, state regulatory bodies, the SEC, FINRA, and other regulatory bodies regularly make inquiries and conduct examinations or investigations concerning the Company s compliance with laws in relation to, but not limited to, insurance, securities and activities of broker-dealers and investment advisors.

The Company s retail broker-dealer subsidiary is in an industry that involves substantial risks of liability. The Company s broker-dealer subsidiary, SFS, has been named as a defendant in several new cases in recent periods. In recent years, regulatory proceedings, litigation, and FINRA arbitration actions related to registered representative activity and securities products (including, mutual funds, variable annuities, and alternative investments, such as real estate investment products and oil and gas investments) have continued to increase. Given the significant decline in the major market indices beginning in 2008, and the generally poor performance of investments that have historically been considered safe and conservative, there is the potential for an increase in the number of proceedings to which a broker-dealer may be named as a party.

In addition to the above, the Company and its subsidiaries are defendants in, or subject to, other claims or legal actions related to insurance and investment products. Some of these claims and legal actions are in jurisdictions where juries are given substantial latitude in assessing damages, including punitive damages.

Although no assurances can be given and no determinations can be made at this time, management believes that the ultimate liability, if any, with respect to these legal actions and other claims would not have a material effect on the Company s business, results of operations or financial position.

Kansas City Life Insurance Company

Notes to Consolidated Financial Statements (Unaudited) Continued

In accordance with applicable accounting guidelines, the Company has established an accrued liability for litigation and regulatory matters when those matters present loss contingencies that are both probable and estimable. As a litigation or regulatory matter develops, it is evaluated on an ongoing basis, in conjunction with outside counsel, as to whether the matter presents a loss contingency that meets conditions indicating the need for accrual and/or disclosure. If and when a loss contingency related to litigation or regulatory matters is deemed to be both probable and estimable, the Company establishes an accrued liability. This accrued liability is then monitored for further developments that may affect the amount of the accrued liability.

18. Guarantees and Indemnifications

The Company is subject to various indemnification obligations issued in conjunction with certain transactions, primarily assumption reinsurance agreements, stock purchase agreements, mortgage servicing agreements, tax credit assignment agreements, construction and lease guarantees and borrowing agreements whose terms range in duration and often are not explicitly defined. Generally, a maximum obligation is not explicitly stated. Therefore, the overall maximum amount of the obligation under the indemnifications cannot be reasonably estimated. The Company is unable to estimate with certainty the ultimate legal and financial liability with respect to these indemnifications. The Company believes that the likelihood is remote that material payments would be required under such indemnifications and therefore such indemnifications would not result in a material adverse effect on the financial position or results of operations.

19. Subsequent Events

On April 23, 2012, the Board of Directors declared a quarterly dividend of $0.27 per share that will be paid May 9, 2012 to stockholders of record as of May 3, 2012.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Amounts are stated in thousands, except share data, or as otherwise noted.

Management s Discussion and Analysis of Financial Condition and Results of Operations is intended to provide in narrative form the perspective of the management of Kansas City Life Insurance Company (the Company) on its financial condition, results of operations, liquidity, and certain other factors that may affect its future results. The following is a discussion and analysis of the results of operations for the quarters ended March 31, 2012 and 2011 and the financial condition of the Company at March 31, 2012. This discussion should be read in conjunction with the consolidated financial statements and accompanying notes included in this document, as well as the Company s 2011 Form 10-K.

Overview

Kansas City Life Insurance Company is a financial services company that is predominantly focused on the underwriting, sales, and administration of life insurance and annuity products. The consolidated entity (the Company) primarily consists of three life insurance companies. Kansas City Life Insurance Company (Kansas City Life) is the parent company. Sunset Life Insurance Company of America (Sunset Life) and Old American Insurance Company (Old American) are wholly-owned subsidiaries. For additional information, please refer to the Overview included in Management s Discussion and Analysis of Financial Condition and Results of Operations in the Company s 2011 Form 10-K.

Cautionary Statement on Forward-Looking Information

This report reviews the Company s financial condition and results of operations, and historical information is presented and discussed. Where appropriate, factors that may affect future financial performance are also identified and discussed. Certain statements made in this report include forward-looking statements that fall within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include any statement that may predict, forecast, indicate or imply future results, performance or achievements rather than historical facts and may contain words like believe, expect, estimate, project, forecast, anticipate, plan, will, shall, and other words, phrases, or similar meaning.

Actual results may differ materially from those included in the forward-looking statements as a result of risks and uncertainties. Those risks and uncertainties include, but are not limited to, the risk factors listed in Item 1A. Risk Factors and Cautionary Factors that may Affect Future Results as filed in the Company s 2011 Form 10-K. For additional information, please refer to the Overview included in Management s Discussion and Analysis of Financial Condition and Results of Operations in the Company s 2011 Form 10-K.

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Consolidated Results of Operations

Summary of Results

The Company earned net income of $19.4 million in the first quarter of 2012 compared to $4.8 million in the first quarter of 2011. Net income per share was $1.72 in the first quarter of 2012 versus $0.42 in same period in the prior year. The following table presents variances between the results for the first quarters ended March 31, 2012 and 2011. Additional information on these items is presented below.

Insurance and other revenues	$ (2,245)
Net investment income	(1,182)
Net realized investment gains	14,876
Policyholder benefits and interest credited to policyholder account balances	6,727
Amortization of deferred acquisition costs	1,683
Operating expenses	1,903
Income tax expense	(7,112)
Total variance	$ 14,650

Sales

The Company measures sales in terms of new premiums and deposits. Sales of traditional life insurance, immediate annuities, and accident and health products are reported as premium income for financial statement purposes. Deposits received from the sale of interest sensitive products, including universal life insurance, fixed deferred annuities, variable universal life, variable annuities, and supplementary contracts without life contingencies are reflected as deposits in the Consolidated Statements of Cash Flows.

The Company s marketing plan for individual products focuses on three main aspects: providing financial security with respect to life insurance, the accumulation of long-term value, and future retirement income needs. The primary emphasis is on the growth of individual life insurance business, including new premiums for individual life products and new deposits for universal life and variable universal life products.

Sales are primarily made through the Company s existing sales force. The Company emphasizes growth of the sales force with the addition of new general agents and agents. The Company believes that increased sales will result through both the number and productivity of general agents and agents. In addition, the Company places an emphasis on training and direct support to the field force to assist new agents in their start-up phase. This assistance includes support to existing agents to stay abreast of the ever-changing regulatory environment and to introduce agents to new products and enhanced features of existing products. On occasion, the Company may also selectively utilize third-party marketing arrangements to enhance its sales objectives. This allows the Company flexibility to identify niches or pursue unique avenues in the existing market environment and to react quickly to take advantage of opportunities when they occur.

The Company also markets a series of group products. These products include group life, dental, disability, and vision products. The primary growth strategies for these products include increased productivity of the existing group representatives; planned expansion of the group distribution system; and to selectively utilize third-party marketing arrangements. Further, growth is to be supported by the addition of new products to the portfolio, particularly voluntary-type products.

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The following table presents gross premiums by new and renewal business, less reinsurance ceded, as included in insurance revenues for the first quarters ended March 31, 2012 and 2011. New premiums are also detailed by product.

	Quarter Ended March 31			
	2012	% Change	2011	% Change
New premiums:				
Individual life insurance	$ 4,356	(1)	$ 4,411	12
Immediate annuities	1,708	(37)	2,709	(50)
Group life insurance	481	(3)	494	(21)
Group accident and health insurance	2,544	(30)	3,624	9
Total new premiums	9,089	(19)	11,238	(15)
Renewal premiums	37,250	5	35,446	2
Total premiums	46,339	(1)	46,684	(3)
Reinsurance ceded	(13,635)	4	(13,059)	1
Premiums, net	$ 32,704	(3)	$ 33,625	(4)

Consolidated total premiums decreased $0.3 million or 1% in the first quarter of 2012 versus the same period in the prior year, as total new premiums decreased $2.1 million or 19% and total renewal premiums increased $1.8 million or 5%. The decrease in total new premiums primarily reflected reductions of $1.1 million or 30% and $1.0 million or 37% in new group accident and health insurance and immediate annuities, respectively. New group accident and health insurance premiums decreased due to declines in short-term disability and dental sales. Immediate annuity receipts can have sizeable fluctuations, as receipts from policyholders largely result from one-time premiums rather than recurring premiums. The decrease in new immediate annuity sales can also be attributed to lower interest rates and increased competition from alternative products. The increase in renewal premiums was largely due to a $1.3 million or 14% increase in group accident and health premiums and a $0.8 million increase in individual life insurance premiums. The increase in group accident and health renewal premiums was largely due to increases in short-term disability product line renewals.

The following table reconciles deposits with the Consolidated Statements of Cash Flows and provides detail by new and renewal deposits for the first quarters ended March 31, 2012 and 2011. New deposits are also detailed by product.

	Quarter Ended March 31			
	2012	% Change	2011	% Change
New deposits:				
Universal life insurance	$ 3,303	17	$ 2,812	(18)
Variable universal life insurance	157	(30)	225	(7)
Fixed deferred annuities	19,150	29	14,892	35
Variable annuities	3,961	3	3,837	(35)
Total new deposits	26,571	22	21,766	6
Renewal deposits	34,892	(2)	35,698	8
Total deposits	$ 61,463	7	$ 57,464	7

Total new deposits increased $4.8 million or 22% in the first quarter of 2012 compared with the first quarter of 2011. This change was primarily due to a $4.3 million or 29% increase in new fixed deferred annuity deposits and a $0.5 million or 17% increase in new universal life deposits. Total renewal deposits decreased $0.8 million or 2% in the first quarter of 2012 versus last year. Renewal variable annuity deposits decreased $1.1 million or 37%. Partially offsetting this was a $0.5 million or 6% increase in renewal fixed deferred annuity deposits.

Insurance Revenues

Insurance revenues consist of premiums, net of reinsurance, and contract charges. In the first quarter of 2012, total insurance revenues decreased $2.0 million or 3%, reflecting a $0.9 million or 3% decrease in net premiums and a $1.1 million or 4% decrease in contract charges. Total individual life premiums increased $0.8 million or 3% and total accident and health premiums were essentially flat compared with last year. Offsetting these, total immediate annuity premiums decreased $1.3 million or 42%.

Contract charges consist of cost of insurance, expense loads, amortization of unearned revenues, and surrender charges on policyholder account balances. Certain contract charges are not recognized in income immediately but are deferred and are amortized into income in proportion to the expected future gross profits of the business, in a manner similar to DAC. Profit expectations are based upon assumptions of future interest spreads, mortality margins, expense margins, and policy and premium persistency experience. At least annually, a review is performed of the assumptions related to profit expectations. If it is determined the assumptions should be revised, the impact is recorded as a change in the revenue reported in the current period as an unlocking adjustment.

Contract charges are impacted by the sales of new products and the persistency of both existing and closed blocks of business. The closed blocks of business reflect policies and companies that the Company has purchased but to which the Company is not actively pursuing marketing efforts to generate new sales and has the intent of servicing to achieve long-term profit streams. Total contract charges on closed blocks equaled 35% of total consolidated contract charges in both the first quarters of 2012 and 2011. Total contract charges on closed blocks declined 3% in the first quarter of 2012 compared to the first quarter of 2011, while total contract charges on open, or ongoing, blocks of business decreased 5%.

Total contract charges on all blocks of business decreased $1.1 million or 4% in the first quarter of 2012 compared to the first quarter of 2011. The largest factor in the 2012 decline was a $0.8 million decrease in deferred revenue, largely resulting from a system upgrade during 2011 that led to enhanced reinsurance modeling capabilities. In addition, cost of insurance charges decreased $0.2 million, largely due to the runoff of closed blocks.

The Company uses reinsurance as a means to mitigate its risks and to reduce the earnings volatility from claims. Reinsurance ceded premiums increased $0.6 million or 4% in the first quarter as compared to the same period in 2011. The Group segment experienced a $0.7 million or 30% increase in reinsurance ceded, reflecting increased disability and group life sales that were reinsured. Reinsurance ceded for the Old American segment declined $0.1 million or 18% in the first quarter of 2012, reflecting the continued runoff of a large closed block of reinsured business. Reinsurance ceded for the Individual Insurance segment remained essentially flat in the first quarter of 2012 compared to one year earlier.

Investment Revenues

Gross investment income is largely composed of interest, dividends and other earnings on fixed maturity securities, equity securities, short-term investments, mortgage loans, real estate, and policy loans. Gross investment income decreased $1.5 million or 3% in the first quarter of 2012, compared with the same period in 2011. While average invested assets increased during 2012, this was more than offset by lower yields earned on certain investments.

Fixed maturity securities provided a majority of the Company s investment income during the quarter ended March 31, 2012. Income on these investments declined $1.5 million or 4% in the first quarter of 2012 compared to the prior year, reflecting declines in average invested assets and yields earned.

Investment income from mortgage loans increased $0.7 million or 8% in the first quarter of 2012 compared to the same period in 2011. This improvement was largely the result of higher mortgage loan portfolio holdings in the first quarter of 2012 compared to the first quarter of 2011, as the Company significantly increased the mortgage loan balance through purchases made during 2011.

In addition, the market value declined on an alternative investment fund, which resulted in a decrease of investment income of $0.3 million in the first quarter of 2012 compared to the first quarter of 2011.

Net investment income is stated net of investment expenses. Investment expenses decreased $0.3 million or 9% in the first quarter of 2012 compared to the same period in 2011. This change is largely attributable to decreased real estate expenses, resulting from the sale of several properties.

The Company realizes investment gains and losses from several sources, including write-downs of investments and sales of investment securities and real estate. Many securities purchased by the Company contain call provisions, which allow the issuer to redeem the securities at a particular price. Depending upon the terms of the call provision and price at which the security was purchased, a gain or loss may be realized.

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The following table provides detail concerning realized investment gains and losses for the first quarters ended March 31, 2012 and 2011.

	Quarter Ended March 31	
	2012	2011
Gross gains resulting from:		
Sales of investment securities	$ 313	$ 311
Investment securities called and other	208	863
Sales of real estate	15,170	-
Total gross gains	15,691	1,174
Gross losses resulting from:		
Investment securities called and other	(53)	(54)
Mortgage loans	(165)	(3)
Total gross losses	(218)	(57)
Change in allowance for potential future losses on mortgage loans	364	-
Amortization of DAC and VOBA	-	(105)
Net realized investment gains, exluding impairment losses	15,837	1,012
Net impairment losses recognized in earnings:		
Total other-than-temporary impairment losses	(268)	(269)
Portion of loss recognized in other comprehensive income	108	58
Net impairment losses recognized in earnings	(160)	(211)
Net realized investment gains	$ 15,677	$ 801

The Company recorded a net realized investment gain of $15.7 million in the first quarter of 2012, compared with a $0.8 million net realized investment gain in the first quarter of 2011. During the first quarter of 2012, investment gains on sales of real estate totaled $15.2 million. In addition, the Company recorded $0.3 million in gains from the sale of investment securities and $0.2 million in gains from investment securities called and other. Partially offsetting these gains, investment losses of $0.2 million were recorded due to write-downs of investment securities that were considered other-than-temporarily impaired. In the above table, investment securities called and other includes, but is not limited to, principal payments and sinking funds.

The Company s analysis of securities for the quarter ended March 31, 2012 resulted in the determination that seven fixed-maturity securities had other-than-temporary impairments and were written down by a combined $0.2 million due to credit impairments. These seven securities accounted for all of the other-than-temporary impairments in the first quarter of 2012. These residential mortgage-backed securities had incremental losses, reflecting deterioration in the present value of expected future cash flows. The additional losses from these residential mortgage-backed securities totaled $0.3 million in the first quarter of 2012, including $0.1 million that was determined to be non-credit and was recognized in other comprehensive income. The total fair value of the affected securities after the write-downs was $52.3 million.

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The following table summarizes securities with other-than-temporary impairments recognized in earnings by business segment during the first quarters of 2012 and 2011 by asset class:

	Quarter Ended March 31 2012
Bonds:	
Corporate private-labeled residential mortgage-backed securities:	
Individual Insurance	$ 143
Old American	17
Total	$ 160
Segment detail:	
Individual Insurance	$ 143
Old American	17
Consolidated total	$ 160

	Quarter Ended March 31 2011
Bonds:	
Corporate private-labeled residential mortgage-backed securities:	
Individual Insurance	$ 188
Old American	23
Total	$ 211
Segment detail:	
Individual Insurance	$ 188
Old American	23
Consolidated total	$ 211

The following table provides detail regarding investment securities that were written down through earnings during the first quarter of 2012 by business segment, none of which exceeded $0.5 million on a consolidated basis.

	Impairment Loss			
Security	Individual Insurance	Old American	Consolidated	Description
Other - 7 securities	$ 143	$ 17	$ 160	
Total	$ 143	$ 17	$ 160	

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The following table provides detail regarding investment securities that were written down through earnings during the first quarter of 2011 by business segment, none of which exceeded $0.5 million on a consolidated basis.

	Impairment Loss			
Security	Individual Insurance	Old American	Consolidated	Description
Other - 4 securities	$ 188	$ 23	$ 211	
Total	$ 188	$ 23	$ 211	

Analysis of Investments

The Company seeks to protect policyholders benefits and achieve a desired level of organizational profitability by optimizing risk and return on an ongoing basis through managing asset and liability cash flows, monitoring credit risk, avoiding high levels of investments that may be redeemed by the issuer, maintaining sufficiently liquid investments and avoiding undue asset concentrations through diversification, among other things.

The primary sources of investment risk to which the Company is exposed include credit risk, interest rate risk, and liquidity risk. The Company s ability to manage these risks is essential to the success of the organization. In particular, the Company devotes considerable resources to both the credit analysis of each new investment and to ongoing credit positions. A default by an issuer usually involves some loss of principal to the investor. Losses can be mitigated by timely sales of affected securities or by active involvement in a restructuring process. However, there can be no assurance that the efforts of an investor will lead to favorable outcomes in a bankruptcy or restructuring. Credit risk is managed primarily through industry, issuer, and structure diversification.

The following table provides information regarding fixed maturity and equity securities by asset class at March 31, 2012.

	Total Fair Value	% of Total	Fair Value of Securities with Gross Unrealized Gains	Gross Unrealized Gains	Fair Value of Securities with Gross Unrealized Losses	Gross Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government	$ 130,171	5%	$ 125,466	$ 11,886	$ 4,705	$ 58
Federal agencies [1]	25,280	1%	25,280	3,075	-	1
Federal agency issued residential mortgage-backed securities [1]	113,153	4%	112,859	9,756	294	-
Subtotal	268,604	10%	263,605	24,717	4,999	59
Corporate obligations:						
Industrial	515,387	18%	482,183	41,500	33,204	2,312
Energy	184,866	6%	174,272	19,033	10,594	144
Communications and technology	212,852	7%	199,804	17,497	13,048	209
Financial	329,346	12%	293,243	18,598	36,103	2,483
Consumer	520,095	18%	466,247	42,792	53,848	862
Public utilities	296,396	11%	277,303	36,009	19,093	579
Subtotal	2,058,942	72%	1,893,052	175,429	165,890	6,589
Corporate private-labeled residential mortgage-backed securities	156,207	6%	84,226	2,425	71,981	9,238
Municipal securities	170,257	6%	169,375	21,608	882	20
Other	104,918	4%	56,122	3,846	48,796	8,768

Redeemable preferred stocks	11,849	1%	7,766	337	4,083	223
Fixed maturities	2,770,777	99%	2,474,146	228,362	296,631	24,897
Equity securities	37,245	1%	36,137	1,890	1,108	149
Total	$ 2,808,022	100%	$ 2,510,283	$ 230,252	$ 297,739	$ 25,046

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

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The following table provides information regarding fixed maturity and equity securities by asset class at December 31, 2011.

	Total Fair Value	% of Total	Fair Value of Securities with Gross Unrealized Gains	Gross Unrealized Gains	Fair Value of Securities with Gross Unrealized Losses	Gross Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government	$ 134,437	5%	$ 133,478	$ 13,856	$ 959	$ 12
Federal agencies [1]	25,881	1%	25,881	3,480	-	-
Federal agency issued residential mortgage-backed securities [1]	119,637	4%	118,694	9,901	943	2
Subtotal	279,955	10%	278,053	27,237	1,902	14
Corporate obligations:						
Industrial	486,880	18%	461,425	43,710	25,455	860
Energy	171,711	6%	171,711	19,131	-	-
Communications and technology	201,393	7%	194,154	16,566	7,239	156
Financial	318,078	12%	250,403	15,155	67,675	5,890
Consumer	496,487	18%	481,033	43,788	15,454	263
Public utilities	296,337	11%	280,475	38,094	15,862	1,366
Subtotal	1,970,886	72%	1,839,201	176,444	131,685	8,535
Corporate private-labeled residential mortgage-backed securities	156,902	6%	53,304	1,856	103,598	12,620
Municipal securities	168,522	6%	164,613	18,316	3,909	61
Other	94,656	4%	38,253	3,576	56,403	9,235
Redeemable preferred stocks	11,221	1%	5,226	226	5,995	740
Fixed maturities	2,682,142	99%	2,378,650	227,655	303,492	31,205
Equity securities	36,689	1%	35,566	1,873	1,123	135
Total	$ 2,718,831	100%	$ 2,414,216	$ 229,528	$ 304,615	$ 31,340

[1] Federal agency securities are not backed by the full faith and credit of the U.S. Government.

At December 31, 2011, the Company had $31.3 million in gross unrealized losses on investment securities which were offset by $229.5 million in gross unrealized gains. At March 31, 2012, the Company s unrealized losses on investment securities had decreased to $25.0 million and were offset by $230.3 million in gross unrealized gains. At March 31, 2012, 26% of the gross unrealized losses were in the category of corporate obligations. The financial sector was the single largest contributor to this category, reflecting the direct and indirect impact of the troubled residential real estate and mortgage markets. In addition, 37% of the gross unrealized losses were in the category of corporate private-labeled residential mortgage-backed securities, also due to the troubled residential real estate and mortgage markets. At March 31, 2012, 89% of the total fair value of the fixed maturities portfolio had unrealized gains, unchanged from December 31, 2011.

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The following table identifies fixed maturity securities available for sale by actual or equivalent Standard & Poor s rating at March 31, 2012 and December 31, 2011.

	March 31, 2012		December 31, 2011	
	Fair Value	% of Total	Fair Value	% of Total
AAA	$ 137,010	5%	$ 161,802	6%
AA	588,203	21%	570,157	21%
A	833,353	30%	799,565	30%
BBB	1,001,802	36%	939,373	35%
Total investment grade	2,560,368	92%	2,470,897	92%
BB	73,589	3%	79,760	3%
B and below	136,820	5%	131,485	5%
Total below investment grade	210,409	8%	211,245	8%
	$			