MORGAN STANLEY
Form FWP
January 09, 2019

Morgan Stanley Finance LLC	Free Writing Prospectus to Preliminary Terms No. 1,408 Registration Statement Nos. 333-221595; 333-221595-01 Dated January 8, 2019 Filed pursuant to Rule 433

Structured Investments

Contingent Income Buffered Auto-Callable Securities due February 2, 2021, with 6-Month Initial Non-Call Period

All Payments on the Securities Based on the Worst Performing of the Russell 2000® Index and the S&P 500® Index

This document provides a summary of the terms of the securities offered by Morgan Stanley Finance LLC. Investors should review carefully the accompanying preliminary terms, product supplement, index supplement and prospectus prior to making an investment decision.

SUMMARY TERMS

Issuer:	Morgan Stanley Finance LLC ("MSFL")
Guarantor:	Morgan Stanley
Underlying indices:	Russell 2000® Index (the "RTY Index") and S&P 500® Index (the "SPX Index"). For more information about the underlying indices, see the accompanying preliminary terms.
Stated principal amount:	$1,000 per security
Pricing date:	January 28, 2019
Original issue date:	January 31, 2019 (3 business days after the pricing date)
Maturity date:	February 2, 2021
Early redemption:	The securities are not subject to automatic early redemption until six months after the original issue date. Following this initial 6-month non-call period, if, on any redemption determination date, beginning on July 29, 2019, the index closing value of **each** underlying index is **greater than or equal to** its respective initial index value, the securities will be automatically redeemed for an early redemption payment on the related early redemption date. No further payments will be made on the securities once they have been redeemed. **The securities will not be redeemed early on any early redemption date if the index closing value of either underlying index is below the respective initial index value for such underlying index on the related redemption determination date.**
Early redemption payment:	The early redemption payment will be an amount equal to the stated principal amount for each security you hold *plus* the contingent monthly coupon with respect to the related observation date.
Contingent monthly coupon:	A *contingent* coupon will be paid on the securities on each coupon payment date ***but only if*** the index closing value of **each** underlying index is at or above its respective **coupon threshold level** on the related observation date. If payable, the contingent monthly coupon will be an amount in cash per stated principal amount corresponding to a return of 6.75% *per annum* for each interest payment period for each applicable observation date.

	If, on any observation date, the index closing value of either underlying index is less than its respective coupon threshold level, we will pay no coupon for the applicable monthly period. It is possible that either underlying index will remain below its respective coupon threshold level for extended periods of time or even throughout the entire 2-year term of the securities so that you will receive few or no contingent monthly coupons.
Payment at maturity:	If the securities have not been automatically redeemed prior to maturity, the payment at maturity will be determined as follows: • If the final index value of **each** underlying index is **greater than or equal to** 85% of its respective initial index value, meaning that the final index value of **each** underlying index has increased, remained unchanged or decreased by an amount less than or equal to the buffer amount of 15% from its respective initial index value: the stated principal amount and the contingent monthly coupon with respect to the final observation date • If final index value of **either** underlying index is **less than** 85% of its respective initial index value, meaning that the final index value of **either** underlying index has decreased by more than the buffer amount of 15% from its respective initial index value: $1,000 + [$1,000 x (index percent change of the worst performing underlying index + 15%)] *Under these circumstances, the payment at maturity will be less than the stated principal amount of $1,000. However, under no circumstances will the securities pay less than the minimum payment at maturity of $150 per security.*
Minimum payment at maturity:	$150 per security (15% of the stated principal amount)
Agent:	Morgan Stanley & Co. LLC, an affiliate of MSFL and a wholly owned subsidiary of Morgan Stanley. See “Supplemental information regarding plan of distribution; conflicts of interest” in the accompanying preliminary terms. The agent commissions will be as set forth in the final pricing supplement.
Estimated value on the pricing date:	Approximately $965.20 per security, or within $15.00 of that estimate. See “Investment Summary” in the accompanying preliminary terms.

Terms continued on the following page

Overview

The securities offered are unsecured obligations of MSFL and are fully and unconditionally guaranteed by Morgan Stanley. The securities have the terms described in the accompanying preliminary terms, product supplement, index supplement and prospectus. The securities do not provide for the regular payment of interest and provide a minimum payment at maturity of only 15% of the stated principal amount. Instead, the securities will pay a contingent monthly coupon **but only if** the index closing value of **each** of the Russell 2000® Index **and** the S&P 500® Index is **at or above** 85% of its respective initial index value, which we refer to as the respective **coupon threshold level**, on the related observation date. However, if the index closing value of **either** underlying index is **less than** its **coupon threshold level** on any observation date, we will pay no interest for the related monthly period. In addition, starting six months after the original issue date, the securities will be automatically redeemed if the index closing value of **each** underlying index is **greater than or equal to** its respective **initial index value** on any monthly redemption determination date, for the early redemption payment equal to the sum of the stated principal amount plus the related contingent monthly coupon. No further payments will be made on the securities once they have been redeemed. At maturity, if the securities have not previously been redeemed and the final index value of **each** underlying index **has increased, remained unchanged or decreased by an amount less than or equal to** the buffer amount of 15% from its respective initial index value, investors will receive the stated principal amount and the related contingent monthly coupon. If, however, the final index value of **either** underlying index has decreased by more than the buffer amount of 15% from its respective initial index value, investors will lose 1% of principal for every 1% decline in the final index value of the worst performing underlying index from its initial index value beyond the buffer amount of 15%. Under these circumstances, the payment at maturity will be **less than the** stated principal amount of the securities. **Accordingly, investors in the securities must be willing to accept the risk of losing up to 85% of their initial investment and also the risk of not receiving any contingent monthly coupons throughout the 2-year term of the securities.** Because all payments on the securities are based on the worst performing of the underlying indices, a decline of more than 15% by either underlying index will result in no contingent coupon payments or a loss of your investment, even if the other underlying index has appreciated or has not declined as much. The securities are for investors who are willing to risk their principal based on the worst performing of two underlying indices and who seek an opportunity to earn interest at a potentially above-market rate in exchange for the risk of receiving no monthly coupons over the entire 2-year term, with no possibility of being called out of the securities until after the initial 6-month non-call period. Investors will not participate in any appreciation of either underlying index. The securities are notes issued as part of MSFL's Series A Global Medium-Term Notes program.

All payments are subject to our credit risk. If we default on our obligations, you could lose some or all of your investment. These securities are not secured obligations and you will not have any security interest in, or otherwise have any access to, any underlying reference asset or assets.

Investing in the securities involves risks. See "Selected Risks" on the following page and "Risk Factors" in the accompanying preliminary terms.

You should read this document together with the accompanying preliminary terms, product supplement, index supplement and prospectus describing the offering before you decide to invest. You may access the preliminary terms through the below link:

https://www.sec.gov/Archives/edgar/data/895421/000095010319000173/dp100475_fwp-ps1408.htm

Terms continued from previous page:

Redemption determination dates:	Beginning after six months, monthly, as set forth under “Observation Dates, Redemption Determination Dates, Coupon Payment Dates and Early Redemption Dates” in the accompanying preliminary terms, subject to postponement for non-index business days and certain market disruption events.
Early redemption dates:	Beginning on August 1, 2019, monthly, as set forth under “Observation Dates, Redemption Determination Dates, Coupon Payment Dates and Early Redemption Dates” in the accompanying preliminary terms, subject to postponement for non-index business days and certain market disruption events.
Coupon threshold level:	With respect to the RTY Index: 85% of its initial index value With respect to the SPX Index: 85% of its initial index value
Buffer amount:	With respect to each underlying index, 15%. As a result of the buffer amount of 15%, the value at or above which each underlying index must close on the final observation date so that investors do not suffer a loss on their initial investment in the securities is as follows: • With respect to the RTY Index: 85% of its initial index value • With respect to the SPX Index: 85% of its initial index value
Initial index value:	With respect to the RTY Index: its index closing value on the pricing date With respect to the SPX Index: its index closing value on the pricing date
Final index value:	With respect to each index, the respective index closing value on the final observation date
Worst performing underlying:	The underlying index with the larger percentage decrease from the respective initial index value to the respective final index value
Index percent change:	With respect to each underlying index: (final index value - initial index value) / initial index value
Coupon payment dates:	Monthly, beginning March 5, 2019, as set forth under “Observation Dates, Redemption Determination Dates, Coupon Payment Dates and Early Redemption Dates” in the accompanying preliminary terms; *provided* that if any such day is not a business day, that coupon payment will be made on the next succeeding business day and no adjustment will be made to any coupon payment made on that succeeding business day. The contingent monthly coupon, if any, with respect to the final observation date will be paid on the maturity date
Observation dates:	Monthly, as set forth under “Observation Dates, Redemption Determination Dates, Coupon Payment Dates and Early Redemption Dates” in the accompanying preliminary terms, subject to postponement for non-index business days and certain market disruption events. We also refer to the observation date immediately prior to the scheduled maturity date as the final observation date.
CUSIP / ISIN:	61768DXC4 / US61768DXC46
Listing:	The securities will not be listed on any securities exchange.

The issuer has filed a registration statement (including a prospectus) with the SEC for the offering to which this communication relates. Before you invest, you should read the prospectus in that registration statement and other documents the issuer has filed with the SEC for more complete information about the issuer and this offering. You may get these documents for free by visiting EDGAR on the SEC Web site at www.sec.gov. Alternatively, the issuer, any underwriter or any dealer participating in the offering will arrange to send you the prospectus if you request it by calling toll-free 1-800-584-6837.

Risk Considerations

The risks set forth below are discussed in more detail in the “Risk Factors” section in the accompanying preliminary terms. Please review those risk factors carefully prior to making an investment decision.

- The securities provide a minimum payment at maturity of only 15% of your principal.
- The securities do not provide for the regular payment of interest.
- You are exposed to the price risk of each underlying index, with respect to both the contingent monthly coupons, if any, and the payment at maturity.
- Because the securities are linked to the performance of the worst performing underlying index, you are exposed to greater risks of receiving no contingent monthly coupons and sustaining a loss on your investment than if the securities were linked to just one index.
- The contingent monthly coupon, if any, is based on the value of each underlying index on only the related monthly observation date at the end of the related interest period.
- Investors will not participate in any appreciation in either underlying index.
- The market price will be influenced by many unpredictable factors.
- The securities are subject to our credit risk, and any actual or anticipated changes to our credit ratings or credit spreads may adversely affect the market value of the securities.
- As a finance subsidiary, MSFL has no independent operations and will have no independent assets.
- The securities are linked to the Russell 2000® Index and are subject to risks associated with small-capitalization companies.
- Not equivalent to investing in the underlying indices.
- Reinvestment risk.
- The securities will not be listed on any securities exchange and secondary trading may be limited. Accordingly, you should be willing to hold your securities for the entire 2-year term of the securities.

- The rate we are willing to pay for securities of this type, maturity and issuance size is likely to be lower than the rate implied by our secondary market credit spreads and advantageous to us. Both the lower rate and the inclusion of costs associated with issuing, selling, structuring and hedging the securities in the original issue price reduce the economic terms of the securities, cause the estimated value of the securities to be less than the original issue price and will adversely affect secondary market prices.

- The estimated value of the securities is determined by reference to our pricing and valuation models, which may differ from those of other dealers and is not a maximum or minimum secondary market price.

- Hedging and trading activity by our affiliates could potentially affect the value of the securities.

- The calculation agent, which is a subsidiary of Morgan Stanley and an affiliate of MSFL, will make determinations with respect to the securities.

- Adjustments to the underlying indices could adversely affect the value of the securities.

- The U.S. federal income tax consequences of an investment in the securities are uncertain.

Tax Considerations

You should review carefully the discussion in the accompanying preliminary terms under the caption “Additional Information About the Securities– Tax considerations” concerning the U.S. federal income tax consequences of an investment in the securities. However, you should consult your tax adviser regarding all aspects of the U.S. federal income tax consequences of an investment in the securities, as well as any tax consequences arising under the laws of any state, local or non-U.S. taxing jurisdiction.

Hypothetical Examples

The following hypothetical examples illustrate how to determine whether a contingent monthly coupon is paid with respect to an observation date and how to calculate the payment at maturity if the securities have not been automatically redeemed early. The following examples are for illustrative purposes only. Whether you receive a contingent monthly coupon will be determined by reference to the index closing value of each underlying index on each monthly observation date, and the amount you will receive at maturity will be determined by reference to the final index value of each underlying index on the final observation date. The actual initial index value and coupon threshold level for each underlying index will be determined on the pricing date. All payments on the securities are subject to our credit risk. The numbers in the hypothetical examples below may have been rounded for the ease of analysis. The below examples are based on the following terms:

Contingent Monthly Coupon:	A *contingent* monthly coupon will be paid on the securities on each coupon payment date ***but only if*** the index closing value of **each** underlying index is at or above its respective **coupon threshold level** on the related observation date. If payable, the contingent monthly coupon will be an amount in cash per stated principal amount corresponding to a return of 6.75% *per annum* for each interest payment period for each applicable observation date. These hypothetical examples reflect the contingent monthly coupon rate of 6.75% *per annum* (corresponding to approximately $5.625 per month per security*).
Automatic Early Redemption (starting after six months):	If the index closing value of **each** underlying index is greater than or equal to its respective **initial index value** on any monthly redemption determination date, the securities will be automatically redeemed for an early redemption payment equal to the stated principal amount *plus* the contingent monthly coupon with respect to the related observation date.
Payment at Maturity (if the securities have not been automatically redeemed early):	If the final index value of **each** underlying index has **increased, remained unchanged or decreased by an amount less than or equal to** the buffer amount of 15% from its respective initial index value, investors will receive the stated principal amount and the contingent monthly coupon with respect to the final observation date. If the final index value of **either** underlying index has **decreased by more than the buffer amount of 15%** from its respective initial index value: $1,000 + [$1,000 x (index percent change of the worst performing underlying index + 15%)]. Under these circumstances, the payment at maturity will be less than the stated principal amount of the securities. However, under no circumstances will the securities pay less than the minimum payment at maturity of $150 per security.
Stated Principal Amount:	$1,000
Hypothetical Initial Index Value:	With respect to the RTY Index: 1,400 With respect to the SPX Index: 2,500
Hypothetical Coupon Threshold Level:	With respect to the RTY Index: 1,190, which is 85% of the hypothetical initial index value for such index

	With respect to the SPX Index: 2,125, which is 85% of the hypothetical initial index value for such index
Buffer Amount:	With respect to each underlying index, 15%

* The actual contingent monthly coupon will be an amount determined by the calculation agent based on the number of days in the applicable payment period, calculated on a 30/360 basis. The hypothetical contingent monthly coupon of $5.625 is used in these examples for ease of analysis.

How to determine whether a contingent monthly coupon is payable with respect to an observation date:

	Index Closing Value		Contingent Monthly Coupon
	RTY Index	SPX Index	
Hypothetical Observation Date 1	1,900 (**at or above** the coupon threshold level)	2,800 (**at or above** the coupon threshold level)	$5.625
Hypothetical Observation Date 2	1,300 (**at or above** the coupon threshold level)	1,850 (**below** the coupon threshold level)	$0
Hypothetical Observation Date 3	950 (**below** the coupon threshold level)	2,200 (**at or above** the coupon threshold level)	$0
Hypothetical Observation Date 4	1,000 (**below** the coupon threshold level)	800 (**below** the coupon threshold level)	$0

On hypothetical observation date 1, each underlying index closes at or above its respective coupon threshold level. Therefore, a contingent monthly coupon of $5.625 is paid on the relevant coupon payment date.

On each of hypothetical observation dates 2 and 3, one underlying index closes at or above its respective coupon threshold level, but the other underlying index closes below its respective coupon threshold level. Therefore, no contingent monthly coupon is paid on the relevant coupon payment date.

On hypothetical observation date 4, each underlying index closes below its respective coupon threshold level, and, accordingly, no contingent monthly coupon is paid on the relevant coupon payment date.

If the index closing value of either underlying index is less than its respective coupon threshold level on each observation date, you will not receive any contingent monthly coupons for the entire 2-year term of the securities.

How to calculate the payment at maturity (if the securities have not been automatically redeemed):

Starting after six months, if the index closing value of each underlying index is greater than or equal to its initial index value on any monthly redemption determination date, the securities will be automatically redeemed for an early redemption payment equal to the stated principal amount for each security you hold *plus* the contingent monthly coupon with respect to the related observation date.

The examples below illustrate how to calculate the payment at maturity if the securities have not been automatically redeemed prior to maturity.

	Final Index Value		Index Percent Change		Payment at Maturity
	RTY Index	SPX Index	RTY Index	SPX Index	
			(final index value – initial index value) / initial index value	(final index value – initial index value) / initial index value	= $1,000 + (index percent change of the worst performing underlying index + 15%)
Example 1:	630 (the RTY Index has decreased by an amount **greater than** the buffer amount)	3,000 (the SPX Index has increased, remained unchanged or decreased by an amount **less than** or equal to the buffer amount)	= (630 – 1,400) / 1,400 = -55%	= (3,000 – 2,500) / 2,500 = 20%	= $1,000 + [$1,000 x (-55% + 15%)] = $1,000 + ($1,000 x -40%) = $600
Example 2:	1,610 (the RTY Index has increased, remained unchanged or decreased by an amount **less than** or equal to the buffer amount)	500 (the SPX Index has decreased by an amount **greater than** the buffer amount)	(1,610 – 1,400) / 1,400 = 15%	(500 – 2,500) / 2,500 = -80%	= $1,000 + [$1,000 x (-80% + 15%)] = $1,000 + ($1,000 x -65%) = $350
Example 3:	1,330 (**at or above** the coupon threshold level; the RTY Index has increased, remained unchanged or decreased by an amount less	2,250 (**at or above** the coupon threshold level; the SPX Index has increased, remained unchanged or decreased by an amount less than or equal to the	(1,330 – 1,400) / 1,400 = -5%	(2,250 – 2,500) / 2,500 = -10%	The stated principal amount + the contingent monthly coupon with respect to the final observation date. For more information, please see above under

than or equal to the buffer amount)	buffer amount)	“How to determine whether a contingent monthly coupon is payable with respect to an observation date.”

In examples 1 and 2, the final index value of one of the underlying indices has increased, remained unchanged or decreased by an amount less than or equal to the buffer amount of 15% from its respective initial index value, but the final index value of the other underlying index has decreased by an amount greater than the buffer amount of 15% from its respective initial index value. Therefore, investors are exposed to the downside performance of the worst performing underlying index at maturity, and investors lose 1% of the principal amount for every 1% decline in the final index value of the worst performing underlying index from its initial index value beyond the buffer amount of 15%. Moreover, investors do not receive any contingent monthly coupon for the final monthly period.

In example 3, the final index value of each underlying index is at or above its respective coupon threshold level, and each underlying index has increased, remained unchanged or decreased by an amount less than or equal to the buffer amount of 15% from its respective initial index value. Therefore, investors receive at maturity the stated principal amount of the securities *plus* the contingent monthly coupon with respect to the final observation date.

If the final index value of EITHER underlying index has decreased by more than the buffer amount of 15% from its respective initial index value, you will be exposed to the downside performance of the worst performing underlying index beyond the buffer amount, and your payment at maturity will be less than the stated principal amount. Under these circumstances, you will lose some, and up to 85%, of your investment in the securities.

Russell 2000® Index Historical Performance

The following graph sets forth the daily index closing values of the Russell 2000® Index for each quarter in the period from January 1, 2013 through December 28, 2018. You should not take the historical values of the Russell 2000® Index as an indication of its future performance, and no assurance can be given as to the index closing value of the Russell 2000® Index on the valuation date.

Russell 2000® Index

Daily Index Closing Values

January 1, 2013 to December 28, 2018

S&P 500® Index Historical Performance

The following graph sets forth the daily index closing values of the S&P 500® Index for each quarter in the period from January 1, 2013 through December 28, 2018. You should not take the historical values of the S&P 500® Index as an indication of its future performance, and no assurance can be given as to the index closing value of the S&P 500® Index on the valuation date.

S&P 500® Index

Daily Index Closing Values

January 1, 2013 to December 28, 2018

IGN="bottom"> 215,163 441,579 436,604

Benefits, losses and expenses

Benefits, claims and settlement expenses

94,969 106,973 197,973 218,428

Interest credited

28,614 26,876 56,694 53,283

Policy acquisition expenses amortized

18,887 17,404 37,168 33,783

Operating expenses

30,653 34,524 60,943 68,131

Amortization of intangible assets

1,316 1,128 3,088 2,454

Interest expense

2,555 1,695 4,328 3,375

Total benefits, losses and expenses

176,994 188,600 360,194 379,454

Income before income taxes

43,957 26,563 81,385 57,150

Income tax expense

10,450 7,626 21,230 16,522

Net income	$33,507	$18,937	$60,155	$40,628
Net income per share				
Basic	$0.78	$0.44	$1.40	$0.95
Diluted	$0.72	$0.41	$1.29	$0.89

Weighted average number of shares and equivalent shares (in thousands)				
Basic	42,886	42,732	42,876	42,727
Diluted	47,832	47,311	47,769	47,294
Comprehensive income (loss)				
Net income	$33,507	$18,937	$60,155	$40,628
Other comprehensive income (loss), net of taxes:				
Change in net unrealized gains on fixed maturities and equity securities	47,313	(17,276)	6,322	(58,267)
Change in minimum pension liability adjustment				
Other comprehensive income (loss)	47,313	(17,276)	6,322	(58,267)

Total	$80,820	$1,661	$66,477	$(17,639)

See accompanying Notes to Consolidated Financial Statements.

See accompanying Report of Independent Registered Public Accounting Firm.

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HORACE MANN EDUCATORS CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (UNAUDITED)

(Dollars in thousands, except per share data)

	Six Months Ended June 30, 2005	Six Months Ended June 30, 2004
Common stock		
Beginning balance	$ 60	$ 60
Options exercised, 2005, 46,674 shares; 2004, 17,502 shares		
Conversion of Director Stock Plan units, 2005, 761 shares; 2004, 20,511 shares		
Ending balance	60	60
Additional paid-in capital		
Beginning balance	343,178	342,306
Options exercised and conversion of Director Stock Plan units	768	665
Catastrophe-linked equity put option premium		(1,125)
Ending balance	343,946	341,846
Retained earnings		
Beginning balance	494,665	456,330
Net income	60,155	40,628
Cash dividends, $0.21 per share	(9,023)	(8,981)
Ending balance	545,797	487,977
Accumulated other comprehensive income (loss), net of taxes:		
Beginning balance	70,880	64,356
Change in net unrealized gains on fixed maturities and equity securities	6,322	(58,267)
Change in minimum pension liability adjustment		
Ending balance	77,202	6,089
Treasury stock, at cost		
Beginning and ending balance, 2005 and 2004, 17,503,371 shares	(332,577)	(332,577)
Shareholders equity at end of period	$ 634,428	$ 503,395

See accompanying Notes to Consolidated Financial Statements.

See accompanying Report of Independent Registered Public Accounting Firm.

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HORACE MANN EDUCATORS CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Dollars in thousands)

	Six Months Ended June 30, 2005	Six Months Ended June 30, 2004
Cash flows - operating activities		
Premiums collected	$ 343,387	$ 348,855
Policyholder benefits paid	(209,172)	(218,651)
Policy acquisition and other operating expenses paid	(114,667)	(103,923)
Federal income taxes recovered (paid)	1,096	(3,933)
Investment income collected	95,588	94,408
Interest expense paid	(4,098)	(2,937)
Other	1,329	863
Net cash provided by operating activities	113,463	114,682
Cash flows - investing activities		
Fixed maturities		
Purchases	(565,174)	(764,228)
Sales	295,710	431,027
Maturities	142,179	166,010
Net cash provided by (used in) short-term and other investments	(24,963)	8,582
Net cash used in investing activities	(152,248)	(158,609)
Cash flows - financing activities		
Dividends paid to shareholders	(9,023)	(8,981)
Principal repayments on Bank Credit Facility	(25,000)	
Exercise of stock options	750	665
Catastrophe-linked equity put option premium		(1,125)
Proceeds from issuance of Senior Notes due 2015	74,245	
Repurchase of Senior Notes due 2006	(29,077)	
Annuity contracts, variable and fixed		
Deposits	159,473	170,027
Benefits and withdrawals	(60,767)	(46,497)
Net transfer to variable annuity assets	(61,202)	(61,570)
Net decrease in life policy account balances	(2,248)	(2,364)
Change in bank overdrafts	(8,366)	(6,228)
Net cash provided by financing activities	38,785	43,927
Net increase (decrease) in cash		
Cash at beginning of period		
Cash at end of period	$	$

See accompanying Notes to Consolidated Financial Statements.

See accompanying Report of Independent Registered Public Accounting Firm.

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HORACE MANN EDUCATORS CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

June 30, 2005 and 2004

(Dollars in thousands, except per share data)

Note 1 - Basis of Presentation

The accompanying unaudited consolidated financial statements of Horace Mann Educators Corporation (HMEC ; and together with its subsidiaries, the Company or Horace Mann) have been prepared in accordance with United States (U.S.) generally accepted accounting principles (GAAP) and with the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. The Company believes that these financial statements contain all adjustments (consisting of normal recurring accruals) necessary to present fairly the Company s consolidated financial position as of June 30, 2005, the consolidated results of operations and comprehensive income for the three and six months ended June 30, 2005 and the consolidated changes in shareholders equity and cash flows for the six months ended June 30, 2005 and 2004. The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The subsidiaries of HMEC market and underwrite tax-qualified retirement annuities and private passenger automobile, homeowners, and life insurance products, primarily to educators and other employees of public schools and their families. The Company s principal operating subsidiaries are Horace Mann Life Insurance Company, Horace Mann Insurance Company, Teachers Insurance Company, Horace Mann Property & Casualty Insurance Company and Horace Mann Lloyds.

It is suggested that these financial statements be read in conjunction with the financial statements and the related notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

The results of operations for the three and six months ended June 30, 2005 are not necessarily indicative of the results to be expected for the full year.

The Company has reclassified the presentation of certain prior period information to conform with the June 30, 2005 presentation.

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Note 2 - Stock Based Compensation

The Company grants stock options to executive officers, other employees and directors. The exercise price of the option is equal to the fair market value of the Company s common stock on the date of grant. Additional information regarding the Company s stock-based compensation plans is contained in Notes to Consolidated Financial Statements Note 6 Shareholders Equity and Stock Options of the Company s Annual Report on Form 10-K for the year ended December 31, 2004. The Company accounts for stock option grants using the intrinsic value based method in accordance with Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees , and accordingly, recognizes no compensation expense for the stock option grants which have an exercise price equal to market price on the date of grant resulting in an intrinsic value of $0.

Alternatively, Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation , allows companies to recognize compensation cost for stock-based compensation plans, determined based on the fair value at the grant dates. If the Company had applied this alternative accounting method, net income and net income per share would have been reduced to the pro forma amounts indicated below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income				
As reported	$ 33,507	$ 18,937	$ 60,155	$ 40,628
Add: Stock-based compensation expense, after tax, included in reported net income				
Deduct: Stock-based compensation expense, after tax, determined under the fair value based method for all awards (1)	12	9,647	23	10,956
Pro forma	$ 33,495	$ 9,290	$ 60,132	$ 29,672
Net income per share basic				
As reported	$ 0.78	$ 0.44	$ 1.40	$ 0.95
Pro forma	$ 0.78	$ 0.22	$ 1.40	$ 0.69
Net income per share diluted				
As reported	$ 0.72	$ 0.41	$ 1.29	$ 0.89
Pro forma	$ 0.72	$ 0.21	$ 1.29	$ 0.66

(1) The fair value of each option grant was estimated on the date of grant using the Modified Roll-Geske option-pricing model with the following weighted average assumptions for 2005 and 2004, respectively: risk-free interest rates of 4.3% and 4.0%; dividend yield of 2.3% and 2.6%; expected lives of 7 and 10 years; and volatility of 19.4% and 25.1%. The six-month expense amounts represent one-half of the full year expense, reflecting options granted through June 30, 2005 and 2004, respectively, and vesting during the respective calendar years. The expense amounts for the three and six months ended June 30, 2004 also include the impact of accelerated vesting of stock options, as described in Notes to Consolidated Financial Statements Note 1 Summary of Significant Accounting Policies Stock Based Compensation of the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

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Note 3 - Debt

Indebtedness outstanding was as follows:

	June 30, 2005	December 31, 2004
Short-term debt:		
Bank Credit Facility	$	$ 25,000
Long-term debt:		
1.425% Senior Convertible Notes, due May 14, 2032. Aggregate principal amount of $244,500 less unaccrued discount of $128,362 (3.0% imputed rate)	116,138	116,138
6.05% Senior Notes, due June 15, 2015. Aggregate principal amount of $75,000 less unaccrued discount of $266 (6.1% imputed rate)	74,734	
6 5/8% Senior Notes, due January 15, 2006. Aggregate principal amount of $28,600 less unaccrued discount of $18 (6.7% imputed rate)		28,582
Total	$ 190,872	$ 169,720

The 1.425% Senior Convertible Notes due 2032 and 6 5/8% Senior Notes due 2006 are described in Notes to Consolidated Financial Statements Note 5 Debt of the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

Credit Agreement with Financial Institutions (Bank Credit Facility)

On May 31, 2005, the Company entered into a new Bank Credit Agreement which provides for unsecured borrowings of up to $100,000 (the Current Bank Credit Facility). The Current Bank Credit Facility expires on May 30, 2009. Interest accrues at varying spreads relative to corporate or eurodollar base rates and is payable monthly or quarterly depending on the applicable base rate. The unused portion of the Current Bank Credit Facility is subject to a variable commitment fee, which was 0.175% on an annual basis at June 30, 2005. On May 31, 2005, the Company borrowed $25,000 and subsequently repaid this balance in full on June 13, 2005, utilizing a portion of the proceeds from the issuance of the Senior Notes due 2015, described below.

On May 29, 2002, Horace Mann Educators Corporation entered into a Bank Credit Agreement that was amended effective June 1, 2004, increasing the commitment amount to $35,000, and May 3, 2005, extending the commitment termination date to June 30, 2005 from the previous termination date of May 31, 2005 (the Previous Bank Credit Agreement). The Previous Bank Credit Agreement was terminated on May 31, 2005, when the Company entered into the Current Bank Credit Facility. The $25,000 balance outstanding under the Previous Bank Credit Agreement was repaid in full on May 31, 2005, utilizing the borrowing under the Current Bank Credit Facility, described above.

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Note 3 Debt-(Continued)

6.05% Senior Notes due 2015 (Senior Notes due 2015)

On June 9, 2005, the Company issued $75,000 face amount of senior notes at an effective yield of 6.1%, which will mature on June 15, 2015. Interest on the Senior Notes due 2015 is payable semi-annually at a rate of 6.05%. The Senior Notes due 2015 are redeemable in whole or in part, at any time, at the Company s option, at a redemption price equal to the greater of (1) 100% of their principal amount or (2) the sum of the present values of the remaining scheduled payments of principal and interest thereon discounted, on a semi-annual basis, at the Treasury yield (as defined in the indenture) plus 30 basis points, plus, in either of the above cases, accrued interest to the date of redemption.

As of June 30, 2005, the net proceeds from the sale of the Senior Notes due 2015 have been used to (1) repay the Current Bank Credit Facility and (2) redeem the Senior Notes due 2006, described below. As of the date of this Report on Form 10-Q, management anticipates utilizing the remaining proceeds to recapture the Company s life reinsurance agreement with the United States branch of Sun Life Assurance Company of Canada. See also Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Financial Resources Capital Resources .

6 ^{5}/8% Senior Notes due 2006 (Senior Notes due 2006)

On June 30, 2005, the Company redeemed all of its outstanding Senior Notes due 2006, $28,600 aggregate principal amount, utilizing a portion of the proceeds from the issuance of the Senior Notes due 2015, described above. The aggregate cost of the repurchase was $29,107.

Universal Shelf Registration

To provide additional capital management flexibility, the Company filed a universal shelf registration on Form S-3 with the SEC in December 2003. The registration statement, which registers the offer and sale by the Company from time to time of up to $300,000 of various securities, which may include debt securities, preferred stock, common stock and/or depositary shares, was declared effective on December 30, 2003. The $75,000 face amount of Senior Notes due 2015 was issued utilizing this registration statement. No other securities associated with the registration statement have been issued as of the date of this Report on Form 10-Q.

Debt Retirement Charges

The repurchase of the Senior Notes due 2006 resulted in a pretax charge to income for the three and six months ended June 30, 2005 of $507, which was reported as a component of interest expense for these periods.

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Note 4 - Investments

Fixed Maturity Securities

The following table presents the composition and value of the Company s fixed maturity securities portfolio by rating category. The Company has classified the entire fixed maturity securities portfolio as available for sale, which is carried at fair value.

Rating of Fixed Maturity Securities (1)	Percent of Fair Value June 30, 2005	Percent of Fair Value December 31, 2004	June 30, 2005 Fair Value (2)	June 30, 2005 Amortized Cost
AAA	41.9%	42.0%	$ 1,544,196	$ 1,519,373
AA	7.8	7.5	286,929	277,360
A	24.3	24.3	895,928	829,940
BBB	20.0	20.3	738,933	691,546
BB	2.4	1.8	87,431	87,044
B	3.4	3.7	125,390	123,553
CCC or lower	0.1	0.3	3,767	1,350
Not rated (3)	0.1	0.1	3,035	3,042
Total	100.0%	100.0%	$ 3,685,609	$ 3,533,208

(1) Ratings are as assigned primarily by Standard & Poor s Corporation (S&P) when available, with remaining ratings as assigned on an equivalent basis by Moody s Investors Service, Inc. (Moody s). Ratings for publicly traded securities are determined when the securities are acquired and are updated monthly to reflect any changes in ratings.

(2) Fair values are based on quoted market prices, when available. Fair values for private placements and certain other securities that are infrequently traded are estimated by the Company with the assistance of its investment advisors utilizing recognized valuation methodology, including cash flow modeling.

(3) This category includes $3,035 of private placement securities not rated by either S&P or Moody s. The National Association of Insurance Commissioners (NAIC) has rated 100% of these private placement securities as investment grade.

The following table presents the distribution of the Company s fixed maturity securities portfolio by estimated expected maturity. Estimated expected maturities differ from contractual maturities by reflecting assumptions regarding borrowers utilization of the right to call or prepay obligations with or without call or prepayment penalties. Estimated expected maturities consider broker dealer survey values and are verified for consistency with the interest rate and economic environments.

	Percent of Total June 30, 2005	Percent of Total December 31, 2004	Fair Value June 30, 2005
Due in 1 year or less	8.6%	7.9%	$ 317,807

Due after 1 year through 5 years	27.1	26.1	997,890
Due after 5 years through 10 years	38.5	40.7	1,417,994
Due after 10 years through 20 years	8.1	7.5	300,196
Due after 20 years	17.7	17.8	651,722
Total	100.0%	100.0%	$ 3,685,609

The average option adjusted duration for the Company s fixed maturity securities was 5.6 years at June 30, 2005.

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Note 4 - Investments-(Continued)

The Company s investment portfolio includes no derivative financial instruments (futures, forwards, swaps, option contracts or other financial instruments with similar characteristics).

Securities Lending

The Company loans fixed income securities to third parties, primarily major brokerage firms. As of June 30, 2005 and December 31, 2004, fixed maturities with a fair value of $290,427 and $0, respectively, were on loan. Loans of securities are required at all times to be secured by collateral from borrowers at least equal to 100% of the market value of the securities loaned. The Company maintains effective control over the loaned securities and therefore reports them as Fixed Maturity Securities in the Consolidated Balance Sheets. Securities lending collateral is classified as investments with a corresponding liability in the Company s Consolidated Balance Sheets.

Note 5 - Pension Plans and Other Postretirement Benefits

The Company has the following retirement plans: a defined contribution plan; a 401(k) plan; a defined benefit plan for employees hired on or before December 31, 1998; and certain employees participate in a supplemental defined benefit plan or a supplemental defined contribution plan or both. Additional information regarding the Company s retirement plans is contained in Notes to Consolidated Financial Statements Note 10 Pension Plans and Postretirement Benefits of the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

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Note 5 - Pension Plans and Other Postretirement Benefits-(Continued)

The following table summarizes the components of net periodic pension cost recognized for the defined benefit plan and the supplemental defined benefit plans for the three and six months ended June 30, 2005 and 2004.

	Defined Benefit Plan		Supplemental Defined Benefit Plans	
	Three Months Ended June 30,		Three Months Ended June 30,	
	2005	2004	2005	2004
Components of net periodic pension expense:				
Service cost	$	$	$ (7)	$ (7)
Interest cost	625	776	229	243
Expected return on plan assets	(594)	(678)		
Recognized net actuarial loss	380	382	156	132
Settlement loss	412	523		
Net periodic pension expense	$ 823	$ 1,003	$ 378	$ 368

	Defined Benefit Plan		Supplemental Defined Benefit Plans	
	Six Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Components of net periodic pension expense:				
Service cost	$	$	$ (14)	$ (14)
Interest cost	1,250	1,552	458	486
Expected return on plan assets	(1,188)	(1,356)		
Recognized net actuarial loss	760	764	312	264
Settlement loss	824	1,047		
Net periodic pension expense	$ 1,646	$ 2,007	$ 756	$ 736

At the time of this Quarterly Report on Form 10-Q, the Company expects to contribute approximately $4,500 to the defined benefit plan and $1,035 to the supplemental defined benefit plans in 2005, of which $510 was contributed to the supplemental defined benefit plans during the six months ended June 30, 2005.

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Note 5 - Pension Plans and Other Postretirement Benefits-(Continued)

In addition to providing pension benefits, the Company also provides certain health care and life insurance benefits to retired employees, who meet the eligibility requirements, and their eligible dependents. The following table summarizes the components of the net periodic benefit cost of postretirement benefits other than pension for the three and six months ended June 30, 2005 and 2004.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	**2004**	**2005**	**2004**
Components of net periodic cost:				
Service cost	$ 22	$ 25	$ 44	$ 51
Interest cost	449	456	898	912
Amortization of prior service cost	(180)	(179)	(360)	(359)
Recognized net actuarial loss	118	33	236	67
Net periodic benefit cost	$ 409	$ 335	$ 818	$ 671

Consistent with disclosure in Notes to Consolidated Financial Statements Note 10 Pension Plans and Postretirement Benefits of the Company s Annual Report on Form 10-K for the year ended December 31, 2004, the Company expects to contribute $2,140 to the postretirement benefit plan in 2005, of which $831 was contributed during the six months ended June 30, 2005.

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Note 6 - Reinsurance

The Company recognizes the cost of reinsurance premiums over the contract periods for such premiums in proportion to the insurance protection provided. Amounts recoverable from reinsurers for unpaid claims and claim settlement expenses, including estimated amounts for unsettled claims, claims incurred but not reported and policy benefits, are estimated in a manner consistent with the insurance liability associated with the policy. The effects of reinsurance on premiums written and contract deposits; premiums and contract charges earned; and benefits, claims and settlement expenses were as follows:

Three months ended June 30, 2005	Gross Amount	Ceded	Assumed	Net
Premiums written and contract deposits	$ 251,089	$ 6,381	$ 2,594	$ 247,302
Premiums and contract charges earned	171,820	6,876	3,258	168,202
Benefits, claims and settlement expenses	98,721	6,367	2,615	94,969
Three months ended June 30, 2004				
Premiums written and contract deposits	$ 257,967	$ 6,437	$ 4,504	$ 256,034
Premiums and contract charges earned	171,257	6,743	4,583	169,097
Benefits, claims and settlement expenses	109,134	5,599	3,438	106,973
Six months ended June 30, 2005				
Premiums written and contract deposits	$ 489,182	$ 13,166	$ 5,036	$ 481,052
Premiums and contract charges earned	344,011	14,126	6,635	336,520
Benefits, claims and settlement expenses	202,330	9,486	5,129	197,973
Six months ended June 30, 2004				
Premiums written and contract deposits	$ 503,662	$ 11,584	$ 8,774	$ 500,852
Premiums and contract charges earned	340,269	12,693	9,084	336,660
Benefits, claims and settlement expenses	221,202	9,349	6,575	218,428

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Note 7 - Segment Information

The Company conducts and manages its business through four segments. The three operating segments, representing the major lines of insurance business, are: property and casualty insurance, principally personal lines automobile and homeowners products; annuity products, principally individual, tax-qualified fixed and variable deposits; and life insurance. The Company does not allocate the impact of corporate level transactions to the insurance segments, consistent with management s evaluation of the results of those segments, but classifies those items in the fourth segment, corporate and other. Historically, in addition to debt service, realized investment gains and losses and certain public company expenses, such charges have included restructuring charges, debt retirement costs, litigation charges and the provision for prior years taxes. Summarized financial information for these segments is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Insurance premiums and contract charges earned				
Property and casualty	$ 139,291	$ 141,392	$ 279,556	$ 280,992
Annuity	4,408	4,116	8,726	8,273
Life	24,503	23,589	48,238	47,395
Total	$ 168,202	$ 169,097	$ 336,520	$ 336,660
Net investment income				
Property and casualty	$ 8,414	$ 8,183	$ 16,437	$ 16,967
Annuity	27,929	26,777	55,616	54,192
Life	12,222	12,220	24,375	24,922
Corporate and other	168	(15)	149	(32)
Intersegment eliminations	(284)	(288)	(568)	(576)
Total	$ 48,449	$ 46,877	$ 96,009	$ 95,473
Net income				
Property and casualty	$ 22,204	$ 15,236	$ 41,923	$ 28,309
Annuity	3,056	2,687	5,480	6,592
Life	4,878	3,233	8,109	6,330
Corporate and other	3,369	(2,219)	4,643	(603)
Total	$ 33,507	$ 18,937	$ 60,155	$ 40,628
Amortization of intangible assets, pretax (included in segment net income)				
Value of acquired insurance in force				
Annuity	$ 944	$ 738	$ 2,344	$ 1,674
Life	372	390	744	780
Total	$ 1,316	$ 1,128	$ 3,088	$ 2,454

	June 30, 2005	December 31, 2004
Assets		
Property and casualty	$ 879,544	$ 870,627
Annuity	3,707,275	3,489,688
Life	1,162,974	962,564
Corporate and other	99,871	94,513
Intersegment eliminations	(25,484)	(45,490)
Total	$ 5,824,180	$ 5,371,902

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MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(Dollars in millions, except per share data)

Forward-looking Information

Statements made in the following discussion that state the Company s or management s intentions, hopes, beliefs, expectations or predictions of future events or the Company s future financial performance are forward-looking statements and involve known and unknown risks, uncertainties and other factors. Horace Mann is not under any obligation to (and expressly disclaims any such obligation to) update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. It is important to note that the Company s actual results could differ materially from those projected in forward-looking statements due to, among other risks and uncertainties inherent in the Company s business, the following important factors:

Changes in the composition of the Company s assets and liabilities which may result from occurrences such as acquisitions, divestitures, impairment in asset values or changes in estimates of insurance reserves.

Fluctuations in the market value of securities in the Company s investment portfolio and the related after-tax effect on the Company s shareholders equity and total capital through either realized or unrealized investment losses. In addition, the impact of fluctuations in the financial markets on the Company s defined benefit pension plan assets and the related after-tax effect on the Company s operating expenses, shareholders equity and total capital.

The impact of fluctuations in the financial markets on the Company s variable annuity fee revenues, valuations of deferred policy acquisition costs and value of acquired insurance in force, and the level of guaranteed minimum death benefit reserves.

The impact of fluctuations in the capital markets on the Company s ability to refinance outstanding indebtedness or repurchase shares of the Company s common stock.

Defaults on interest or dividend payments in the Company s investment portfolio due to credit issues and the resulting impact on investment income.

Prevailing interest rate levels, including the impact of interest rates on (i) unrealized gains and losses in the Company s investment portfolio and the related after-tax effect on the Company s shareholders equity and total capital, (ii) the book yield of the Company s investment portfolio and (iii) the Company s ability to maintain appropriate interest rate spreads over the fixed rates guaranteed in the Company s life and annuity products.

The cyclicality of the insurance industry and the related effects of changes in price competition and industry-wide underwriting results.

The frequency and severity of catastrophes such as hurricanes, earthquakes, storms and wildfires and the ability of the Company to provide accurate estimates of ultimate catastrophe costs in its consolidated financial statements in light of such factors as: the proximity of the catastrophe occurrence date to the date of the consolidated financial statements, potential inflation of property repair costs in the affected area and the occurrence of multiple catastrophes in a geographic area over a relatively short period of time.

Based on property and casualty direct earned premiums for 2004, the Company s ten largest states represented 55% of the segment total. Included in this top ten group are certain states in which catastrophe occurrences are relatively common: California, Florida, North Carolina, South Carolina, Louisiana and Texas.

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The ability of the Company to maintain a favorable catastrophe reinsurance program considering both availability and cost; and the collectibility of reinsurance receivables.

Adverse development of property and casualty loss experience and its impact on estimated claims and claim settlement expenses for losses occurring in prior years.

Business risks inherent in the Company s restructuring of its property and casualty claims operation.

Adverse changes in business persistency, policyholder mortality and morbidity rates and the resulting impact on both estimated reserves and the valuations of deferred policy acquisition costs and value of acquired insurance in force.

Changes in insurance regulations, including (i) those affecting the ability of the Company s insurance subsidiaries to distribute cash to the holding company and (ii) those impacting the Company s ability to profitably write property and casualty insurance policies in one or more states.

Changes in accounting or financial reporting standards issued by the FASB, SEC or other standard-setting bodies which may have an adverse effect on the Company s results of operations, financial condition and/or cost of doing business.

Changes in federal income tax laws and changes resulting from federal tax audits affecting corporate tax rates or taxable income.

Changes in federal and state laws and regulations which affect the relative tax and other advantages of the Company s life and annuity products to customers, including, but not limited to, adverse changes in IRS regulations governing 403(b) plans.

The resolution of legal proceedings and related matters including the potential adverse impact on the Company s reputation and charges against the Company s earnings resulting from legal defense costs, a settlement agreement and/or an adverse finding or findings against the Company from the proceedings.

The Company s ability to maintain favorable claims-paying ability, financial strength and debt ratings.

The competitive impact of new entrants such as mutual funds and banks into the tax-deferred annuity products markets, and the Company s ability to profitably expand its property and casualty business in highly competitive environments.

The Company s ability to develop and expand its agent force and its direct product distribution systems, as well as the Company s ability to maintain and secure product sponsorships by local, state and national education associations.

The risk related to the Company s dated and complex information systems, which are more prone to error than advanced technology systems.

Disruptions of the general business climate, investments, capital markets and consumer attitudes caused by geopolitical acts such as terrorism, war or other similar events.

The impact of a disaster or catastrophic event affecting the Company s employees or its home office facilities and the Company s ability to recover and resume its business operations on a timely basis.

Executive Summary

For the six months ended June 30, 2005, the Company s net income increased compared to the same period in the prior year, primarily reflecting improved property and casualty segment earnings. This improvement was driven by aggressive underwriting and pricing actions taken in 2003 and 2004, ongoing improvements in claims processes, cost containment initiatives and a continuing low level of non-catastrophe claim frequency. Along with the rest of the insurance industry, the Company also benefited in the current period from a relatively low level of catastrophe losses.

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In addition to the strong operating results, Horace Mann received refunds from the Internal Revenue Service (IRS) in April 2005, including amounts related to tax years 1996 and 1997, which are now deemed to be closed. This resulted in the elimination of the contingent tax liability related to those two years which reduced second quarter 2005 federal income tax expense by $2.7 million. In addition, $1.4 million of interest on the tax refund amounts was received and recorded as pretax income in the second quarter.

Premiums written and contract deposits decreased 4% compared to the first six months of 2004, due primarily to a reduction in new annuity single premium and rollover deposit receipts. In addition, property and casualty premiums written declined as increases in average voluntary automobile and homeowners premium per policy which were moderated to some extent by the improvement in quality in the books of business were more than offset by the decline in policies in force in these lines.

Critical Accounting Policies

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires the Company s management to make estimates and assumptions based on information available at the time the consolidated financial statements are prepared. These estimates and assumptions affect the reported amounts of the Company s consolidated assets, liabilities, shareholders equity and net income. Certain accounting estimates are particularly sensitive because of their significance to the Company s consolidated financial statements and because of the possibility that subsequent events and available information may differ markedly from management s judgements at the time the consolidated financial statements were prepared. Management has discussed with the Audit Committee the quality, not just the acceptability, of the Company s accounting principles as applied in its financial reporting. The discussions generally included such matters as the consistency of the Company s accounting policies and their application, and the clarity and completeness of the Company s consolidated financial statements, which include related disclosures. For the Company, the areas most subject to significant management judgements include: liabilities for property and casualty claims and claim settlement expenses, liabilities for future policy benefits, deferred policy acquisition costs, value of acquired insurance in force for annuity and interest-sensitive life products, valuation of investments and valuation of assets and liabilities related to the defined benefit pension plan.

Liabilities for Property and Casualty Claims and Claim Settlement Expenses

Underwriting results of the property and casualty segment are significantly influenced by estimates of the Company s ultimate liability for insured events. There is a high degree of uncertainty inherent in the estimates of ultimate losses underlying the liability for unpaid claims and claim settlement expenses. This inherent uncertainty is particularly significant for liability-related exposures due to the extended period, often many years, that transpires between a loss event, receipt of related claims data from policyholders and ultimate settlement of the claim. Reserves for property and casualty claims include provisions for payments to be made on reported claims, claims incurred but not yet reported and associated settlement expenses. The process by which these reserves are established requires reliance upon estimates based on known facts and on interpretations of circumstances, including the Company s experience with similar cases and historical trends involving claim payments and related patterns, pending levels of unpaid claims and product mix, as well as other factors including court decisions, economic conditions and public attitudes.

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The Company continually updates loss estimates using both quantitative information from its reserving actuaries and qualitative information derived from other sources. Adjustments may be required as information develops which varies from experience, or, in some cases, augments data which previously were not considered sufficient for use in determining liabilities. The effects of these adjustments may be significant and are charged or credited to income for the period in which the adjustments are made. Detailed discussion of the impact of adjustments recorded during recent years is included in Notes to Consolidated Financial Statements Note 4 Property and Casualty Unpaid Claims and Claim Expenses of the Company s Annual Report on Form 10-K for the year ended December 31, 2004. Due to the nature of the Company s personal lines business, the Company has no exposure to claims for toxic waste cleanup, other environmental remediation or asbestos-related illnesses other than claims under homeowners insurance policies for environmentally related items such as mold.

The Company completes a detailed study of property and casualty reserves based on information available at the end of each quarter and year. Trends of reported losses (paid amounts and case reserves on claims reported to the Company) for each accident year are reviewed and ultimate loss costs for those accident years are estimated. The Company engages an independent property and casualty actuarial consulting firm to prepare an independent study of the Company s property and casualty reserves at June 30 and December 31 of each year.

Liabilities for Future Policy Benefits

Liabilities for future benefits on life and annuity policies are established in amounts adequate to meet the estimated future obligations on policies in force. Liabilities for future policy benefits on certain life insurance policies are computed using the net level premium method and are based on assumptions as to future investment yield, mortality and withdrawals. Mortality and withdrawal assumptions for all policies have been based on actuarial tables which are consistent with the Company s own experience. Liabilities for future benefits on annuity contracts and certain long-duration life insurance contracts are carried at accumulated policyholder values without reduction for potential surrender or withdrawal charges. In the event actual experience varies from the estimated liabilities, adjustments are charged or credited to income for the period in which the adjustments are made.

Deferred Policy Acquisition Costs and Value of Acquired Insurance in Force for Annuity and Interest-Sensitive Life Products

Policy acquisition costs, consisting of commissions, policy issuance and other costs, which vary with and are primarily related to the production of business, are capitalized and amortized on a basis consistent with the type of insurance coverage. For investment (annuity) contracts, acquisition costs, and also the value of annuity business acquired in the 1989 acquisition of the Company (Annuity VIF), are amortized over 20 years in proportion to estimated gross margins. Capitalized acquisition costs for interest-sensitive life contracts are also amortized over 20 years in proportion to estimated gross margins.

The most significant assumptions that are involved in the estimation of annuity gross margins include future financial market performance, interest rate spreads, business surrender/lapse rates and the impact of realized investment gains and losses. For the variable deposit portion of the annuity segment, the Company amortizes policy acquisition costs and the

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Annuity VIF utilizing a future financial market performance assumption of a 10% reversion to the mean approach with a 200 basis point corridor around the mean. At June 30, 2005, the ratio of capitalized annuity policy acquisition costs and the Annuity VIF asset to the total annuity accumulated cash value was approximately 4%.

In the event actual experience differs significantly from assumptions or assumptions are significantly revised, the Company may be required to record a material charge or credit to amortization expense for the period in which the adjustment is made. As noted above, there are a number of assumptions involved in the valuation of capitalized policy acquisition costs and the Annuity VIF. As one example of the volatility of this amortization, if all other assumptions are met, a 1% deviation from the targeted financial market performance for the underlying mutual funds of the Company s variable annuities would currently impact amortization between $0.1 million and $0.2 million. This result may change depending on the magnitude and direction of the deviation. Detailed discussion of the impact of adjustments to the amortization of capitalized acquisition costs and Annuity VIF is included in Results of Operations Amortization of Policy Acquisition Expenses and Intangible Assets .

Valuation of Investments

The Company s methodology of assessing other-than-temporary impairments is based on security-specific facts and circumstances as of the date of the reporting period. Based on these facts, if management believes it is probable that amounts due will not be collected according to the contractual terms of a debt security not impaired at acquisition, or if the Company does not have the ability or intent to hold a security with an unrealized loss until it matures or recovers in value, an other-than-temporary impairment shall be considered to have occurred. As a general rule, if the fair value of a debt security has fallen below 80% of book value for more than six months, this security will be reviewed for an other-than-temporary impairment. Additionally, if events become known that call into question whether the security issuer has the ability to honor its contractual commitments, whether or not such security has been trading above an 80% fair value to book value relationship, such security holding will be evaluated to determine whether or not such security has suffered an other-than-temporary decline in value.

The Company reviews the fair value of all investments in its portfolio on a monthly basis to assess whether an other-than-temporary decline in value has occurred. These reviews, in conjunction with the Company s investment managers monthly credit reports and relevant factors such as (1) the financial condition and near-term prospects of the issuer, (2) the Company s ability or intent to retain the investment long enough to allow for the anticipated recovery in fair value, (3) the stock price trend of the issuer, (4) the market leadership position of the issuer, (5) the debt ratings of the issuer and (6) the cash flows of the issuer, are all considered in the impairment assessment. A write-down of an investment is recorded when a decline in the fair value of that investment is deemed to be other-than-temporary, with a realized investment loss charged to income for the period.

A decline in fair value below amortized cost is not assumed to be other-than-temporary for fixed maturity investments with unrealized losses due to market conditions or industry-related events where there exists a reasonable expectation that fair value will recover versus historical cost and the Company has the intent and ability to hold the investment until maturity or a market recovery is realized. An other-than-temporary impairment loss will be recognized based upon all relevant facts and circumstances for each investment, as appropriate.

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Valuation of Assets and Liabilities Related to the Defined Benefit Pension Plan

Effective April 1, 2002, participants stopped accruing benefits under the defined benefit pension plan but continue to retain the benefits they had accrued to date.

The Company s cost estimates for its defined benefit pension plan are determined annually based on assumptions which include the discount rate, expected return on plan assets, anticipated retirement rate and estimated lump sum distributions. A discount rate of 5.75% was used by the Company for estimating accumulated benefits under the plan at December 31, 2004, which was based on the average yield for long-term, high grade securities having maturities generally consistent with the defined benefit pension payout period. To set its discount rate, the Company looks to leading indicators, including Moody s Aa long-term bond index. The expected annual return on plan assets assumed by the Company at December 31, 2004 was 7.50%. The assumption for the long-term rate of return on plan assets was determined by considering actual investment experience during the lifetime of the plan, balanced with reasonable expectations of future growth considering the various classes of assets and percentage allocation for each asset class. Management believes that it has adopted realistic assumptions for investment returns, discount rates and other key factors used in the estimation of pension costs and asset values.

To the extent that actual experience differs from the Company s assumptions, subsequent adjustments may be required, with the effects of those adjustments charged or credited to income and/or shareholders equity for the period in which the adjustments are made. Generally, a change of 50 basis points in the discount rate would inversely impact pension expense and accumulated other comprehensive income (AOCI) by approximately $0.2 million and $2 million, respectively. In addition, for every $1 million increase in the value of pension plan assets, there is an equal increase in AOCI.

Results of Operations

Insurance Premiums and Contract Charges

Insurance Premiums Written and Contract Deposits

(Includes annuity and life contract deposits)

	Six Months Ended June 30,		Increase (Decrease)	
	2005	**2004**	**Percent**	**Amount**
Property & casualty				
Automobile and property (voluntary)	$ 268.8	$ 276.8	-2.9%	$ (8.0)
Involuntary and other property & casualty	1.3	1.3		
Total property & casualty	270.1	278.1	-2.9%	(8.0)
Annuity deposits	159.5	170.0	-6.2%	(10.5)

Life	51.5	52.8	-2.5%	(1.3)
Total	$ 481.1	$ 500.9	-4.0%	$ (19.8)

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Insurance Premiums and Contract Charges Earned

(Excludes annuity and life contract deposits)

	Six Months Ended June 30,		Increase (Decrease)	
	2005	**2004**	**Percent**	**Amount**
Property & casualty				
Automobile and property (voluntary)	$ 275.2	$ 276.9	-0.6%	$ (1.7)
Involuntary and other property & casualty	4.4	4.1	7.3%	0.3
Total property & casualty	279.6	281.0	-0.5%	(1.4)
Annuity	8.7	8.3	4.8%	0.4
Life	48.2	47.4	1.7%	0.8
Total	$ 336.5	$ 336.7	-0.1%	$ (0.2)

For the first six months of 2005, the Company s premiums written and contract deposits decreased 4.0% compared to the prior year, primarily as a result of a reduced level of new annuity single premium and rollover deposit receipts. In addition, property and casualty premiums written declined as increases in average voluntary automobile and homeowners premium per policy which were moderated to some extent by the improvement in quality in the books of business were more than offset by the decline in policies in force in these lines. Voluntary property and casualty business represents policies sold through the Company s marketing organization and issued under the Company s underwriting guidelines. Involuntary property and casualty business consists of allocations of business from state mandatory insurance facilities and assigned risk business.

The Company s exclusive agent force totaled 837 at June 30, 2005, reflecting an increase of 4.6% compared to 800 agents at December 31, 2004 and an increase of 4.0% compared to 805 agents at June 30, 2004. Management currently anticipates additional growth in the size of the Company s exclusive agent force throughout the remainder of 2005, although at a more moderate rate than the first six months. During 2005, additional emphasis is being placed on further improvements in agent retention, as well as on hiring an increased number of quality candidates. Of the current period-end total, 264 agents were in their first 24 months with the Company, reflecting a decrease of 12.6% compared to June 30, 2004, largely due to the reduced number of new hires in 2004 and retention levels in the last six months of 2004. A greater number of new agents were hired in the first six months of 2005 compared to prior year. Terminations of agents in their first 24 months with the Company were approximately one-third of the level experienced in the first six months of the prior year. The number of experienced agents in the agent force, 573, increased 13.9% compared to a year earlier as a result of improved retention. In the first six months of 2005, average agent productivity was comparable to the same period in 2004 in total and for all product lines. Average agent productivity is measured as new sales premiums from the exclusive agent force per the average number of exclusive agents for the period.

For the first six months of 2005, total sales, which include the independent agent distribution channel, decreased 9.1% compared to a year earlier, largely due to a decrease in new annuity business. Compared to a record level of annuity sales in the prior year, total new annuity sales decreased 10.7% in the first six months of 2005. This decline was due primarily to a lower level of annuity new business from independent agents, reflecting the Company s desired shift in mix of business from this channel. While total career agent sales decreased in the current six month period compared to a year earlier in all product lines, second quarter results reduced the rate of decline for annuity, automobile and homeowners.

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Total voluntary automobile and homeowners premium written decreased 2.9% in the first six months of 2005. While the quality of the Company s voluntary automobile and homeowners business continues to improve, the premium impact of increases in average premium per policy for both lines were more than offset by the decline in policies in force. Voluntary automobile insurance premium written decreased 4.8% ($9.7 million) compared to the first six months of 2004, while homeowners premium increased 2.3% ($1.7 million). Average written premium increased approximately 2% for voluntary automobile and approximately 8% for homeowners compared to the prior year. Average earned premium also increased 4% for voluntary automobile and 11% for homeowners compared to the first six months of 2004. Through June 30, 2005, approved rate increases for the Company s automobile and homeowners business were minimal compared to approved increases of 7% and 15%, respectively, during the first six months of 2004. As of June 30, 2005, automobile policies in force decreased by 12,000 compared to December 31, 2004 and 28,000 compared to June 30, 2004. The Company continues to increase educator business as a percentage of both new and total voluntary automobile policies. Homeowners policies in force decreased 5,000 compared to December 31, 2004 and 8,000 compared to June 30, 2004, reflecting expected reductions primarily in non-educator policies due to the Company s pricing and underwriting actions. At June 30, 2005, there were 533,000 voluntary automobile and 268,000 homeowners policies in force, for a total of 801,000 policies, compared to a total of 818,000 policies at December 31, 2004 and 837,000 policies at June 30, 2004. To curtail the decline in automobile policies in force, in 2005 the Company is implementing both short- and medium-term initiatives to increase new business and improve policy retention.

Based on policies in force, the total property and casualty 12-month retention rate for new and renewal policies was 84% at June 30, 2005, compared to 85% at June 30, 2004.

Due to rate limitations for coastal homeowners policies in Florida and to further reduce exposure to catastrophic losses, the Company has undertaken a reunderwriting program which is anticipated to result in non-renewal of approximately 3,300 homeowners policies. Following state mandated delays as a result of the four hurricanes that impacted Florida in 2004, the Company s non-renewal process resumed in the first quarter of 2005 and is expected to result in a full year reduction of approximately $3 million and $2 million in direct written premiums and direct earned premiums, respectively. In the Spring 2005 session, the Florida legislature implemented measures, including a single deductible per hurricane season and requiring up-front payment by insurance companies of full replacement cost, to address the impact of future and past multi-hurricane seasons. In addition, an independent financial audit has determined a $515 million deficit in the Citizens Property Insurance Corporation s (Citizens) high-risk account as a result of the four hurricanes in Florida in 2004. Following their installation in August 2005, the new Citizens board of governors may address the need for a possible assessment to replenish the surplus of Citizens. If there is an industry assessment, the Company will in turn assess its Florida property policyholders. The impact on the Company of these measures and possible assessments is not determinable at the time of this Quarterly Report on Form 10-Q.

New annuity deposits decreased 6.2% compared to the first six months of 2004. The decline reflected a 6.9% increase in new scheduled annuity deposits offset by a 20.1% decrease in single premium and rollover deposits. While new deposits to fixed accounts decreased 12.1%, or $12.6 million, compared to the prior year due to the current low interest rate environment, new deposits to variable accounts increased 3.2%, or $2.1 million, compared to the first six months of 2004.

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In 2001, the Company began building a nationwide network of independent agents who will comprise a second distribution channel for the Company s 403(b) tax-qualified annuity products. The independent agent distribution channel included 627 authorized agents at June 30, 2005. During the first six months of 2005, this channel generated $16.7 million in annualized new annuity sales for the Company compared to $26.5 million for the first six months of 2004 and $38.0 million for the full year 2004, with the lack of growth in the current period reflecting the Company s efforts to change the product mix from this channel to more tax-qualified and variable annuity sales.

Total annuity accumulated cash value of $3.2 billion at June 30, 2005 increased 8.6% compared to a year earlier, reflecting the increase from new business over the 12 months, continued favorable retention and improving financial markets compared to June 30, 2004. At June 30, 2005, the number of annuity contracts outstanding of 160,000 increased 0.6%, or 1,000 contracts, compared to December 31, 2004 and increased 2.6%, or 4,000 contracts, compared to June 30, 2004.

Variable annuity accumulated balances were 8.3% higher at June 30, 2005 than at June 30, 2004, while annuity segment contract charges earned increased 4.8%, or $0.4 million, compared to the first six months of 2004.

Life segment premiums and contract deposits declined 2.5%, or $1.3 million, compared to the first six months of 2004, primarily reflecting the shift in new business mix toward partner company products. The ordinary life insurance in force lapse ratio was 6.9% for the 12 months ended June 30, 2005, compared to 7.3% for the same period a year earlier.

Net Investment Income

Pretax investment income of $96.0 million for the six months ended June 30, 2005 increased 0.5%, or $0.5 million, (0.3%, or $0.2 million, after tax) compared to the prior year. Growth in the size of the investment portfolio more than offset a decrease of approximately $2.5 million pretax in prepayment income along with a decline in the portfolio yield. Average invested assets (excluding securities lending collateral) increased 8.7% over the past 12 months. The average pretax yield on the investment portfolio was 5.4% (3.7% after tax) for the first six months of 2005, compared to a pretax yield of 5.8% (4.0% after tax) for the same period in 2004.

Net Realized Investment Gains and Losses

Net realized investment gains were $9.0 million for the first six months of 2005 compared to net realized investment gains of $4.5 million in the prior year. There were no impairment charges from the Company s fixed income security portfolio in either period. Gains realized in the current period included $1.9 million from sales of securities for which impairment charges were recorded in 2003. The net gains in both years were realized from ongoing investment portfolio management activity.

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The table below presents the Company s fixed maturity securities portfolio as of June 30, 2005 by major asset class, including the ten largest sectors of the Company s corporate bond holdings.

Fixed Maturity Securities

	Number of Issuers	Fair Value	Amortized Cost	Pretax Unrealized Gain
Corporate bonds				
Banking and Finance	40	$ 406.9	$ 382.6	$ 24.3
Energy	48	224.6	204.6	20.0
Utilities	29	192.8	179.1	13.7
Telecommunications	21	140.4	129.7	10.7
Food and Beverage	26	121.4	115.1	6.3
Insurance	13	104.7	97.0	7.7
Health Care	23	95.8	92.1	3.7
Transportation	12	86.9	83.7	3.2
Real Estate	13	71.8	68.1	3.7
Industry, Manufacturing	20	60.2	54.6	5.6
All Other Corporates (1)	164	531.0	506.1	24.9
Total corporate bonds	409	2,036.5	1,912.7	123.8
Mortgage-backed securities				
U.S. government and federally sponsored agencies	439	693.8	689.5	4.3
Other	16	53.0	50.9	2.1
Municipal bonds	165	570.8	553.2	17.6
Government bonds				
U.S.	7	214.1	213.7	0.4
Foreign	10	39.0	34.9	4.1
Collateralized debt obligations (2)	3	15.7	15.3	0.4
Asset-backed securities	10	62.7	63.0	(0.3)
Total fixed maturity securities	1,059	$ 3,685.6	$ 3,533.2	$ 152.4

(1) The All Other Corporates category contains 19 additional industry classifications. Automobiles; broadcasting and media; defense; building and materials; consumer products and paper represented $308.1 million of fair value at June 30, 2005, with the remaining 13 classifications each representing less than $34 million of the fair value at June 30, 2005.

(2) All of the securities were rated investment grade by Standard and Poor s Corporation and/or Moody s Investors Service, Inc. at June 30, 2005.

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At June 30, 2005, the Company s diversified fixed maturity portfolio consisted of 1,261 investment positions, issued by 1,059 entities, and totaled approximately $3.7 billion in fair value. The portfolio was 94.0% investment grade, based on fair value, with an average quality rating of AA-. At June 30, 2005, the portfolio had $10.9 million pretax of total gross unrealized losses related to 271 positions. At December 31, 2004, the total pretax gross unrealized losses were $8.8 million related to 178 positions. The following table provides information regarding fixed maturity securities that had an unrealized loss at June 30, 2005, including the length of time that the securities have continuously been in an unrealized loss position.

Investment Positions With Unrealized Losses Segmented by Quality

and Period of Continuous Unrealized Loss

As of June 30, 2005

	Number of Positions	Fair Value	Amortized Cost	Pretax Unrealized Loss
Investment grade				
6 Months or less	69	$ 360.7	$ 363.7	$ (3.0)
7 through 12 months	32	149.8	151.3	(1.5)
13 through 24 months	41	251.6	254.6	(3.0)
25 through 36 months	6	34.6	36.0	(1.4)
37 through 48 months				
Greater than 48 months				
Total	148	$ 796.7	$ 805.6	$ (8.9)
Non-investment grade				
6 Months or less	92	$ 51.1	$ 52.8	$ (1.7)
7 through 12 months	24	9.9	10.2	(0.3)
13 through 24 months	3	1.2	1.2	*
25 through 36 months				
37 through 48 months				
Greater than 48 months				
Total	119	$ 62.2	$ 64.2	$ (2.0)
Not rated				
Total, all 25 through 36 months	4	$ 2.4	$ 2.4	*
Grand total	271	$ 861.3	$ 872.2	$ (10.9)

* Less than $(0.1) million

Of the investment positions with unrealized losses, no issuers had pretax unrealized losses greater than $1.0 million. One security, redeemable preferred stock issued by the Federal National Mortgage Association (FNMA), was trading below 80% of book value (at 79.5% of the $2.7 million amortized cost) at June 30, 2005. This security was purchased in June 2003 when interest rates were at a 40 year low. The Company views the decrease in value of all of the securities with unrealized losses at June 30, 2005 as temporary, expects recovery in fair value, anticipates continued payments under the terms of the securities, and has the intent and ability to hold these securities until maturity or a recovery in fair value occurs. Therefore, no impairment of these securities was recorded at June 30, 2005. Future changes in circumstances related to these and other securities could require subsequent impairment in value. The Company s investment

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guidelines generally limit single corporate issuer concentrations to 4.0% (after tax) of shareholders equity for AA or AAA rated securities, 2.5% (after tax) of shareholders equity for A rated securities, 2.0% (after tax) of shareholders equity for BBB rated securities, and 1.0% (after tax) of shareholders equity for non-investment grade securities.

Benefits, Claims and Settlement Expenses

	Six Months Ended June 30,		Increase (Decrease)	
	2005	**2004**	**Percent**	**Amount**
Property and casualty				
Before catastrophe losses	$ 172.8	$ 192.6	-10.3%	$ (19.8)
Catastrophe losses	4.0	3.7	8.1%	0.3
Total property and casualty	176.8	196.3	-9.9%	(19.5)
Annuity	(0.1)	0.7		(0.8)
Life	21.3	21.4	-0.5%	(0.1)
Total	$ 198.0	$ 218.4	-9.3%	$ (20.4)

Property and Casualty Claims and Claim Expenses

	Six Months Ended June 30,	
	2005	**2004**
Incurred claims and claim expenses:		
Claims occurring in the current year	$ 178.4	$ 196.3
Decrease in estimated reserves for claims occurring in prior years (1):		
Policies written by the Company	(1.6)	
Business assumed from state reinsurance facilities		
Total decrease	(1.6)	
Total claims and claim expenses incurred	$ 176.8	$ 196.3
Property and casualty loss ratio:		
Before catastrophe losses	61.7%	68.5%
After catastrophe losses	63.3%	69.9%

(1) Shows the amounts by which the Company decreased its reserves in each of the periods indicated for claims occurring in previous periods to reflect subsequent information on such claims and changes in their projected final settlement costs.

For the six months ended June 30, 2005, the Company s benefits, claims and settlement expenses decreased compared to the prior year, primarily reflecting improvements in non-catastrophe property and casualty current accident year trends, particularly in claim frequencies. The Company s catastrophe losses were comparable for the two periods. Development of prior years property and casualty reserves had a minimal favorable effect on benefits, claims and settlement expenses for the six months ended June 30, 2005 and no effect for the same period in 2004.

For the six months ended June 30, 2005, the voluntary automobile loss ratio of 68.8% decreased by 3.4 percentage points compared to the same period a year earlier and improved 1.8 percentage points compared to the loss ratio of 70.6% for full year 2004. The Company s benefits, claims and settlement expenses also reflected improvements in the homeowners non-catastrophe loss ratio of 12.9 percentage points compared to the first six months of 2004 and 7.2 percentage

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points compared to the 12 months ended December 31, 2004 as a result of the favorable impact of underwriting initiatives and rate increases on earned premiums, as well as the Company s claims initiatives, which have focused on loss and expense control.

The homeowners loss ratio of 47.5% for the six months ended June 30, 2005, including the effect of catastrophe losses, decreased 12.4 percentage points compared to a year earlier, reflecting an increase in average premium per policy and an improvement in non-catastrophe loss frequency as a result of loss containment initiatives such as tightened underwriting guidelines, deductible management, an aggressive reunderwriting program and benefits of the Company s claims initiatives.

The Company s GAAP guaranteed minimum death benefits (GMDB) reserve was $0.2 million at June 30, 2005, compared to $0.1 million at December 31, 2004 and zero at June 30, 2004.

Interest Credited to Policyholders

	Six Months Ended June 30,		Increase (Decrease)	
	2005	**2004**	**Percent**	**Amount**
Annuity	$ 39.7	$ 37.0	7.3%	$ 2.7
Life	17.0	16.3	4.3%	0.7
Total	$ 56.7	$ 53.3	6.4%	$ 3.4

Compared to prior year, the current period increase in annuity segment interest credited reflected a 9.7% increase in average accumulated fixed deposits, partially offset by a 9 basis point decline in the average annual interest rate credited to 4.4%. Life insurance interest credited increased as a result of the growth in interest-sensitive life insurance reserves.

The net interest spread on fixed annuity account value on deposit measures the difference between the rate of income earned on the underlying invested assets and the rate of interest which policyholders are credited on their account values. Fixed annuity crediting rates were lowered throughout 2004 and 2003 to reflect the decline in the rate of income on invested assets caused by lower investment rates on new and reinvested funds. The annualized net interest spreads for the six months ended June 30, 2005 and 2004 were 136 basis points and 166 basis points, respectively. Excluding the benefit of prepayment income on a structured mortgage-backed security, the corresponding annualized net interest spreads were 134 and 152 basis points.

As of June 30, 2005, fixed annuity account values totaled $1.9 billion, including $1.6 billion of deferred annuities. Approximately 20% of the deferred annuity account values had minimum guaranteed interest rates ranging from 3.0% to 4.0% while approximately 77% of account values had minimum guaranteed rates of 4.5% or greater. For $1.5 billion of the deferred annuity account values, the credited interest rate was equal to the minimum guaranteed rate. Due to limitations on the Company s ability to further lower interest crediting rates, coupled with the potential for continued low interest rates and expected reductions in prepayment income in 2005, the Company expects to experience additional fixed annuity spread compression in future periods.

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Operating Expenses

For the first six months of 2005, operating expenses decreased 10.9%, or $7.4 million, compared to the prior year, primarily reflecting benefits from the Company s expense control initiatives. The property and casualty expense ratio of 22.1% for the six months ended June 30, 2005 decreased 0.2 percentage point compared to the prior year, reflecting this segment s portion of corporate-wide expense reductions.

The Company offers long-term care and variable and fixed interest rate universal life policies, with three third-party vendors underwriting and bearing the risk of such insurance (Life Partner Products) and the Company receiving a commission on the sale of that business. The volume of Life Partner Product sales by the Company s agents decreased slightly during the first six months of 2005. The amount of commissions received by the Company in the first six months of 2005 in excess of costs for agent commissions and commission related expenses was approximately $0.5 million, comparable to the same period in 2004.

Amortization of Policy Acquisition Expenses and Intangible Assets

For the six months ended June 30, 2005, the combined amortization of policy acquisition expenses and intangible assets was $40.3 million compared to $36.3 million recorded for the same period in the prior year. Amortization of intangible assets was $3.1 million for the six months ended June 30, 2005 compared to $2.5 million for the same period a year earlier. The June 30, 2005 valuation of Annuity VIF resulted in a $0.4 million increase in amortization compared to a $0.1 million decrease from a similar valuation at June 30, 2004.

Amortized policy acquisition expenses were $37.2 million for the first six months of 2005 compared to $33.8 million for the same period in 2004. The June 30, 2005 valuation of annuity deferred policy acquisition costs resulted in a $2.4 million increase in amortization compared to a $0.4 million decrease in amortization resulting from a similar valuation at June 30, 2004. For the life segment, the June 30, 2005 valuation of deferred policy acquisition costs resulted in a $0.5 million decrease in amortization compared to a $0.7 million increase from the 2004 valuation. The remaining increase in amortized policy acquisition costs was due to scheduled amortization of capitalized costs.

Income Tax Expense

The effective income tax rate on the Company s pretax income, including realized investment gains and losses, was 26.0% for the six months ended June 30, 2005 compared to 28.9% for the same period in 2004. Income from investments in tax-advantaged securities reduced the effective income tax rate 4.6 and 5.8 percentage points for the six months ended June 30, 2005 and 2004, respectively.

The Company records contingent tax liabilities for exposures from uncertain tax filing positions based upon management s assessment of the amounts that are probable of being sustained upon Internal Revenue Service (IRS) audit. These liabilities are reevaluated routinely and are adjusted appropriately based upon changes in facts or law. The Company has no unrecorded contingent tax exposures.

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At June 30, 2005, the Company had federal income tax returns for the 1998 through 2004 tax years still open and subject to adjustment upon IRS examination. The Company has recorded $9.4 million of contingent tax liabilities related to those open tax years.

In April 2005, the Company received refunds for tax years 1996 through 2001 from the IRS totaling $8.1 million, an amount consistent with the Company s tax refund accruals related to those years. In addition to the refund amounts, interest of $1.4 million was received, which was recorded by the Company as pretax income in the second quarter of 2005. Furthermore, as a result of the receipt of IRS refunds for tax years 1996 and 1997, which are now deemed to be closed, the contingent tax liability related to those two years was eliminated, which resulted in a decrease in federal income tax expense of $2.7 million in the second quarter of 2005. The remaining refunds received relate to tax years that are still considered open and subject to potential adjustment upon IRS examination. Pending an examination or a request to extend the statutes of limitations of the remaining tax years by the IRS, an additional reduction in the contingent tax liability of up to approximately $6 million may be recorded in the third quarter of 2005.

Net Income

For the six months ended June 30, 2005, the Company s net income increased compared to the prior year, primarily reflecting improved property and casualty segment earnings. This improvement was driven by aggressive underwriting and pricing actions taken in 2003 and 2004, ongoing improvements in claims processes, cost containment initiatives and continuing favorable non-catastrophe claims frequency trends. Along with the rest of the insurance industry, the Company also benefited in the current period from a relatively low level of catastrophe losses.

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Net income by segment and net income per share were as follows:

	Six Months Ended June 30,		Increase (Decrease)	
	2005	2004	Percent	Amount
Analysis of net income by segment:				
Property and casualty				
Before catastrophe costs	$ 44.8	$ 30.7	45.9%	$ 14.1
Catastrophe costs, after tax	(2.9)	(2.4)		(0.5)
Total including catastrophe costs	41.9	28.3	48.1%	13.6
Annuity	5.5	6.6	-16.7%	(1.1)
Life	8.1	6.3	28.6%	1.8
Corporate and other (1)	4.7	(0.6)		5.3
Net income	$ 60.2	$ 40.6	48.3%	$ 19.6
Diluted:				
Net income per share	$ 1.29	$ 0.89	44.9%	$ 0.40
Weighted average number of shares and equivalent shares (in millions)	47.8	47.3	1.1%	0.5
Property and casualty combined ratio:				
Before catastrophe costs	83.7%	90.8%		-7.1%
After catastrophe costs	85.4%	92.2%		-6.8%

(1) The corporate and other segment includes interest expense on debt, realized investment gains and losses, certain public company expenses and other corporate level items. The Company does not allocate the impact of corporate level transactions to the insurance segments, consistent with management s evaluation of the results of those segments.

For the six months ended June 30, 2005, net income for the property and casualty segment increased as described above.

Compared to the first six months of 2004, annuity segment net income for the current period decreased primarily as a result of the negative impact of valuations of deferred policy acquisition costs and Annuity VIF. Annuity segment net income for the current period also reflected a decline in the interest margin, which was partially offset by lower operating expenses.

Life segment net income increased compared to the first half of 2004, also due primarily to lower expenses, including a favorable impact from the valuation of deferred policy acquisition costs between periods.

The change in net income for the corporate and other segment compared to the first half of 2004 included differences in the amount of realized investment gains and a $2.7 million reduction in federal income tax expense in the current period from the elimination of the contingent tax liability for the 1996 and 1997 tax years.

Return on shareholders   equity based on net income was 13% and 9% for the trailing 12 months ended June 30, 2005 and 2004, respectively.

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Based on results for the first half of the year, at the time of this Quarterly Report on Form 10-Q, management anticipates that 2005 full year net income before realized investment gains and losses will be within a range of $1.80 to $1.90 per share. In addition to the second quarter 2005 tax refund benefit, this projection reflects management s anticipation of continued favorable property and casualty underwriting trends, while remaining appropriately cautious regarding potential catastrophe losses in the last six months of the year. As described in Critical Accounting Policies , certain of the Company s significant accounting measurements require the use of estimates and assumptions. As additional information becomes available, adjustments may be required. Those adjustments are charged or credited to income for the period in which the adjustments are made and may impact actual results compared to management s current estimate. A projection of net income is not accessible on a forward-looking basis because it is not possible to provide a reliable forecast of realized investment gains and losses, which can vary substantially from one period to another and may have a significant impact on net income.

Liquidity and Financial Resources

Special Purpose Entities

At June 30, 2005 and 2004, the Company did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or for other contractually narrow or limited purposes. As such, the Company is not exposed to any financing, liquidity, market or credit risk that could arise if the Company had engaged in such relationships.

Related Party Transactions

The Company does not have any contracts or other transactions with related parties that are required to be reported under the applicable securities laws and regulations.

Ariel Capital Management, Inc., HMEC s largest shareholder with 24% of the common shares outstanding per their SEC filing on Form 13G as of March 31, 2005, is the investment adviser for two of the mutual funds offered to the Company s annuity customers. In addition, T. Rowe Price Associates, Inc., HMEC s third largest shareholder with 5% of the common shares outstanding per their SEC filing on Form 13G as of March 31, 2005, is the investment advisor for three of the mutual funds offered to the Company s annuity customers.

Investments

Information regarding the Company s investment portfolio, which is comprised primarily of investment grade, fixed income securities, is located in Results of Operations Net Realized Investment Gains and Losses and in the Notes to Consolidated Financial Statements Note 4 Investments .

Cash Flow

The short-term liquidity requirements of the Company, within a 12-month operating cycle, are for the timely payment of claims and benefits to policyholders, operating expenses, interest payments and federal income taxes. Cash flow generated from operations has been, and is expected to be, adequate to meet the Company s operating cash needs in the next 12 months. Cash flow in excess of operational needs has been used to fund business growth, retire short-term

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debt, pay dividends to shareholders and repurchase shares of the Company s common stock. Long-term liquidity requirements, beyond one year, are principally for the payment of future insurance policy claims and benefits and retirement of long-term debt.

Operating Activities

As a holding company, HMEC conducts its principal operations in the personal lines segment of the property and casualty and life insurance industries through its subsidiaries. HMEC s insurance subsidiaries generate cash flow from premium and investment income, generally well in excess of their immediate needs for policy obligations, operating expenses and other cash requirements. Cash provided by operating activities primarily reflects net cash generated by the insurance subsidiaries. For the first six months of 2005, net cash provided by operating activities decreased slightly compared to the same period in 2004 primarily reflecting timing of operating expense payments.

Payment of principal and interest on debt, fees related to the catastrophe-linked equity put option and reinsurance agreement, dividends to shareholders and parent company operating expenses, as well as the share repurchase program, are dependent upon the ability of the insurance subsidiaries to pay cash dividends or make other cash payments to HMEC, including tax payments pursuant to tax sharing agreements. The insurance subsidiaries are subject to various regulatory restrictions which limit the amount of annual dividends or other distributions, including loans or cash advances, available to HMEC without prior approval of the insurance regulatory authorities. Dividends which may be paid by the insurance subsidiaries to HMEC during 2005 without prior approval are approximately $73 million, of which $8 million was paid during the six months ended June 30, 2005. Although regulatory restrictions exist, dividend availability from subsidiaries has been, and is expected to be, adequate for HMEC s capital needs.

Investing Activities

HMEC s insurance subsidiaries maintain significant investments in fixed maturity securities to meet future contractual obligations to policyholders. In conjunction with its management of liquidity and other asset/liability management objectives, the Company, from time to time, will sell fixed maturity securities prior to maturity and reinvest the proceeds in other investments with different interest rates, maturities or credit characteristics. Accordingly, the Company has classified the entire fixed maturity securities portfolio as available for sale .

Financing Activities

Financing activities include primarily payment of dividends, the receipt and withdrawal of funds by annuity contractholders, repurchases of the Company s common stock, fluctuations in bank overdraft balances and borrowings, repayments and repurchases related to its debt facilities. Fees related to the catastrophe-linked equity put option and reinsurance agreement, which through May 7, 2005 augmented the Company s traditional reinsurance program, were charged directly to additional paid-in capital.

In June 2005, the Company issued $75.0 million aggregate principal amount of 6.05% senior notes which will mature on June 15, 2015 (Senior Notes due 2015) at a discount of 0.05%. As of June 30, 2005, the net proceeds from the sale of the Senior Notes due 2015 have been used to (1) repay the $25.0 million balance outstanding on the Bank Credit Facility and (2) redeem all of the Senior Notes due 2006 at an aggregate cost of $29.1 million. As of the date of this report on Form 10-Q, management anticipates utilizing the remaining proceeds to recapture the Company s

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life reinsurance agreement with the United States branch of Sun Life Assurance Company of Canada. See also Capital Resources for additional description of the Senior Notes due 2015 and the recapture of the life reinsurance agreement.

For the six months ended June 30, 2005, receipts from annuity contracts decreased 6.2%. Annuity contract benefits and withdrawals increased 30.8% compared to the prior year. Cash value retentions for variable and fixed annuity options were 92.4% and 95.1%, respectively, for the 12 month period ended June 30, 2005, each slightly lower than the respective retention level for the 12 month period ended June 30, 2004. Net transfers to variable annuity accumulated cash values were comparable to the prior year.

Contractual Obligations

	Payments Due By Period As of June 30, 2005				
	Total	Less Than 1 Year (2005)(1)	1 - 3 Years (2006 and 2007)	3 - 5 Years (2008 and 2009)	More Than 5 Years (2010 and beyond)
Short-term Debt Obligations (2):					
Bank Credit Facility (expires May 30, 2009) (3)					
Long-Term Debt Obligations (2):					
Senior Convertible Notes Due May 14, 2032	$ 251.4	$ 1.7	$ 5.2		$ 244.5
Senior Notes Due June 15, 2015 (4)	120.4	2.3	9.1	$ 9.1	99.9
Senior Notes Due January 15, 2006 (5)					
Total	$ 371.8	$ 4.0	$ 14.3	$ 9.1	$ 344.4

(1) July 1, 2005 through December 31, 2005.
(2) Includes principal and interest.
(3) Repaid on June 13, 2005. See also Capital Resources .
(4) Issued on June 9, 2005. See also Capital Resources .
(5) Redeemed on June 30, 2005. See also Capital Resources .

As of June 30, 2005, the Company had purchase obligations of approximately $2 million to be completed in the following 12 months. The Company has entered into various operating lease agreements, primarily for computer equipment, computer software and real estate (agency and claims offices across the country and portions of the home office complex). These leases have varying commitment periods with most in the 1 to 3 year range. Payments on these leases were approximately $10 million in 2004. It is anticipated that the Company s payments under operating leases for the full year 2005 will be comparable to the 2004 payments. The Company does not have any other arrangements that expose it to material liability that are not recorded in the financial statements.

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Capital Resources

The Company has determined the amount of capital which is needed to adequately fund and support business growth, primarily based on risk-based capital formulas including those developed by the National Association of Insurance Commissioners (NAIC). Historically, the Company s insurance subsidiaries have generated capital in excess of such needed capital. These excess amounts have been paid to HMEC through dividends. HMEC has then utilized these dividends and its access to the capital markets to service and retire long-term debt, pay dividends to its shareholders, fund growth initiatives, repurchase shares of its common stock and for other corporate purposes. Management anticipates that the Company s sources of capital will continue to generate capital in excess of the needs for business growth, debt interest payments and shareholder dividends.

The total capital of the Company was $825.3 million at June 30, 2005, including $190.9 million of long-term debt and no short-term debt outstanding. Total debt represented 26.0% of capital excluding unrealized investment gains and losses (23.1% including unrealized investment gains and losses) at June 30, 2005, slightly above the Company s long-term target of 25%.

Shareholders equity was $634.4 million at June 30, 2005, including a net unrealized gain in the Company s investment portfolio of $92.2 million after taxes and the related impact on deferred policy acquisition costs and the value of acquired insurance in force associated with annuity and interest-sensitive life policies. The market value of the Company s common stock and the market value per share were $807.3 million and $18.82, respectively, at June 30, 2005. Book value per share was $14.79 at June 30, 2005 ($12.64 excluding investment fair value adjustments).

As of June 30, 2005, the Company had outstanding $244.5 million aggregate principal amount of 1.425% Senior Convertible Notes (Senior Convertible Notes), which will mature on May 14, 2032, issued at a discount of 52.5% resulting in an effective yield of 3.0%. Interest on the Senior Convertible Notes is payable semi-annually at a rate of 1.425% from November 14, 2002 until May 14, 2007. After that date, cash interest will not be paid on the Senior Convertible Notes prior to maturity unless contingent cash interest becomes payable. From May 15, 2007 through maturity of the Senior Convertible Notes, interest will be recognized at the effective rate of 3.0% and will represent the accrual of discount, excluding any contingent cash interest that may become payable. Contingent cash interest becomes payable if the average market price of a Senior Convertible Note for a five trading day measurement period preceding the applicable six-month period equals 120% or more of the sum of the Senior Convertible Note s issue price, accrued original issue discount and accrued cash interest, if any, for such Senior Convertible Note. The contingent cash interest payable per Senior Convertible Note with respect to any quarterly period within any six-month period will equal the then applicable conversion rate multiplied by the greater of (1) $0.105 or (2) any regular cash dividends paid by the Company per share on HMEC s common stock during that quarterly period.

The Senior Convertible Notes will be convertible at the option of the holders into shares of HMEC s common stock at a conversion price of $26.74 if the conditions for conversion are satisfied. The Senior Convertible Notes are potentially convertible into 4,343,054 shares (17.763 shares per $1 thousand face amount) and with the implementation of the Financial Accounting Standards Board s Emerging Issues Task Force (EITF) consensus on issue 04-8, The Effect of Contingently Convertible Instruments on Diluted Earnings per Share , these shares are included in the calculation of diluted earnings per share to the extent dilutive. The Company may elect to pay holders surrendering notes cash or a combination of cash and shares of HMEC s common stock for the notes surrendered. Holders may also surrender Senior Convertible Notes for conversion during any period in which the credit rating assigned to the Senior Convertible Notes is Ba2 or lower by Moody s or BB+ or lower by S&P, the Senior Convertible Notes are no longer rated by either Moody s or S&P, or the credit rating assigned to the Senior Convertible Notes has been suspended or withdrawn by either Moody s or S&P. The Senior Convertible Notes will cease to be convertible pursuant to this credit rating criteria during any period or periods in which all of the credit ratings are increased above such levels. The Senior Convertible Notes are redeemable by HMEC in whole or in part, at any time on or after May 14, 2007, at redemption prices equal to the sum of the issue price plus accrued original issue discount and accrued cash interest, if any, on the applicable redemption date. The holders of the Senior Convertible Notes may require HMEC to purchase all or a portion of their Senior Convertible Notes on either May 14, 2007, 2012, 2017, 2022, or 2027 at stated prices plus accrued cash interest, if any, to the purchase date. HMEC may pay the purchase price in cash or shares of HMEC common stock or in a combination of cash and shares of HMEC common stock.

The Senior Convertible Notes have an investment grade rating from Standard & Poor s Corporation (S&P) (BBB), Moody s Investors Service, Inc. (Moody s) (Baa3), A.M. Best Company, Inc. (A.M. Best) (bbb-) and Fitch Ratings, Ltd. (Fitch) (BBB+). Also see Financial Ratings . The Senior Convertible Notes are traded in the open market (HMN 1.425).

On June 9, 2005, the Company issued $75.0 million face amount of senior notes at an effective yield of 6.1%, which will mature on June 15, 2015 (Senior Notes due 2015). Interest on the Senior Notes due 2015 is payable semi-annually at a rate of 6.05%. The Senior Notes due 2015 are redeemable in whole or in part, at any time, at the Company s option, at a redemption price equal to the greater of (1) 100% of their principal amount or (2) the sum of the present values of the remaining scheduled payments of principal and interest thereon discounted, on a semi-annual basis, at the Treasury yield (as defined in the indenture) plus 30 basis points, plus, in either of the above cases, accrued interest to the date of redemption. For information regarding the use of proceeds, see Liquidity and Financial Resources Cash Flow Financing Activities .

The Senior Notes due 2015 have an investment grade rating from S&P (BBB), Moody s (Baa3), A.M. Best (bbb-) and Fitch (BBB+). Also see Financial Ratings . The Senior Notes due 2015 are traded in the open market (HMN 6.05).

On June 30, 2005, the Company redeemed all of its outstanding $28.6 million aggregate principal amount of 6 5/8% Senior Notes due 2006 (Senior Notes due 2006). For information regarding the funding of the redemption, see Liquidity and Financial Resources Cash Flow Financing Activities .)

As of June 30, 2005, the Company had no balance outstanding under its Bank Credit Agreement. On May 31, 2005, the Company entered into a new Bank Credit Agreement which provides for unsecured borrowings of up to $100.0 million (the Current Bank Credit Facility). The Current Bank Credit Facility expires on May 30, 2009. Interest accrues at varying spreads relative to corporate or eurodollar base rates and is payable monthly or quarterly depending on the applicable base rate. The unused portion of the Current Bank Credit Facility is subject to a variable commitment fee, which was 0.175% on an annual basis at June 30, 2005. On May 31, 2005, the Company borrowed $25.0 million and subsequently repaid this balance in full on June 13, 2005 utilizing a portion of the proceeds from the issuance of the Senior Notes due 2015.

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On May 29, 2002, Horace Mann Educators Corporation entered into a Bank Credit Agreement that was amended effective June 1, 2004, increasing the commitment amount to $35.0 million, and May 3, 2005, extending the commitment termination date to June 30, 2005 from the previous termination date of May 31, 2005 (the Previous Bank Credit Agreement). The Previous Bank Credit Agreement was terminated on May 31, 2005, when the Company entered into the Current Bank Credit Facility. The $25.0 million balance outstanding under the Previous Bank Credit Agreement was repaid in full on May 31, 2005 utilizing the borrowing under the Current Bank Credit Facility, described above.

To provide additional capital management flexibility, the Company filed a universal shelf registration on Form S-3 with the SEC in December 2003. The registration statement, which registers the offer and sale by the Company from time to time of up to $300 million of various securities, which may include debt securities, preferred stock, common stock and/or depositary shares, was declared effective on December 30, 2003. The $75.0 million face amount of Senior Notes due 2015 was issued utilizing this registration statement. No other securities associated with the registration statement have been issued as of the date of this Quarterly Report on Form 10-Q.

The Company s ratio of earnings to fixed charges for the six months ended June 30, 2005 was 19.9x, compared to 17.8x for the same period in 2004.

Total shareholder dividends were $9.0 million for the six months ended June 30, 2005. In March and June 2005, the Board of Directors announced regular quarterly dividends of $0.105 per share.

Information regarding the reinsurance program for the Company s property and casualty segment is located in Business Property and Casualty Segment Property and Casualty Reinsurance of the Company s Annual Report on Form 10-K for the year ended December 31, 2004. In addition to the Company s excess and catastrophe reinsurance program, the Company s predominant insurance subsidiary for property and casualty business written in Florida reinsures 90% of hurricane losses in that state above an estimated retention of $14.0 million up to $66.2 million with the Florida Hurricane Catastrophe Fund (FHCF), based on the FHCF s financial resources. The FHCF contract is a 12-month contract, beginning on June 1. Effective June 1, 2005, each company will be required to keep a full retention on the two largest hurricane loss occurrences and will be reimbursed by the FHCF on a retention equal to one-third of the full retention for all other occurrences within the contract period. For the contract period June 1, 2004 through May 31, 2005, the Company s predominant insurance subsidiary for property and casualty business written in Florida was able to reinsure 90% of hurricane losses in that state above an estimated retention of $15.6 million up to $73.3 million with the FHCF. Prior to June 1, 2005, retention limits were required to be met for each hurricane occurrence. Effective May 7, 2002, the Company entered into a 36-month equity put and reinsurance agreement with a subsidiary of Swiss Reinsurance Company, which provided a source of up to $75 million of contingent capital for catastrophe losses above the Company s reinsurance coverage limits. Due to relatively unfavorable pricing and terms, the Company elected not to renew this agreement on the May 7, 2005 expiration date. Management believes that the Company s current catastrophe protection as well as other potential sources of capital would be sufficient in the event of excessive catastrophe losses.

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Information regarding the interest-sensitive life reinsurance program for the Company s life segment is located in Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Financial Resources Capital Resources of the Company s Annual Report on Form 10-K for the year ended December 31, 2004. As of the date of this Report on Form 10-Q, management has delivered notice of its intention to utilize a portion of the proceeds from the issuance of the Senior Notes due 2015 for an early recapture of the reinsurance agreement with the United States branch of Sun Life Assurance Company of Canada. It is expected that this agreement will be terminated during the third quarter of 2005. This early recapture will result in the reduction of total anticipated pretax fees of approximately $1.2 million, including $0.2 million over the balance of 2005, $0.5 million in 2006 and the remainder over subsequent years.

Financial Ratings

The Company s principal insurance subsidiaries are rated by Standard & Poor s Corporation (S&P), Moody s Investors Service, Inc. (Moody s), A.M. Best Company, Inc. (A.M. Best) and Fitch Ratings, Ltd. (Fitch). These rating agencies have also assigned ratings to the Company s long-term debt securities.

Assigned ratings as of August 1, 2005 were as follows (the insurance financial strength ratings for the Company s property and casualty insurance subsidiaries and the Company s principal life insurance subsidiary are the same):

	Insurance Financial Strength Ratings (Outlook)	Debt Ratings (Outlook)
As of August 1, 2005		
S&P (1)	A (stable)	BBB (stable)
Moody s (1)	A3 (stable)	Baa3 (stable)
A.M. Best	A- (stable)	bbb- (stable)
Fitch	A+ (negative)	BBB+ (negative)

(1) This agency has not yet rated Horace Mann Lloyds.

The ratings above were unchanged from the disclosure in the Company s Annual Report on Form 10-K for 2004. In June 2005, each of the rating agencies affirmed the above debt ratings as they assigned a rating to the Senior Notes due 2015. In April 2005, Fitch affirmed the Company s insurance financial strength and debt ratings and the accompanying Negative outlook. While acknowledging the insurance subsidiaries solid risk-based capitalization, high-quality liquid investment portfolios, well-defined niche in the educators market and Fitch s heightened comfort with the Company s reserve adequacy, Fitch s rating outlook reflects their continuing concerns about the Company s ability to generate run-rate underwriting profitability supportive of its current ratings and their belief that the Company s level of catastrophe-related losses in 2004 raises concerns about the Company s comparatively high operating leverage and risk management capabilities.

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Market Value Risk

Market value risk, the Company s primary market risk exposure, is the risk that the Company s invested assets will decrease in value. This decrease in value may be due to a change in (1) the yields realized on the Company s assets and prevailing market yields for similar assets, (2) an unfavorable change in the liquidity of the investment, (3) an unfavorable change in the financial prospects of the issuer of the investment, or (4) a downgrade in the credit rating of the issuer of the investment. See also Results of Operations Net Realized Investment Gains and Losses .

Significant changes in interest rates expose the Company to the risk of experiencing losses or earning a reduced level of income based on the difference between the interest rates earned on the Company s investments and the credited interest rates on the Company s insurance liabilities.

The Company manages its market value risk by coordinating the projected cash outflows of assets with the projected cash outflows of liabilities. For all its assets and liabilities, the Company seeks to maintain reasonable durations, consistent with the maximization of income without sacrificing investment quality, while providing for liquidity and diversification. The investment risk associated with variable annuity deposits and the underlying mutual funds is assumed by those contractholders, and not by the Company. Certain fees that the Company earns from variable annuity deposits are based on the market value of the funds deposited.

More detailed descriptions of the Company s exposure to market value risks and the management of those risks is presented in Management s Discussion and Analysis of Financial Condition and Results of Operations Market Value Risk and Results of Operations for the Three Years Ended December 31, 2004 Interest Credited to Policyholders of the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

Recent Accounting Changes

SFAS No. 154

In May 2005, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 154, Accounting Changes and Error Corrections . This standard will be effective for accounting changes and corrections of errors in fiscal years beginning after December 15, 2005. SFAS No. 154 replaces Accounting Principles Board Opinion No. 20, Accounting Changes , and FASB SFAS No. 3, Reporting Changes in Interim Financial Statements . SFAS No. 154 changes the accounting for, and reporting of, a change in accounting principle and also requires retrospective application to prior period s financial statements of voluntary changes in accounting principle and changes required by new accounting standards when the standard does not include specific transition provisions, unless it is impracticable to do so. At the time of this Quarterly Report on Form 10-Q, management is not aware of outstanding circumstances that would result in a currently quantifiable impact on the Company s operating results or financial position.

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SFAS No. 123 (revised 2004) (SFAS No. 123(R)   ), SAB 107 and SEC Release 34-51558

In April 2005, the Securities and Exchange Commission (SEC   ) issued Release No. 34-51558,   Amendment to Rule 4-01(a) of Regulation S-X Regarding the Compliance Date for SFAS No. 123 (Revised 2004),   Share-Based Payment   . This amendment to Regulation S-X states that each registrant that is not a small business issuer will be required to adopt the provisions of FASB SFAS No. 123 (revised 2004),   Share-Based Payment   beginning with the first interim or annual reporting period of the registrant   s first fiscal year beginning on or after June 15, 2005, which for the Company will be January 1, 2006. Release No. 34-51558 does not change the accounting required by SFAS No. 123 (R); it changes only the dates for compliance with the Standard.

In March 2005, the SEC released Staff Accounting Bulletin (SAB   ) No. 107 which summarizes the views of the SEC staff regarding the interaction between SFAS No. 123(R) and certain SEC rules and regulations and provides the SEC staff   s views regarding the valuation of share-based payment arrangements for public companies.

In December 2004, the FASB issued SFAS No. 123(R) and, as issued by the FASB, this standard was to be effective as of the beginning of the first interim or annual reporting period that begins after June 15, 2005 for public entities that do not file as small business issuers, which for the Company was to be July 1, 2005. See discussion above regarding the delay in the effective date. This statement revises SFAS No. 123,   Accounting for Stock-Based Compensation   and supersedes Accounting Principles Board (APB   ) Opinion No. 25,   Accounting for Stock Issued to Employees   , and its related implementation guidance. SFAS No. 123(R) establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services and identifies required disclosures for share-based payment arrangements. It also addresses transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity   s equity instruments or that may be settled by the issuance of those equity instruments. In addition, the statement addresses the accounting and financial statement presentation for income tax benefits resulting from share-based payments.

This statement focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions and requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the fair value of the award. That cost will be recognized as expense in the Consolidated Statement of Operations over the period during which an employee is required to provide service in exchange for the award.

The Company has accounted for share-based payments using the intrinsic value based method in accordance with APB Opinion No. 25 and, accordingly, recognized no compensation expense for awards representing options to purchase shares of the Company   s common stock which have an exercise price equal to market price on the date of grant resulting in an intrinsic value of $0. Disclosures regarding the pro forma effect of stock-based compensation expense have been included in the Company   s quarterly and annual consolidated financial statements in compliance with SFAS No. 123. Excluding the acceleration of stock option vesting which occurred in 2004, pro forma pretax stock-based compensation expense was approximately $7 million to $8 million in each of the three years ended December 31, 2004. Although the evaluation of the impact of SFAS No. 123(R) is not yet complete, at the time of this Report on Form 10-Q management anticipates that the impact of adopting SFAS No. 123(R) will be comparable to the historical pro forma expense assuming that the number and characteristics of equity instruments granted in the future are similar to past awards.

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FASB Staff Position Regarding EITF Issue No. 03-1

In September 2004, the Financial Accounting Standards Board issued a FASB Staff Position (FSP) to delay the effective date for the measurement and recognition guidance contained in paragraphs 10 through 20 of the Emerging Issues Task Force (EITF) Consensus regarding EITF Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments . The delay resulting from FSP No. EITF Issue 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, The Meaning of Other-Than-Temporary Impairments and Its Application to Certain Investments , will be superseded concurrent with the final issuance of FSP EITF Issue 03-1-a. This FSP did not have a material impact on the Company s operating results or financial position.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

The information required by Item 305 of Regulation S-K is contained in Management s Discussion and Analysis of Financial Condition and Results of Operations contained in this Quarterly Report on Form 10-Q.

Item 4: Controls and Procedures

Management s Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of the Company s management, including the Company s Chief Executive Officer and Chief Financial Officer, the Company conducted an evaluation of the effectiveness of the design and operation of the Company s disclosure controls and procedures, as such term is defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 as amended (the Exchange Act), as of June 30, 2005 pursuant to Rule 13a-15(b) of the Exchange Act. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures were not effective as of June 30, 2005 due to the two material weaknesses disclosed in Item 9A. Controls and Procedures of the Company s Annual Report on Form 10-K for the year ended December 31, 2004. No additional material weaknesses in the Company s disclosure controls and procedures were identified in the current evaluation.

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Changes in Internal Control Over Financial Reporting

The following changes have been made subsequent to December 31, 2004 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

Income Tax Financial Reporting

While the Company has not fully remediated the material weakness in its internal control over income tax deferred assets and liabilities, management is in the process of implementing the following remedial actions, the status of which is reviewed periodically with the Company s Audit Committee:

A remediation plan to compute and reconcile the book to tax basis differences at an asset and liability transaction level, including documentation and testing of enhanced processes and procedures by November 30, 2005;

A qualified tax officer was employed by the Company in March 2005 to allow for appropriate segregation of duties and to strengthen processes related to the preparation and review of tax asset and liability documentation and an additional tax accountant will be hired as soon as practicable to assist in the reconciliation process; and

A tax consulting firm was engaged to review the Company s first quarter and second quarter 2005 federal income tax provisions, along with related reconciliations and supporting documentation, for validity and consistency and will perform such reviews on a quarterly basis during 2005 and annually, if warranted, thereafter.

Reporting of Cash Balances

While the Company has not fully remediated the material weakness in its internal control over the reporting of cash balances, management is in the process of implementing the following remedial actions, the status of which is reviewed periodically with the Company s Audit Committee:

Bank Account and Suspense Account Reconciliations

A remediation plan to reconcile and clear all suspense accounts on a timely basis, including a review of staffing levels and proficiencies, training, documentation and testing of enhanced processes and procedures by November 30, 2005;

A remediation plan to enhance and document processes and procedures for the timely completion, review and testing of bank account reconciliations, including a review of staffing levels, proficiencies and training by November 30, 2005; and

Initial phases of the remediation plan to address controller department staffing and training needs have been initiated, including redeployment and retraining of existing staff and increased utilization of temporary employees. Additional full-time employees will be hired and trained as soon as practicable.

Accounting Policy for Outstanding Check Amounts

Documentation of processes and procedures, along with appropriate training, to ensure that the Company s accounting policy, which has been corrected to conform with U.S. generally accepted accounting principles, is consistently applied on a going forward basis has been completed.

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PART II: OTHER INFORMATION

Item 4: Submission of Matters to a Vote of Security Holders

The Company s Annual Meeting of Shareholders was held on May 26, 2005. The results of the matters submitted to a vote of security holders are shown in the table below.

	Votes For	Votes Against	Abstentions
Votes representing 39,867,785 shares of Common Stock were represented and cast regarding Proposal 1.			
Election of the following nominees to hold the office of Director until the next Annual Meeting of Shareholders and until their respective successors have been duly elected and qualified:			
William W. Abbott	38,441,162	1,426,623	
Mary H. Futrell	38,493,410	1,374,375	
Stephen J. Hasenmiller	39,543,556	324,229	
Louis G. Lower II	39,469,552	398,233	
Joseph J. Melone	38,440,879	1,426,906	
Jeffrey L. Morby	39,398,452	469,333	
Shaun F. O Malley	39,518,059	349,726	
Charles A. Parker	39,520,304	347,481	
Votes representing 39,867,786 shares of Common Stock were represented and cast regarding Proposal 2.			
Approval of the Company s Amended and Restated 2002 Incentive Compensation Plan.	31,513,582	5,552,251	2,801,953
Votes representing 39,867,785 shares of Common Stock were represented and cast regarding Proposal 3.			
Ratification of the appointment of KPMG LLP, an independent registered public accounting firm, as the Company s auditors for the year ended December 31, 2005.	39,266,333	554,363	47,089

Item 5: Other Information

The Company is not aware of any information required to be disclosed in a report on Form 8-K during the six months ended June 30, 2005 which has not been filed with the SEC.

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Item 6: Exhibits

Exhibit No.	Description

(a) The following items are filed as Exhibits. Management contracts and compensatory plans are indicated by an asterisk (*).

(10) Material contracts:

10.1 Credit Agreement dated as of May 31, 2005 among HMEC, certain financial institutions named therein and Bank of America, N.A., as administrative agent (the Agent).

10.2* Horace Mann Educators Corporation Amended and Restated 2002 Incentive Compensation Plan.

(11) Statement re computation of per share earnings.

(15) KPMG LLP letter regarding unaudited interim financial information.

(31) Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.1 Certification by Louis G. Lower II, Chief Executive Officer of HMEC.

31.2 Certification by Peter H. Heckman, Chief Financial Officer of HMEC.

(32) Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.1 Certification by Louis G. Lower II, Chief Executive Officer of HMEC.

32.2 Certification by Peter H. Heckman, Chief Financial Officer of HMEC.

(99.1) Glossary of Selected Terms.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	HORACE MANN EDUCATORS CORPORATION (Registrant)
Date August 9, 2005	/s/ Louis G. Lower II
	Louis G. Lower II President and Chief Executive Officer
Date August 9, 2005	/s/ Peter H. Heckman
	Peter H. Heckman Executive Vice President and Chief Financial Officer
Date August 9, 2005	/s/ Bret A. Conklin
	Bret A. Conklin Senior Vice President and Controller

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HORACE MANN EDUCATORS CORPORATION

EXHIBITS

To

FORM 10-Q

For the Quarter Ended June 30, 2005

VOLUME 1 OF 1

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The following items are filed as Exhibits to Horace Mann Educators Corporation s Quarterly Report on Form 10-Q for the quarter ended June 30, 2005. Management contracts and compensatory plans are indicated by an asterisk (*).

EXHIBIT INDEX

Exhibit No.	Description
(10)	Material contracts:
	10.1 Credit Agreement dated as of May 31, 2005 among HMEC, certain financial institutions named therein and Bank of America, N.A., as administrative agent (the Agent).
	10.2* Horace Mann Educators Corporation Amended and Restated 2002 Incentive Compensation Plan.
(11)	Statement re computation of per share earnings.
(15)	KPMG LLP letter regarding unaudited interim financial information.
(31)	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
	31.1 Certification by Louis G. Lower II, Chief Executive Officer of HMEC.
	31.2 Certification by Peter H. Heckman, Chief Financial Officer of HMEC.
(32)	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
	32.1 Certification by Louis G. Lower II, Chief Executive Officer of HMEC.
	32.2 Certification by Peter H. Heckman, Chief Financial Officer of HMEC.
(99.1)	Glossary of Selected Terms