UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

**FORM 10-Q**

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the Quarterly Period Ended September 30, 2021**

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

For the transition period from __________ to __________

Commission File Number: **000-55522**

# NATIONAL WESTERN LIFE GROUP, INC.

(Exact name of Registrant as specified in its charter)

| | |
|---|---|
| **Delaware** | **47-3339380** |
| (State or Other Jurisdiction of Incorporation) | (IRS Employer Identification No.) |
| **10801 N. Mopac Expy Bldg 3**<br>**Austin, Texas**<br>**78759** | **(512) 836-1010** |
| (Address of Principal Executive Offices) (Zip Code) | (Telephone Number, including area code) |

Securities registered pursuant to Section 12 (b) of the Act:

| Title of each class to be so registered: | Trading Symbol | Name of each exchange on which each class is to be registered: |
|---|---|---|
| **Class A Common Stock, $0.01 par value** | **NWLI** | **The NASDAQ Stock Market LLC** |

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

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

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

Large Accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer (Do not check if a smaller reporting company) ☐ Smaller reporting company ☐ Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

As of November 5, 2021, the number of shares of Registrant's common stock outstanding was: Class A – 3,436,020 and Class B - 200,000.

National Western Life Group, Inc.

**TABLE OF CONTENTS**

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## NATIONAL WESTERN LIFE GROUP, INC.
## CONDENSED CONSOLIDATED BALANCE SHEETS
## (In thousands)

| ASSETS | (Unaudited) September 30, 2021 | December 31, 2020 |
|---|---|---|
| Investments: | | |
| Debt securities available-for-sale, at fair value (cost: $8,795,673 and $9,874,543) | $ 9,364,083 | 10,770,923 |
| Debt securities trading, at fair value (cost: $1,076,099 and $0) | 1,085,654 | — |
| Mortgage loans, net of allowance for credit losses ($3,956 and $2,486), ($6,439 and $0 at fair value) | 462,882 | 332,521 |
| Policy loans | 71,668 | 74,083 |
| Derivatives, index options | 82,390 | 132,821 |
| Equity securities, at fair value (cost: $12,079 and $12,069) | 21,186 | 17,744 |
| Other long-term investments | 124,772 | 104,113 |
| Total investments | 11,212,635 | 11,432,205 |
| Cash and cash equivalents | 540,226 | 581,059 |
| Deferred policy acquisition costs | 539,294 | 382,080 |
| Deferred sales inducements | 71,677 | 43,845 |
| Value of business acquired | 156,259 | 162,968 |
| Cost of reinsurance | 92,578 | 102,840 |
| Accrued investment income | 91,842 | 88,323 |
| Federal income tax receivable | 9,485 | 10,408 |
| Amounts recoverable from reinsurer | 1,580,907 | 1,709,232 |
| Other assets | 126,739 | 135,310 |
| Total assets | $ 14,421,642 | 14,648,270 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**(In thousands, except share amounts)**

| LIABILITIES AND STOCKHOLDERS' EQUITY | (Unaudited) September 30, 2021 | December 31, 2020 |
|---|---|---|
| LIABILITIES: | | |
| Future policy benefits: | | |
| Universal life and annuity contracts | $ 9,001,837 | 9,035,316 |
| Traditional life reserves | 904,803 | 898,103 |
| Other policyholder liabilities | 132,029 | 138,480 |
| Funds withheld liability | 1,540,384 | 1,697,591 |
| Deferred Federal income tax liability | 117,486 | 145,126 |
| Other liabilities | 168,869 | 193,904 |
| | | |
| Total liabilities | 11,865,408 | 12,108,520 |
| | | |
| COMMITMENTS AND CONTINGENCIES (Note 8) | | |
| | | |
| STOCKHOLDERS' EQUITY: | | |
| | | |
| Common stock: | | |
| Class A - $0.01 par value; 7,500,000 shares authorized; 3,436,020 issued and outstanding in 2021 and 2020 | 34 | 34 |
| Class B - $0.01 par value; 200,000 shares authorized, issued, and outstanding in 2021 and 2020 | 2 | 2 |
| Additional paid-in capital | 41,716 | 41,716 |
| Accumulated other comprehensive income | 260,036 | 395,421 |
| Retained earnings | 2,254,446 | 2,102,577 |
| | | |
| Total stockholders' equity | 2,556,234 | 2,539,750 |
| | | |
| Total liabilities and stockholders' equity | $ 14,421,642 | 14,648,270 |

Note: The Condensed Consolidated Balance Sheet at December 31, 2020 has been derived from the audited Consolidated Financial Statements as of that date.

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS**
**For the Three Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands, except per share amounts)**

| | 2021 | 2020 |
|---|---|---|
| Premiums and other revenues: | | |
| Universal life and annuity contract charges | $ 32,850 | 40,303 |
| Traditional life premiums | 22,244 | 22,693 |
| Net investment income | 88,970 | 129,679 |
| Other revenues | 5,806 | 3,977 |
| Net realized investment gains: | | |
| Total other-than-temporary impairment (“OTTI”) gains | — | 1 |
| Portion of OTTI (gains) recognized in other comprehensive income | — | (1) |
| Net OTTI recognized in earnings | — | — |
| Other net investment gains | 5,011 | 6,050 |
| Total net realized investment gains | 5,011 | 6,050 |
| Total revenues | 154,881 | 202,702 |
| Benefits and expenses: | | |
| Life and other policy benefits | 70,633 | 26,940 |
| Amortization of deferred transaction costs | (8,389) | 50,800 |
| Universal life and annuity contract interest | 11,663 | 85,879 |
| Other operating expenses | 30,793 | 25,754 |
| Total benefits and expenses | 104,700 | 189,373 |
| Earnings before Federal income taxes | 50,181 | 13,329 |
| Federal income taxes | 10,341 | 2,504 |
| Net earnings | $ 39,840 | 10,825 |
| Basic earnings per share: | | |
| Class A | $ 11.27 | $ 3.06 |
| Class B | $ 5.63 | $ 1.53 |
| Diluted earnings per share: | | |
| Class A | $ 11.27 | $ 3.06 |
| Class B | $ 5.63 | $ 1.53 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS**
**For the Nine Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands, except per share amounts)**

| | 2021 | 2020 |
|---|---|---|
| Premiums and other revenues: | | |
| Universal life and annuity contract charges | $ 101,799 | 112,478 |
| Traditional life premiums | 66,940 | 68,956 |
| Net investment income | 411,589 | 261,894 |
| Other revenues | 17,254 | 15,217 |
| Net realized investment gains: | | |
| Total other-than-temporary impairment (“OTTI”) gains | — | 5 |
| Portion of OTTI (gains) recognized in other comprehensive income | — | (5) |
| Net OTTI recognized in earnings | — | — |
| Other net investment gains | 9,842 | 12,660 |
| Total net realized investment gains | 9,842 | 12,660 |
| Total revenues | 607,424 | 471,205 |
| Benefits and expenses: | | |
| Life and other policy benefits | 144,426 | 94,005 |
| Amortization of deferred transaction costs | 46,723 | 111,937 |
| Universal life and annuity contract interest | 134,481 | 119,625 |
| Other operating expenses | 90,596 | 74,730 |
| Total benefits and expenses | 416,226 | 400,297 |
| Earnings before Federal income taxes | 191,198 | 70,908 |
| Federal income taxes | 39,329 | 13,732 |
| Net earnings | $ 151,869 | 57,176 |
| Basic earnings per share: | | |
| Class A | $ 42.95 | $ 16.17 |
| Class B | $ 21.47 | $ 8.08 |
| Diluted earnings per share: | | |
| Class A | $ 42.95 | $ 16.17 |
| Class B | $ 21.47 | $ 8.08 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**For the Three Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Net earnings | $ 39,840 | 10,825 |
| | | |
| Other comprehensive income, net of effects of deferred costs and taxes: | | |
| Unrealized gains (losses) on securities: | | |
| Net unrealized holding gains (losses) arising during period | (21,319) | 24,357 |
| Net unrealized liquidity gains (losses) | — | 1 |
| Reclassification adjustment for net amounts included in net earnings | (3,970) | (702) |
| | | |
| Net unrealized gains (losses) on securities | (25,289) | 23,656 |
| | | |
| Foreign currency translation adjustments | (96) | 85 |
| | | |
| Benefit plans: | | |
| Amortization of net prior service cost and net gain (loss) | 1,934 | (2,066) |
| | | |
| Other comprehensive income (loss) | (23,451) | 21,675 |
| | | |
| Comprehensive income | $ 16,389 | 32,500 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**For the Nine Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Net earnings | $ 151,869 | 57,176 |
| | | |
| Other comprehensive income, net of effects of deferred costs and taxes: | | |
| Unrealized gains (losses) on securities: | | |
| Net unrealized holding gains (losses) arising during period | (132,118) | 53,569 |
| Net unrealized liquidity gains (losses) | — | 2 |
| Reclassification adjustment for net amounts included in net earnings | (8,899) | (2,670) |
| | | |
| Net unrealized gains (losses) on securities | (141,017) | 50,901 |
| | | |
| Foreign currency translation adjustments | (172) | (46) |
| | | |
| Benefit plans: | | |
| Amortization of net prior service cost and net gain (loss) | 5,804 | (6,199) |
| | | |
| Other comprehensive income (loss) | (135,385) | 44,656 |
| | | |
| Comprehensive income | $ 16,484 | 101,832 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**
**For the Three Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Common stock: | | |
| Balance at beginning of period | $ 36 | 36 |
| Balance at end of period | 36 | 36 |
| Additional paid-in capital: | | |
| Balance at beginning of period | 41,716 | 41,716 |
| Balance at end of period | 41,716 | 41,716 |
| Accumulated other comprehensive income: | | |
| Unrealized gains (losses) on non-impaired securities: | | |
| Balance at beginning of period | 303,013 | 97,909 |
| Change in unrealized gains (losses) during period, net of tax | (25,289) | 23,655 |
| Balance at end of period | 277,724 | 121,564 |
| Unrealized losses on impaired held-to-maturity securities: | | |
| Balance at beginning of period | — | (3) |
| Amortization | — | 1 |
| Balance at end of period | — | (2) |
| Unrealized losses on impaired available-for-sale securities: | | |
| Balance at beginning of period | — | (2) |
| Balance at end of period | $ — | (2) |

Continued on Next Page

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (continued)**
**For the Three Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Foreign currency translation adjustments: | | |
| Balance at beginning of period | 5,040 | 4,970 |
| Change in translation adjustments during period | (96) | 85 |
| Balance at end of period | 4,944 | 5,055 |
| Benefit plan liability adjustment: | | |
| Balance at beginning of period | (24,566) | (19,785) |
| Amortization of net prior service cost and net gain (loss), net of tax | 1,934 | (2,066) |
| Balance at end of period | (22,632) | (21,851) |
| Accumulated other comprehensive income at end of period | 260,036 | 104,764 |
| Retained earnings: | | |
| Balance at beginning of period | 2,214,606 | 2,057,889 |
| Net earnings | 39,840 | 10,825 |
| Balance at end of period | 2,254,446 | 2,068,714 |
| Total stockholders' equity | $ 2,556,234 | 2,215,230 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**
**For the Nine Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Common stock: | | |
| Balance at beginning of period | $ 36 | 36 |
| Balance at end of period | 36 | 36 |
| Additional paid-in capital: | | |
| Balance at beginning of period | 41,716 | 41,716 |
| Balance at end of period | 41,716 | 41,716 |
| Accumulated other comprehensive income: | | |
| Unrealized gains (losses) on non-impaired securities: | | |
| Balance at beginning of period | 418,741 | 70,665 |
| Change in unrealized gains (losses) during period, net of tax | (141,017) | 50,899 |
| Balance at end of period | 277,724 | 121,564 |
| Unrealized losses on impaired held to maturity securities: | | |
| Balance at beginning of period | — | (4) |
| Amortization | — | 4 |
| Change in shadow deferred policy acquisition costs | — | (2) |
| Balance at end of period | — | (2) |
| Unrealized losses on impaired available for sale securities: | | |
| Balance at beginning of period | — | (2) |
| Balance at end of period | — | (2) |

Continued on Next Page

**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (continued)**
**For the Nine Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Foreign currency translation adjustments: | | |
| Balance at beginning of period | 5,116 | 5,101 |
| Change in translation adjustments during period | (172) | (46) |
| Balance at end of period | 4,944 | 5,055 |
| Benefit plan liability adjustment: | | |
| Balance at beginning of period | (28,436) | (15,652) |
| Amortization of net prior service cost and net loss, net of tax | 5,804 | (6,199) |
| Balance at end of period | (22,632) | (21,851) |
| Accumulated other comprehensive income at end of period | 260,036 | 104,764 |
| Retained earnings: | | |
| Balance at beginning of period | 2,102,577 | 2,014,570 |
| Cumulative effect of change in accounting principle, net of tax (Note 2) | — | (3,032) |
| Net earnings | 151,869 | 57,176 |
| Balance at end of period | 2,254,446 | 2,068,714 |
| Total stockholders' equity | $ 2,556,234 | 2,215,230 |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**For the Nine Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net earnings | $ 151,869 | 57,176 |
| Adjustments to reconcile net earnings to net cash from operating activities: | | |
| Universal life and annuity contract interest | 134,481 | 119,625 |
| Surrender charges and other policy revenues | (19,900) | (21,219) |
| Realized (gains) losses on investments | (9,842) | (12,660) |
| Accretion/amortization of discounts and premiums, investments | 1,887 | 1,580 |
| Depreciation and amortization | 9,803 | 8,892 |
| Increase (decrease) in estimated credit losses on investments | 1,470 | 2,930 |
| (Increase) decrease in value of debt securities trading | (9,556) | — |
| (Increase) decrease in value of equity securities | (3,714) | 3,107 |
| (Increase) decrease in value of derivative options | (70,474) | 34,866 |
| (Increase) decrease in deferred policy acquisition and sales inducement costs, and value of business acquired | (28,871) | 75,604 |
| (Increase) decrease in accrued investment income | (3,519) | (32) |
| (Increase) decrease in reinsurance recoverable | 128,325 | 9,758 |
| (Increase) decrease in cost of reinsurance | 10,262 | — |
| (Increase) decrease in other assets | (5,563) | (1,012) |
| Increase (decrease) in liabilities for future policy benefits | (103,396) | (5,288) |
| Increase (decrease) in other policyholder liabilities | (6,451) | 8,785 |
| Increase (decrease) in Federal income tax liability | 923 | (4,550) |
| Increase (decrease) in deferred Federal income tax | 8,349 | 5,224 |
| Increase (decrease) in funds withheld liability | (157,207) | — |
| Increase (decrease) in other liabilities | (31,539) | (3,391) |
| Net cash provided by (used in) operating activities | (2,663) | 279,395 |
| Cash flows from investing activities: | | |
| Proceeds from sales of: | | |
| Debt securities available-for-sale | 1,153,113 | — |
| Other investments | 26,166 | 5,786 |
| Proceeds from maturities, redemptions, and prepayments of: | | |
| Debt securities held-to-maturity | — | 619,984 |
| Debt securities available-for-sale | 1,143,075 | 240,398 |
| Debt securities trading | 18,958 | — |
| Other investments | 20,195 | 9,753 |
| Derivatives, index options | 155,142 | 84,778 |
| Purchases of: | | |
| Debt securities held-to-maturity | — | (318,138) |
| Debt securities available-for-sale | (1,128,594) | (181,162) |

Continued on Next Page

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)**
**For the Nine Months Ended September 30, 2021 and 2020**
**(Unaudited)**
**(In thousands)**

| | 2021 | 2020 |
|---|---|---|
| Debt securities trading | (1,092,445) | — |
| Equity securities | (10,592) | (1,019) |
| Derivatives, index options | (34,494) | (51,318) |
| Other investments | (41,928) | (23,268) |
| Property, equipment, and other productive assets | (8,143) | (7,223) |
| Principal payments on mortgage loans | 19,927 | 6,022 |
| Cost of mortgage loans acquired | (151,402) | (41,530) |
| Decrease (increase) in policy loans | 2,415 | 4,294 |
| Other (increases) decreases to funds withheld | (71,077) | — |
| Net cash provided by investing activities | 316 | 347,357 |
| Cash flows from financing activities: | | |
| Deposits to account balances for universal life and annuity contracts | 479,063 | 348,583 |
| Return of account balances on universal life and annuity contracts | (517,027) | (721,496) |
| Principal payments under finance lease obligation | (303) | (280) |
| Net cash provided by (used in) financing activities | (38,267) | (373,193) |
| Effect of foreign exchange | (219) | (59) |
| Net increase (decrease) in cash, cash equivalents, and restricted cash | (40,833) | 253,500 |
| Cash, cash equivalents, and restricted cash at beginning of period | 581,059 | 253,525 |
| Cash, cash equivalents and restricted cash at end of period | $ 540,226 | 507,025 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION: | | |
| Cash paid during the period for: | | |
| Interest | $ 56 | 56 |
| Income taxes | $ 30,042 | 13,229 |
| Noncash operating activities: | | |
| Net deferral and amortization of sales inducements | $ 4,576 | (12,755) |

See accompanying notes to Condensed Consolidated Financial Statements (unaudited).

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

## (1) CONSOLIDATION AND BASIS OF PRESENTATION

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete annual financial statements. In the opinion of management, the accompanying Condensed Consolidated Financial Statements contain all adjustments necessary to present fairly the financial position and results of operations of National Western Life Group, Inc. ("NWLGI") and its wholly owned subsidiaries (collectively, the "Company"), on a basis consistent with the prior audited consolidated financial statements, as of September 30, 2021, and for the three and nine months ended September 30, 2021 and September 30, 2020. Such adjustments are of a normal recurring nature. Certain reclasses of prior year balances have been made for comparison. In addition, certain segment information disclosed in Note 6 has been revised. The results of operations for the nine months ended September 30, 2021 are not necessarily indicative of the results to be expected for the full year. It is recommended that these Condensed Consolidated Financial Statements be read in conjunction with the audited consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2020 which is accessible free of charge through the Company's internet site at www.nwlgi.com or the Securities and Exchange Commission internet site at www.sec.gov. The Condensed Consolidated Balance Sheet at December 31, 2020 has been derived from the audited consolidated financial statements as of that date.

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of NWLGI and its wholly owned subsidiaries: National Western Life Insurance Company ("NWLIC" or "National Western"), Regent Care San Marcos Holdings, LLC, NWL Services, Inc., and N.I.S. Financial Services, Inc. ("NIS"). National Western's wholly owned subsidiaries include The Westcap Corporation, NWL Financial, Inc., NWLSM, Inc., Braker P III, LLC, and Ozark National Life Insurance Company ("Ozark National"). All significant intercorporate transactions and accounts have been eliminated in consolidation.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. Significant estimates in the accompanying Condensed Consolidated Financial Statements include: (1) liabilities for future policy benefits, (2) valuation of derivative instruments, (3) recoverability and amortization of deferred policy acquisition costs ("DPAC"), deferred sales inducements ("DSI"), the value of business acquired ("VOBA"), and the cost of reinsurance ("COR"), (4) valuation allowances for deferred tax assets, (5) goodwill, (6) allowances for credit losses on debt securities and mortgage loans, and (7) commitments and contingencies.

As a result of executing a funds withheld coinsurance agreement at December 31, 2020, the Company implemented accounting policies related to trading debt securities and the embedded derivative on reinsurance in its financial statements. Trading securities represent debt securities that are included in the fund assets withheld as part of the funds withheld coinsurance agreements to support the policyholder liability obligations ceded to the reinsurer. Trading debt securities are reported in the accompanying Condensed Consolidated Financial Statements at their fair values with changes in their fair values reflected as a component of Net investment income in the Condensed Consolidated Statements of Earnings. Since these trading debt securities pertain to investment activities related to coinsurance agreements rather than as an income strategy based on active trading, they are classified as investing activities in the Condensed Consolidated Statements of Cash Flows. Under the terms of the coinsurance funds withheld agreement, while the assets are withheld, the associated interest and credit risk of these assets are transferred to the reinsurer creating an embedded derivative on reinsurance in the funds withheld liability. Accordingly, the Company is required to bifurcate the embedded derivative from the host contract in accordance with ASC 815-15. The bifurcated embedded derivative on reinsurance is computed as the fair value unrealized gain (loss) on the underlying funds withheld assets. This amount is included as a component of the funds withheld liability balance reported on the Condensed Consolidated Balance Sheets, with changes in the embedded derivative on reinsurance reported in Net investment income (loss) in the Condensed Consolidated Statements of Earnings. The embedded derivative on reinsurance is classified as a Level 2 financial instrument in the fair value hierarchy because its valuation input is the fair value market adjustments on the underlying Level 2 debt securities. See Note (10) *Fair Values of Financial Instruments* for further details of fair value disclosures. In the Condensed Consolidated Statements of Cash Flows, changes in the funds withheld liability are reported as operating activities. Realized gains on funds withheld assets are transferred to the reinsurer and reported as investing activities in the Condensed Consolidated Statements of Cash Flows.

The table below shows the net unrealized gains and losses on available-for-sale securities that were reclassified out of accumulated other comprehensive income for the three and nine months ended September 30, 2021 and September 30, 2020.

| Affected Line Item in the Condensed Consolidated Statements of Earnings | Amount Reclassified From Accumulated Other Comprehensive Income | | | |
|---|---|---|---|---|
| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Other net investment gains | $ 5,025 | 889 | 11,265 | 3,380 |
| Earnings before Federal income taxes | 5,025 | 889 | 11,265 | 3,380 |
| Federal income taxes | 1,055 | 187 | 2,366 | 710 |
| Net earnings | $ 3,970 | 702 | 8,899 | 2,670 |

## (2) NEW ACCOUNTING PRONOUNCEMENTS

***Recent accounting pronouncements not yet adopted***

In August 2018, the FASB issued ASU 2018-12 *Financial Services-Insurance (Topic 944) - Targeted Improvements to the Accounting for Long-Duration Contracts*. This update is aimed at improving the Codification as it relates to long-duration contracts which will improve the timeliness of recognizing changes in the liability for future policy benefits, simplify accounting for certain market-based options, simplify the amortization of deferred acquisition costs, and improve the effectiveness of required disclosures. Amendments include the following:

A. Require insurance entity to (1) review and update assumptions used to measure cash flows at least annually (with changes recognized in net income) and (2) update discount rate assumption at each reporting date (with changes recognized in other comprehensive income).

B. Require insurance entity to measure all market risk benefits associated with deposit (i.e. account balance) contracts at fair value, with change in fair value attributable to change in instrument-specific credit risk recognized in other comprehensive income.

C. Simplify amortization of deferred acquisition costs and other balances amortized in proportion to premiums, gross profits, or gross margins and require those balances be amortized on constant level basis over expected term of related contract. Deferred acquisition costs are required to be written off for unexpected contract terminations but are not subject to impairment test.

D. Require insurance entity to add disclosures of disaggregated rollforwards of beginning to ending balances of the liability for future policy benefits, policyholder account balances, market risk benefits, separate account liabilities, and deferred acquisition costs. Insurance entity must also disclose information about significant inputs, judgments, assumptions, and methods used in measurement, including changes in those inputs, judgments, and assumptions, and the effect of those changes on measurement.

These updates are required to be applied retrospectively to the earliest period presented in the financial statements for fiscal periods beginning after December 15, 2022, with early adoption permitted. The Company has performed a preliminary gap analysis and created a roadmap for implementation of this standard by the effective date and is evaluating the impact of the new guidance on its Consolidated Financial Statements.

***Accounting pronouncements adopted***

In December 2019, the FASB issued ASU 2019-12 *Income Taxes - Simplifying the Accounting for Income Taxes (Topic 740)*, which simplifies various aspects of the income tax accounting guidance and will be applied using different approaches depending on the specific amendment. The amendments are effective for fiscal periods beginning after December 15, 2020. Earlier adoption was permitted. The adoption of this ASU did not have a material effect on the results of operations or financial position of the Company.

In June 2016, the FASB released ASU 2016-13, *Financial Instruments - Credit Losses*, which revises the credit loss recognition criteria for certain financial assets measured at amortized cost. The new guidance replaces the existing incurred loss recognition model with an expected loss recognition model ("CECL"). The objective of the CECL model is for the reporting entity to recognize its estimate of current expected credit losses for affected financial assets in a valuation allowance deducted from the amortized cost basis of the related financial assets that results in presenting the net carrying value of the financial assets at the amount expected to be collected. In April 2019, the FASB issued ASU 2019-04, *Codification Improvements to Topic 326, Financial Instruments - Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments.* The amendments in this Update add clarification and correction to ASU 2016-13 around expected recoveries for purchased financial assets with credit deterioration, transition relief for troubled debt restructurings, disclosures related to accrued interest receivables, and financial assets secured by collateral maintenance provisions. The guidance for these pronouncements was effective for interim and annual periods beginning after December 15, 2019, and for most affected instruments required adoption using a modified retrospective approach, with a cumulative effect adjustment recorded to beginning retained earnings. Effective January 1, 2020, the Company adopted the expected loss recognition model related to mortgage loans, debt securities held-to-maturity, and reinsurance recoverable using a modified retrospective approach. The change in accounting, net of tax, of $3.0 million was recorded as a charge to retained earnings in the first quarter of 2020 reflecting initial allowance for estimated credit losses balances of $1.2 million on mortgage loans and $3.3 million on debt securities held to maturity. The estimated credit losses for reinsurance recoverable were immaterial to the financial statements, but are monitored quarterly for any changes. Refer to Note (9) *Investments* for more information. Certain disclosures required by ASU 2016-13 are not included in the Consolidated Financial Statements as the impact of this standard was not material.

Other recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the AICPA, and the SEC did not, or are not believed by management to, have a material impact on the Company’s present or future Consolidated Financial Statements.

## (3) STOCKHOLDERS' EQUITY

Robert L. Moody, Sr., through the Robert L. Moody Revocable Trust, controls 99.0% of the total outstanding shares of the Company's Class B common stock as of September 30, 2021. Holders of the Company's Class A common stock elect one-third of the Board of Directors of the Company, and holders of the Class B common stock elect the remainder. Any cash or in-kind dividends paid on each share of Class B common stock are limited to one-half of the cash or in-kind dividends paid on each share of Class A common stock. In the event of liquidation of the Company, the Class A stockholders will receive the par value of their shares; then the Class B stockholders shall receive the par value of their shares; and the remaining net assets of the Company shall be divided between the stockholders of both Class A and Class B stock based upon the number of shares held.

As the sole owner of National Western, all dividends declared by National Western are payable entirely to NWLGI and are eliminated in consolidation. National Western is restricted by state insurance laws as to dividend amounts which may be paid to stockholders without prior approval from the Colorado Division of Insurance. The restrictions are based on the lesser of statutory earnings from operations, excluding capital gains, or 10% of statutory surplus of National Western as of the previous year-end. Under these guidelines the maximum dividend payment which may be made without prior approval in 2021 is $10.0 million.

Ozark National is similarly restricted under the state insurance laws of Missouri as to dividend amounts which may be paid to stockholders without prior approval to the greater of 10.0% of the statutory surplus of the company from the preceding year-end or the company's net gain from operations, excluding capital gains, from the prior calendar year. Based upon this restriction, the maximum dividend payment which may be made in 2021 without prior approval is $20.0 million. All dividends declared by Ozark National are payable entirely to NWLIC as the sole owner and are eliminated in consolidation.

National Western did not declare or pay cash dividends to NWLGI during the nine months ended September 30, 2021 and 2020. NWLGI also did not declare or pay cash dividends on its common shares during the nine months ended September 30, 2021 and 2020.

## (4) EARNINGS PER SHARE

Basic earnings per share of common stock are computed by dividing net earnings available to each class of common stockholders on an as if distributed basis by the weighted-average number of common shares outstanding for the period. Diluted earnings per share, by definition, reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock, that then shared in the distributed earnings of each class of common stock. U.S. GAAP requires a two-class presentation for the Company's two classes of common stock. The Company currently has no share-based compensation awards outstanding that could be redeemed for shares of common stock.

Net earnings for the periods shown below are allocated between Class A shares and Class B shares based upon (1) the proportionate number of shares issued and outstanding as of the end of the period, and (2) the per share dividend rights of the two classes under the Company's Restated Certificate of Incorporation (the Class B dividend per share is equal to one-half the Class A dividend per share).

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | Three Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2021 | | 2020 | |
| | Class A | Class B | Class A | Class B |
| | (In thousands except per share amounts) | | | |
| *Numerator for Basic and Diluted Earnings Per Share:* | | | | |
| Net earnings | $ 39,840 | | 10,825 | |
| Dividends - Class A shares | — | | — | |
| Dividends - Class B shares | — | | — | |
| Undistributed earnings | $ 39,840 | | 10,825 | |
| Allocation of net earnings: | | | | |
| Dividends | $ — | — | — | — |
| Allocation of undistributed earnings | 38,713 | 1,127 | 10,519 | 306 |
| Net earnings | $ 38,713 | 1,127 | 10,519 | 306 |
| *Denominator:* | | | | |
| Basic earnings per share - weighted-average shares | 3,436 | 200 | 3,436 | 200 |
| Effect of dilutive stock options | — | — | — | — |
| Diluted earnings per share - adjusted weighted-average shares for assumed conversions | 3,436 | 200 | 3,436 | 200 |
| Basic earnings per share | $ 11.27 | 5.63 | 3.06 | 1.53 |
| Diluted earnings per share | $ 11.27 | 5.63 | 3.06 | 1.53 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | Nine Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2021 | | 2020 | |
| | Class A | Class B | Class A | Class B |
| | (In thousands except per share amounts) | | | |
| *Numerator for Basic and Diluted Earnings Per Share:* | | | | |
| Net earnings | $ 151,869 | | 57,176 | |
| Dividends - Class A shares | — | | — | |
| Dividends - Class B shares | — | | — | |
| Undistributed earnings | $ 151,869 | | 57,176 | |
| Allocation of net earnings: | | | | |
| Dividends | $ — | — | — | — |
| Allocation of undistributed earnings | 147,574 | 4,295 | 55,560 | 1,616 |
| Net earnings | $ 147,574 | 4,295 | 55,560 | 1,616 |
| *Denominator:* | | | | |
| Basic earnings per share - weighted-average shares | 3,436 | 200 | 3,436 | 200 |
| Effect of dilutive stock options | — | — | — | — |
| Diluted earnings per share - adjusted weighted-average shares for assumed conversions | 3,436 | 200 | 3,436 | 200 |
| Basic earnings per share | $ 42.95 | 21.47 | 16.17 | 8.08 |
| Diluted earnings per share | $ 42.95 | 21.47 | 16.17 | 8.08 |

NATIONAL WESTERN LIFE GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

## (5) PENSION AND OTHER POSTRETIREMENT PLANS

### (A) Defined Benefit Pension Plans

National Western sponsors a qualified defined benefit pension plan covering employees enrolled prior to 2008. The plan provides benefits based on the participants' years of service and compensation. The Company makes annual contributions to the plan that comply with the minimum funding provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"). On October 19, 2007, National Western's Board of Directors approved an amendment to freeze the pension plan as of December 31, 2007. The freeze ceased future benefit accruals to all participants and closed the plan to any new participants. In addition, all participants became immediately 100% vested in their accrued benefits as of that date. As participants are no longer earning a credit for service, future qualified defined benefit plan expense is projected to be minimal. Fair values of plan assets and liabilities are measured as of the prior December 31 for each year. The following table summarizes the components of net periodic benefit cost.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Service cost | $ 29 | 27 | 89 | 81 |
| Interest cost | 133 | 168 | 396 | 505 |
| Expected return on plan assets | (356) | (315) | (1,068) | (946) |
| Amortization of net loss | 135 | 145 | 404 | 435 |
| Net periodic benefit cost | $ (59) | 25 | (179) | 75 |

The service cost shown above for each period represents plan expenses expected to be paid out of plan assets. Under the clarified rules of the Pension Protection Act, plan expenses paid from plan assets are to be included in the plan's service cost component.

The Company's minimum required contribution for the 2021 plan year is $0.0 million. There were no planned contributions remaining for the 2020 plan year as of September 30, 2021. As of September 30, 2021, the Company has made $0.9 million in contributions to the plan for the 2020 plan year and $0.0 million in contributions to the plan for the 2021 plan year.

The components of net periodic benefit cost including service cost are reported in the line item “Other operating expenses” in the Condensed Consolidated Statements of Earnings.

National Western also sponsors three non-qualified defined benefit pension plans. The first plan covers certain senior officers and provides benefits based on the participants' years of service and compensation. The primary pension obligations and administrative responsibilities of the plan are maintained by a pension administration firm, which is a subsidiary of American National Group, Inc. ("American National"), a related party. American National has guaranteed the payment of pension obligations under the plan. However, the Company has a contingent liability with respect to the plan should these entities be unable to meet their obligations under the existing agreements. Also, the Company has a contingent liability with respect to the plan in the event that a plan participant continues employment with National Western beyond age seventy, the aggregate average annual participant salary increases exceed 10% per year, or any additional employees become eligible to participate in the plan. If any of these conditions are met, the Company would be responsible for any additional pension obligations resulting from these items. Amendments were made to the plan to allow an additional employee to participate and to change the benefit formula for the then Chairman of the Company. As previously mentioned, these additional obligations are a liability to the Company. Effective December 31, 2004, this plan was frozen with respect to the continued accrual of benefits of the then Chairman and the then President of the Company in order to comply with law changes under the American Jobs Creation Act of 2004 ("Act").

Effective July 1, 2005, National Western established a second non-qualified defined benefit plan for the benefit of the then Chairman of the Company. This plan is intended to provide for post-2004 benefit accruals that mirror and supplement the pre-2005 benefit accruals under the previously discussed non-qualified plan, while complying with the requirements of the Act.

Effective November 1, 2005, National Western established a third non-qualified defined benefit plan for the benefit of the then President of the Company. This plan is intended to provide for post-2004 benefit accruals that supplement the pre-2005 benefit accruals under the first non-qualified plan as previously discussed, while complying with the requirements of the Act.

The following table summarizes the components of net periodic benefit costs for the non-qualified defined benefit plans.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Service cost | $ 309 | 302 | 927 | 907 |
| Interest cost | 262 | 337 | 783 | 1,012 |
| Amortization of prior service cost | 14 | 14 | 44 | 44 |
| Amortization of net loss | 1,283 | 1,446 | 3,848 | 4,336 |
| Net periodic benefit cost | $ 1,868 | 2,099 | 5,602 | 6,299 |

As the plans are not funded, there is no expected return on plan assets shown in the net periodic benefit cost table above. The Company expects to contribute $2.0 million to these plans in 2021. As of September 30, 2021, the Company has contributed $1.3 million to the plans.

The components of net periodic benefit cost including service cost are reported in the line item “Other operating expenses” in the Condensed Consolidated Statements of Earnings.

Ozark National and NIS have no defined benefit plans.

**(B) Postretirement Employment Plans Other Than Pension**

National Western sponsors two healthcare plans that were amended in 2004 to provide postretirement benefits to certain fully-vested individuals. The plans are unfunded. The following table summarizes the components of net periodic benefit costs.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Interest cost | $ 37 | 41 | 111 | 124 |
| Amortization of net loss | 73 | 40 | 219 | 119 |
| Net periodic benefit cost | $ 110 | 81 | 330 | 243 |

As the plans are not funded, there is no expected return on plan assets shown in the net periodic benefit cost table above. The Company expects to contribute minimal amounts to the plans in 2021. Ozark National and NIS do not offer postemployment benefits.

The components of net periodic benefit cost including service cost are reported in the line item "Other operating expenses" in the Condensed Consolidated Statements of Earnings.

## (6) SEGMENT AND OTHER OPERATING INFORMATION

The Company defines its reportable operating segments as domestic life insurance, international life insurance, annuities, and ONL and Affiliates (previously referred to as "Acquired Businesses"). These segments are organized based on product types, geographic marketing areas, and business groupings. Ozark National and NIS have been combined into a separate segment given its inter-related marketing and sales approach which consists of a coordinated sale of a non-participating whole life insurance product (Ozark National) and a mutual fund investment product (NIS). A fifth category "All Others" primarily includes investments and earnings of non-operating subsidiaries as well as other remaining investments and assets not otherwise supporting specific segment operations.

A summary of segment information as of September 30, 2021 and December 31, 2020 for the Condensed Consolidated Balance Sheet items and for the three and nine months ended September 30, 2021 and September 30, 2020 for the Condensed Consolidated Statements of Earnings is provided below.

*Condensed Consolidated Balance Sheet Items:*

| | September 30, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
| | (In thousands) | | | | | |
| Deferred transaction costs | $ 140,391 | 149,919 | 403,157 | 166,341 | — | 859,808 |
| Total segment assets | 1,759,778 | 997,222 | 9,454,359 | 1,113,961 | 351,616 | 13,676,936 |
| Future policy benefits | 1,481,187 | 752,342 | 6,894,890 | 778,221 | — | 9,906,640 |
| Other policyholder liabilities | 18,486 | 14,759 | 82,965 | 15,819 | — | 132,029 |
| Funds withheld liability | — | — | 1,540,384 | — | — | 1,540,384 |

| | December 31, 2020 | | | | | |
|---|---|---|---|---|---|---|
| | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
| | (In thousands) | | | | | |
| Deferred transaction costs | $ 94,100 | 124,480 | 302,397 | 170,756 | — | 691,733 |
| Total segment assets | 3,242,794 | 1,034,280 | 7,976,588 | 1,117,509 | 382,149 | 13,753,320 |
| Future policy benefits | 1,337,174 | 798,952 | 7,028,860 | 768,433 | — | 9,933,419 |
| Other policyholder liabilities | 16,378 | 11,086 | 94,049 | 16,967 | — | 138,480 |
| Funds withheld liability | — | — | 1,697,591 | — | — | 1,697,591 |

Table of Contents

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

*Condensed Consolidated Statements of Earnings:*

| | Three Months Ended September 30, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
| | (In thousands) | | | | | |
| Premiums and contract revenues | $ 12,122 | 19,570 | 4,243 | 19,159 | — | 55,094 |
| Net investment income | 6,599 | 9,172 | 62,150 | 6,763 | 4,286 | 88,970 |
| Other revenues | 28 | 19 | 1,305 | 3,169 | 1,285 | 5,806 |
| Total revenues | 18,749 | 28,761 | 67,698 | 29,091 | 5,571 | 149,870 |
| Life and other policy benefits | 6,752 | 10,272 | 36,079 | 17,530 | — | 70,633 |
| Amortization of deferred transaction costs | 2,479 | (27,896) | 14,916 | 2,112 | — | (8,389) |
| Universal life and annuity contract interest | 3,015 | (7,056) | 15,704 | — | — | 11,663 |
| Other operating expenses | 5,891 | 4,640 | 13,544 | 5,229 | 1,489 | 30,793 |
| Federal income taxes | 126 | 10,042 | (2,560) | 839 | 842 | 9,289 |
| Total expenses | 18,263 | (9,998) | 77,683 | 25,710 | 2,331 | 113,989 |
| Segment earnings (loss) | $ 486 | 38,759 | (9,985) | 3,381 | 3,240 | 35,881 |

| | Nine Months Ended September 30, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
| | (In thousands) | | | | | |
| Premiums and contract revenues | $ 38,495 | 60,406 | 11,915 | 57,923 | — | 168,739 |
| Net investment income | 58,689 | 35,135 | 282,073 | 20,117 | 15,575 | 411,589 |
| Other revenues | 80 | 91 | 4,068 | 9,368 | 3,647 | 17,254 |
| Total revenues | 97,264 | 95,632 | 298,056 | 87,408 | 19,222 | 597,582 |
| Life and other policy benefits | 17,869 | 19,949 | 55,909 | 50,699 | — | 144,426 |
| Amortization of deferred transaction costs | 8,092 | (16,341) | 47,741 | 7,231 | — | 46,723 |
| Universal life and annuity contract interest | 50,102 | 15,969 | 68,410 | — | — | 134,481 |
| Other operating expenses | 18,820 | 14,060 | 38,338 | 14,908 | 4,470 | 90,596 |
| Federal income taxes | 490 | 12,752 | 18,031 | 2,954 | 3,035 | 37,262 |
| Total expenses | 95,373 | 46,389 | 228,429 | 75,792 | 7,505 | 453,488 |
| Segment earnings | $ 1,891 | 49,243 | 69,627 | 11,616 | 11,717 | 144,094 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | Three Months Ended September 30, 2020 | | | | | |
|---|---|---|---|---|---|---|
| | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
| | (In thousands) | | | | | |
| Premiums and contract revenues | $ 17,734 | 21,551 | 4,187 | 19,524 | — | 62,996 |
| Net investment income | 21,201 | 10,354 | 87,889 | 6,434 | 3,801 | 129,679 |
| Other revenues | 10 | 6 | 84 | 2,628 | 1,249 | 3,977 |
| Total revenues | 38,945 | 31,911 | 92,160 | 28,586 | 5,050 | 196,652 |
| Life and other policy benefits | 3,785 | 2,278 | 3,383 | 17,494 | — | 26,940 |
| Amortization of deferred transaction costs | 10,540 | 6,496 | 31,794 | 1,970 | — | 50,800 |
| Universal life and annuity contract interest | 20,352 | (14,023) | 79,550 | — | — | 85,879 |
| Other operating expenses | 5,185 | 5,434 | 9,205 | 4,498 | 1,432 | 25,754 |
| Federal income taxes | (161) | 5,169 | (5,294) | 963 | 556 | 1,233 |
| Total expenses | 39,701 | 5,354 | 118,638 | 24,925 | 1,988 | 190,606 |
| Segment earnings (loss) | $ (756) | 26,557 | (26,478) | 3,661 | 3,062 | 6,046 |

| | Nine Months Ended September 30, 2020 | | | | | |
|---|---|---|---|---|---|---|
| | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
| | (In thousands) | | | | | |
| Premiums and contract revenues | $ 40,971 | 67,479 | 13,536 | 59,448 | — | 181,434 |
| Net investment income | 23,293 | 12,507 | 196,187 | 19,284 | 10,623 | 261,894 |
| Other revenues | 40 | 54 | 80 | 7,369 | 7,674 | 15,217 |
| Total revenues | 64,304 | 80,040 | 209,803 | 86,101 | 18,297 | 458,545 |
| Life and other policy benefits | 13,831 | 9,293 | 20,452 | 50,429 | — | 94,005 |
| Amortization of deferred transaction costs | 16,322 | 19,392 | 70,159 | 6,064 | — | 111,937 |
| Universal life and annuity contract interest | 17,831 | (15,368) | 117,162 | — | — | 119,625 |
| Other operating expenses | 15,123 | 13,047 | 28,787 | 13,361 | 4,412 | 74,730 |
| Federal income taxes | 199 | 8,907 | (4,440) | 4,103 | 2,304 | 11,073 |
| Total expenses | 63,306 | 35,271 | 232,120 | 73,957 | 6,716 | 411,370 |
| Segment earnings (loss) | $ 998 | 44,769 | (22,317) | 12,144 | 11,581 | 47,175 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

Reconciliations of segment information to the Company's Condensed Consolidated Financial Statements are provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| *Premiums and Other Revenues*: | | | | |
| Premiums and contract revenues | $ 55,094 | 62,996 | 168,739 | 181,434 |
| Net investment income | 88,970 | 129,679 | 411,589 | 261,894 |
| Other revenues | 5,806 | 3,977 | 17,254 | 15,217 |
| Realized gains on investments | 5,011 | 6,050 | 9,842 | 12,660 |
| Total condensed consolidated premiums and other revenues | $ 154,881 | 202,702 | 607,424 | 471,205 |

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| *Federal Income Taxes*: | | | | |
| Total segment Federal income taxes | $ 9,289 | 1,233 | 37,262 | 11,073 |
| Taxes on realized gains on investments | 1,052 | 1,271 | 2,067 | 2,659 |
| Total condensed consolidated Federal income taxes | $ 10,341 | 2,504 | 39,329 | 13,732 |

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| *Net Earnings*: | | | | |
| Total segment earnings | $ 35,881 | 6,046 | 144,094 | 47,175 |
| Realized gains on investments, net of taxes | 3,959 | 4,779 | 7,775 | 10,001 |
| Total condensed consolidated net earnings | $ 39,840 | 10,825 | 151,869 | 57,176 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | September 30, 2021 | December 31, 2020 |
|---|---|---|
| | (In thousands) | |
| *Assets*: | | |
| Total segment assets | $ 13,676,936 | 13,753,320 |
| Other unallocated assets | 744,706 | 894,950 |
| | | |
| Total condensed consolidated assets | $ 14,421,642 | 14,648,270 |

**(7) SHARE-BASED PAYMENTS**

Effective June 20, 2008, the Company's shareholders approved a 2008 Incentive Plan (“2008 Plan”) which provided for the grant of any or all of the following types of awards to eligible employees: (1) stock options, including incentive stock options and nonqualified stock options; (2) stock appreciation rights ("SARs"), in tandem with stock options or freestanding; (3) restricted stock or restricted stock units; and, (4) performance awards. The number of shares of Class A, $1.00 par value, common stock which were allowed to be issued under the 2008 Plan, or as to which SARs or other awards were allowed to be granted, could not exceed 300,000. This plan was assumed by NWLGI from National Western pursuant to the terms of the holding company reorganization in 2015. On June 15, 2016, stockholders of NWLGI approved an amended and restated 2008 Plan ("Incentive Plan"), which extended the term of the 2008 Plan for ten years from the date of stockholder approval. The Incentive Plan includes additional provisions, most notably regarding the definition of performance objectives which could be used in the issuance of the fourth type of award noted above (performance awards).

All of the employees of the Company and its subsidiaries are eligible to participate in the current Incentive Plan. In addition, directors of the Company are eligible to receive the same types of awards as employees except that they are not eligible to receive incentive stock options. Company directors, including members of the Compensation and Stock Option Committee, are eligible for nondiscretionary stock options. At the end of 2018, all stock options granted under the 2008 Plan had been exercised, forfeited, or expired. SARs granted prior to 2016 vest 20% annually following three years of service following the grant date. Employee SARs granted 2016 and thereafter vest 33.3% annually following one year of service from the date of the grant. Directors' SARs grants vest 20% annually following one year of service from the date of grant.

Effective during August 2008, the Company adopted and implemented a limited stock buy-back program with respect to the 2008 Plan which provided stock option holders the additional alternative of selling shares acquired through the exercise of options directly back to the Company. Option holders could elect to sell such acquired shares back to the Company at any time within ninety (90) days after the exercise of options at the prevailing market price as of the date of notice of election. The buy-back program did not alter the terms and conditions of the 2008 Plan. This plan was assumed as well by NWLGI from National Western pursuant to the terms of the holding company reorganization. There are currently no stock options issued and outstanding.

The Incentive Plan allows for certain other share or unit awards which are solely paid out in cash based on the value of the Company's shares, or changes therein, as well as the financial performance of the Company under pre-determined target performance metrics. Certain awards, such as restricted stock units ("RSUs") provide solely for cash settlement based upon the market price of the Company's Class A common shares, often referred to as "phantom stock-based awards" in equity compensation plans. Unlike share-settled awards, which have a fixed grant-date fair value, the fair value of unsettled or unvested liability awards is remeasured at the end of each reporting period based on the change in fair value of a share. The liability and corresponding expense are adjusted accordingly until the award is settled. For employees, the vesting period for RSUs is 100% at the end of 3 years from the grant date. RSUs granted prior to 2019 are payable in cash at the vesting date equal to the closing price of the Company's Class A common share on the three year anniversary date. RSUs granted in 2019 and forward are payable in cash at the 3 years vesting date equal to the 20-day moving average closing price of the Company’s Class A common share at that time.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

Other awards may involve performance share units ("PSUs") which are units granted at a specified dollar amount per unit, typically linked to the Company's Class A common share price, that are subsequently multiplied by an attained performance factor to derive the number of PSUs to be paid as cash compensation at the vesting date. PSUs also vest three years from the date of grant. For PSUs, the performance period begins the first day of the calendar year for which the PSUs are granted and runs three calendar years. At that time, the three-year performance outcome will be measured against the pre-defined target amounts to determine the number of PSUs earned as compensation. PSUs granted prior to 2019 are paid at the closing price of the Company's Class A common share on the vesting date. PSUs granted in 2019 and forward are payable at the 20-day moving average closing price of the Company’s Class A common share at the vesting date.

PSU awards covering the three year measurement period ended December 31, 2019 were paid out in the first quarter of 2020. The performance factor during the measurement period used to determine compensation payouts was 101.19% of the pre-defined metric target.

PSU awards covering the three year measurement period ended December 31, 2020 were paid out in April 2021. The performance factor during the measurement period used to determine compensation payouts was 85.16% of the pre-defined metric target.

Directors of the Company are eligible to receive RSUs under the Incentive Plan. Unlike RSUs granted to officers, the RSUs granted to directors vest one year from the date of grant. RSUs granted prior to 2019 are payable in cash at the vesting date equal to the closing price of the Company's Class A common share at that time. RSUs granted in 2019 and forward are payable in cash at the vesting date equal to the 20-day moving average closing price of the Company’s Class A common share at that time.

No awards were granted to officers and directors during the nine months ended September 30, 2021 and 2020.

The Company uses the current fair value method to measure compensation costs for awards granted under the share-based plans. As of September 30, 2021 and December 31, 2020, the liability balance was $8.4 million and $6.2 million, respectively. A summary of awards by type and related activity is detailed below.

| | | Stock Options Outstanding | |
|---|---|---|---|
| | Shares Available For Grant | Shares | Weighted-Average Exercise Price |
| *Stock Options:* | | | |
| Balance at January 1, 2021 | 291,000 | — | $ — |
| Exercised | — | — | $ — |
| Forfeited | — | — | $ — |
| Expired | — | — | $ — |
| Stock options granted | — | — | $ — |
| Balance at September 30, 2021 | 291,000 | — | $ — |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | Liability Awards | | |
|---|---|---|---|
| | SAR | RSU | PSU |
| *Other Share/Unit Awards:* | | | |
| Balance at January 1, 2021 | 144,248 | 16,449 | 24,282 |
| Exercised | (11,063) | — | (3,863) |
| Forfeited | (1,310) | (157) | — |
| Granted | — | — | — |
| Balance at September 30, 2021 | 131,875 | 16,292 | 20,419 |

SARs, RSUs, and PSUs shown as forfeited in the above tables represent vested and unvested awards not exercised by plan participants upon their termination from the Company in accordance with the expiration provisions of the awards.

The total intrinsic value of share-based compensation exercised and paid was $2.0 million and $1.9 million for the nine months ended September 30, 2021 and 2020, respectively. The total fair value of SARs, RSUs, and PSUs vested during the nine months ended September 30, 2021 and 2020 was $0.0 million and $1.8 million, respectively. No cash amounts were received from the exercise of stock options under the Plans during the periods reported.

The following table summarizes information about SARs outstanding at September 30, 2021.

| | SARs Outstanding | | |
|---|---|---|---|
| | Number Outstanding | Weighted-Average Remaining Contractual Life | Number Exercisable |
| Exercise prices: | | | |
| $132.56 | 8,318 | 0.2 years | 8,318 |
| $210.22 | 23,250 | 2.2 years | 23,250 |
| $216.48 | 11,086 | 4.4 years | 11,086 |
| $311.16 | 9,395 | 5.3 years | 9,395 |
| $310.55 | 203 | 5.6 years | 203 |
| $334.34 | 8,880 | 6.2 years | 8,880 |
| $303.77 | 11,068 | 7.2 years | 7,373 |
| $252.91 | 19,127 | 8.2 years | 6,393 |
| $192.10 | 40,548 | 9.2 years | — |
| Totals | 131,875 | | 74,898 |
| Aggregate intrinsic value (in thousands) | $ 1,407 | | $ 658 |

The aggregate intrinsic value in the table above is based on the closing Class A stock price of $210.59 per share on September 30, 2021.

The SARs shown above with exercise price of $132.56 have a remaining contractual life of less than one year. The holders for this grant have until the end of the contractual life of December 14, 2021 to exercise these holdings or otherwise forfeit the SAR grants held.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

In estimating the fair value of the SARs outstanding at September 30, 2021 and December 31, 2020, the Company employed the Black-Scholes option pricing model with assumptions detailed below.

| | September 30, 2021 | December 31, 2020 |
|---|---|---|
| Expected term | 0.2 to 9.2 years | 1.0 to 9.9 years |
| Expected volatility weighted-average | 34.90 % | 33.47 % |
| Expected dividend yield | 0.17 % | 0.17 % |
| Risk-free rate weighted-average | 0.61 % | 0.19 % |

The Company reviewed the contractual term relative to the SARs as well as perceived future behavior patterns of exercise. Volatility is based on the Company's historical volatility over the expected term of the SARs by expected exercise date.

The pre-tax compensation cost/(benefit) recognized in the financial statements related to these plans was $0.3 million and $4.2 million for the three and nine months ended September 30, 2021 and $(0.5) million and $(4.4) million for the three and nine months ended September 30, 2020, respectively. The related tax expense/(benefit) recognized was $(0.1) million and $(0.9) million for the three and nine months ended September 30, 2021 and $0.1 million and $0.9 million for the three and nine months ended September 30, 2020, respectively.

As of September 30, 2021, the total pre-tax compensation expense related to non-vested share-based awards not yet recognized was $5.5 million. This amount is expected to be recognized over a weighted-average period of 1.3 years. The Company recognizes compensation cost over the graded vesting periods.

## (8) COMMITMENTS AND CONTINGENCIES

### (A) Legal Proceedings

In the normal course of business, the Company is involved or may become involved in various legal actions in which claims for alleged economic and punitive damages have been or may be asserted, some for substantial amounts. In recent years, carriers offering life insurance and annuity products have faced litigation, including class action lawsuits, alleging improper product design, improper sales practices, and similar claims. As previously disclosed, the Company has been a defendant in prior years in such class action lawsuits. Given the uncertainty involved in these types of actions, the ability to make a reliable evaluation of the likelihood of an unfavorable outcome or an estimate of the amount of or range of potential loss is endemic to the particular circumstances and evolving developments of each individual matter on its own merits.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

On September 28, 2017, a purported shareholder derivative lawsuit was filed in the 122nd District Court of Galveston County, State of Texas entitled Robert L. Moody, Jr. derivatively on behalf of National Western Life Insurance Company and National Western Life Group, Inc. v. Ross Rankin Moody, et al., naming certain current and former directors and current officers as defendants. The complaint challenged the directors' oversight of insurance sales to non-U.S. residents and alleged that the defendants breached their fiduciary duties in the conduct of their duties as board members by failing to act (i) on an informed basis and (ii) in good faith or with the honest belief that their actions were in the best interests of the Company. The complaint sought an undetermined amount of damages, attorneys' fees and costs, and equitable relief, including the removal of the Company's Chairman and Chief Executive Officer and other board members and/or officers of the Company. The Company believes that the claims in the complaint were baseless and without merit, vigorously defended this lawsuit, and was awarded reimbursement of legal costs and expenses from plaintiff as detailed below. The companies and directors filed their respective Pleas to the Jurisdiction ("Pleas") contesting the plaintiff's standing to even pursue this action, along with their Answers, on October 27, 2017. On December 14, 2017, plaintiff filed a Response to the Pleas and on December 21, 2017, the Court heard oral argument on the Pleas. Plaintiff then filed a First Amended Petition on January 11, 2018. The companies and directors filed a Supplement to the Pleas on January 30, 2018, to which plaintiff responded on February 1, 2018, and the companies and directors replied on February 9, 2018. On May 3, 2018, the Court issued a memorandum to all attorneys of record stating that the Court would grant the defendants' Pleas and asked the attorney for defendants to prepare and submit proposed orders/ judgments granting the requested relief for consideration by the Court. The defendants filed such proposed order granting the Pleas on May 7, 2018. On May 16, 2018 the Court issued an Order granting the Pleas and dismissing Robert L. Moody, Jr.'s claims with prejudice, and plaintiff then filed a Motion to Transfer Venue ("MTTV"). Defendants filed an Application for Fees, seeking to recover defendants' legal costs and expenses from plaintiff, and a Response to the MTTV on June 8, 2018. In response plaintiff filed a Motion to Vacate, a Response to the Application for Fees, and his own Request for Attorney's Fees on July 5, 2018. Defendants filed a Response to the Motion to Vacate and to plaintiff's Request for Attorney's Fees on July 11, 2018, and the Court heard oral arguments on July 16, 2018. Plaintiff filed supplemental briefing in support of his July 5, 2018 filings on July 25, 2018, and defendants filed their response to plaintiff's supplemental briefing on July 27, 2018. On August 8, 2018 the Court issued an Order denying plaintiff's Motion to Vacate. Pursuant to the Court's instructions, on October 5, 2018, defendants filed an Order Granting Application for Expenses. Defendants then filed a Motion for Entry of Final Judgment and a Request for Submission Date on Motion for Entry of Final Judgment on October 11, 2018, which the Court set as October 30, 2018. Plaintiff filed his Objection to Proposed Final Judgment and Objection to Proposed Order on Attorneys' Fees on October 25, 2018, to which defendants filed a response on October 30, 2018. On November 11, 2018, the Court issued its Final Judgment: ordering Plaintiff to pay the companies $1,314,054 for reasonable and necessary fees and expenses, denying Plaintiff's Motion to Transfer Venue, and dismissing Plaintiff's counterclaim. Plaintiff appealed the Court's Final Judgment to the First District Court of Appeals in Houston, TX. The court of appeals issued a panel decision on December 10, 2020 affirming the dismissal and award of attorneys' fees and expenses to the companies. On January 22, 2021, Plaintiff filed a motion for rehearing of the affirmance of the award of attorneys' fees and expenses. On July 27, 2021, the Court of Appeals vacated its December 10, 2020 judgment and withdrew its earlier opinion, and issued a new judgment and opinion again affirming the dismissal and award of attorneys' fees and expenses to the companies. Plaintiff filed an Extension for Filing Review with the Texas Supreme Court on September 10, 2021, which expired on October 12, 2021. On October 15, 2021, Defendants received final payment in satisfaction of judgment from Robert L. Moody, Jr. for a total amount of $1,803,503. The Court of Appeals stated in its opinion that the evidence supported the trial court's implied finding that Robert L. Moody, Jr.'s suit was filed without reasonable cause and for an improper purpose, and therefore, the court's order that he pay $1,803,503 in attorneys' fees to the Defendants was proper. Defendants filed a Notice of Satisfaction of Judgment with the trial court on October 19, 2021. Judgment in the Defendants' favor is now final and not subject to any further appeals.

In April of 2019, National Western defended a two-week jury trial in which it was alleged that it committed actionable Financial Elder Abuse in its issuance of a $100,000 equity indexed annuity to the Plaintiff in the case of *Williams v Pantaleoni et al*, Case No. 17CV03462, Butte County California Superior Court. The Court entered an Amended Judgment on the Jury Verdict on July 27, 2019 against National Western in the amount of $14,949 for economic damages and $2.9 million in non-economic and punitive damages. National Western vigorously disputes the verdicts and the amounts awarded, and in furtherance of such, filed a Motion for Judgment Notwithstanding Jury Verdict and a Motion for New Trial, both of which were rejected by the Court. On September 9, 2019, NWLIC filed its Notice of Appeal. On November 11, 2019, the judge awarded the Plaintiff attorney's fees in the amount of $1.26 million. Both the Plaintiff and NWLIC appealed this ruling. On June 11, 2021, the appellate court reversed the judgment and directed the trial court to enter judgment in favor of NWLIC. Plaintiff has filed an appeal with the Supreme Court of California. On September 22, 2021, the California Supreme Court granted review and transferred the case back to the appellate court with instructions to vacate its decision and reconsider its finding that Mr. Pantaleoni did not have an agency relationship with NWLIC.

NATIONAL WESTERN LIFE GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

In the Form 10-Q for the period ended September 30, 2020, the Company reported that it experienced a data event in which an intruder accessed and exfiltrated certain data from the Company's network. As a result of this event, the Company reported in its Form 10-K for the year ended December 31, 2020, that it was aware of two proposed class actions filed against National Western, *Mildred Baldwin, on behalf of herself and others similarly situated vs. National Western Life Insurance Company*, Missouri Circuit Court for the 18th Judicial Circuit (Pettis County) filed February 16, 2021, and *Douglas Dyrssen Sr., individually and on behalf of all others similarly situated vs. National Western Life Insurance Company and National Western Life Group, Inc.*, United States District Court for the Eastern District of California filed March 8, 2021. The parties agreed to consolidate those two proposed class actions into a single proposed class action, *Mildred Baldwin, on behalf of herself and others similarly situated vs. National Western Life Insurance Company*, United States District Court for the Western District of Missouri. Baldwin is seeking an undetermined amount of damages, attorneys' fees and costs, injunctive relief, declaratory and other equitable relief, and enjoinment. National Western filed a Motion to Dismiss on July 16, 2021. On July 26, 2021, the parties filed a Joint Motion to Stay Pending Mediation, which the court denied. On September 15, 2021, the court granted in part and denied in part National Western's Motion to Dismiss. At the mediation held on October 12, 2021, the parties agreed on preliminary terms to settle the litigation. The parties filed a Joint Notice of Settlement and Motion to Stay Deadlines with the court on October 20, 2021. The settlement terms are subject to court approval. The Company accrued $4.4 million at September 30, 2021 for this matter.

Although there can be no assurances, at the present time, the Company does not anticipate that the ultimate liability arising from such other potential, pending, or threatened legal actions will have a material adverse effect on the financial condition or operating results of the Company.

Separately, in 2015 Brazilian authorities commenced an investigation into possible violations of Brazilian criminal law in connection with the issuance of National Western insurance policies to Brazilian residents, and in assistance of such investigation a Commissioner appointed by the U.S. District Court for the Western District of Texas issued a subpoena in March of 2015 upon NWLIC to provide information relating to such possible violations. National Western cooperated with the relevant governmental authorities in regard to this matter. No conclusion can be drawn at this time as to its outcome or how such outcome may impact the Company's business, results of operations or financial condition.

**(B) Financial Instruments**

In order to meet the financing needs of its customers in the normal course of business, the Company is a party to financial instruments with off-balance sheet risk. These financial instruments are commitments to extend credit which involve elements of credit and interest rate risk in excess of the amounts recognized in the Condensed Consolidated Balance Sheets.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amounts, assuming that the amounts are fully advanced and that collateral or other security is of no value. Commitments to extend credit are legally binding agreements to lend to a customer that generally have fixed expiration dates or other termination clauses and may require payment of a fee. Commitments do not necessarily represent future liquidity requirements, as some could expire without being drawn upon. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company controls the credit risk of these transactions through credit approvals, limits, and monitoring procedures.

The Company had $10.5 million commitments to fund new loans and no commitments to extend credit relating to existing loans at September 30, 2021. The Company evaluates each customer's creditworthiness on a case-by-case basis. The Company had commitments to make capital contributions to alternative investment funds of $257.1 million as of September 30, 2021. The Company had no commitments to extend credit relating to revolving credit facilities at September 30, 2021.

NATIONAL WESTERN LIFE GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

## (9) INVESTMENTS

### (A) Investment Gains and Losses

The Company uses the specific identification method in computing realized gains and losses. The table below presents realized gains and losses for the periods indicated.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Available-for-sale debt securities: | | | | |
| Realized gains on disposal | $ 5,025 | 888 | 11,264 | 3,379 |
| Realized losses on disposal | — | — | — | — |
| Held-to-maturity debt securities: | | | | |
| Realized gains on disposal | — | 2,501 | — | 6,620 |
| Realized losses on disposal | — | — | — | — |
| Real estate gains (losses) | (14) | 2,661 | (1,421) | 2,661 |
| Other | — | — | (1) | — |
| Totals | $ 5,011 | 6,050 | 9,842 | 12,660 |

Disposals in the held-to-maturity category during the three and nine months ended September 30, 2020 represent calls initiated by the credit issuer of the debt security. At year-end 2020, the Company transferred all of its held-to-maturity debt securities to the available-for-sale category as the result of entering into a funds withheld reinsurance agreement effective December 31, 2020. The Company's policy was to initiate disposals of debt securities in the held-to-maturity category only in instances in which the credit status of the issuer came into question and the realization of all or a significant portion of the investment principal of the holding was deemed to be in jeopardy.

For the three months ended September 30, 2021 and 2020 the percentage of total gains on bonds due to the call of securities was 100.0% and 99.9%, respectively. For the nine months ended September 30, 2021 and 2020 the percentage of gains on bonds due to the call of securities was 100.0% and 99.8%, respectively.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

**(B) Debt Securities**

The Company transferred all of its debt securities to the available-for-sale classification as of December 31, 2020. The table below presents amortized costs and fair values of debt securities available-for-sale at September 30, 2021.

| | Debt Securities Available-for-Sale | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Allowance for Credit Losses |
| | (In thousands) | | | | |
| U.S. agencies | $ 50,096 | 1,419 | — | 51,515 | — |
| U.S. Treasury | 3,165 | 43 | — | 3,208 | — |
| States and political subdivisions | 475,739 | 29,223 | (637) | 504,325 | — |
| Foreign governments | 62,986 | 98 | (1,521) | 61,563 | — |
| Public utilities | 780,753 | 50,945 | (276) | 831,422 | — |
| Corporate | 6,460,995 | 468,475 | (10,854) | 6,918,616 | — |
| Commercial mortgage-backed | 27,049 | 1,159 | — | 28,208 | — |
| Residential mortgage-backed | 642,474 | 26,679 | — | 669,153 | — |
| Asset-backed | 292,416 | 4,134 | (477) | 296,073 | — |
| Totals | $ 8,795,673 | 582,175 | (13,765) | 9,364,083 | — |

The table below presents amortized costs and fair values of debt securities available-for-sale at December 31, 2020.

| | Debt Securities Available-for-Sale | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Allowance for Credit Losses |
| | (In thousands) | | | | |
| U.S. agencies | $ 72,945 | 2,496 | — | 75,441 | — |
| U.S. Treasury | 3,152 | 126 | — | 3,278 | — |
| States and political subdivisions | 528,266 | 37,909 | (86) | 566,089 | — |
| Foreign governments | 11,115 | 334 | — | 11,449 | — |
| Public utilities | 831,990 | 77,920 | — | 909,910 | — |
| Corporate | 7,376,104 | 727,470 | (4,601) | 8,098,973 | — |
| Commercial mortgage-backed | 30,108 | 1,363 | — | 31,471 | — |
| Residential mortgage-backed | 902,974 | 50,970 | (156) | 953,788 | — |
| Asset-backed | 117,889 | 2,635 | — | 120,524 | — |
| Totals | $ 9,874,543 | 901,223 | (4,843) | 10,770,923 | — |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

Unrealized losses for debt securities available-for-sale increased at September 30, 2021 from comparable balances at December 31, 2020 primarily due to increases in interest rate levels during 2021.

Debt securities balances at September 30, 2021 and December 31, 2020 include Ozark National holdings of $813.4 million and $811.6 million in available-for-sale. As part of the acquisition effective January 31, 2019 the Company employed purchase accounting procedures in accordance with GAAP which revalued the acquired investment portfolio to their fair values as of the date of the acquisition. These fair values became the book values for Ozark National from that point going forward. Accordingly, unrealized gains and losses for the Ozark National debt securities represent the changes subsequent to the purchase accounting book values established at the acquisition.

The following table shows the gross unrealized losses and fair values of the Company's available-for-sale debt securities by investment category and length of time the individual securities have been in a continuous unrealized loss position at September 30, 2021.

| | Debt Securities Available-for-Sale | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 Months | | 12 Months or Greater | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| States and political subdivisions | $ 16,810 | (515) | 1,789 | (122) | 18,599 | (637) |
| Foreign governments | 60,358 | (1,521) | — | — | 60,358 | (1,521) |
| Public utilities | 9,392 | (276) | — | — | 9,392 | (276) |
| Corporate | 456,494 | (10,443) | 9,575 | (411) | 466,069 | (10,854) |
| Asset-backed | 85,270 | (477) | — | — | 85,270 | (477) |
| Totals | $ 628,324 | (13,232) | 11,364 | (533) | 639,688 | (13,765) |

The following table shows the gross unrealized losses and fair values of the Company's available-for-sale debt securities by investment category and length of time that the individual securities have been in a continuous unrealized loss position at December 31, 2020.

| | Debt Securities Available-for-Sale | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 Months | | 12 Months or Greater | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| States and political subdivisions | $ — | — | 1,762 | (86) | 1,762 | (86) |
| Public utilities | — | — | — | — | — | — |
| Corporate | 174,252 | (3,836) | 36,152 | (765) | 210,404 | (4,601) |
| Residential mortgage-backed | — | — | 500 | (156) | 500 | (156) |
| Totals | $ 174,252 | (3,836) | 38,414 | (1,007) | 212,666 | (4,843) |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

*Debt securities.* The gross unrealized losses for debt securities are made up of 76 individual issues, or 6.1% of the total debt securities held available-for-sale by the Company at September 30, 2021. The market value of these bonds as a percent of amortized cost approximates 97.9%. Of the 76 securities, 3, or 4.0%, fall in the 12 months or greater aging category and 74 were rated investment grade at September 30, 2021.

The amortized cost and fair value of investments in debt securities available-for-sale at September 30, 2021, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Debt Securities Available-for-Sale | |
|---|---|---|
| | Amortized Cost | Fair Value |
| | (In thousands) | |
| Due in 1 year or less | $ 429,973 | 435,102 |
| Due after 1 year through 5 years | 3,291,218 | 3,502,340 |
| Due after 5 years through 10 years | 2,241,655 | 2,430,838 |
| Due after 10 years | 1,870,888 | 2,002,369 |
| | 7,833,734 | 8,370,649 |
| Mortgage and asset-backed securities | 961,939 | 993,434 |
| Totals before allowance for credit losses | 8,795,673 | 9,364,083 |
| Allowance for credit losses | — | — |
| Totals | $ 8,795,673 | 9,364,083 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

As disclosed in the Notes to Condensed Consolidated Financial Statements, the Company adopted new accounting guidance as of January 1, 2020 for credit loss recognition of certain financial assets, including debt securities classified in the held-to-maturity category. The Company employed a cohort cumulative loss rate method in estimating current expected credit losses with respect to its held-to-maturity debt securities. This method applies publicly available industry wide statistics of default incidence by defined segmentations of debt security investments combined with future assumptions regarding economic conditions (i.e. GDP forecasts) both in the near term and the long term. The Company utilized Moody's loss rates by industry type and credit ratings and applied them to each major bond category. These bond categories were further segmented by credit ratings and by maturities of two years and less and more than two years. The following table presents the allowance for debt securities credit losses for the three and nine months ended September 30, 2021 and 2020.

| | Three Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | Debt Securities Held-to-Maturity | | Debt Securities Available-for-Sale | |
| | (In thousands) | | | |
| Balance, beginning of period | $ — | 4,940 | — | — |
| Provision January 1, 2020 for adoption of new accounting guidance | — | — | — | — |
| (Releases)/provision during period | — | 146 | — | — |
| Balance, end of period | $ — | 5,086 | — | — |

| | Nine Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | Debt Securities Held-to- Maturity | | Debt Securities Available-for- Sale | |
| | (In thousands) | | | |
| Balance, beginning of period | — | — | — | — |
| Provision January 1, 2020 for adoption of new accounting guidance | — | 3,334 | — | — |
| (Releases)/provision during period | — | 1,752 | — | — |
| Balance, end of period | — | 5,086 | — | — |

As previously noted, the Company reclassified all held-to-maturity debt securities to available-for-sale as of December 31, 2020. Provisions to and releases from the allowance for credit losses in 2020 are recorded in net investment income in the Condensed Consolidated Statements of Earnings.

The Company determines current expected credit losses for available-for-sale debt securities in accordance with FASB ASC Subtopic 326-30 when fair value is less than amortized cost, interest payments are missed, and the security is experiencing credit issues. Based on its review, the Company determined none of these investments required an allowance for credit loss at September 30, 2021 or 2020. The Company's operating procedures include monitoring the investment portfolio on an ongoing basis for any changes in issuer facts and circumstances that might lead to future need for a credit loss allowance.

**(C) Transfer of Securities**

The Company reassessed its classification of its held-to-maturity portfolio at December 31, 2020 as a result of a funds withheld coinsurance agreement entered into with a third party reinsurer. A portion of the transferred debt securities was added to a funds withheld account for which the reinsurer provides investment management services and does not intend to hold the securities until maturity. Consequently, the Company determined that its continued classification of held-to-maturity debt securities was not appropriate and transferred the entire balance at that time to available-for-sale.

**(D) Mortgage Loans and Real Estate**

A financing receivable is a contractual right to receive money on demand or on fixed or determinable dates that is recognized as an asset in a company's statement of financial position. The Company's mortgage, participation and mezzanine loans on real estate are the only financing receivables included in the Condensed Consolidated Balance Sheets.

Credit and default risk are minimized through strict underwriting guidelines and diversification of underlying property types and geographic locations. In addition to being secured by the property, mortgage loans with leases on the underlying property are often guaranteed by the lease payments. This approach has proved to result in quality mortgage loans with few defaults. Mortgage loan interest income is recognized on an accrual basis with any premium or discount amortized over the life of the loan. Prepayment and late fees are recorded on the date of collection.

The Company targets a minimum specified yield on mortgage loan investments determined by reference to currently available debt security instrument yields plus a desired amount of incremental basis points. The low interest rate environment and competitive marketplace have caused fewer loan opportunities available meeting the Company's required rate of return. During the first half of 2020, mortgage loan originations were further impeded by the COVID-19 pandemic and its effects upon the commercial real estate market. Despite this backdrop, the Company has actively pursued mortgage loan opportunities consistent with its strategic asset allocation guidelines and mortgage loans originated by the Company totaled $151.4 million in the nine months ended September 30, 2021 compared with $80.2 million in the year ended December 31, 2020.

Loans in foreclosure, loans considered impaired or loans past due 90 days or more are placed on a non-accrual status. If a mortgage loan is determined to be on non-accrual status, the mortgage loan does not accrue any revenue into the Condensed Consolidated Statements of Earnings. The loan is independently monitored and evaluated as to potential impairment or foreclosure. If delinquent payments are made and the loan is brought current, then the Company returns the loan to active status and accrues income accordingly. The Company had no mortgage loans past due 90 days or more at September 30, 2021 or 2020 and as a result all interest income was recognized at September 30, 2021 and 2020. As a result of the economic climate change induced by the COVID-19 virus, various mortgage loan borrowers of the Company requested a temporary forbearance of principal payments on loans in the range of three to nine months. During 2020 there were eight loans representing an aggregate principal balance of $29.2 million with borrowers meeting specified criteria of the Company that forbearance terms were agreed to by the Company. All forbearance loans returned to the terms of the original loan agreements during the first quarter of 2021.

The following table represents the mortgage loan portfolio by loan-to-value ratio.

| | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | Amount | % | Amount | % |
| | (In thousands) | | (In thousands) | |
| Mortgage Loans by Loan-to-Value Ratio (1): | | | | |
| Less than 50% | $ 96,124 | 20.6 | $ 66,635 | 19.9 |
| 50% to 60% | 134,701 | 28.9 | 64,536 | 19.3 |
| 60% to 70% | 191,794 | 41.1 | 153,414 | 45.8 |
| 70% to 80% | 43,963 | 9.4 | 50,422 | 15.0 |
| Gross balance | 466,582 | 100.0 | 335,007 | 100.0 |
| | | | | |
| Market value adjustment | 256 | 0.1 | — | — |
| Allowance for credit losses | (3,956) | (0.9) | (2,486) | (0.7) |
| | | | | |
| Totals | $ 462,882 | 99.2 | $ 332,521 | 99.3 |

(1) Loan-to-Value Ratio is determined using the most recent appraised value. Appraisals are required at the time of funding and may be updated if a material change occurs from the original loan agreement.

Market value adjustments are recorded for mortgage loan investments for which the Company has elected to measure the loan at fair value. During the nine months ended September 30, 2021, the investment manager associated with the funds withheld coinsurance arrangement executed mortgage loan investments for the funds withheld assets under the reinsurance treaty. The Company elected fair value measurement for these mortgage loans, which will be included in the funds withheld portfolio.

All mortgage loans are analyzed quarterly in order to monitor the financial quality of these assets. Based on ongoing monitoring, mortgage loans with a likelihood of becoming delinquent are identified and placed on an internal “watch list.” Among the criteria that may indicate a potential problem include: major tenant vacancies or bankruptcies, late payments, and loan relief/restructuring requests. The mortgage loan portfolio is analyzed for the need for a valuation allowance on any loan that is on the internal watch list, in the process of foreclosure or that currently has a valuation allowance.

Effective January 1, 2020, the Company implemented FASB ASU 2016-13, *Financial Instruments-Credit Losses*, which revised the credit loss recognition criteria for certain financial assets measured at amortized cost. The guidance replaced the existing incurred loss recognition model with an expected loss recognition model (“CECL”). The objective of the CECL model is for the reporting entity to recognize its estimate of current expected credit losses for affected financial assets in a valuation allowance deducted from the amortized cost basis of the related financial assets that results in presenting the net carrying value of the financial assets at the amount expected to be collected. For mortgage loan investments the Company is using the Weighted Average Remaining Maturity ("WARM") method, which uses an average annual charge-off rate applied to each mortgage loan risk category. At January 1, 2020, a CECL balance of $1.2 million was recorded for mortgage loans which incorporated the previous year-end balance under the prior accounting method. The adjustment resulted in a charge to retained earnings as a change in accounting, net of tax, of $0.4 million. Subsequent changes in the allowance for current expected credit losses for mortgage loans are reported in net investment income in the Condensed Consolidated Statements of Earnings.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The following table represents the mortgage loan allowance for credit losses.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Balance, beginning of the period | $ 3,238 | 2,227 | 2,486 | 675 |
| Provision January 1, 2020 for adoption of new accounting guidance | — | — | — | 504 |
| Provision during the period | 718 | 130 | 1,470 | 1,178 |
| Total ending allowance for credit losses | $ 3,956 | 2,357 | 3,956 | 2,357 |

The Company's direct investments in real estate are not a significant portion of its total investment portfolio and totaled approximately $28.8 million and $33.8 million at September 30, 2021 and December 31, 2020, respectively. During the first nine months of 2021, Ozark National recorded an impairment of $1.4 million on certain real estate and home office property located in Kansas City, Missouri which was re-classified as "held-for-sale" at its combined asset group's fair value less cost to sell of $12.2 million. In the third quarter of 2021, the home office, parking garage and parking lot all located in Kansas City, Missouri were sold at a net realized loss of $1.4 million. The Company recognized operating income on real estate properties of approximately $2.2 million and $2.2 million for the first nine months of 2021 and 2020, respectively. In the third quarter of 2020, the Company sold a property located in Travis County, Texas for a realized gain of $2.7 million.

## (10) FAIR VALUES OF FINANCIAL INSTRUMENTS

For financial instruments, the FASB provides guidance which defines fair value, establishes a framework for measuring fair value under GAAP, and requires additional disclosures about fair value measurements. In compliance with this GAAP guidance, the Company has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into a three level hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities ("Level 1") and the lowest priority to unobservable inputs ("Level 3"). If the inputs used to measure fair value fall within different levels of the hierarchy, the category level is based on the lowest priority level input that is significant to the fair value measurement of the instrument.

Financial assets and liabilities recorded at fair value on the Condensed Consolidated Balance Sheets are categorized as follows:

**Level 1:** Fair value is based on unadjusted quoted prices in active markets that are accessible to the Company for identical assets or liabilities. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis. These generally provide the most reliable evidence and are used to measure fair value whenever available. The Company's Level 1 assets are equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets.

**Level 2:** Fair value is based upon significant inputs other than quoted prices in active markets included in Level 1, which are either directly or indirectly observable for substantially the full term of the asset or liability through corroboration with observable market data as of the reporting date. Level 2 inputs include quoted market prices in active markets for similar assets and liabilities, quoted market prices in markets that are not active for identical or similar assets or liabilities, model-derived valuations whose inputs are observable or whose significant value drivers are observable and other observable inputs. The Company’s Level 2 assets include fixed maturity debt securities (corporate and private bonds, government or agency securities, asset-backed and mortgage-backed securities). The Company's Level 2 liabilities include the embedded derivative on reinsurance. Valuations are generally obtained from third party pricing services for identical or comparable assets or determined through use of valuation methodologies using observable market inputs.

**Level 3:** Fair value is based on significant unobservable inputs which reflect the entity’s or third party pricing service’s assumptions about the assumptions market participants would use in pricing an asset or liability. The Company’s Level 3 assets are over-the-counter derivative contracts and mortgage loans. The Company’s Level 3 liabilities consist of share-based compensation obligations and certain equity-index product-related embedded derivatives. Valuations are estimated based on non-binding broker prices or internally developed valuation models or methodologies, discounted cash flow models and other similar techniques.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The following tables set forth the Company's assets and liabilities that are measured at fair value on a recurring basis as of the date indicated:

| | September 30, 2021 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Debt securities, available-for-sale | $ 9,364,083 | — | 9,364,083 | — |
| Debt securities, trading | 1,085,654 | — | 1,085,654 | — |
| Equity securities | 21,186 | 21,186 | — | — |
| Mortgage loans | 6,439 | — | — | 6,439 |
| Derivatives, index options | 82,390 | — | — | 82,390 |
| Total assets | $ 10,559,752 | 21,186 | 10,449,737 | 88,829 |
| Policyholder account balances (a) | $ 122,016 | — | — | 122,016 |
| Other liabilities (b) | (68,079) | — | (76,486) | 8,407 |
| Total liabilities | $ 53,937 | — | (76,486) | 130,423 |

During the three and nine months ended September 30, 2021, the Company made no transfers from Level 2 to Level 3 for debt securities available-for-sale.

| | December 31, 2020 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Debt securities, available-for-sale | $ 10,770,923 | — | 10,770,923 | — |
| Equity securities | 17,744 | 17,744 | — | — |
| Derivatives, index options | 132,821 | — | — | 132,821 |
| Total assets | $ 10,921,488 | 17,744 | 10,770,923 | 132,821 |
| Policyholder account balances (a) | $ 161,351 | — | — | 161,351 |
| Other liabilities (c) | 6,202 | — | — | 6,202 |
| Total liabilities | $ 167,553 | — | — | 167,553 |

(a) Represents the fair value of certain product-related embedded derivatives that were recorded at fair value.
(b) Represents the liability for share-based compensation and the embedded derivative for funds withheld.
(c) Represents the liability for share-based compensation.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The following tables present, by pricing source and fair value hierarchy level, the Company's assets that are measured at fair value on a recurring basis:

| | September 30, 2021 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Debt securities, available-for-sale: | | | | |
| Priced by third-party vendors | $ 9,280,647 | — | 9,280,647 | — |
| Priced internally | 83,436 | — | 83,436 | — |
| Subtotal | 9,364,083 | — | 9,364,083 | — |
| Debt securities, trading: | | | | |
| Priced by third-party vendors | 1,085,654 | — | 1,085,654 | — |
| Priced internally | — | — | — | — |
| Subtotal | 1,085,654 | — | 1,085,654 | — |
| Equity securities: | | | | |
| Priced by third-party vendors | 21,186 | 21,186 | — | — |
| Priced internally | — | — | — | — |
| Subtotal | 21,186 | 21,186 | — | — |
| Mortgage loans: | | | | |
| Priced by third-party vendors | — | — | — | — |
| Priced internally | 6,439 | — | — | 6,439 |
| Subtotal | 6,439 | — | — | 6,439 |
| Derivatives, index options: | | | | |
| Priced by third-party vendors | 82,390 | — | — | 82,390 |
| Priced internally | — | — | — | — |
| Subtotal | 82,390 | — | — | 82,390 |
| Total | $ 10,559,752 | 21,186 | 10,449,737 | 88,829 |
| Percent of total | 100.0 % | 0.2 % | 99.0 % | 0.8 % |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | December 31, 2020 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Debt securities, available-for-sale: | | | | |
| Priced by third-party vendors | $ 10,770,923 | — | 10,770,923 | — |
| Priced internally | — | — | — | — |
| Subtotal | 10,770,923 | — | 10,770,923 | — |
| Equity securities: | | | | |
| Priced by third-party vendors | 17,744 | 17,744 | — | — |
| Priced internally | — | — | — | — |
| Subtotal | 17,744 | 17,744 | — | — |
| Derivatives, index options: | | | | |
| Priced by third-party vendors | 132,821 | — | — | 132,821 |
| Priced internally | — | — | — | — |
| Subtotal | 132,821 | — | — | 132,821 |
| Total | $ 10,921,488 | 17,744 | 10,770,923 | 132,821 |
| Percent of total | 100.0 % | 0.2 % | 98.6 % | 1.2 % |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The following tables provide additional information about fair value measurements for Level 3 for which significant unobservable inputs were utilized to determine fair value.

| | For the Three Months Ended September 30, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Assets | | | Liabilities | | |
| | Derivatives, Index Options | Mortgage Loans | Total Assets | Policyholder Account Balances | Stock Options | Total Liabilities |
| | (In thousands) | | | | | |
| Beginning balance, July 1, 2021 | $ 114,840 | 2,729 | 117,569 | 155,265 | 8,144 | 163,409 |
| Total realized and unrealized gains (losses): | | | | | | |
| Included in net earnings | 2,284 | 221 | 2,505 | 1,485 | 270 | 1,755 |
| Included in other comprehensive income | — | — | — | — | — | — |
| Purchases, sales, issuances and settlements, net: | | | | | | |
| Purchases | 12,011 | 3,500 | 15,511 | 12,011 | — | 12,011 |
| Sales | — | — | — | — | — | — |
| Issuances | — | — | — | — | — | — |
| Settlements | (46,745) | (11) | (46,756) | (46,745) | (7) | (46,752) |
| Transfers into (out of) Level 3 | — | — | — | — | — | — |
| Balance at end of period | $ 82,390 | 6,439 | 88,829 | 122,016 | 8,407 | 130,423 |
| Change in unrealized gains or losses for the period included in earnings (or changes in net assets) for assets/ liabilities held at the end of the reporting period: | | | | | | |
| Net investment income | $ (21,202) | 221 | (20,981) | — | — | — |
| Benefits and expenses | — | — | — | (21,202) | 270 | (20,932) |
| Total | $ (21,202) | 221 | (20,981) | (21,202) | 270 | (20,932) |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | For the Three Months Ended September 30, 2020 | | | | | |
|---|---|---|---|---|---|---|
| | Assets | | Liabilities | | | |
| | Derivatives, Index Options | Total Assets | Policyholder Account Balances | Stock Options | Contingent Consideration | Total Liabilities |
| | (In thousands) | | | | | |
| Beginning balance, July 1, 2020 | $ 66,738 | 66,738 | 87,573 | 5,497 | — | 93,070 |
| Total realized and unrealized gains (losses): | | | | | | |
| Included in net earnings | 31,520 | 31,520 | 34,119 | (546) | — | 33,573 |
| Included in other comprehensive income | — | — | — | — | — | — |
| Purchases, sales, issuances and settlements, net: | | | | | | |
| Purchases | 11,426 | 11,426 | 11,427 | — | — | 11,427 |
| Sales | — | — | — | — | — | — |
| Issuances | — | — | — | — | — | — |
| Settlements | (16,317) | (16,317) | (16,317) | — | — | (16,317) |
| Transfers into (out of) Level 3 | — | — | — | — | — | — |
| Balance at end of period | $ 93,367 | 93,367 | 116,802 | 4,951 | — | 121,753 |
| Change in unrealized gains or losses for the period included in earnings (or changes in net assets) for assets/liabilities held at the end of the reporting period: | | | | | | |
| Net investment income | $ 50,636 | 50,636 | — | — | — | — |
| Benefits and expenses | — | — | 50,636 | (546) | — | 50,090 |
| Total | $ 50,636 | 50,636 | 50,636 | (546) | — | 50,090 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | For the Nine Months Ended September 30, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Assets | | | Other Liabilities | | |
| | Derivatives, Index Options | Mortgage Loans | Total Assets | Policyholder Account Balances | Stock Options | Total Other Liabilities |
| | (In thousands) | | | | | |
| Beginning balance, January 1, 2021 | $ 132,821 | — | 132,821 | 161,351 | 6,202 | 167,553 |
| Total realized and unrealized gains (losses): | | | | | | |
| Included in net earnings | 70,474 | 256 | 70,730 | 81,570 | 4,187 | 85,757 |
| Included in other comprehensive income | — | — | — | — | — | — |
| Purchases, sales, issuances and settlements, net: | | | | | | |
| Purchases | 34,194 | 6,198 | 40,392 | 34,194 | — | 34,194 |
| Sales | — | — | — | — | — | — |
| Issuances | — | — | — | — | — | — |
| Settlements | (155,099) | (15) | (155,114) | (155,099) | (1,982) | (157,081) |
| Transfers into (out of) Level 3 | — | — | — | — | — | — |
| Balance at end of period | $ 82,390 | 6,439 | 88,829 | 122,016 | 8,407 | 130,423 |
| Change in unrealized gains or losses for the period included in earnings (or changes in net assets) for assets/liabilities held at the end of the reporting period: | | | | | | |
| Net investment income | $ 30,159 | 256 | 30,415 | — | — | — |
| Benefits and expenses | — | — | — | 30,159 | 4,187 | 34,346 |
| Total | $ 30,159 | $ 256 | 30,415 | 30,159 | 4,187 | 34,346 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | For the Nine Months Ended September 30, 2020 | | | | | |
|---|---|---|---|---|---|---|
| | Assets | | Other Liabilities | | | |
| | Derivatives, Index Options | Total Assets | Policyholder Account Balances | Stock Options | Contingent Consideration | Total Other Liabilities |
| | (In thousands) | | | | | |
| Beginning balance, January 1, 2020 | $ 157,588 | 157,588 | 155,902 | 11,225 | 4,076 | 171,203 |
| Total realized and unrealized gains (losses): | | | | | | |
| Included in net earnings | (34,865) | (34,865) | (9,744) | (4,395) | (4,076) | (18,215) |
| Included in other comprehensive income | — | — | — | — | — | — |
| Purchases, sales, issuances and settlements, net: | | | | | | |
| Purchases | 50,287 | 50,287 | 50,287 | — | — | 50,287 |
| Sales | — | — | — | — | — | — |
| Issuances | — | — | — | — | — | — |
| Settlements | (79,643) | (79,643) | (79,643) | (1,879) | — | (81,522) |
| Transfers into (out of) Level 3 | — | — | — | — | — | — |
| Balance at end of period | $ 93,367 | 93,367 | 116,802 | 4,951 | — | 121,753 |
| Change in unrealized gains or losses for the period included in earnings (or changes in net assets) for assets/liabilities held at the end of the reporting period: | | | | | | |
| Net investment income | $ 6,966 | 6,966 | — | — | — | — |
| Benefits and expenses | — | — | 6,966 | (4,395) | (4,076) | (1,505) |
| Total | $ 6,966 | 6,966 | 6,966 | (4,395) | (4,076) | (1,505) |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The following table presents the valuation method for financial assets and liabilities categorized as level 3, as well as the unobservable inputs used in the valuation of those financial instruments:

| | September 30, 2021 | | | |
|---|---|---|---|---|
| | Fair Value | Valuation Technique | Unobservable Input | Range (Weighted Average) |
| | (In thousands) | | | |
| Assets: | | | | |
| Derivatives, index options | $ 82,390 | Broker prices | Implied volatility | 11.76% - 17.97% (15.50%) |
| Mortgage loans | 6,439 | Discounted cash flow | Spread | 148 - 248 bps |
| Total assets | $ 88,829 | | | |
| Liabilities: | | | | |
| Policyholder account balances | $ 122,016 | Deterministic cash flow model | Projected option cost | 0.01% - 14.84% (2.14%) |
| Share-based compensation | 8,407 | Black-Scholes model | Expected term | 0.2 to 9.2 years |
| | | | Expected volatility | 34.90% |
| Total liabilities | $ 130,423 | | | |

| | December 31, 2020 | | | |
|---|---|---|---|---|
| | Fair Value | Valuation Technique | Unobservable Input | Range (Weighted Average) |
| | (In thousands) | | | |
| Assets: | | | | |
| Derivatives, index options | $ 132,821 | Broker prices | Implied volatility | 12.96% - 53.69% (20.70%) |
| Total assets | $ 132,821 | | | |
| Liabilities: | | | | |
| Policyholder account balances | $ 161,351 | Deterministic cash flow model | Projected option cost | 0.0% - 45.04% (3.27%) |
| Share-based compensation | 6,202 | Black-Scholes model | Expected term | 1.0 to 9.9 years |
| | | | Expected volatility | 33.47% |
| Total liabilities | $ 167,553 | | | |

Realized gains (losses) on debt securities are reported in the Condensed Consolidated Statements of Earnings as net investment gains (losses) with liabilities reported as expenses. Unrealized gains (losses) on available-for-sale debt securities are reported as Other comprehensive income (loss) within the stockholders' equity section of the Condensed Consolidated Balance Sheets.

**NATIONAL WESTERN LIFE GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)**

The fair value hierarchy classifications are reviewed each reporting period. Reclassification of certain financial assets and liabilities may result based on changes in the observability of valuation attributes. Reclassifications are reported as transfers into and out of Level 3 at the beginning fair value for the reporting period in which the changes occur.

The carrying amounts and fair values of the Company's financial instruments are as follows:

| | September 30, 2021 | | | | |
|---|---|---|---|---|---|
| | | | Fair Value Hierarchy Level | | |
| | Carrying Values | Fair Values | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | | |
| ASSETS | | | | | |
| Debt securities, available-for-sale | $ 9,364,083 | 9,364,083 | — | 9,364,083 | — |
| Debt securities, trading | 1,085,654 | 1,085,654 | — | 1,085,654 | — |
| Cash and cash equivalents | 540,226 | 540,226 | 540,226 | — | — |
| Mortgage loans | 462,882 | 476,712 | — | — | 476,712 |
| Real estate | 28,750 | 47,027 | — | — | 47,027 |
| Policy loans | 71,668 | 110,951 | — | — | 110,951 |
| Other loans | 25,136 | 25,461 | — | — | 25,461 |
| Derivatives, index options | 82,390 | 82,390 | — | — | 82,390 |
| Equity securities | 21,186 | 21,186 | 21,186 | — | — |
| Life interest in Libbie Shearn Moody Trust | 9,083 | 12,775 | — | — | 12,775 |
| Other investments | 4,513 | 24,852 | — | — | 24,852 |
| | | | | | |
| LIABILITIES | | | | | |
| Deferred annuity contracts | $ 6,519,899 | 5,193,022 | — | — | 5,193,022 |
| Immediate annuity and supplemental contracts | 422,051 | 458,609 | — | — | 458,609 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

| | December 31, 2020 | | | | |
|---|---|---|---|---|---|
| | | | Fair Value Hierarchy Level | | |
| | Carrying Values | Fair Values | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | | |
| ASSETS | | | | | |
| Debt securities, available-for-sale | $ 10,770,923 | 10,770,923 | — | 10,770,923 | — |
| Cash and cash equivalents | 581,059 | 581,059 | 581,059 | — | — |
| Mortgage loans | 332,521 | 348,175 | — | — | 348,175 |
| Real estate | 33,783 | 48,577 | — | — | 48,577 |
| Policy loans | 74,083 | 121,260 | — | — | 121,260 |
| Other loans | 23,396 | 23,691 | — | — | 23,691 |
| Derivatives, index options | 132,821 | 132,821 | — | — | 132,821 |
| Equity securities | 17,744 | 17,744 | 17,744 | — | — |
| Life interest in Libbie Shearn Moody Trust | 9,083 | 12,775 | — | — | 12,775 |
| Other investments | 4,513 | 22,580 | — | — | 22,580 |
| | | | | | |
| LIABILITIES | | | | | |
| Deferred annuity contracts | $ 6,662,730 | 5,192,663 | — | — | 5,192,663 |
| Immediate annuity and supplemental contracts | 412,526 | 467,538 | — | — | 467,538 |

Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instruments. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

## (11) DERIVATIVES

Fixed-index products provide traditional fixed annuities and universal life contracts with the option to have credited interest rates linked in part to an underlying equity index or a combination of equity indices. The equity return component of such policy contracts is identified separately and accounted for in future policy benefits as embedded derivatives on the Condensed Consolidated Balance Sheets. The remaining portions of these policy contracts are considered the host contracts and are recorded separately as fixed annuity or universal life contracts. The host contracts are accounted for under debt instrument type accounting in which future policy benefits are recorded as discounted debt instruments and accreted, using the effective yield method, to their minimum account values at their projected maturities or termination dates.

The Company purchases over-the-counter index options, which are derivative financial instruments, to hedge the equity return component of its fixed-index annuity and life products. The index options act as hedges to match closely the returns on the underlying index or indices. The amounts which may be credited to policyholders are linked, in part, to the returns of the underlying index or indices. As a result, changes to policyholders' liabilities are substantially offset by changes in the value of the options. Cash is exchanged upon purchase of the index options and no principal or interest payments are made by either party during the option periods. Upon maturity or expiration of the options, cash may be paid to the Company depending on the performance of the underlying index or indices and terms of the contract.

The Company does not elect hedge accounting relative to these derivative instruments. The index options are reported at fair value in the accompanying Condensed Consolidated Financial Statements. The changes in the values of the index options and the changes in the policyholder liabilities are both reflected in the Condensed Consolidated Statements of Earnings. Any changes relative to the embedded derivatives associated with policy contracts are reflected in contract interest in the Condensed Consolidated Statements of Earnings. Any gains or losses from the sale or expiration of the options, as well as period-to-period changes in values, are reflected as net investment income in the Condensed Consolidated Statements of Earnings.

Although there is credit risk in the event of nonperformance by counterparties to the index options, the Company does not expect any of its counterparties to fail to meet their obligations, given their high credit ratings. In addition, credit support agreements are in place with all counterparties for option holdings in excess of specific limits, which may further reduce the Company's credit exposure.

Effective December 31, 2020, the Company entered into a coinsurance funds withheld reinsurance agreement under which identified assets are maintained in a funds withheld account but the associated interest and credit risk of these assets has been transferred to the reinsurer, representing a total return swap with a floating rate leg. Accordingly, the Company bifurcates the embedded derivative for reinsurance from the host contract in accordance with GAAP. The fair value of the embedded derivative funds withheld liability is computed as the unrealized gain (loss) on the underlying funds withheld assets and is included in the funds withheld liability on the Condensed Consolidated Balance Sheets, with the change reported in net investment income in the Condensed Consolidated Statements of Earnings. Changes in the funds withheld liability are reported in operating activities in the Condensed Consolidated Statements of Cash Flows.

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The tables below present the fair value of derivative instruments as of September 30, 2021 and December 31, 2020, respectively.

| | September 30, 2021 | | | |
|---|---|---|---|---|
| | Asset Derivatives | | Liability Derivatives | |
| | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| | | (In thousands) | | (In thousands) |
| Derivatives not designated as hedging instruments | | | | |
| Equity index options | Derivatives, Index Options | $ 82,390 | | |
| Fixed-index products | | | Universal Life and Annuity Contracts | $ 122,016 |
| Embedded derivative on reinsurance contract | | | Funds Withheld Liability | (76,486) |
| Total | | $ 82,390 | | $ 45,530 |

| | December 31, 2020 | | | |
|---|---|---|---|---|
| | Asset Derivatives | | Liability Derivatives | |
| | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| | | (In thousands) | | (In thousands) |
| Derivatives not designated as hedging instruments | | | | |
| Equity index options | Derivatives, Index Options | $ 132,821 | | |
| Fixed-index products | | | Universal Life and Annuity Contracts | $ 161,351 |
| Total | | $ 132,821 | | $ 161,351 |

**NATIONAL WESTERN LIFE GROUP, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

The table below presents the effect of derivative instruments in the Condensed Consolidated Statements of Earnings for the three months ended September 30, 2021 and 2020.

| Derivatives Not Designated As Hedging Instruments | Location of Gain or (Loss) Recognized In Income on Derivatives | September 30, 2021 | September 30, 2020 |
|---|---|---|---|
| | | Amount of Gain or (Loss) Recognized in Income on Derivatives | |
| | | (In thousands) | |
| Equity index options | Net investment income | $ 2,284 | 31,520 |
| Fixed-index products | Universal life and annuity contract interest | (1,484) | (34,119) |
| Embedded derivative on reinsurance contract | Net investment income | 4,147 | — |
| | | $ 4,947 | (2,599) |

The table below presents the effect of derivative instruments in the Condensed Consolidated Statements of Earnings for the nine months ended September 30, 2021 and 2020.

| Derivatives Not Designated As Hedging Instruments | Location of Gain or (Loss) Recognized In Income on Derivatives | September 30, 2021 | September 30, 2020 |
|---|---|---|---|
| | | Amount of Gain or (Loss) Recognized in Income on Derivatives | |
| | | (In thousands) | |
| Equity index options | Net investment income | $ 70,474 | (34,865) |
| Fixed-index products | Universal life and annuity contract interest | (81,570) | 9,744 |
| Embedded derivative on reinsurance contract | Net investment income | 76,486 | — |
| | | $ 65,390 | (25,121) |

The embedded derivative liability on fixed-index products, the change of which is recorded in universal life and annuity contract interest in the Condensed Consolidated Statements of Earnings, includes projected interest credits that are offset by the expected collectability by the Company of asset management fees on fixed-index products. The anticipated asset management fees to be collected increases or decreases based upon the most recent performance of index options and adds to or reduces the offset applied to the embedded derivative liability (increasing or decreasing contract interest expense). For the three months ended September 30, 2021 and 2020, the change in the embedded derivative liability due to the expected collectability of asset management fees increased/(decreased) contract interest expense by $0.0 million and $3.7 million, respectively. For the nine months ended September 30, 2021 and 2020, contract interest expense was increased/(decreased) by $6.5 million and $29.3 million, respectively, for the expected collectability of asset management fees.

Beginning in the second quarter of 2020, the Company changed its budget for purchasing these options to match the collection of asset management fees with the payoff from out-of-the-money options, thereby removing the option premium that was previously being paid for the probability or expectation of collecting asset management fees ("out-of-the-money" hedging). Consequently, the remaining one year options purchased under the prior method expired and have been replaced by out-of-the-money hedges as of June 30, 2021. Accordingly, the embedded derivative liability component due to the projected collectability of asset management fees no longer exists as of the third quarter of 2021 and for all subsequent reporting periods.

## (12) INTANGIBLES, VALUE OF BUSINESS ACQUIRED, AND GOODWILL

*Identifiable Intangible Assets*

The gross carrying amounts and accumulated amortization for intangible assets are as follows for the dates shown.

| | | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|---|
| | Weighted-Average Amortization Period | Gross Carrying Amount | Accumulated Amortization | Gross Carrying Amount | Accumulated Amortization |
| | | (In thousands) | | | |
| Trademarks/trade names | 15 | $ 2,800 | (497) | 2,800 | (358) |
| Internally developed software | 7 | 3,800 | (1,448) | 3,800 | (1,040) |
| Insurance licenses | N/A | 3,000 | — | 3,000 | — |
| | | $ 9,600 | (1,945) | 9,600 | (1,398) |

The value of trademarks was estimated using the relief from royalty method, based on the assumption that in lieu of ownership, an organization would be willing to pay a royalty in order to receive the related benefits of using the brand. The value of insurance licenses was estimated using the market approach to value, based on values paid for licenses in recent shell company transactions. The value of internally developed software was estimated using the replacement cost method. Trademarks, trade names and internally developed software are amortized using a straight-line method over the estimated useful lives. These intangible assets will be evaluated for impairment if indicators of impairment arise. Insurance licenses were determined to have an indefinite useful life. The Company evaluates the useful life of insurance licenses at each reporting period to determine whether the useful life remains indefinite.

As of September 30, 2021, expected amortization expense relating to purchased intangible assets for each of the next 5 years and thereafter is as follows:

| | Expected Amortization |
|---|---|
| | (In thousands) |
| Remainder of 2021 | $ 182 |
| 2022 | 730 |
| 2023 | 730 |
| 2024 | 730 |
| 2025 | 730 |
| Thereafter | 1,553 |

Table of Contents



*Value of Business Acquired ("VOBA")*

VOBA is a purchase accounting convention for life insurance companies in business combinations based upon an actuarial determination of the difference between the fair value of policyholder liabilities acquired and the same policyholder liabilities measured in accordance with the acquiring company's accounting policies. The difference, referred to as VOBA, is an intangible asset subject to periodic amortization. Changes in VOBA were as follows for the periods shown:

| | September 30, 2021 | December 31, 2020 |
|---|---|---|
| | (In thousands) | |
| Balance, beginning of year | $ 162,968 | 138,071 |
| Other increase | — | 35,125 |
| Amortization: | | |
| Amortization, excluding unlocking | (6,709) | (10,228) |
| | | |
| Balance as of end of period | $ 156,259 | 162,968 |

Estimated future amortization of VOBA, net of interest (in thousands), as of September 30, 2021, is as follows:

| | Expected Amortization |
|---|---|
| | (In thousands) |
| Remainder of 2021 | $ 2,557 |
| 2022 | 9,753 |
| 2023 | 9,368 |
| 2024 | 9,015 |
| 2025 | 8,804 |

*Goodwill*

The changes in the carrying amount of goodwill (in thousands) were as follows:

| | September 30, 2021 | December 31, 2020 |
|---|---|---|
| | (In thousands) | |
| Gross goodwill as of beginning of year | $ 13,864 | 13,864 |
| Goodwill resulting from business acquisition | — | — |
| Gross goodwill, before impairments | 13,864 | 13,864 |
| Accumulated impairment as of beginning of year | — | — |
| Current year impairments | — | — |
| Net goodwill as of end of period | $ 13,864 | 13,864 |

Goodwill is evaluated for impairment annually, or more frequently if indicators of impairment arise.

## (13) SUBSEQUENT EVENTS

Subsequent events have been evaluated through the date of filing and no reportable items were identified.

# ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## FORWARD-LOOKING STATEMENTS

The Private Securities Litigation Reform Act of 1995 provides a “safe harbor” for forward-looking statements. Certain information contained herein or in other written or oral statements made by or on behalf of National Western Life Group, Inc. and its subsidiaries (the "Company") are or may be viewed as forward-looking. Although the Company has taken appropriate care in developing any such information, forward-looking information involves risks and uncertainties that could significantly impact actual results. These risks and uncertainties include, but are not limited to, matters described in the Company's Securities and Exchange Commission (SEC) filings such as exposure to market risks, anticipated cash flows or operating performance, future capital needs, and statutory or regulatory related issues. However, as a matter of policy, the Company does not make any specific projections as to future earnings, nor does it endorse any projections regarding future performance that may be made by others. Whether or not actual results differ materially from forward-looking statements may depend on numerous foreseeable and unforeseeable events or developments. Also, the Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future developments, or otherwise.

Management's discussion and analysis of the financial condition and results of operations (“MD&A”) of National Western Life Group, Inc. ("NWLGI") for the three and nine months ended September 30, 2021 follows. Where appropriate, discussion specific to the insurance operations of National Western Life Insurance Company is denoted by "National Western" or "NWLIC". This discussion should be read in conjunction with the Company's Condensed Consolidated Financial Statements and related notes beginning on page 3 of this report and with the 2020 Annual Report filed on Form 10-K with the SEC.

## Overview

National Western provides life insurance products for the savings and protection needs of policyholders and annuity contracts for the asset accumulation and retirement needs of contract holders. The Company accepts funds from policyholders or contract holders and establishes a liability representing future obligations to pay the policy or contract holders and their beneficiaries. To ensure the Company will be able to pay these future commitments, the funds received as premium payments and deposits are invested in high quality investments, primarily fixed income securities. National Western maintains its home office in Austin, Texas where substantially all of its 269 employees at September 30, 2021 are located.

Due to the business of accepting funds to pay future obligations in later years and the underlying economics, the relevant factors affecting the Company’s overall business and profitability include the following:

- the level of sales and premium revenues collected
- the volume of life insurance and annuity business in force
- persistency of policies and contracts
- the ability to price products to earn acceptable margins over benefit costs and expenses
- return on investments sufficient to produce acceptable spread margins over interest crediting rates
- investment credit quality which minimizes the risk of default or impairment
- levels of policy benefits and costs to acquire business
- the ability to manage the level of operating expenses
- effect of interest rate changes on revenues and investments including asset and liability matching
- maintaining adequate levels of capital and surplus
- corporate tax rates and the treatment of financial statement items under tax rules and accounting
- actual levels of surrenders, withdrawals, claims and interest spreads
- changes in assumptions for amortization of deferred policy acquisition expenses and deferred sales inducements
- changes in the fair value of derivative index options and embedded derivatives pertaining to fixed-index life and annuity products
- pricing and availability of adequate counterparties for reinsurance and index option contracts
- litigation subject to unfavorable judicial development, including the time and expense of litigation

The Company monitors these factors continually as key business indicators. The discussion that follows in this Item 2 includes these indicators and presents information useful to an overall understanding of the Company's business performance for the three and nine months ended September 30, 2021, incorporating required disclosures in accordance with the rules and regulations of the SEC.

**Insurance Operations - Domestic**

National Western is currently licensed to do business in all states, except New York, and the District of Columbia. Products marketed are annuities, universal life insurance, fixed-index universal life, and traditional life insurance, which include both term and whole life products. Domestic sales in terms of premium levels have historically been more heavily weighted toward annuities. Most of these annuities can be sold either as tax qualified or non-qualified products. More recently, a greater proportion of sales activity has been derived from single premium life insurance products, predominantly those with an equity-index crediting mechanism. Presently, nearly all of National Western's domestic life premium sales come from single premium life products. At September 30, 2021, National Western maintained approximately 107,710 annuity contracts in force and 46,260 domestic life insurance policies in force representing $3.6 billion in face amount of coverage.

National Western markets and distributes its domestic products primarily through independent national marketing organizations ("NMOs"). These NMOs assist the Company in recruiting, contracting, and managing independent agents. National Western's agents are independent contractors who are compensated on a commission basis. It currently has approximately 29,900 domestic independent agent contracts.

Effective January 31, 2019, the Company completed its previously announced acquisition of Ozark National Life Insurance Company ("Ozark National") and N.I.S. Financial Services, Inc. ("NIS"). All of the outstanding stock of Ozark National is owned by National Western while NIS is wholly owned by NWLGI. Although reported separately for segment disclosure purposes, domestic insurance operations include the activities of Ozark National. Ozark National is a Missouri domiciled, stock life insurance company currently licensed to conduct business in thirty states. Organized and incorporated in 1964, its largest markets by state are Missouri, Iowa, Minnesota, Nebraska, and Kansas. Ozark National utilizes a unique distribution system to market its flagship Balanced Program which consists of a coordinated sale of a non-participating whole life insurance product with a mutual fund investment product offered through NIS, its affiliated broker-dealer. Due to Ozark National's coordinated sale, their agents hold a securities license in addition to an insurance license. At September 30, 2021, Ozark National maintained approximately 176,220 life insurance policies in force representing $5.9 billion in face amount of coverage. It maintains its home office facility in Kansas City, Missouri along with NIS where most of their combined employees are located.

**Insurance Operations - International**

National Western's international operations consists of a closed block of in force policies. The Company had progressively discontinued accepting applications from various countries ultimately ceasing applications for new policies from all remaining countries in 2018. At September 30, 2021, National Western had approximately 42,190 international life insurance policies in force representing nearly $11.6 billion in face amount of coverage. The Company did not conduct business or maintain offices or employees in any other country, but historically did accept applications at its home office in Austin, Texas, and issued policies from there to foreign nationals in upper socioeconomic classes of other countries. Insurance products, issued primarily to residents of countries in South America, consisted almost entirely of universal life and traditional life insurance products not available in the local markets.

Issuing universal life and traditional life insurance policies to residents of countries in different regions provided diversification that helped to minimize large fluctuations that could arise due to various economic, political, and competitive pressures occurring from one country to another. These policies also provided diversification of earnings relative to the Company's domestic life insurance segment. Although there were some inherent risks of accepting international applications not present within the domestic market, they were reduced substantially by the Company in several ways. Most notably National Western's customer profile consisted of foreign nationals of other countries in upper socioeconomic classes who had substantial financial resources. This, coupled with National Western's conservative underwriting practices, has historically resulted in claims experience, due to natural causes, similar to that in the United States. Foreign currency risks were minimized by requiring payment of premiums and claims in United States dollars. In addition, the Company adopted an extensive anti-money laundering compliance program in order to fully comply with all applicable U.S. monitoring and reporting requirements pertaining to money laundering and other illegal activities. All of the above served to minimize risks.

**SALES**

**Life Insurance**

The following table sets forth information regarding life insurance sales activity as measured by total premium for single premium life insurance products and annualized first year premiums for all other universal life and traditional life insurance products. While the figures shown below are in accordance with industry practice and represent the amount of new business sold during the periods indicated, they are considered a non-GAAP financial measure. The Company believes sales are a measure of distribution productivity and are an indicator of future revenue trends. However, revenues are driven by sales in prior periods as well as in the current period and therefore, a reconciliation of sales to revenues is not meaningful or determinable.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Single premium life | $ 52,578 | 56,610 | 157,024 | 141,557 |
| Traditional life | 922 | 798 | 2,855 | 2,139 |
| Universal life | — | — | — | 6 |
| Totals | $ 53,500 | 57,408 | 159,879 | 143,702 |

Life insurance sales, as measured by total and annualized first year premiums, decreased (7)% in the third quarter of 2021 as compared to the third quarter of 2020 reflecting a pullback in consumer spending in the current period. Sales for the three months ended September 30, 2021, included $0.9 million from Ozark National, exceeding the $0.8 million reported in the third quarter of 2020, representing their traditional life sales activity. Ozark National's business model, which is heavily dependent upon in person contact for agent recruiting and obtaining applications for coverage from prospective policyholders, has been steadily recovering from the disruption of the pandemic effects upon its business. For the nine months ended September 30, 2021, total life insurance sales increased 11% from the level in 2020. Included in these nine-month amounts were $2.9 million and $2.1 million in sales from Ozark National for 2021 and 2020, respectively.

National Western's life insurance product portfolio includes single premium universal life ("SPUL") and equity-index universal life ("EIUL") products as well as hybrids of the EIUL and SPUL products, combining features of these core products. Equity-index universal life products have been the predominant product sold in the domestic life market for a number of years. Most of these sales are single premium mode products (one year, five year, or ten year) designed for transferring accumulated wealth tax efficiently into life insurance policies with limited underwriting due to lesser net insurance amounts at risk (face amount of the insurance policy less cash premium contributed). These products were designed and implemented years ago targeting the accumulated savings of the segment of the population entering their retirement years. The wealth transfer life products have been valuable offerings for the Company's distributors as evidenced by their comprising over 98% of total life sales in the first nine months of 2021.

The average new policy face amounts, excluding insurance riders, since 2017 are as shown in the following table.

| | Average New Policy Face Amount | | |
|---|---|---|---|
| | NWLIC Domestic | Ozark National | NWLIC International |
| Year ended December 31, 2017 | 148,100 | — | 299,300 |
| Year ended December 31, 2018 | 162,600 | — | 290,900 |
| Year ended December 31, 2019 | 179,900 | 45,200 | — |
| Year ended December 31, 2020 | 209,900 | 46,230 | — |
| Nine Months Ended September 30, 2021 | 191,100 | 47,620 | — |

Contracts issued to international residents historically had larger face amounts of life insurance coverage per policy compared to those issued to domestic policyholders as National Western's efforts were directed toward accepting applications from upper socioeconomic residents of international countries. The average face amount of insurance coverage per policy for domestic life insurance contracts reflects the sales of single premium life products, primarily fixed-index, as part of its wealth transfer strategy for domestic life sales.

The table below sets forth information regarding life insurance in force for each date presented.

| | Insurance In Force as of | |
|---|---|---|
| | September 30, 2021 | December 31, 2020 |
| | ($ in thousands) | |
| National Western | | |
| Universal life: | | |
| Number of policies | 29,200 | 31,150 |
| Face amounts | $ 4,048,080 | 4,354,530 |
| | | |
| Traditional life: | | |
| Number of policies | 24,890 | 26,260 |
| Face amounts | $ 2,295,840 | 2,409,110 |
| | | |
| Fixed-index life: | | |
| Number of policies | 34,360 | 35,060 |
| Face amounts | $ 8,838,800 | 9,157,010 |
| | | |
| Total life insurance: | | |
| Number of policies | $ 88,450 | 92,470 |
| Face amounts | $ 15,182,720 | 15,920,650 |
| | | |
| Ozark National | | |
| Total life insurance (all traditional): | | |
| Number of policies | 176,220 | 179,000 |
| Face amounts | $ 5,918,770 | 6,033,510 |

At September 30, 2021, National Western’s face amount of life insurance in force was comprised of $11.6 billion from the international line of business and $3.6 billion from the domestic line of business. At December 31, 2020, these amounts were $12.4 billion and $3.5 billion for the international and domestic lines of business, respectively.

**Annuities**

The following table sets forth information regarding the Company's annuity sales activity as measured by single and annualized first year premiums. Similar to life insurance sales, these figures are considered a non-GAAP financial measure but are shown in accordance with industry practice and depict the Company's sales productivity.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Fixed-index annuities | $ 102,322 | 76,255 | 333,146 | 221,992 |
| Other deferred annuities | 1,008 | 1,875 | 2,965 | 5,475 |
| Immediate annuities | 5,380 | 2,270 | 19,460 | 10,991 |
| Totals | $ 108,710 | 80,400 | 355,571 | 238,458 |

Annuity sales increased 35% in the third quarter of 2021 compared to 2020 and were 49% higher in the nine months ended September 30, 2021 relative to the comparable period in 2020. Sales activity in 2020 was dampened by the onset of the COVID-19 pandemic at that time, while 2021 sales activity reflects expansion of sales and marketing initiatives in this line of business as well as an overall increase in market demand.

The Company's mix of annuity sales has historically shifted with interest rate levels and the relative performance of the equity market. With the decline in interest rates subsequent to the subprime crisis, fixed-index products have comprised the majority of annuity sales, generally accounting for 90% or more of all annuity sales over this span. During the first nine months of 2021, this percentage approximated 94% reflecting both the historically low levels in interest rates and the overall continuing upward trend in equities. For all fixed-index products, the Company purchases over the counter call options to hedge the equity return feature. The options are purchased relative to the issuance of the annuity contracts in such a manner to minimize timing risk. Generally, the index return during the indexing period (if the underlying index increases) becomes a component in a formula (set forth in the annuity), the result of which is credited as interest to contract holders electing the index formula crediting method at the beginning of the indexing period. The formula result can never be less than zero with these products. The Company does not deliberately mismatch or under hedge for the equity feature of the products. Fixed-index products also provide the contract holder the alternative to elect a fixed interest rate crediting option.

While National Western does not subsidize its interest crediting rates on new policies in order to obtain market share, similar to some other annuity product providers, the Company has faced a scenario of declining yields on its investment portfolio as securities backing annuity policies and their credited rates were subsequently reinvested at substantially lower yields in depressed interest rate environments. The compression on interest rate margins resulted in decrements to fixed interest rate renewal rates provided to annuity contractholders often to the minimum interest rate guarantee levels prescribed by state insurance regulators under non-forfeiture laws.

As a result of the foregoing, the Company entered into a coinsurance funds withheld reinsurance arrangement at December 31, 2020 under which 100% of the policyholder obligations associated with its fixed rate and payout annuity block of policies at that time were reinsured with a third party. With the transfer of the risk of these policies experiencing compression on interest rate margins, the Company has redirected its attention on rebuilding sales momentum in its annuity sales by developing products targeting new channels of distribution to supplement its current partnerships with national marketing organizations and focusing its offerings away from fixed interest rate products.

The following table sets forth information regarding annuities in force for each date presented. These amounts include the policies and reserves associated with the funds withheld reinsurance transaction discussed above.

| | Annuities In Force as of | |
|---|---|---|
| | September 30, 2021 | December 31, 2020 |
| | ($ in thousands) | |
| Fixed-index annuities | | |
| Number of policies | 65,680 | 68,020 |
| GAAP annuity reserves | $ 5,184,069 | 5,254,089 |
| | | |
| Other deferred annuities | | |
| Number of policies | 30,850 | 33,250 |
| GAAP annuity reserves | $ 1,152,083 | 1,264,042 |
| | | |
| Immediate annuities | | |
| Number of policies | 11,180 | 11,650 |
| GAAP annuity reserves | $ 372,837 | 363,983 |
| | | |
| Total annuities | | |
| Number of policies | $ 107,710 | 112,920 |
| GAAP annuity reserves | $ 6,708,989 | 6,882,114 |

**Impact of Recent Business Environment**

The Company's business is generally aided by an economic environment experiencing growth, whether moderate or vibrant, characterized by improving employment data and increases in personal income. Important metrics indicating sustained economic growth over the longer term principally revolve around employment and confidence, both consumer and business sentiment.

While the morbidity exposure of COVID-19 to the life insurance industry is uncertain at this point, it is not expected to result in significant excess mortality claims. During the first nine months of 2021, the Company (National Western and Ozark National) incurred approximately $26.4 million in net death claims, after reinsurance, for which COVID-19 was identified as the cause of death. Additional risk to life insurance companies has been the decline in value of invested assets due to downgrades in credit market securities, derivative investments experiencing fair value declines resulting in unrealized losses, impairment-related losses or sizable additions being made to the allowance for current credit expected losses in financial statements. Consequently, there have been instances of balance sheet asset deterioration, charges to capital, and lower reported earnings.

In recent years, in the attempt to acquire additional investment yield in the low rate environment, life insurers substantially increased allocations to BBB- rated bonds. In a recession, many of these investment grade corporate credits are at risk for downgrades, as well as the potential to default. Risk-based capital (RBC) formulas assess higher required capital charges as investment quality declines. A meaningful shift of BBB- rated debt securities to non-investment grade categories could have significant implications in terms of required capital levels which would depress RBC ratios of impacted insurers. Life insurance companies also have a large exposure to real estate in its investment portfolios through commercial mortgage, direct real estate investment, and mortgage-backed securities. These investments are highly dependent upon occupancy and payment of rent and lease obligations.

With regard to the credit market, although not probable in the current environment, industry analysts and observers generally agree that a sudden jump in interest rate levels would be harmful to life insurers with interest-sensitive products as it could provide an impetus for abnormal levels of product surrenders and withdrawals at the same time fixed debt securities held by insurers declined in market value. Ultimately, a mix of monetary policy adjustments, fiscal policy, and economic fundamentals will determine the future direction of interest rate movements and the speed of such shifts. It is uncertain at what pace interest rate movements may occur in the future and what impact, if any, such movements would have on the Company's business, results of operations, cash flows, or financial condition.

In an environment such as this, the need for a strong capital position that can cushion against unexpected bumps is critical for stability and ongoing business activity. The Company's operating strategy continues to be focused on maintaining capital levels substantially above regulatory and rating agency requirements. In addition, its business model is predicated upon steady growth in invested assets while managing the block of business within profitability objectives. A key premise of the Company's financial management is maintaining a high quality investment portfolio, well matched in terms of duration with policyholder obligations, that continues to outperform the industry with respect to adverse impairment experience. This discipline enables the Company to sustain resources more than adequate to fund future growth and absorb abnormal periods of cash outflows.

## RESULTS OF OPERATIONS

The Company's Condensed Consolidated Financial Statements are prepared in accordance with U.S. generally accepted accounting principles (“GAAP”). In addition, the Company regularly evaluates operating performance using non-GAAP financial measures which exclude or segregate derivative and realized investment gains and losses from operating revenues. Similar measures are commonly used in the insurance industry in order to assess profitability and results from ongoing operations. The Company believes that the presentation of these non-GAAP financial measures enhances the understanding of the Company's results of operations by highlighting the results from ongoing operations and the underlying profitability factors of the Company's business. The Company excludes or segregates derivative and realized investment gains and losses because such items are often the result of events which may or may not be at the Company's discretion and the fluctuating effects of these items could distort trends in the underlying profitability of the Company's business. Therefore, in the following sections discussing condensed consolidated operations and segment operations, appropriate reconciliations have been included to report information management considers useful in enhancing an understanding of the Company's operations to reportable GAAP balances reflected in the Condensed Consolidated Financial Statements.

### Consolidated Operations

*Premiums and other revenues.* The following details Company revenues.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Universal life and annuity contract charges | $ 32,850 | 40,303 | 101,799 | 112,478 |
| Traditional life premiums | 22,244 | 22,693 | 66,940 | 68,956 |
| Net investment income | 86,686 | 98,159 | 341,115 | 296,759 |
| Other revenues | 5,806 | 3,977 | 17,254 | 15,217 |
| Index option derivative gain (loss) | 2,284 | 31,520 | 70,474 | (34,865) |
| Net realized investment gains | 5,011 | 6,050 | 9,842 | 12,660 |
| Total revenues | $ 154,881 | 202,702 | 607,424 | 471,205 |

Universal life and annuity contract charges - Revenues for universal life and annuity contracts were lower for the first nine months in 2021 compared to 2020 with the component sources shown below. Revenues for universal life and annuity products consist of policy charges for the cost of insurance, administration charges, surrender charges assessed against policyholder account balances, and amortization of deferred premium loads less reinsurance premiums, as shown in the following table.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Contract Revenues: | | | | |
| Cost of insurance and administrative charges | $ 30,608 | 30,975 | 91,870 | 93,122 |
| Surrender charges | 6,599 | 6,192 | 19,900 | 21,219 |
| Other charges | 241 | 7,668 | 3,605 | 11,007 |
| Gross contract revenues | 37,448 | 44,835 | 115,375 | 125,348 |
| Reinsurance premiums | (4,598) | (4,532) | (13,576) | (12,870) |
| Net contract revenues | $ 32,850 | 40,303 | 101,799 | 112,478 |

Cost of insurance charges were $23.7 million in the quarter ended September 30, 2021 compared to $24.6 million in the third quarter of 2020, and were $72.1 million for the nine months ended September 30, 2021 compared to $74.2 million for the same period in 2020. Cost of insurance charges typically trend with the size of the universal life insurance block in force and the amount of new business issued during the period. The volume of universal life insurance in force at September 30, 2021 declined to $12.9 billion from approximately $13.5 billion at December 31, 2020 and $14.4 billion at December 31, 2019. Administrative charges pertaining to new business issued increased to $6.9 million for the three months ended September 30, 2021 from $6.4 million for the same period in 2020, and to $19.8 million for the first nine months of 2021 compared to $18.9 million for the first nine months of 2020, reflecting higher sales activity in the current periods.

Surrender charges assessed against policyholder account balances upon withdrawal increased in the third quarter of 2021 compared to 2020 but were lower for the nine months ended September 30, 2021 versus the comparable prior year period. While the Company earns surrender charge income that is assessed upon policy terminations, the Company's overall profitability is enhanced when policies remain in force and additional contract revenues are realized and the Company continues to make an interest rate spread equivalent to the difference it earns on its investments and the amount that it credits to policyholders. In the nine months ended September 30, 2021, lapse rates on annuity products were higher than the prior year periods. However, surrender charge income recognized is also dependent upon the duration of policies at the time of surrender (i.e. later duration policy surrenders have lower surrender charges assessed and earlier policy surrenders having a higher surrender charge assessed). The lower surrender charge revenue reflects later duration policies terminating having lower surrender charges.

Other charges include the net amortization into income of the premium load on single premium life insurance products which is deferred at the inception of the policy. These products have become a substantial portion of domestic life insurance sales and current period activity reflects the net of amortization of accumulated deferrals against the current period level of premium loads deferred. During the three and nine months ended September 30, 2020, the Company unlocked certain actuarial assumptions impacting the amortization of this unearned revenue reserve the effect of which was to increase the amortization into income by $5.8 million. The Company also unlocked during the three and nine months ended September 30, 2021 the effect of which was to reduce the amortization into income by $(0.6) million.

Traditional life premiums - Traditional life premiums include the activity of Ozark National. Ozark National's principal product is a non-participating whole life insurance policy with premiums remitted primarily on a monthly basis. The product is sold in tandem with a mutual fund investment product offered through its broker-dealer affiliate, NIS. Traditional life insurance premiums for products such as whole life and term life are recognized as revenues over the premium-paying period. A sizable portion of National Western's traditional life business resided in the International Life segment. However, National Western's overall life insurance sales focus has historically been primarily centered around universal life products. The addition of Ozark National's business of repetitive paying permanent life insurance adds an important complement to National Western's life insurance sales. Included in the amount for the quarter ended September 30, 2021 is $18.2 million of life insurance renewal premium from Ozark National compared to $18.5 million in the third quarter of 2020. For the nine months ended September 30, 2021 and 2020, the Ozark National life insurance renewal premium amounts were $55.3 million and $56.1 million, respectively. Universal life products, especially National Western's equity indexed universal life products, which offer the opportunity for consumers to acquire life insurance protection and receive credited interest linked in part to an outside market index, have been the more popular product offerings in the Company's markets.

Net investment income - To ensure the Company will be able to honor future commitments to policyholders and provide a financial return, the funds received as premium payments and deposits are invested in high quality investments, primarily fixed maturity debt securities. The income from these investments is closely monitored by the Company due to its significant impact on the business. A detail of net investment income is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Gross investment income: | | | | |
| Debt and equities | $ 74,579 | 92,892 | 231,484 | 276,971 |
| Mortgage loans | 4,779 | 3,350 | 12,577 | 8,974 |
| Policy loans | 676 | 812 | 1,978 | 2,447 |
| Short-term investments | 48 | 261 | 243 | 1,959 |
| Other invested assets | 3,860 | 1,610 | 10,946 | 8,555 |
| Total investment income | 83,942 | 98,925 | 257,228 | 298,906 |
| Less: investment expenses | 688 | 766 | 2,155 | 2,147 |
| Net investment income (excluding derivatives and trading securities) | 83,254 | 98,159 | 255,073 | 296,759 |
| Index option derivative gain (loss) | 2,284 | 31,520 | 70,474 | (34,865) |
| Embedded derivative on reinsurance | 4,147 | — | 76,486 | — |
| Trading securities market adjustment | (715) | — | 9,556 | — |
| Net investment income | $ 88,970 | 129,679 | 411,589 | 261,894 |

For the nine months ended September 30, 2021, debt and equity securities generated approximately 90% of total investment income, excluding index option derivative gain (loss), embedded derivative on reinsurance, and market adjustments on trading securities. The Company's strategy is to invest substantially all of its cash flows in fixed debt securities within its guidelines for credit quality, duration, and diversification. National Western's debt securities investment income continues to experience higher yielding debt securities maturing or being called by borrowers and being replaced with lower yielding securities in the current interest rate environment. Investment yields on new bond purchases during the first nine months of 2021 approximated 2.99% as compared to the 3.33% yield achieved during the full year 2020. During the first nine months of 2021, the ten-year treasury bond increased nearly 60 basis points, however corporate bond credit spreads narrowed substantially from 2020 levels. National Western's weighted average bond portfolio yield was 3.64% at September 30, 2021 declining from 3.68% at December 31, 2020 and 3.78% at December 31, 2019. Ozark National's weighted average portfolio yield at September 30, 2021 was 3.63%.

Changes in fair values of equity securities are included in net investment income in the Condensed Consolidated Statements of Earnings. For the three months ended September 30, 2021 and 2020, unrealized gains of $0.1 million and $0.9 million, respectively, are included in investment income. For the nine months ended September 30th, unrealized gains of $3.4 million are included in net investment income in 2021 while unrealized losses of $(3.2) million are netted in investment income in the same period for 2020. The carrying value of the Company's portfolio of equity securities was $21.2 million at September 30, 2021.

The Company's mortgage loan activity in 2020 was initially impacted by the pandemic crisis and the low interest rate levels which subsequently materialized. This environment slowed down the underwriting of new loan applications until clarity regarding the impacts of closing down the economy upon commercial real estate became available. As stability in the market slowly returned, the Company commenced underwriting of new loans. As a result, the portfolio balance has increased to $462.9 million at September 30, 2021 from $332.5 million at December 31, 2020 and $302.7 million at September 30, 2020. During the nine months ended September 30, 2021 the Company originated new mortgage loans in the amount of $151.4 million compared to $41.5 million in the comparable period of 2020.

As disclosed in the accompanying Notes to Condensed Consolidated Financial Statements included in this report, in 2020 the Company adopted new accounting guidance pertaining to current expected credit losses on financial instruments ("CECL"). The adoption as of January 1, 2020 was reported as a change in accounting with initial balances recorded and charged to retained earnings. Remeasurement of the CECL allowance for mortgage loans is performed quarterly and for the quarter ended September 30, 2021 resulted in an increase in the allowance of $0.7 million which is included in gross investment income. The provision for the quarter ended September 30, 2020 was an increase in the mortgage loan allowance of $0.3 million. For the nine months ended September 30, 2021 and 2020, the increase in the allowance included in gross investment income for mortgage loans was $1.5 million and $1.2 million, respectively.

Credit loss allowances for available-for-sale debt securities are recorded when unrealized losses and missed payments indicate a credit loss has occurred in which a full recovery of the investment principal is not expected. Credit loss allowances are recorded through net investment income in the Condensed Consolidated Statements of Earnings. No credit loss allowances for available-for-sale debts securities were recorded during the three and nine months ended September 30, 2021 or 2020.

In order to evaluate underlying profitability and results from ongoing operations, net investment income performance is analyzed excluding index option derivative gain (loss), embedded derivative on reinsurance, and trading securities market adjustments, which is a common practice in the insurance industry. Although this is considered a non-GAAP financial measure, Company management believes this financial measure provides useful supplemental information by removing the swings associated with fair value changes in derivative instruments. Net investment income and average invested assets shown below includes cash and cash equivalents. Net investment income performance is summarized as follows:

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2021 | 2020 |
| | (In thousands) | |
| Excluding derivatives and funds withheld securities: | | |
| Net investment income | $ 255,073 | 296,759 |
| Average invested assets, at amortized cost | $ 9,377,407 | 10,982,593 |
| Annual yield on average invested assets | 3.63 % | 3.60 % |
| | | |
| Including derivatives and funds withheld securities: | | |
| Net investment income | $ 411,589 | 261,894 |
| Average invested assets, at amortized cost | $ 11,145,890 | 11,108,071 |
| Annual yield on average invested assets | 4.92 % | 3.14 % |

The increase in average invested asset yield, excluding derivatives and trading securities, for the first nine months of 2021 is due to the Company obtaining incremental yields on newly invested cash flows into mortgage loans as well as lower yielding debt securities being transferred to the funds withheld account at year-end 2020.

The average yield on bond purchases during the nine months ended September 30, 2021 to fund National Western insurance operations was 2.99% representing a 1.26% spread over treasury rates. The weighted average quality of new purchases during the first nine months of 2021 was "BBB+" which was consistent with purchases during 2020. The composite duration of purchases during the first nine months of 2021 continued to be longer than that of purchases prior to 2019 as the Company purchased a higher proportion of investments for its life insurance line of business which has a longer liability duration than that of the annuity line of business. The Company's general investment strategy is to purchase debt securities with maturity dates approximating ten years in the future. Accordingly, an appropriate measure for benchmarking the direction of interest rate levels for the Company's debt security purchases is the ten year treasury bond rate. After ending 2020 at a rate of 0.92%, the daily closing yield of the ten-year treasury bond ranged as low as 0.91% during the first nine months of 2021 and as high as 1.74% before finishing the period at 1.49%.

The pattern in average invested asset yield, including derivatives, incorporates increases and decreases in the fair value of index options purchased by National Western to support its fixed-index products. Fair values of the purchased call options recorded a net gain during the first nine months of 2021 while a net loss was recorded during the first nine months of 2020, corresponding to the movement in the S&P 500 Index during these periods (the primary index the fixed-index products employ). Refer to the derivatives discussion below for a more detailed explanation. In addition, the funds withheld reinsurance agreement executed December 31, 2020 introduced embedded derivative accounting with respect to the policyholder obligations reinsured. During the nine months ended September 30, 2021, the embedded derivative liability for reinsurance decreased by $76.5 million which was recorded as investment income. Debt securities supporting the funds withheld policyholder obligations classified as trading incurred a $9.6 million market value increase which was also recorded as a component of net investment income. The sum of these two amounts, or $86.1 million, increased net investment income during the nine months ended September 30, 2021.

Other revenues - Other revenues include the operations of NIS, the broker-dealer affiliate of Ozark National, the operations of Braker P III ("BP III"), a subsidiary which owns and manages a commercial office building which includes the home office operations of National Western, and a maintenance expense allowance earned by National Western for administering the funds withheld block of annuity policies ceded to a third party reinsurer.

Revenues associated with NIS were $3.1 million and $2.6 million for the three months ended September 30, 2021 and 2020, respectively. For the nine months ended September 30, 2021 and 2020, NIS revenues were $9.3 million and $7.2 million, respectively.

Third party revenues associated with BP III were $1.3 million and $1.1 million for the three months ended September 30, 2021 and 2020, respectively. For the nine months ended September 30, 2021 and 2020 revenues were $3.8 million and $3.4 million, respectively. The facility is currently fully leased.

Under terms of the funds withheld reinsurance contract, National Western earns a monthly expense allowance equal to the average policy count of the funds withheld reinsured block of business multiplied by a stated amount per policy. In the three and nine months ended September 30, 2021, the Company reported $1.3 million and $4.1 million, respectively, as maintenance expense allowance revenue.

In the nine months ended September 30, 2020, the Company recognized as other revenue $4.1 million related to the release of a contingent payment liability associated with National Western's acquisition of Ozark National. During the second quarter of 2020, the Company executed an agreement with the seller under which both parties agreed that the Company had fulfilled its payment obligation under the Stock Purchase Agreement executed October 3, 2018 thus allowing it to reverse the contingent payment amounts previously accrued.

Derivative gain (loss) - Index options are derivative financial instruments used to hedge the equity return component of National Western's fixed-index products. Derivative gain or loss includes the amounts realized from the sale or expiration of the options. Since the index options do not meet the requirements for hedge accounting under GAAP, they are marked to fair value on each reporting date and the resulting unrealized gain or loss is reflected as a component of net investment income. As the options hedging the notional amount of policyholder contract obligations are purchased as close as possible to like amounts, the amount of the option returns tends to correlate closely with indexed interest credited.

Gains and losses from index options are substantially due to changes in equity market conditions. Index options are intended to act as hedges to match the returns on the product's underlying reference index and the rise or decline in the index relative to the index level at the time of the option purchase which causes option values to likewise rise or decline. As income from index options fluctuates with the underlying index, the contract interest expense to policyholder accounts for the Company's fixed-index products also fluctuates in a similar manner and direction. For the three and nine months ended September 30, 2021 and 2020, the Company recorded realized and unrealized gains/(losses) from index options as shown below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Index option derivatives: | | | | |
| Unrealized gain (loss) | $ (33,034) | 35,075 | (34,338) | (58,077) |
| Realized gain (loss) | 35,318 | (3,555) | 104,812 | 23,212 |
| Total gain (loss) included in net investment income | $ 2,284 | 31,520 | 70,474 | (34,865) |
| Total contract interest | $ 11,663 | 85,879 | 134,481 | 119,625 |

The economic impact of option performance in the Company's financial statements is not generally determined solely by the option gain or loss included in net investment income as there is a corresponding amount recorded in the contract interest expense line. The Company's profitability with respect to these options is largely dependent upon the purchase cost of the option remaining within the financial budget for acquiring options embedded in the product pricing. Option prices vary with interest rates, volatility, and dividend yields among other things. As option prices vary, the Company manages for the variability by making offsetting adjustments to product caps, participation rates, and management fees. For the periods shown, the Company's option costs have been close to or within the product pricing budgets.

The financial statement investment spread, the difference between investment income and interest credited to contract holders, is subject to variations from option performance during any given period. For example, many of the Company's equity-index annuity products provide for the collection of asset management fees. These asset management fees are assessed when returns on expiring options are positive, and they are collected prior to passing any additional returns above the assessed management fees to the policy contractholders. During periods of positive returns, the collected asset management fees serve to increase the financial statement spread by increasing option realized gains reported as investment income in an amount greater than interest credited to policy contractholders which is reported as contract interest expense. Asset management fees collected in the third quarter of 2021 and 2020 were approximately $0.0 million and $6.7 million, respectively. For the nine months ended September 30, 2021 and 2020, asset management fees collected were $5.8 million and $24.7 million, respectively. The lower amounts in the 2021 periods compared to 2020 are the result of the Company's change in option hedging to an "out-of-the-money" basis during 2020. As of the end of the second quarter of 2021, all options outstanding were acquired on an out-of-the-money basis. Accordingly, no asset management fees were collected in the third quarter of 2021 nor will there be any future asset management fees collected under the current hedging methodology. While asset management fees are no longer being collected, the costs to purchase the out-of-the-money options similarly decreases.

Net realized investment gains (losses) - Realized gains (losses) on investments include proceeds from bond calls, sales and impairment write-downs as well as gains and losses on the sale of real estate property. The net gains reported for the nine months ended September 30, 2021 consisted of gross gains of $11.3 million, primarily related to bond calls of debt securities in the available-to-sale category, offset by gross losses of $(1.4) million. Gross losses in the nine months ended September 30, 2021 include $1.4 million pertaining to property held by Ozark National which recorded a valuation allowance to reflect the property at its estimated fair value less anticipated costs to sell. The final sale during the third quarter approximated the recorded property amount net of the valuation allowance previously recorded. The net gains reported for the nine months ended September 30, 2020 consisted of gross gains of $12.7 million offset by gross losses of $0.0 million. The gross gains in the first nine months of 2020 included proceeds from bonds calls of securities classified in the held-to-maturity category at that time.

*Benefits and Expenses.* The following table details benefits and expenses.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Life and other policy benefits | $ 70,633 | 26,940 | 144,426 | 94,005 |
| Amortization of deferred transaction costs | (8,389) | 50,800 | 46,723 | 111,937 |
| Universal life and annuity contract interest | 11,663 | 85,879 | 134,481 | 119,625 |
| Other operating expenses | 30,793 | 25,754 | 90,596 | 74,730 |
| | | | | |
| Totals | $ 104,700 | 189,373 | 416,226 | 400,297 |

Life and other policy benefits - Death claim benefits, the largest component of policy benefits, were $74.6 million in the first nine months of 2021 compared to $50.9 million for the first nine months of 2020. Of the amount included in the nine months ended September 30, 2021, $45.4 million was associated with National Western business and $29.2 million pertained to Ozark National. In the first nine months of 2020, these amounts were $25.1 million and $25.8 million for National Western and Ozark National, respectively. Death claim amounts are subject to variation from period to period. For the first nine months of 2021, the number of National Western life insurance claims increased 3% versus the comparable period in 2020 while the average dollar amount per net claim increased to $61,300 from approximately $40,200. National Western's overall mortality experience has generally been consistent with or better than its product pricing assumptions. The average net claim for Ozark National during the 2021 and 2020 nine-month periods was $16,000 and $15,300, respectively. Mortality exposure is managed through reinsurance treaties under which National Western's retained maximum net amount at risk on any one life is capped at $500,000. Ozark National's retained maximum net amount at risk is capped at $200,000 under its reinsurance treaties with limited exceptions related to the conversion of child protection and guaranteed insurability riders.

Both National Western and Ozark National have established specific coding to track the death claim experience associated with COVID-19. During the nine months ended September 30, 2021, National Western incurred 174 death claims on life insurance policies in which the reported cause of death was due to the coronavirus (COVID-19) totaling a net claim amount (after reinsurance) of $20.5 million. For the comparable nine-month period in 2020, National Western incurred 51 COVID-19 related death claims on life insurance policies totaling a net amount after reinsurance of $2.4 million. During the nine months ended September 30, 2021, Ozark National incurred 343 confirmed COVID-19 death claims aggregating to a net claim amount of approximately $5.9 million. For the nine months ended September 30, 2020, Ozark National reported 76 COVID-19 death claims totaling to a net claim amount of $1.2 million. The COVID-19 claim activity is included in the claim disclosures made in the preceding paragraph.

Life and other policy benefits also includes policy liabilities held associated with the Company's traditional life products, policies with life contingencies, and riders such as the guaranteed minimum withdrawal benefit rider ("WBR"), a popular rider to National Western's equity-indexed annuity products. Prior to unlocking adjustments, the increases in these liabilities for National Western were $4.3 million and $6.2 million in the quarters ended September 30, 2021 and 2020, respectively, and $9.1 million and $16.9 million, respectively, for the nine months then ended. In the third quarters ended September 30, 2021 and 2020, the Company unlocked its assumptions pertaining to the WBR benefit, the effect of which was to increase the liability for policy benefits by $27.4 million in the third quarter of 2021 and to decrease the liability for policy benefits by $11.9 billion in the third quarter of 2020.

Life and other policy benefits in the quarters ended September 30, 2021 and 2020 includes changes in traditional life reserves and miscellaneous benefit payments associated with Ozark National's operations of $8.4 million and $7.6 million, respectively, and $21.5 million and $24.6 million, respectively, for the nine months then ended.

Amortization of deferred transaction costs - Life insurance companies are required to defer certain expenses that vary with, and are primarily related to, the cost of acquiring new business. The majority of these acquisition expenses consist of commissions paid to agents, underwriting costs, and certain marketing expenses. Recognition of these deferred policy acquisition costs ("DPAC") as an expense in the Condensed Consolidated Financial Statements occurs over future periods in relation to the expected emergence of profits priced into the products sold. This emergence of profits is based upon assumptions regarding premium payment patterns, mortality, persistency, investment performance, and expense patterns. Companies are required to review universal life and annuity contract assumptions periodically to ascertain whether actual experience has deviated significantly from that assumed. If it is determined that a significant deviation has occurred, the emergence of profits pattern is to be "unlocked" and reset based upon actual experience. DPAC balances are also adjusted each period to reflect current policy lapse or termination rates, expense levels and credited rates on policies compared to anticipated experience ("true-up") with the adjustment reflected in current period amortization expense. In accordance with GAAP guidance, the Company must also write-off deferred acquisition costs and unearned revenue liabilities upon internal replacement of certain contracts as well as annuitizations of deferred annuities.

The following table identifies the effects of unlocking adjustments on DPAC balances recorded through amortization expense separate from recurring amortization expense components for the three and nine months ended September 30, 2021 and 2020.

| *Amortization of DPAC* | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Unlocking adjustments | $ (36,510) | 22,358 | (36,510) | 22,358 |
| Other amortization components | 23,081 | 26,597 | 66,262 | 83,933 |
| Totals | $ (13,429) | 48,955 | 29,752 | 106,291 |

Amortization expense for the three and nine months ended September 30, 2021 was comprised of DPAC amortization by National Western of $(13.6) million and $29.2 million, respectively, and by Ozark National of $0.2 million and $0.5 million, respectively. Amortization expense for National Western for the three and nine months ended September 30, 2021, was reduced by $1.6 million and $5.0 million, respectively, for amounts pertaining to the policies ceded under the funds withheld reinsurance agreement.

The Company's practice is to annually review its actuarial assumptions during the third quarter regarding the emergence of profits pertaining to its blocks of businesses and to update or "unlock" those assumptions which deviate significantly from actual experience. During the three and nine months ended September 30, 2021, the Company unlocked DPAC balances associated with its Life and Annuity segments the effect of which was to increase DPAC balances by $36.5 million (and decrease amortization expense). The primary unlocking adjustment giving rise to the DPAC balance increase was cost of insurance ("COI") charge increases on International universal life products inforce. The increased COI charges create higher expected gross profits in future years which causes DPAC amortization to shift to these periods. The Company also unlocked DPAC balances during the three and nine months ended September 30, 2020, the effect of which was to decrease DPAC balances by $22.4 million (and increase amortization expense). Life and Annuity DPAC balances were unlocked for assumptions involving lapse rates, surrender rates, annuitization rates, mortality experience, investment portfolio yield rates, and withdrawal benefit rider election rates.

The Company is required to evaluate its emergence of profits continually and management believes that the current amortization patterns of deferred policy acquisition costs are reflective of actual experience.

As the DPAC balance is an asset on the Company's Condensed Consolidated Balance Sheets, GAAP provides for an earned interest return on the unamortized balance each period. The earned interest serves to increase the DPAC balance and reduce other amortization component expense. The rate at which the DPAC balance earns interest is the average credited interest rate on the Company's universal life and annuity policies in force, including credited interest on equity-indexed policies. The amount of earned interest on DPAC balances recorded for the three months ended September 30, 2021 and 2020 was $8.6 million and $2.7 million, respectively, decreasing other amortization component expense. The amount of interest earned on DPAC balances for the nine months ended September 30, 2021 and 2020 was $24.1 million and $13.3 million, respectively. The increased interest amount in 2021 compared to 2020 reflects higher crediting rate returns on equity-index products, particularly life insurance products.

As part of the purchase accounting required with the acquisition of Ozark National effective January 31, 2019, the Company recorded an intangible asset of $180.9 million referred to as the value of business acquired ("VOBA"). VOBA represents the difference between the acquired assets and liabilities of Ozark National measured in accordance with the Company's accounting policies and the fair value of these same assets and liabilities. The VOBA balance sheet amount is amortized following a methodology similar to that used for amortizing deferred policy acquisition costs. In the quarters ended September 30, 2021 and 2020, the Company's VOBA amortization expense was $1.9 million and $1.8 million, respectively, and $6.7 million and $5.6 million, respectively, for the nine months then ended.

At December 31, 2020, the Company recorded as an asset on its Consolidated Balance Sheet a deferred Cost of Reinsurance ("COR") amount of $102.8 million associated with the funds withheld reinsurance transaction. This represents the amount of assets transferred at the closing date of funds withheld agreement (debt securities, policy loans, and cash) in excess of the GAAP liability ceded plus a $48 million ceding commission paid to the reinsurer. The COR balance is amortized commensurate with the runoff of the ceded block of funds withheld business. In the three and nine months ended September 30, 2021, COR amortization expense of $3.1 million and $10.3 million, respectively, is included in Amortization of deferred transaction costs.

Universal life and annuity contract interest - The Company closely monitors its credited interest rates on interest sensitive policies (National Western products), taking into consideration such factors as profitability goals, policyholder benefits, product marketability, and economic market conditions. As long term interest rates change, the Company's credited interest rates are often adjusted accordingly, taking into consideration the factors described above. The difference between yields earned on investments over policy credited rates is often referred to as the "interest spread" within the industry.

Contract interest reported in financial statements also encompasses the performance of the index options associated with the Company's fixed-index products. As previously noted, the market value changes of these derivative features resulted in net realized and unrealized gains/(losses) of $70.5 million and $(34.9) million for the nine months ended September 30, 2021 and 2020, respectively. These amounts consisted of realized gains of $104.8 million and unrealized losses of $(34.3) million for the year-to-date 2021 period, and realized gains of $23.2 million and unrealized losses of $(58.1) million for the comparable 2020 time frame. In the third quarter of 2021, the figure was comprised of realized gains of $35.3 million and unrealized losses of $(33.0) million. In the third quarter of 2020, this amount was made up of realized losses of $(3.6) million and unrealized gains of $35.1 million. These returns similarly increased/(decreased) the computed average credited rates for the periods shown above. Policyholders of equity-indexed products cannot receive an interest credit below 0% according to the policy contract terms.

Contract interest expense includes other items which may increase or decrease reported contract interest in a particular reporting period. For the three and nine months ended September 30, 2021 and 2020, these other items include the amounts shown in the table below.

| *Contract Interest Expense* | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Gross reserve changes | $ 330 | 4,052 | 16,342 | 16,405 |
| Ceded reserve changes under funds withheld | (2,773) | — | (19,916) | — |
| Unlocking adjustments, net | (14,547) | 17,180 | (14,547) | 17,180 |
| Asset management fees collected | — | (6,740) | (5,835) | (24,682) |
| Projected asset management fees | — | 3,657 | 6,477 | 29,292 |
| Other embedded derivative components | (1,291) | 822 | 5,748 | (6,455) |
| Totals | $ (18,281) | 18,971 | (11,731) | 31,740 |

Contract interest expense includes gross reserve changes for immediate annuities, two tier annuities, excess death benefit reserves, excess annuitizations, and amortization of deferred sales inducement balances. These gross reserve items are offset by policy charges assessed for policies having the withdrawal benefit rider (WBR). As changes in these items collectively impact contract interest expense, financial statement interest spread is also affected. Netted against gross reserve changes for the first nine months of 2021 is $19.9 million for assessed WBR policy charges compared to $18.0 million in the same period for 2020.

Beginning in 2021, reserve changes associated with funds withheld annuity policies are ceded to the reinsurer and no longer reflected in the financial statements of the Company. Accordingly, contract interest expense is adjusted to remove these expense items which are shown in the above table for the three and nine months ended September 30, 2021. In addition to these amounts, the Company also cedes the fixed interest credited on the funds withheld annuity policies. For the three and nine months ended September 30, 2021, the fixed interest credited ceded was $7.4 million and $22.6 million, respectively.

Generally, the impact of the market value change of index options on asset values aligns closely with the movement of the embedded derivative liability held for the Company's fixed-index products such that the net effect upon pretax earnings is negligible (i.e. net realized and unrealized gains/(losses) included in net investment income approximate the change in contract interest associated with the corresponding embedded derivative liability change). However, other aspects of the embedded derivatives can cause deviations to occur between the change in index option asset values included in net investment income and the change in the embedded derivative liability included in contract interest. As noted in the discussion of net investment income, the collection of asset management fees in a period can cause investment income to increase marginally higher than contract interest expense since these collected fees are deducted from indexed interest credited to policyholders. As shown in the table above, the collection of asset management fees are deductions from contract interest expense.

Accounting rules require the embedded derivative liability to include a projection of asset management fees estimated to be collected in the succeeding fiscal year due to the Company's historical practice of purchasing options priced to incorporate an expected probability of collecting asset management fees (referred to as "at-the-money hedging"). This projection for the embedded derivative liability is based upon the most recent performance of the reference equity index. Increases in projected asset management fees to be collected reduce contract interest expense while decreases in projected asset management fees to be collected increase contract interest expense. In the nine month periods ended September 30, 2021 and 2020 contract interest was increased by $6.5 million and $29.3 million, respectively, for the projected change in asset management fees to be collected. In the second quarter of 2020, the Company changed its embedded derivative hedging process to incorporate "out of the money" hedging which reduces option costs and eliminates the requirement for estimating probability projections of collected asset management fees. The remaining inventory of annual at the money option hedges completed its roll over to out of the money hedges during the second quarter of 2021. Consequently, the embedded derivative liability component for projected asset management fees to be collected progressively diminished and was phased out as of the end of the 2021 second quarter.

Another contract interest expense component is the amortization of deferred sales inducements (included in Reserve changes above). Similar to deferred policy acquisition costs, the Company defers sales inducements in the form of first year credited interest bonuses on annuity products that are directly related to the production of new business. These bonus interest charges are deferred and amortized using the same methodology and assumptions used to amortize other capitalized acquisition costs and the amortization is included in contract interest. In addition, deferred sales inducement balances are also reviewed periodically to ascertain whether actual experience has deviated significantly from that assumed (unlock) and are adjusted to reflect current policy lapse or termination rates, expense levels and credited rates on policies compared to anticipated experience (true-up). These unlocking adjustments, plus or minus, are included in contract interest expense. As previously discussed in the amortization of deferred policy acquisition costs section, the Company unlocked its assumptions for the annuity line of business in the third quarters of 2021 and 2020 including the deferred sales inducement balance (which is amortized as credited interest). The effect of these prospective unlockings was to increase the deferred sales inducement balance by $1.0 million in the quarter ended September 30, 2021 (and decrease contract interest expense) and to decrease the sales inducement balance by $4.4 million in the quarter ended September 30, 2020 (and increase contract interest expense).

Other operating expenses - Other operating expenses consist of general administrative expenses, licenses and fees, commissions not subject to deferral, real estate expenses, brokerage expenses, compensation costs, and reinsurance ceded commission expense. These expenses for the three and nine months ended September 30, 2021 and 2020 are summarized in the table that follows.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| General insurance expenses | $ 14,043 | 9,589 | 37,675 | 30,747 |
| Compensation expenses | 8,745 | 7,629 | 29,473 | 19,855 |
| Commission expenses | 2,392 | 2,927 | 8,052 | 8,502 |
| Real estate expenses | 1,471 | 1,395 | 4,400 | 4,335 |
| Brokerage expenses (NIS) | 1,523 | 1,372 | 4,481 | 3,745 |
| Reinsurance ceded commission expense | — | — | 10 | — |
| Taxes, licenses and fees | 2,619 | 2,842 | 6,505 | 7,546 |
| Totals | $ 30,793 | 25,754 | 90,596 | 74,730 |

General insurance expenses include software amortization expense associated with National Western's proprietary policy administration systems as well as other acquired software. Expenses pertaining to these items were $3.0 million and $3.0 million in the third quarter of 2021 and 2020, respectively, and $10.4 million and $9.1 million in the first nine months of 2021 and 2020, respectively. This category of expenses also includes legal fees and expenses which were $(0.7) million and $0.7 million in the quarters ended September 30, 2021 and 2020, respectively, and $1.1 million and $1.6 million, respectively, for the nine months year-to-date. Legal fees and expenses for the quarter ended September 30, 2021 were a negative amount due to the recovery of $1.9 million from the plaintiff in the shareholder derivative lawsuit. The 2021 legal fees and expenses include amounts pertaining to the security incident reported in Part II. Item 1. of this filing. In addition to these amounts, in the quarter ended September 30, 2021, the Company accrued $4.4 million for the class action lawsuit filed related to the security incident. Other costs associated with the incident include consulting fees and information services associated costs. Total expenses in these categories for consulting fees and information services, including those for the security incident, were $3.8 million and $9.3 million for the three and nine months ended September 30, 2021, versus $1.7 million and $5.6 million in the comparable periods of 2020.

Compensation expenses include share-based compensation costs related to outstanding vested and nonvested stock appreciation rights ("SARs"), restricted stock units ("RSUs") and performance share units ("PSUs"). The related share-based compensation costs move in tandem not only with the number of awards outstanding but also with the movement in the market price of the Company's Class A common stock as a result of marking the SARs, RSUs, and PSUs to fair value under the liability method of accounting. Consequently, the related expense amount varies positive or negative in any given period. In the amounts shown above, share-based compensation expense totaled $0.3 million in the third quarter of 2021 and $(0.5) million in the third quarter of 2020. For the nine-month periods shown, share-based compensation expense was $4.2 million in 2021 and $(4.4) million in 2020. The Company's Class A common share price increased from $206.44 at December 31, 2020 to $210.59 at September 30, 2021, compared to dropping from $290.88 at December 31, 2019 to $182.77 at September 30, 2020. No performance share awards were granted in the first nine months of 2021 and 2020. Ozark National compensation expenses were $1.0 million and $0.9 million in the third quarter of 2021 and 2020, respectively, and $2.9 million and $2.6 million in the nine months ended 2021 and 2020, respectively.

Federal Income Taxes. Federal income taxes on earnings from operations reflect an effective tax rate of 20.6% for the nine months ended September 30, 2021 compared to 19.4% for the nine months ended September 30, 2020. The Federal corporate tax rate was set at 21% under the 2017 Tax Cuts and Jobs Act ("Tax Act"). The Company's effective tax rate is typically lower than the Federal statutory rate due to tax-exempt investment income related to municipal securities and dividends-received deductions on income from stocks, absent other permanent tax items.

While the Company's overall effective tax rate remains close to the statutory rate level, the Company's current tax expense is elevated due to a provision of the Tax Act which imposed a limitation on the amount of tax reserves a life insurer is able to deduct in arriving at its taxable income. The limitation is the greater of net surrender value or 92.81% of the reserve method prescribed by the National Association of Insurance Commissioners. Implementation of this provision was required as of January 1, 2018 and the Company ultimately determined that the resultant tax reserve adjustment was a decrease of $332.9 million. The Tax Act provided that this tax reserve adjustment could be brought into taxable income ratably over a period of eight (8) years. Based upon the tax reserve adjustment derived, the effect of the Tax Act limiting the tax reserve deductible in the current tax computation serves to increase the Company's taxable income by approximately $41.6 million per year through 2025. At the Federal statutory rate of 21%, the impact upon current tax expense is an increase of approximately $8.7 million per year or approximately $2.2 million each quarter.

**Segment Operations**

***Summary of Segment Earnings***

A summary of segment earnings for the three and nine months ended September 30, 2021 and 2020 is provided below. The segment earnings exclude realized gains and losses on investments, net of taxes.

| | | Domestic Life Insurance | International Life Insurance | Annuities | ONL & Affiliates | All Others | Totals |
|---|---|---|---|---|---|---|---|
| | | | | (In thousands) | | | |
| Segment earnings: | | | | | | | |
| Three months ended: | | | | | | | |
| September 30, 2021 | $ | 486 | 38,759 | (9,985) | 3,381 | 3,240 | 35,881 |
| September 30, 2020 | $ | (756) | 26,557 | (26,478) | 3,661 | 3,062 | 6,046 |
| | | | | | | | |
| Nine months ended: | | | | | | | |
| September 30, 2021 | $ | 1,891 | 49,243 | 69,627 | 11,616 | 11,717 | 144,094 |
| September 30, 2020 | $ | 998 | 44,769 | (22,317) | 12,144 | 11,581 | 47,175 |

***Domestic Life Insurance Operations***

A comparative analysis of results of operations for the Company's domestic life insurance segment is detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Premiums and other revenues: | | | | |
| Premiums and contract revenues | $ 12,122 | 17,734 | 38,495 | 40,971 |
| Net investment income | 6,599 | 21,201 | 58,689 | 23,293 |
| Other revenues | 28 | 10 | 80 | 40 |
| Total premiums and other revenues | 18,749 | 38,945 | 97,264 | 64,304 |
| Benefits and expenses: | | | | |
| Life and other policy benefits | 6,752 | 3,785 | 17,869 | 13,831 |
| Amortization of deferred transaction costs | 2,479 | 10,540 | 8,092 | 16,322 |
| Universal life insurance contract interest | 3,015 | 20,352 | 50,102 | 17,831 |
| Other operating expenses | 5,891 | 5,185 | 18,820 | 15,123 |
| Total benefits and expenses | 18,137 | 39,862 | 94,883 | 63,107 |
| Segment earnings (loss) before Federal income taxes | 612 | (917) | 2,381 | 1,197 |
| Provision for Federal income taxes | 126 | (161) | 490 | 199 |
| Segment earnings (loss) | $ 486 | (756) | 1,891 | 998 |

Revenues from domestic life insurance operations include life insurance premiums on traditional type products and contract revenues from universal life insurance. Revenues from traditional products are simply premiums collected, while revenues from universal life insurance consist of policy charges for the cost of insurance, policy administration fees, and surrender charges assessed during the period. A comparative detail of premiums and contract revenues is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Universal life insurance revenues | $ 14,148 | 19,739 | 44,399 | 46,426 |
| Traditional life insurance premiums | 985 | 894 | 2,888 | 2,790 |
| Reinsurance premiums | (3,011) | (2,899) | (8,792) | (8,245) |
| Totals | $ 12,122 | 17,734 | 38,495 | 40,971 |

National Western's domestic life insurance in force, in terms of policy count, has been declining for some time. The pace of new policies issued has lagged the number of policies terminated from death or surrender causing a declining level of policies in force from which contract revenue is received. Consequently, the number of domestic life insurance policies in force has declined from 47,920 at December 31, 2019 to 46,940 at December 31, 2020, and to 46,260 at September 30, 2021. Policy lapse rates in the first nine months of 2021 approximated 6.3% compared to 6.5% and 6.0% in the first nine months of 2020 and 2019, respectively. The lapse rate in the first nine months of 2020 includes the effect of the pandemic induced economic crisis which caused consumers to access available sources of liquidity. While policy count rates have declined, the face amount of life insurance in force has risen steadily from $3.4 billion at December 31, 2019 to $3.5 billion at December 31, 2020 and to $3.6 billion at September 30, 2021.

Universal life insurance revenues are also generated with the issuance of new business based upon amounts per application and percentages of the face amount (volume) of insurance issued. The number of domestic life policies issued in the first nine months of 2021 was 11% higher than in the comparable period for 2020 and the volume of insurance issued was 12% higher than that in 2020.

Universal life insurance revenues also include surrender charge income realized on terminating policies and, in the case of domestic universal life, amortization into income of the premium load on single premium policies which is deferred. The net premium load amortization was $0.2 million and $7.7 million in the three months ended September 30, 2021 and 2020, respectively, and $3.6 million and $11.0 million in the nine months ended September 30, 2021 and 2020, respectively. During the third quarters of 2021 and 2020, the Company unlocked the actuarial assumptions pertaining to the recognition of this unearned revenue reserve. The effect of the prospective unlocking was to decrease the amortization of revenue by $(0.5) million in 2021 and to increase the amortization of revenue by $5.9 million in 2020.

Premiums collected on universal life products are not reflected as revenues in the Company's Condensed Consolidated Statements of Earnings in accordance with GAAP. Actual domestic universal life premiums collected are detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Universal life insurance: | | | | |
| First year and single premiums | $ 51,986 | 56,330 | 156,801 | 141,191 |
| Renewal premiums | 4,436 | 5,084 | 12,719 | 13,474 |
| Totals | $ 56,422 | 61,414 | 169,520 | 154,665 |

Domestic life insurance sales for some time have consisted substantially of single premium policies which do not have much in the way of recurring premium payments. These products are targeting wealth transfer strategies involving the movement of accumulated wealth in alternative investment vehicles, including annuities, into life insurance products. As a result, renewal premium levels have not been exhibiting a corresponding level of increase.

Net investment income for this segment of business, excluding derivative gain/(loss), has been gradually increasing due to the increased new business activity described above (single premium policies) and a higher level of investments needed to support the corresponding growth in policy obligations, especially those for single premium policies. The increase in net investment income has been partially muted by lower investment yields from debt security investment purchases during this time frame. Net investment income also includes the gains and losses on index options purchased to back the index crediting mechanism on fixed-index universal products.

A detail of net investment income for domestic life insurance operations is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Net investment income (excluding derivatives) | $ 12,865 | 11,760 | 38,413 | 34,040 |
| Index option derivative gain (loss) | (6,266) | 9,441 | 20,276 | (10,747) |
| Net investment income | $ 6,599 | 21,201 | 58,689 | 23,293 |

As seen in the above table, reported net investment income includes the gains and losses on index options purchased to back the index crediting mechanism on fixed-index universal life products. The gain or loss on index options follows the movement of the S&P 500 Index (the primary index for the Company's fixed-index products) with realized gains or losses being recognized on the anniversary of each index option based upon the S&P 500 Index level at each expiration date relative to the index level at the time the index option was purchased, and unrealized gains and losses being recorded for index options outstanding based upon the S&P 500 Index at the balance sheet reporting date as compared to the index level at the time each respective option was purchased.

Life and policy benefits for a smaller block of business are subject to variation from period to period. Claim count activity during the first nine months of 2021 decreased 3% compared to the first nine months of 2020 while the average net claim amount (after reinsurance) increased to $36,700 from $29,200. Reported claims in the nine months ended September 30, 2021 for which the cause of death was identified as COVID-19 were $4.2 million after reinsurance. The low face amount per claim relative to current issued amounts of insurance per policy reflects the older block of domestic life insurance policies sold consisting of final expense type products (i.e. purchased to cover funeral costs) which typically had smaller face amounts of insurance coverage. Claims on these older blocks of policies are more susceptible to COVID-19 mortality given the higher attained ages of this business. GAAP reporting requires that claims be recorded net of any cash value amounts that have been accumulated in the policies. The Company's overall mortality experience for this segment has been consistent with pricing assumptions.

Included in amortization of deferred transaction costs is DPAC amortization. As noted previously in the discussion of Results of Operations, the Company records true-up adjustments to DPAC balances each period to reflect current policy lapse or termination rates, expense levels and credited rates on policies as compared to anticipated experience with the adjustment reflected in current period amortization expense. To the extent required, unlocking adjustments may also be recorded to DPAC balances. The following table identifies the effects of unlocking adjustments on domestic life insurance DPAC balances recorded through amortization expense separate from recurring amortization expense components for the three and nine months ended September 30, 2021 and 2020.

| *Amortization of DPAC* | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Unlocking adjustments | $ 495 | 7,391 | 495 | 7,391 |
| DPAC amortization expense | 1,984 | 3,149 | 7,597 | 8,931 |
| Totals | $ 2,479 | 10,540 | 8,092 | 16,322 |

During the quarters ended September 30, 2021 and 2020, the Company unlocked DPAC balances associated with its Domestic Life segment for mortality, lapse rates, and portfolio investment yield (interest spread). The effect of the prospective unlocking was to decrease DPAC balances (and increase amortization expense) by $0.5 million and $7.4 million, respectively.

In the Consolidated Operations discussion of amortization of deferred acquisition costs it was noted that interest earned on DPAC balances serves to offset (decrease) amortization expense and that the interest rate used is the crediting rate experience during the period. The decrease in amortization expense in 2021 relative to 2020 reflects higher interest earned on universal life DPAC balances due to increased realized gains from index options. Credited interest rates during the third quarter of 2021 approximated 9% on indexed universal life as compared to 3% in the third quarter of 2020.

Contract interest expense includes the fluctuations that are the result of the effect upon the embedded derivative for the performance of underlying equity indices associated with fixed-index universal life products. For liability purposes, the embedded option in the Company's policyholder obligations for this feature is bifurcated and reserved for separately. Accordingly, the impact for the embedded derivative component in the equity-index universal life product is reflected in contract interest expense for approximately the same amounts as in net investment income for each respective period.

***International Life Insurance Operations***

A comparative analysis of results of operations for the Company's international life insurance segment is detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Premiums and other revenues: | | | | |
| Premiums and contract revenues | $ 19,570 | 21,551 | 60,406 | 67,479 |
| Net investment income | 9,172 | 10,354 | 35,135 | 12,507 |
| Other revenues | 19 | 6 | 91 | 54 |
| Total premiums and other revenues | 28,761 | 31,911 | 95,632 | 80,040 |
| Benefits and expenses: | | | | |
| Life and other policy benefits | 10,272 | 2,278 | 19,949 | 9,293 |
| Amortization of deferred transaction costs | (27,896) | 6,496 | (16,341) | 19,392 |
| Universal life insurance contract interest | (7,056) | (14,023) | 15,969 | (15,368) |
| Other operating expenses | 4,640 | 5,434 | 14,060 | 13,047 |
| Total benefits and expenses | (20,040) | 185 | 33,637 | 26,364 |
| Segment earnings before Federal income taxes | 48,801 | 31,726 | 61,995 | 53,676 |
| Provision for Federal income taxes | 10,042 | 5,169 | 12,752 | 8,907 |
| Segment earnings | $ 38,759 | 26,557 | 49,243 | 44,769 |

As with domestic life operations, revenues from the international life insurance segment include both premiums on traditional type products and contract revenues from universal life insurance. A comparative detail of premiums and contract revenues is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Universal life insurance revenues | $ 19,055 | 20,910 | 59,059 | 65,386 |
| Traditional life insurance premiums | 2,101 | 2,274 | 6,130 | 6,718 |
| Reinsurance premiums | (1,586) | (1,633) | (4,783) | (4,625) |
| Totals | $ 19,570 | 21,551 | 60,406 | 67,479 |

Universal life revenues and operating earnings are largely generated from the amount of life insurance in force. The volume of in force for this segment, primarily universal life, has contracted from $13.7 billion at December 31, 2019 to $12.4 billion at December 31, 2020 and to $11.6 billion at September 30, 2021.

Another component of international universal life revenues includes surrender charges assessed upon surrender of contracts by policyholders. In addition to termination rates trending lower, the resulting surrender charge fee revenue has been less due to policy contract provisions which provide for lower surrender charge fees to be assessed later in the contract term. The following table illustrates National Western's recent international life termination experience.

| | Amount in $'s | Annualized Termination Rate |
|---|---|---|
| | (millions) | |
| *Volume In Force Terminations* | | |
| Nine Months Ended September 30, 2021 | 850.6 | 9.1 % |
| Year ended December 31, 2020 | 1,295.2 | 9.5 % |
| Year ended December 31, 2019 | 1,671.5 | 10.9 % |
| Year ended December 31, 2018 | 1,706.3 | 10.0 % |
| Year ended December 31, 2017 | 2,309.7 | 12.2 % |
| Year ended December 31, 2016 | 2,340.6 | 11.6 % |

As noted previously, premiums collected on universal life products are not reflected as revenues in the Company's Condensed Consolidated Statements of Earnings in accordance with GAAP. Actual international universal life premiums collected are detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Universal life insurance: | | | | |
| First year and single premiums | $ — | — | — | — |
| Renewal premiums | 12,720 | 13,756 | 37,754 | 40,733 |
| | | | | |
| Totals | $ 12,720 | 13,756 | 37,754 | 40,733 |

National Western's most popular international products were its fixed-index universal life products in which the policyholder could elect to have the interest rate credited to their policy account values linked in part to the performance of an outside equity index. These products issued were not generally available in the local markets when sold. Included in the totals in the above table are collected renewal premiums for fixed-index universal life products of approximately $21.7 million and $23.9 million for the first nine months of 2021 and 2020, respectively. The declining trend in renewal premiums during these periods corresponds with the decline in policies in force due to increased termination activity as discussed above.

As previously noted, net investment income and contract interest include period-to-period changes in fair values pertaining to call options purchased to hedge the interest crediting feature on the fixed-index universal life products. With the relatively large size of the fixed-index universal life block of business, the period-to-period changes in fair values of the underlying options have a significant effect on net investment income and universal life contract interest. A detail of net investment income for international life insurance operations is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Net investment income (excluding derivatives) | $ 5,841 | 6,761 | 17,404 | 20,407 |
| Index option derivative gain (loss) | 3,331 | 3,593 | 17,731 | (7,900) |
| Net investment income | $ 9,172 | 10,354 | 35,135 | 12,507 |

The gain or loss on index options follows the movement of the reference indice with realized gains or losses being recognized on the anniversary of each index option based upon the reference indice level at expiration date relative to the index level at the time the index option was purchased. Unrealized gains and losses are recorded for index options outstanding based upon their fair values, largely determined by the reference indice level, at the balance sheet reporting date as compared to the original purchase cost of each respective option.

Life and policy benefits primarily consist of death claims on policies. National Western's clientèle for international products are generally wealthy individuals with access to U.S. dollars and quality medical care. Consequently, the amounts of coverage purchased historically tended to be larger amounts. Life and policy benefit expense for the international life segment reflects the larger policies historically purchased, however mortality due to natural causes is comparable to that in the United States. The Company's maximum risk exposure per insured life is capped at $500,000 through reinsurance. The average international life net claim amount (after reinsurance) in the first nine months of 2021 increased to $199,300 from $142,000 in the first nine months of 2020 while the number of claims incurred increased 60%. Nearly all of the increase in number of claims were from deaths due to COVID-19. Net claims, after reinsurance, associated with COVID-19 were $16.3 million in the nine months ended September 30, 2021.

Included in amortization of deferred transaction costs is DPAC amortization. The Company records true-up adjustments to DPAC balances each period to reflect current policy lapse or termination rates, expense levels, and credited rates on policies as compared to anticipated experience as well as unlocking adjustments as necessary. The following table identifies the effects of unlocking adjustments on international life insurance DPAC balances recorded through amortization expense separate from recurring amortization expense components for the three and nine months ended September 30, 2021 and 2020.

| *Amortization of DPAC* | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Unlocking adjustments | $ (33,800) | (20) | (33,800) | (20) |
| DPAC amortization expense | 5,904 | 6,516 | 17,459 | 19,412 |
| Totals | $ (27,896) | 6,496 | (16,341) | 19,392 |

During the quarter ended September 30, 2021, the Company unlocked DPAC balances associated with its International Life segment for lapse rates, mortality, investment portfolio yields and cost of insurance ("COI") charge increases. The effect of the prospective unlocking was to increase DPAC balances (and decrease amortization expense) by $33.8 million, largely driven by the increased COI charges. During the quarter ended September 30, 2020, the Company unlocked DPAC balances for lapse rates, mortality, and investment portfolio yields the overall net effect of which was to marginally increase the DPAC balance by $20,000.

Contract interest expense includes fluctuations that are the result of the effect upon the embedded derivative for the performance of underlying equity indices associated with fixed-index universal life products. For liability purposes, the embedded option in the Company's policyholder obligations for this feature is bifurcated and reserved for separately. Accordingly, the impact of the embedded derivative component in the equity-index universal life product is reflected in the contract interest expense for approximately the same amounts as the purchased call options are reported in net investment income for each respective period. Amounts realized on purchase call options generally approximate the amounts credited to policyholders.

***Annuity Operations***

A comparative analysis of results of operations for National Western's annuity segment is detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Premiums and other revenues: | | | | |
| Premiums and contract revenues | $ 4,243 | 4,187 | 11,915 | 13,536 |
| Net investment income | 62,150 | 87,889 | 282,073 | 196,187 |
| Other revenues | 1,305 | 84 | 4,068 | 80 |
| Total premiums and other revenues | 67,698 | 92,160 | 298,056 | 209,803 |
| Benefits and expenses: | | | | |
| Life and other policy benefits | 36,079 | 3,383 | 55,909 | 20,452 |
| Amortization of deferred transaction costs | 14,916 | 31,794 | 47,741 | 70,159 |
| Annuity contract interest | 15,704 | 79,550 | 68,410 | 117,162 |
| Other operating expenses | 13,544 | 9,205 | 38,338 | 28,787 |
| Total benefits and expenses | 80,243 | 123,932 | 210,398 | 236,560 |
| Segment earnings (loss) before Federal income taxes | (12,545) | (31,772) | 87,658 | (26,757) |
| Provision for Federal income taxes | (2,560) | (5,294) | 18,031 | (4,440) |
| Segment earnings (loss) | $ (9,985) | (26,478) | 69,627 | (22,317) |

Premiums and contract charges primarily consist of surrender charge income recognized on terminated policies. The amount of the surrender charge income recognized is determined by the volume of surrendered contracts as well as the duration of each contract at the time of surrender given the pattern of declining surrender charge rates over time that is common to most annuity contracts. The Company's lapse rate for annuity contracts in the first nine months of 2021 was 8.9% which was slightly higher compared to the 8.3% rate during the same period in 2020. An outcome of the COVID-19 pandemic crisis has been a movement of consumers toward fortifying liquidity positions. This has manifested in greater withdrawal and surrender activity. In addition, annuity contracts with fixed interest rates are more prone to terminate as contracts approach the end of their surrender charge period and in periods of rising interest rates.

Deposits collected on annuity contracts are not reflected as revenues in the Company's Condensed Consolidated Statements of Earnings in accordance with GAAP. Actual annuity deposits collected for the three and nine months ended September 30, 2021 and 2020 are detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Fixed-index annuities | $ 103,932 | 76,199 | 337,661 | 224,591 |
| Other deferred annuities | 1,012 | 2,210 | 2,973 | 6,293 |
| Immediate annuities | 5,843 | 2,348 | 23,024 | 15,423 |
| Totals | $ 110,787 | 80,757 | 363,658 | 246,307 |

Fixed-index products are attractive for consumers when interest rate levels remain low and equity markets produce positive returns. Since National Western does not offer variable products or mutual funds, fixed-index products provide an important alternative to the Company's existing fixed interest rate annuity products. Fixed-index annuity deposits as a percentage of total annuity deposits were 93% and 91% for the nine months ended September 30, 2021 and 2020, respectively. The percentage of fixed-index products to total annuity sales reflects the low interest rate environment and the overall positive performance in the equities market.

Some of the Company's deferred products, including fixed-index annuity products, contain a first year interest bonus, in addition to the base first year interest rate, which is credited to the account balance when premiums are applied. These sales inducements are deferred in conjunction with other capitalized policy acquisition costs. The amounts currently deferred to be amortized over future periods amounted to approximately $14.6 million and $5.7 million during the first nine months of 2021 and 2020, respectively. Amortization of deferred sales inducements is included as a component of annuity contract interest as described later in this discussion of Annuity Operations.

A detail of net investment income for annuity operations is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Net investment income (excluding derivatives and trading securities) | $ 53,500 | 69,403 | 163,564 | 212,405 |
| Index option derivative gain (loss) | 5,219 | 18,486 | 32,467 | (16,218) |
| Embedded derivative liability decrease | 4,146 | — | 76,486 | — |
| Trading securities market adjustment | (715) | — | 9,556 | — |
| Net investment income | $ 62,150 | 87,889 | 282,073 | 196,187 |

In the three and nine months ended September 30, 2021, net investment income was reduced by $14.3 million and $41.4 million, respectively, for amounts ceded to the reinsurer in the funds withheld reinsurance transaction executed December 31, 2020.

As seen in the above table, net investment income also includes the derivative gains and losses on index options purchased to back the index crediting mechanism on fixed-index products. The derivative gain or loss on index options follows the movement of the reference indice with realized gains or losses being recognized on the anniversary of each index option based upon the reference indice at the expiration date relative to the index level at the time the index option was purchased. Unrealized gains and losses are recorded for index options outstanding based upon their fair value, largely determined by the reference indice level, at the balance sheet reporting date as compared to the original purchase cost of each respective option.

Since the embedded derivative option in the policies is bifurcated when determining the contract reserve liability, the impact of the market value change of index options on asset values generally aligns closely with the movement of the embedded derivative liability such that the net effect upon pretax earnings is negligible (i.e. net realized and unrealized gains/(losses) included in net investment income approximate the change in contract interest associated with the corresponding embedded derivative liability change). See further discussion below regarding contract interest activity.

The funds withheld reinsurance agreement executed December 31, 2020 introduced embedded derivative accounting with respect to the annuity policyholder obligations reinsured. During the three and nine months ended September 30, 2021, the embedded derivative liability decreased by $4.1 million and $76.5 million, respectively, which was recorded as a component of investment income. Debt securities supporting the funds withheld policyholder obligations classified as trading securities incurred a $(0.7) million market value decrease in the three months ended September 30, 2021 and a $9.6 million market value increase in the nine months ended September 30, 2021, which was also recorded as a component of net investment income. The total of these two amounts, the embedded liability decrease and the change in market value of trading securities, or $3.4 million and $86.1 million in the three and nine months ended September 30, 2021, increased net investment income for the Annuity segment.

Other revenues in the three and nine months ended September 30, 2021 include $1.3 million and $4.0 million, respectively, of maintenance expense allowance revenue. Under terms of the funds withheld reinsurance contract, National Western earns from the reinsurer a monthly expense allowance equal to the average policy count of the funds withheld reinsured block of business multiplied by a stated amount per policy.

Included in amortization of deferred transaction costs is DPAC amortization. Consistent with the domestic and international life segments, the Company records true-up adjustments to DPAC balances each period to reflect current policy lapse and termination rates, expense levels and credited rates on policies as compared to anticipated experience, as well as unlocking adjustments as necessary. The following table identifies the effects of unlocking adjustments on annuity DPAC balances recorded through amortization expense separate from recurring amortization expense components for the three and nine months ended September 30, 2021 and 2020.

| *Amortization of deferred transaction costs* | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Unlocking adjustments | $ (3,205) | 14,987 | (3,205) | 14,987 |
| DPAC amortization expense | 14,989 | 16,807 | 40,684 | 55,172 |
| COR amortization expense | 3,132 | — | 10,262 | — |
| Totals | $ 14,916 | 31,794 | 47,741 | 70,159 |

During the quarter ended September 30, 2021, the Company unlocked DPAC balances associated with its Annuity segment for assumptions pertaining to lapse rates, annuitization rates, portfolio investment yield rates, and expenses. The effect of the prospective unlocking was to increase DPAC balances by $3.2 million (and decrease amortization expense). The Company also unlocked its DPAC balances in the third quarter of 2020 the effect of which was to decrease DPAC balances by $15.0 million (and increase amortization expense).

Amortization of DPAC balances is proportional to estimated expected gross profits ("EGPs") for a line of business. The EGPs of the block of annuity policies have been steadily decreasing with the declining amount of policies in force, as well as DPAC unlocking in recent years for unfavorable experience. In addition, experience which deviates from the EGPs assumed, such as the amounts of asset fees collected, can similarly increase or decrease the amortization of DPAC. In the three and nine months ended September 30, 2021, amortization expense was reduced by $1.6 million and $5.0 million, respectively, for DPAC ceded to a reinsurer under the funds withheld reinsurance agreement entered into at December 31, 2020.

Amortization of deferred transaction costs includes amortization of the cost of reinsurance recorded at year-end 2020 associated with the funds withheld reinsurance agreement. At December 31, 2020, the Company recorded as an asset on the Consolidated Balance Sheet a deferred Cost of Reinsurance ("COR") amount of $102.8 million associated with the funds withheld reinsurance transaction. This represents the amount of assets transferred at the closing date of the funds withheld agreement (debt securities, policy loans, and cash) in excess of the GAAP liability ceded plus a $48 million ceding commission paid to the reinsurer. The COR balance is amortized commensurate with the runoff of the ceded block of funds withheld business. In the three and nine months ended September 30, 2021, COR amortization expense of $3.1 million and $10.3 million, respectively, is included in Amortization of deferred transaction costs.

Annuity contract interest includes the equity component return associated with the call options purchased to hedge National Western's fixed-index annuities. The detail of fixed-index annuity contract interest as compared to contract interest for all other annuities is as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Fixed-index annuities | $ 15,920 | 33,435 | 73,862 | 31,076 |
| All other annuities | 700 | 40,010 | (877) | 73,331 |
| Gross contract interest | 16,620 | 73,445 | 72,985 | 104,407 |
| Bonus interest deferred and capitalized | (3,869) | (2,829) | (14,580) | (5,700) |
| Bonus interest amortization | 2,953 | 8,934 | 10,005 | 18,455 |
| Total contract interest | $ 15,704 | 79,550 | 68,410 | 117,162 |

The fluctuation in reported contract interest amounts for fixed-index annuities is driven by sales levels, the level of the business in force and the effect of positive or negative market returns of option values on projected interest credits. As noted in the net investment income discussion, the amounts shown for contract interest for fixed-index annuities generally align with the derivative gains/(losses) included in net investment income as due to the market change of index options aligning closely with the movement of the embedded derivative liability held for these products.

Collection of asset management fees on positive returns of expiring options is subtracted from contract interest credited to policyholders. This offset serves to lessen the increase in contract interest expense relative to the option gains reported in the Company's net investment income. Asset management fees collected during the three and nine months ended September 30, 2021 were $0.0 million and $5.8 million compared to $6.7 million and $24.7 million in the corresponding periods of 2020. As noted in the discussion in the Consolidated Operations section, the Company changed its option hedging methodology during 2020 to an "out-of-the-money" approach. By the end of the second quarter of 2021, all outstanding options had been converted to this methodology which no longer hedges for the collection of asset management fees. As a result, there were no asset management fees collected during the third quarter of 2021.

As previously noted, accounting rules require the embedded derivative liability to include a projection of asset management fees estimated to be collected in the succeeding fiscal year due to the Company's historical practice of purchasing options priced to incorporate an expected probability of collecting asset management fees (referred to as "at the money hedging"). This projection for the embedded derivative liability is based upon the most recent performance of the reference equity index. Increases in projected asset management fees to be collected reduce contract interest expense while decreases in projected asset management fees to be collected increase contract interest expense. In the three month periods ended September 30, 2021 and 2020, contract interest was increased $0.0 million and $3.7 million, respectively, for the projected change in asset management fees to be collected. In the nine month periods ended September 30, 2021 and 2020, contract interest was increased $6.5 million and $29.3 million, respectively, for the projected change in asset management fees to be collected. Since the Company changed its embedded derivative hedging process to incorporate "out-of-the-money" hedging, probability projections of collected asset management fees are no longer applicable as of the third quarter of 2021 (as the inventory of annual at the money hedges rolled over to only out-of-the-money hedges).

Annuity contract interest includes true-up adjustments for the deferred sales inducement balance which are done each period similar to that done with respect to DPAC balances with the adjustment reflected in current period contract interest expense. To the extent required, the Company may also record unlocking adjustments to deferred sales inducement balances in conjunction with DPAC balance unlockings. In conjunction with the unlocking adjustments previously discussed, the Company unlocked its deferred sales inducement balance in the third quarters of 2021 and 2020 the effect of which was to increase the balance by $1.0 million in 2021 (and reduce contract interest expense) and to decrease the balance by $4.4 million in 2020 (and increase contract interest expense).

***ONL & Affiliates***

Ozark National and NIS are combined into a separate segment "ONL & Affiliates" given their inter-related marketing and sales approach which consists of a coordinated sale of a non-participating whole life insurance product (Ozark National) and a mutual fund investment product (NIS). An analysis of results of operations for the ONL & Affiliates segment is detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Premiums and other revenues: | | | | |
| Premiums and contract charges | $ 19,159 | 19,524 | 57,923 | 59,448 |
| Net investment income | 6,763 | 6,434 | 20,117 | 19,284 |
| Other revenues | 3,169 | 2,628 | 9,368 | 7,369 |
| Total premiums and other revenues | 29,091 | 28,586 | 87,408 | 86,101 |
| Benefits and expenses: | | | | |
| Life and other policy benefits | 17,530 | 17,494 | 50,699 | 50,429 |
| Amortization of deferred transaction costs | 2,112 | 1,970 | 7,231 | 6,064 |
| Other operating expenses | 5,229 | 4,498 | 14,908 | 13,361 |
| Total benefits and expenses | 24,871 | 23,962 | 72,838 | 69,854 |
| Segment earnings before Federal income taxes | 4,220 | 4,624 | 14,570 | 16,247 |
| Provision for Federal income taxes | 839 | 963 | 2,954 | 4,103 |
| Segment earnings | $ 3,381 | 3,661 | 11,616 | 12,144 |

Revenues from ONL & Affiliates principally include life insurance premiums on traditional type products. Unlike universal life, revenues from traditional products are simply life premiums recognized as income over the premium-paying period of the related policies. The detail of premiums is provided below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Traditional life insurance premiums | $ 19,686 | 20,049 | 59,656 | 61,153 |
| Other insurance premiums and considerations | 98 | 105 | 327 | 328 |
| Reinsurance premiums | (625) | (630) | (2,060) | (2,033) |
| Totals | $ 19,159 | 19,524 | 57,923 | 59,448 |

Ozark National's traditional life block of business at September 30, 2021 included approximately 176,220 policies in force representing over $5.9 billion of life insurance coverage. The repetitive pay nature of Ozark National's business promotes a higher level of persistency with an annualized lapse rate of 4.2% through September 30, 2021 as compared to the 4.1% rate experienced in the first nine months of 2020. Traditional life premiums by first year and renewal are detailed below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Traditional life insurance premiums: | | | | |
| First year premiums | $ 904 | 905 | 2,462 | 3,151 |
| Renewal premiums | 18,782 | 19,144 | 57,194 | 58,002 |
| Totals | $ 19,686 | 20,049 | 59,656 | 61,153 |

Other revenues consists primarily of brokerage revenue of NIS. Brokerage revenues of $9.3 million and $7.2 million for the nine months ended September 30, 2021 and 2020, respectively, had associated brokerage expense of $4.5 million and $3.7 million which is included in Other operating expenses. Brokerage revenues of $3.1 million and $2.6 million for the three months ended September 30, 2021 and 2020, respectively, had associated brokerage expense of $1.5 million and $1.4 million.

The average face value of Ozark National's policies in force at September 30, 2021 was approximately $33,600. Life and policy benefits are subject to variation from quarter to quarter. Incurred net death claims, after reinsurance, for the first nine months of 2021 were $29.2 million representing an average net claim of $16,000. Incurred net death claims in the nine month period ended September 30, 2020 were $25.8 million representing a net average claim of $15,300. Included in the activity for 2021 were reported COVID-19 net claims of approximately $5.9 million. Of this amount, $1.1 million was reported in the quarter ended September 30, 2021. Ozark National's maximum retention on any single insured life is $200,000 with limited exceptions related to the conversion of child protection and guaranteed insurability riders. The balance of life and policy benefits during the three and nine months ended September 30, 2021 and 2020 consisted of increases in insurance reserves and payments of other policy benefits.

Amortization of deferred transaction costs for this segment includes amortization of DPAC and the value of business acquired ("VOBA"). VOBA represents the difference between the acquired assets and liabilities of Ozark National at the acquisition date measured in accordance with the Company's accounting policies and the fair value of these same assets and liabilities. The VOBA balance sheet amount is amortized following a methodology similar to that used for amortizing deferred policy acquisition costs. Subsequent to its acquisition effective January 31, 2019, Ozark National began deferring policy acquisition costs and amortizing these deferrals similar to the methodology employed by National Western. The following table identifies the amortization expense of Ozark National's DPAC and VOBA for the three and nine months ended September 30, 2021 and 2020.

| *Amortization of deferred transaction costs* | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| Unlocking | $ — | — | — | — |
| VOBA amortization expense | 1,908 | 1,845 | 6,709 | 5,646 |
| DPAC amortization expense | 204 | 125 | 522 | 418 |
| Totals | $ 2,112 | 1,970 | 7,231 | 6,064 |

***Other Operations***

The Company's primary business encompasses its domestic and international life insurance operations, its annuity operations, and ONL & Affiliates. However, the Company also has real estate and other investment operations through its wholly owned subsidiaries.

Pre-tax operating amounts include the results of BP III, the entity owning and operating the Company's home office facility in Austin, Texas. BP III incurred pre-tax losses of $(0.6) million and $(0.9) million for the nine months ended September 30, 2021 and 2020, respectively. National Western maintains its home office in this facility leasing approximately 40% of the space available. The lease payments made by National Western to BP III have been eliminated in consolidation.

The remaining pre-tax earnings of $15.6 million and $14.8 million in Other Operations during the nine-month periods includes investment income from real estate, municipal bonds, and common and preferred equities held in subsidiary company portfolios principally for tax-advantage purposes. Included in these amounts are semi-annual distributions from a life interest in the Libbie Shearn Moody Trust which is held in NWLSM, Inc. Pre-tax distributions from this trust were $2.7 million and $2.8 million in the nine-month periods ended September 30, 2021 and 2020, respectively. The Company holds a modest portfolio of equity securities, primarily in NWL Financial, Inc., whose fair value changes are recorded in net investment income. For the three months ended September 30, 2021 and 2020, the market value changes for these securities were $0.1 million and $0.9 million, respectively, and for the nine months there ended were $3.4 million and $(3.2) million, respectively. Pre-tax earnings for the three and nine months ended September 30, 2020 also includes $4.1 million pertaining to the release of a contingent purchase price liability associated with the Ozark National acquisition which the buyer (National Western) and seller mutually agreed had been satisfied.

## INVESTMENTS

### General

The Company's investment philosophy emphasizes the careful handling of policyowners' and stockholders' funds to achieve security of principal, to obtain the maximum possible yield while maintaining security of principal, and to maintain liquidity in a measure consistent with current and long-term requirements of the Company.

The Company's overall conservative investment philosophy is reflected in the allocation of its investments, which is detailed below. The Company emphasizes investment grade debt securities.

| | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | Carrying Value | % | Carrying Value | % |
| | (In thousands) | | (In thousands) | |
| Debt securities available-for-sale | $ 9,364,083 | 83.5 | $ 10,770,923 | 94.2 |
| Debt securities trading | 1,085,654 | 9.7 | — | — |
| Mortgage loans | 462,882 | 4.1 | 332,521 | 2.9 |
| Policy loans | 71,668 | 0.6 | 74,083 | 0.6 |
| Derivatives, index options | 82,390 | 0.7 | 132,821 | 1.2 |
| Real estate | 28,750 | 0.3 | 33,783 | 0.3 |
| Equity securities | 21,186 | 0.2 | 17,744 | 0.2 |
| Other | 96,022 | 0.9 | 70,330 | 0.6 |
| Totals | $ 11,212,635 | 100.0 | $ 11,432,205 | 100.0 |

Invested assets at September 30, 2021 include Ozark National and NIS amounts as follows: Debt securities of $813.4 million; Policy loans of $23.7 million; and Real estate of $0.0 million. These invested asset amounts at December 31, 2020 were: Debt securities of $811.6 million; Policy loans of $25.5 million; and Real Estate of $4.6 million.

**Debt Securities**

GAAP accounting requires investments in debt securities to be classified into one of three categories: (a) trading securities; (b) securities available-for-sale; or (c) securities held-to-maturity. The Company generally purchases securities with the intent to hold to maturity and has historically classified its debt securities into either the held-to-maturity or available-for-sale categories. As an outcome of the funds withheld reinsurance agreement executed December 31, 2020, the Company reclassified all of its debt security holdings at that time into the available-for-sale category. The discussion that follows reflects this category classification.

The Company maintains a diversified portfolio which consists mostly of corporate, mortgage-backed, and public utility fixed income securities. Investments in mortgage-backed securities primarily include U.S. Government agency pass-through securities and collateralized mortgage obligations ("CMO"). The Company's investment guidelines prescribe limitations by type of security as a percent of the total investment portfolio and all holdings were within these threshold limits. As of September 30, 2021 and December 31, 2020, the Company's available-for-sale debt securities portfolio consisted of the following classes of securities:

| | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | Carrying Value | % | Carrying Value | % |
| | (In thousands) | | (In thousands) | |
| Corporate | $ 6,918,616 | 73.8 | $ 8,098,973 | 75.2 |
| Residential mortgage-backed securities | 669,153 | 7.1 | 953,788 | 8.9 |
| Public utilities | 831,422 | 8.9 | 909,910 | 8.4 |
| State and political subdivisions | 504,325 | 5.4 | 566,089 | 5.3 |
| U.S. agencies | 51,515 | 0.6 | 75,441 | 0.7 |
| Asset-backed securities | 296,073 | 3.2 | 120,524 | 1.1 |
| Commercial mortgage-backed | 28,208 | 0.3 | 31,471 | 0.3 |
| Foreign governments | 61,563 | 0.7 | 11,449 | 0.1 |
| U.S. Treasury | 3,208 | — | 3,278 | — |
| Totals | $ 9,364,083 | 100.0 | $ 10,770,923 | 100.0 |

The Company holds minimal levels of U.S. Treasury securities due to their low yields and deposits most of these holdings with various state insurance departments in order to meet security deposit on hand requirements in these jurisdictions.

The Company has de-emphasized mortgage-backed securities for a number of years given the low interest rate environment and the lack of incremental yield relative to other classes of debt securities. Rating agencies generally view mortgage-backed securities as having additional risk for insurers holding interest sensitive liabilities given the potential for asset/liability disintermediation. Consequently, the Company holds predominantly agency mortgage-backed securities. Because mortgage-backed securities are subject to prepayment and extension risk, the Company has substantially reduced these risks by investing in collateralized mortgage obligations ("CMO"), which have more predictable cash flow patterns than pass-through securities. These securities, known as planned amortization class I ("PAC I"), very accurately defined maturity ("VADM"), and sequential tranches, are designed to amortize in a more predictable manner than other CMO classes or pass-throughs. The Company does not purchase tranches, such as PAC II and support tranches, that subject the portfolio to greater than average prepayment risk. Using this strategy, the Company can more effectively manage and reduce prepayment and extension risks, thereby helping to maintain the appropriate matching of the Company's assets and liabilities.

The majority of the Company's investable cash flows are directed toward the purchase of long-term debt securities. The Company's investment practice has been to invest in debt securities that are investment grade, meet quality and yield objectives, and provide adequate liquidity for obligations to policyholders. Particular attention is paid to avoiding concentration in any one industry classification or in large singular credit exposures. Debt securities with intermediate maturities are targeted by the Company as they more closely match the intermediate nature of the Company's policy liabilities and provide an appropriate strategy for managing cash flows. Long-term debt securities purchased to fund National Western insurance company operations are summarized below.

| | Nine Months Ended September 30, 2021 | Year Ended December 31, 2020 |
|---|---|---|
| | ($ In thousands) | |
| Cost of acquisitions | $ 936,078 | $ 727,947 |
| Average credit quality | BBB+ | BBB+ |
| Effective annual yield | 2.99 % | 3.33 % |
| Spread to treasuries | 1.26 % | 2.10 % |
| Effective duration | 10.9 years | 12.2 years |

Over the past several years, the Company has been purchasing a greater proportion of longer maturity debt securities to match the increased duration of its growing life insurance policy liabilities. Purchases in previous periods, prior to 2019, were concentrated in effective durations between eight and nine years.

In addition to diversification, an important aspect of the Company's investment approach is managing the credit quality of its investment in debt securities. Thorough credit analysis is performed on potential corporate investments including examination of a company's credit and industry outlook, financial ratios and trends, and event risks. This emphasis is reflected in the high average credit rating of the Company's debt securities portfolio with 97.7%, as of September 30, 2021, held in investment grade securities. In the table below, investments in available-for-sale debt securities are classified according to credit ratings by nationally recognized statistical rating organizations.

| | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | Carrying Value | % | Carrying Value | % |
| | (In thousands) | | (In thousands) | |
| AAA | $ 115,909 | 1.2 | $ 116,147 | 1.1 |
| AA | 2,596,212 | 27.7 | 1,818,879 | 16.9 |
| A | 1,796,525 | 19.2 | 3,188,008 | 29.6 |
| BBB | 4,641,042 | 49.6 | 5,344,412 | 49.6 |
| BB and other below investment grade | 214,395 | 2.3 | 303,477 | 2.8 |
| Totals | $ 9,364,083 | 100.0 | $ 10,770,923 | 100.0 |

Historically, the Company's investment guidelines have not permitted the purchase of below investment grade securities. Recently, these guidelines were amended to allow for purchases of below investment grade securities that are part of an alternative investment ("Schedule BA assets"). The Company continues its longstanding practice of not purchasing any other below investment grade securities. Investments held in available-for-sale debt securities may become below investment grade as a result of subsequent downgrades of the securities. These below investment grade holdings, including those in the Schedule BA assets category, are further summarized below.

| | Available-for-Sale Below Investment Grade Debt Securities | | | |
|---|---|---|---|---|
| | Amortized Cost | Carrying Value | Fair Value | % of Invested Assets |
| | (In thousands, except percentages) | | | |
| September 30, 2021 | $ 208,087 | 214,395 | 214,395 | 1.9 % |
| December 31, 2020 | $ 300,417 | 303,477 | 303,477 | 2.7 % |

The Company's percentage of below investment grade securities as of September 30, 2021 compared with the percentage at December 31, 2020 decreased mostly due to the disposal of below investment grade securities in the first nine months of 2021. The Company's holdings of below investment grade securities are relatively small and as a percentage of total invested assets remain low compared to industry averages.

Holdings in below investment grade securities as of September 30, 2021 are summarized below by category, including their comparable fair value as of December 31, 2020. The Company continually monitors developments in these industries for issues that may affect security valuation.

| | Available-for-Sale Below Investment Grade Debt Securities | | | |
|---|---|---|---|---|
| | Amortized Cost | Carrying Value | Fair Value | Fair Value |
| Industry Category | September 30, 2021 | September 30, 2021 | September 30, 2021 | December 31, 2020 |
| | (In thousands) | | | |
| Retail | $ 4,478 | 4,650 | 4,650 | 4,460 |
| Asset-backed securities | 1,292 | 1,319 | 1,319 | 1,314 |
| Oil & gas | 105,611 | 108,238 | 108,238 | 104,072 |
| Manufacturing | 62,177 | 64,099 | 64,099 | 64,925 |
| Utilities | 15,984 | 17,285 | 17,285 | 17,527 |
| Other | 18,545 | 18,804 | 18,804 | 9,823 |
| Total before Allowance for credit losses | 208,087 | 214,395 | 214,395 | 202,121 |
| Allowance for credit losses | — | — | — | — |
| Totals | $ 208,087 | 214,395 | 214,395 | 202,121 |

The Company closely monitors its below investment grade holdings by reviewing investment performance indicators, including information such as issuer operating performance, debt ratings, analyst reports and other economic factors that may affect these specific investments. While losses are not currently anticipated, based on the existing status and condition of these securities, credit deterioration of some securities or the markets in general is possible, which may result in future allowances or write-downs.

The Company adopted new accounting guidance effective January 1, 2020 for credit loss recognition of certain financial assets, including debt securities classified in the "held-to-maturity" category. The Company employed a cohort cumulative loss rate method in estimating current expected credit losses with respect to its held-to-maturity debt securities. This method applied publicly available industry wide statistics of default incidence by defined segmentations of debt security investments combined with future assumptions regarding economic conditions (i.e. GDP forecasts) both in the near term and the long term. The following table presents the allowance for credit losses for the three and nine months ended September 30, 2020.

| | Three Months Ended September 30, 2020 | Nine Months Ended September 30, 2020 |
|---|---|---|
| | (In thousands) | |
| *Debt Securities Allowance for Credit Losses:* | | |
| Balance, beginning of the period | $ 4,940 | — |
| Provision at January 1, 2020 for adoption of new accounting guidance | — | 3,334 |
| (Releases)/provision during the period | 146 | 1,752 |
| Balance, end of period | $ 5,086 | 5,086 |

As described previously, at December 31, 2020, the Company was required to reclassify all of its held-to-maturity debt securities to the available-for-sale category eliminating the need for an allowance in 2021.

The Company's holdings in available-for-sale provide flexibility (a) to react to market opportunities and conditions and (b) to practice active management within the portfolio to provide adequate liquidity to meet policyholder obligations and other cash needs.

| | September 30, 2021 | | | |
|---|---|---|---|---|
| | Fair Value | Amortized Cost | Allowance for Credit Losses | Unrealized Gains (Losses) |
| | (In thousands) | | | |
| Debt securities available-for-sale | $ 9,364,083 | 8,795,673 | — | 568,410 |
| Debt securities trading | 1,085,654 | 1,076,099 | — | 9,556 |
| Totals | $ 10,449,737 | 9,871,772 | — | 577,966 |

Under terms of the funds withheld reinsurance agreement, effective December 31, 2020, the Company, on behalf of the reinsurer, transferred debt securities approximating $1.7 billion to a funds withheld account. Due to the nature of the reinsurance transaction, these debt securities remained as invested assets on the Company's financial statements and were included in the available-for-sale category. In accordance with the terms of the agreement, the reinsurer, or their appointed sub-advisor, was granted investment management authority with respect to these securities following agreed upon investment guidelines defined in the reinsurance agreement. During the first nine months of 2021, the reinsurer actively engaged in selling debt securities in the funds withheld account and purchasing other debt securities. The debt securities acquired by the reinsurer remain as invested assets on the Company's financial statements and have been classified as trading debt securities. The designation as trading debt securities allows the market value fluctuation of these securities to be recorded directly in the Condensed Consolidated Statements of Earnings. This results in offsetting the embedded derivative liability change due to market value fluctuations which is also recorded directly in the Condensed Consolidated Statements of Earnings.

The Company's trading debt securities portfolio consisted of the following classes of securities:

| | September 30, 2021 | | | December 31, 2020 | | |
|---|---|---|---|---|---|---|
| | Carrying Value | | % | Carrying Value | | % |
| | (In thousands) | | | (In thousands) | | |
| Corporate | $ | 426,458 | 39.3 | $ | — | — |
| Residential mortgage-backed securities | | 53,667 | 4.9 | | — | — |
| Public utilities | | 36,227 | 3.3 | | — | — |
| State and political subdivisions | | 17,013 | 1.6 | | — | — |
| Asset-backed securities | | 328,596 | 30.3 | | — | — |
| Commercial mortgage-backed | | 223,693 | 20.6 | | — | — |
| Totals | $ | 1,085,654 | 100.0 | $ | — | — |

In the table below, investments in trading debt securities are classified according to credit ratings by nationally recognized statistical rating organizations.

| | September 30, 2021 | | | December 31, 2020 | | |
|---|---|---|---|---|---|---|
| | Carrying Value | | % | Carrying Value | | % |
| | (In thousands) | | | (In thousands) | | |
| AAA | $ | 7,089 | 0.7 | $ | — | — |
| AA | | 225,337 | 20.8 | | — | — |
| A | | 213,498 | 19.7 | | — | — |
| BBB | | 595,814 | 54.8 | | — | — |
| BB and other below investment grade | | 43,916 | 4.0 | | — | — |
| Totals | $ | 1,085,654 | 100.0 | $ | — | — |

The investments in the trading debt securities below investment grade are summarized below.

| | Below Investment Grade Trading Debt Securities | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | | Carrying Value | Fair Value | % of Invested Assets |
| | (In thousands, except percentages) | | | | |
| September 30, 2021 | $ | 43,569 | 43,916 | 43,916 | 0.4 % |

**Mortgage Loans and Real Estate**

The Company originates loans on high quality, income-producing properties such as shopping centers, freestanding retail stores, office buildings, industrial and sales or service facilities, selected apartment buildings, hotels, and health care facilities. The location of these properties is typically in major metropolitan areas that offer a potential for property value appreciation. Credit and default risk is minimized through strict underwriting guidelines and diversification of underlying property types and geographic locations. In addition to being secured by the property, mortgage loans with leases on the underlying property are often further secured by the lease payments. This approach has proved over time to result in quality mortgage loans with few defaults. Mortgage loan interest income is recognized on an accrual basis with any premium or discount amortized over the life of the loan. Prepayment and late fees are recorded on the date of collection.

The Company targets a minimum specified yield on mortgage loan investments determined by reference to currently available debt security instrument yields plus a desired amount of incremental basis points. During the past several years, the low interest rate environment, along with a competitive marketplace, resulted in fewer loan opportunities being available that met the Company's required rate of return. During the first half of 2020, mortgage loan originations were further impeded by the COVID-19 pandemic and its effects upon the commercial real estate market. Improvements in the commercial mortgage marketplace subsequently materialized which assisted the Company's new origination efforts. Mortgage loans originated by the Company totaled $151.4 million in the nine months ended September 30, 2021 compared to $80.2 million for the year ended December 31, 2020.

Loans in foreclosure, loans considered impaired, or loans past due 90 days or more are placed on a non-accrual status. If a mortgage loan is determined to be on non-accrual status, the mortgage loan does not accrue any revenue in the Condensed Consolidated Statements of Earnings. The loan is independently monitored and evaluated as to potential impairment or foreclosure. If delinquent payments are made and the loan is brought current, then the Company returns the loan to active status and accrues income accordingly. The Company currently has no loans past due 90 days. As a result of the economic climate change induced by the COVID-19 virus, various mortgage loan borrowers of the Company requested a temporary forbearance of principal payments on loans in the range of three to nine months. During the year ended December 31, 2020 there were eight loans representing an aggregate principal balance of $29.2 million with borrowers meeting specified criteria of the Company that forbearance terms were agreed to. All forbearance loans returned to the terms of the original loan agreements during the first quarter of 2021.

The Company held net investments in mortgage loans, after allowances for possible losses, totaling $462.9 million and $332.5 million at September 30, 2021 and December 31, 2020, respectively. The diversification of the portfolio by geographic region and by property type was as follows:

| | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | Amount | % | Amount | % |
| | (In thousands) | | (In thousands) | |
| *Mortgage Loans by Geographic Region:* | | | | |
| West South Central | $ 243,783 | 52.2 | $ 201,501 | 60.1 |
| South Atlantic | 59,751 | 12.8 | 51,857 | 15.5 |
| East North Central | 61,563 | 13.2 | 16,478 | 4.9 |
| West North Central | 12,279 | 2.7 | 12,423 | 3.7 |
| East South Central | 20,152 | 4.3 | 27,590 | 8.2 |
| Pacific | 6,059 | 1.3 | 6,228 | 1.9 |
| Middle Atlantic | 36,296 | 7.8 | 1,975 | 0.6 |
| Mountain | 26,699 | 5.7 | 16,955 | 5.1 |
| Gross balance | 466,582 | 100.0 | 335,007 | 100.0 |
| Market value adjustment | 256 | 0.1 | — | — |
| Allowance for credit losses | (3,956) | (0.9) | (2,486) | (0.7) |
| Totals | $ 462,882 | 99.2 | $ 332,521 | 99.3 |

| | September 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | Amount | % | Amount | % |
| | (In thousands) | | (In thousands) | |
| *Mortgage Loans by Property Type:* | | | | |
| Retail | $ 166,166 | 35.6 | $ 92,173 | 27.5 |
| Office | 139,362 | 29.9 | 111,735 | 33.3 |
| Storage facility | 70,095 | 15.0 | 53,591 | 16.0 |
| Apartments | 39,054 | 8.4 | 29,743 | 8.9 |
| Industrial | 34,394 | 7.4 | 29,131 | 8.7 |
| Hotel | 7,486 | 1.6 | 8,372 | 2.5 |
| Land/Lots | 4,594 | 1.0 | 4,680 | 1.4 |
| All other | 5,431 | 1.1 | 5,582 | 1.7 |
| Gross balance | 466,582 | 100.0 | 335,007 | 100.0 |
| Market value adjustment | 256 | 0.1 | — | — |
| Allowance for credit losses | (3,956) | (0.9) | (2,486) | (0.7) |
| Totals | $ 462,882 | 99.2 | $ 332,521 | 99.3 |

As noted previously, in 2020 the Company adopted new accounting guidance for credit loss recognition criteria for certain financial assets, including mortgage loans. The Company employed the Weighted Average Remaining Maturity ("WARM") method in estimating current expected losses with respect to mortgage loan investments as of January 1, 2020 and each succeeding calendar quarter-end. The WARM method applies publicly available data of default incidence of commercial real estate properties by several defined segmentations combined with future assumptions regarding economic conditions (i.e. GDP forecasts) both in the near term and the long term. Under this accounting guidance, at January 1, 2020, a balance of $1.2 million was recorded which incorporated the previous year-end balance under the prior accounting method. The adjustment resulted in a charge to retained earnings as a change in accounting, net of tax, of $0.4 million. Subsequent changes in the allowance for current expected credit losses are reported in net investment income in the Consolidated Statements of Earnings.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| *Mortgage Loans Allowance for Credit Losses:* | | | | |
| Balance, beginning of the period | $ 3,238 | 2,227 | 2,486 | 675 |
| Provision January 1, 2020 for adoption of new accounting guidance | — | — | — | 504 |
| Provision during the period | 718 | 130 | 1,470 | 1,178 |
| Balance, end of period | $ 3,956 | 2,357 | 3,956 | 2,357 |

The Company's direct investments in real estate are not a significant portion of its total investment portfolio and consist primarily of income-producing properties which are being operated by a wholly owned subsidiary of National Western. The Company's real estate investments totaled approximately $28.8 million and $33.8 million at September 30, 2021 and December 31, 2020, respectively. During the second quarter of 2021 the Company recorded an impairment of $1.4 million on certain real estate and home office property located in Kansas City, Missouri which was re-classified as "held-for-sale" at its combined asset group's fair value less cost to sell of $12.2 million. In the third quarter of 2021 the home office, parking garage and parking lot all located in Kansas City, Missouri were sold for a total net loss of $1.4 million.

The Company recognized operating income of approximately $2.2 million and $2.2 million on real estate properties in the first nine months of 2021 and 2020, respectively. The Company monitors the conditions and market values of these properties on a regular basis and makes repairs and capital improvements to keep the properties in good condition.

**Market Risk**

Market risk is the risk of change in market values of financial instruments due to changes in interest rates, currency exchange rates, commodity prices, or equity prices. The most significant market risk exposure for the Company is interest rate risk. Substantial and sustained increases and decreases in market interest rates can affect the profitability of insurance products and fair value of investments. The yield realized on new investments generally increases or decreases in direct relationship with interest rate changes. The fair values of fixed income debt securities correlate to external market interest rate conditions as market values typically increase when market interest rates decline and decrease when market interest rates rise. However, market values may fluctuate for other reasons, such as changing economic conditions, market dislocations, declination in credit quality, or increasing event-risk concerns.

*Interest Rate Risk*

A gradual increase in interest rates from current levels would generally be a positive development for the Company. Rate increases would be expected to provide incremental net investment income, produce increased sales of fixed rate products, and limit the potential erosion of the Company's interest rate spread on products due to minimum guaranteed crediting rates in products. Alternatively, a rise in interest rates would reduce the fair value of the Company's investment portfolio and if long-term rates rise dramatically within a relatively short time period the Company could be exposed to disintermediation risk. Disintermediation risk is the risk that policyholders will surrender their policies in a rising interest rate environment forcing the Company to liquidate assets when they are in an unrealized loss position.

A decline in interest rates could cause certain mortgage-backed securities in the Company's portfolio to be more likely to pay down or prepay. In this situation, the Company typically will be unable to reinvest the proceeds at comparable yields. Lower interest rates will likely also cause lower net investment income, subject the Company to reinvestment rate risks, and possibly reduce profitability through reduced interest rate margins associated with products with minimum guaranteed crediting rates. Alternatively, the fair value of the Company's investment portfolio will increase when interest rates decline.

The movement of interest rates and fair values of available-for-sale debt securities is reflected in the tables below.

| | September 30, 2021 | June 30, 2021 | December 31, 2020 |
|---|---|---|---|
| | (In thousands except percentages) | | |
| Debt securities - fair value | $ 9,364,083 | 9,617,027 | 10,770,923 |
| Debt securities - amortized cost | $ 8,795,673 | 8,973,860 | 9,874,543 |
| Fair value as a percentage of amortized cost | 106.46 % | 107.17 % | 109.08 % |
| Net unrealized gain (loss) balance | $ 568,410 | 643,167 | 896,380 |
| Ten-year U.S. Treasury bond – (decrease) increase in yield for the period | 0.02 % | (0.27)% | (1.00)% |

The Company's unrealized gain (loss) balance for debt securities held at September 30, 2021 and December 31, 2020 is shown in the following table. The change in unrealized balance pertaining to debt securities available-for-sale is recorded in Other comprehensive income in the Condensed Consolidated Statements of Comprehensive Income while the change in unrealized balance pertaining to debt securities trading is recorded in net investment income in the Condensed Consolidated Statements of Earnings.

| | Net Unrealized Gain (Loss) Balance | | | | |
|---|---|---|---|---|---|
| | At September 30, 2021 | At June 30, 2021 | At December 31, 2020 | Quarter Change in Unrealized Balance | Year-to-date Change in Unrealized Balance |
| | (In thousands) | | | | |
| Debt securities available-for-sale | $ 568,410 | 643,167 | 896,380 | (74,757) | (327,970) |
| Debt securities trading | 9,556 | 10,271 | — | (715) | 9,556 |
| Totals | $ 577,966 | 653,438 | 896,380 | (75,472) | (318,414) |

Changes in interest rates can have a sizable effect on the fair values of the Company's debt securities. The market interest rate of the ten-year U.S. Treasury bond increased 57 basis points from 0.92% at year-end 2020 to 1.49% by the end of the first nine months of 2021. Therefore the decrease in the unrealized gain balance position is an expected portfolio value movement.

The Company manages interest rate risk principally through ongoing cash flow testing as required for insurance regulatory purposes. Computer models are used to perform cash flow testing under various commonly used stress test interest rate scenarios to determine if existing assets would be sufficient to meet projected liability outflows. Sensitivity analysis allows the Company to measure the potential gain or loss in fair value of its interest-sensitive instruments and to protect its economic value and achieve a predictable spread between what is earned on invested assets and what is paid on liabilities. The Company seeks to minimize the impact of interest risk through surrender charges that are imposed to discourage policy surrenders. Interest rate changes can be anticipated in computer models and the corresponding risk addressed by management actions affecting asset and liability instruments. However, potential changes in the values of financial instruments indicated by hypothetical interest rate changes will likely be different from actual changes experienced, and the differences could be significant.

The Company has the ability to adjust interest rates, participation rates, and asset management fees and caps, as applicable, in response to changes in investment portfolio yields for a substantial portion of its business in force. The ability to adjust these rates is subject to competitive forces in the market for the Company’s products. Surrender rates could increase and new sales could be negatively affected if crediting rates are not competitive with the rates on competing products offered by other insurance companies and financial service entities. The Company designs its interest sensitive and annuity products with features encouraging persistency, such as surrender and withdrawal penalty provisions. Typically, surrender charge rates gradually decrease each year the contract is in force.

The Company performed detailed sensitivity analysis as of December 31, 2020, for its interest rate-sensitive assets and liabilities. The changes in market values of the Company's debt securities in the first nine months of 2021 were reasonable given the expected range of results of this analysis.

*Credit Risk*

The Company is exposed to credit risk through counterparties and within its investment portfolio. Credit risk relates to the uncertainty associated with an obligor's continued ability to make timely payments of principal and interest in accordance with the contractual terms of an instrument or contract. As previously discussed, the Company manages credit risk through established investment credit policies and guidelines which address the quality of creditors and counterparties, concentration limits, diversification practices and acceptable risk levels. These policies and guidelines are regularly reviewed and approved by senior management and the Company's Board of Directors.

In connection with the Company's use of call options to hedge the equity return component of its fixed-indexed annuity and life products, the Company is exposed to the risk that a counterparty fails to perform under terms of the option contract. The Company purchases one-year option contracts from multiple counterparties and evaluates the creditworthiness of all counterparties prior to the purchase of the contracts. For consideration in contracting with a counterparty, the rating required by the Company is a credit rating of "A" or higher. Accordingly, all options are purchased from nationally recognized financial institutions with a demonstrated performance for honoring their financial obligations and possessing substantial financial capacity. In addition, each counterparty is required to execute a credit support agreement obligating the counterparty to provide collateral to the Company when the fair value of the Company's exposure to the counterparty exceeds specified amounts. Counterparty credit ratings and credit exposure are monitored continuously by National Western's Investment Department with adjustments to collateral levels managed as incurred under the credit support agreements.

The Company follows the industry practice of reinsuring (ceding) portions of its insurance risks with a variety of reinsurance companies on either a coinsurance or a modified coinsurance basis in order to limit risk. Use of reinsurance does not relieve the Company of its primary liability to pay the full amount of the insurance benefit in the event the reinsurer (counterparty) fails to honor its contractual obligation. Consequently, the Company avoids concentrating reinsurance counterparty credit risk with any one reinsurer and only maintains reinsurance agreements with reputable carriers which are well-capitalized and highly rated by independent rating agencies. With respect to the funds withheld coinsurance arrangement entered into by National Western, assets backing the reserves for the policyholder obligations under the agreement are retained by the Company and are available to meet benefit payment commitments. In addition, National Western is the beneficiary of an incremental collateral trust account provided by the reinsurer providing additional security for the payment of all amounts due under the reinsurance agreement.

The Company is also exposed to credit spread risk related to market prices of investment securities and cash flows associated with changes in credit spreads. Credit spread tightening will reduce net investment income associated with new purchases of fixed debt securities and will increase the fair value of the investment portfolio. Credit spread widening will reduce the fair value of the investment portfolio and will increase net investment income on new purchases.

## LIQUIDITY AND CAPITAL RESOURCES

### Liquidity

Liquidity requirements are met primarily by funds provided from operations. Premium deposits and annuity considerations, investment income, and investment maturities and prepayments are the primary sources of funds while investment purchases, policy benefits in the form of claims, and payments to policyholders and contract holders in connection with surrenders and withdrawals as well as operating expenses are the primary uses of funds. To ensure the Company will be able to pay future commitments, the funds received as premium payments and deposits are invested in high quality investments, primarily fixed income securities. Funds are invested with the intent that the income from investments, plus proceeds from maturities, will meet the ongoing cash flow needs of the Company. The approach of matching asset and liability durations and yields requires an appropriate mix of investments. Although the Company historically has not been put in the position of having to liquidate invested assets to provide cash flow, its investments consist primarily of marketable debt securities that could be readily converted to cash for liquidity needs. National Western maintains a line of credit facility of $75 million which it may access for short-term cash needs. There were no borrowings under the line of credit as of September 30, 2021. In addition, as previously reported, National Western became a member of the Federal Home Loan Bank of Dallas (FHLB) during 2020 through an initial minimum required stock investment of $4.3 million. Through this membership, National Western is able to create a specified borrowing capacity based upon the amount of collateral it elects to establish.

A primary liquidity concern for life insurers is the risk of an extraordinary level of early policyholder withdrawals, particularly with respect to annuity products which can move more rapidly with interest rate changes. The Company includes provisions within its annuity and universal life insurance policies, such as surrender and market value adjustments, that help limit and discourage early withdrawals.

The actual amounts paid by product line in connection with surrenders and withdrawals, before reinsurance, for the three and nine months ended September 30, 2021 and 2020, are noted in the table below.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | (In thousands) | | | |
| *Product Line:* | | | | |
| Traditional Life | $ 3,611 | 4,142 | 12,595 | 12,804 |
| Universal Life | 27,335 | 22,065 | 73,672 | 78,864 |
| Annuities | 157,262 | 146,238 | 497,882 | 490,622 |
| Total | $ 188,208 | 172,445 | 584,149 | 582,290 |

The above contractual withdrawals, as well as the level of surrenders experienced, and the associated cash outflows did not have an adverse impact on overall liquidity. Individual life insurance policies are typically less susceptible to withdrawal than annuity reserves and deposit liabilities because policyholders may need to undergo a new underwriting process in order to obtain a new insurance policy elsewhere. Annuity dollar outflows are generally more sensitive to economic conditions, interest rate levels, and the level of surrender charges assessed upon withdrawal or termination. Cash flow projections and tests under various market interest rate scenarios and assumptions are performed to assist in evaluating liquidity needs and adequacy. With the economic decline precipitated by the COVID-19 pandemic, Company management conducted additional liquidity scenario testing using more severe assumptions and concluded that liquid assets were more than adequate under these scenarios. Accordingly, the Company currently expects available liquidity sources and future cash flows to be more than adequate to meet the demand for funds.

Cash flows from the Company's insurance operations have historically been sufficient to meet current needs. Cash flows from operating activities were $(2.7) million and $279.4 million for the nine months ended September 30, 2021 and 2020, respectively. The Company also has significant cash flows from both scheduled and unscheduled investment security maturities, redemptions, and prepayments. These cash flows totaled $1,162.0 million and $860.4 million for the nine months ended September 30, 2021 and 2020, respectively. Operating and investing activity cash flow items could be reduced if interest rates rise at an accelerated rate in the future. Net cash inflows/(outflows) from the Company's universal life and investment annuity deposit product operations totaled $(38.0) million and $(372.9) million during the nine months ended September 30, 2021 and 2020, respectively. The lower net outflow in the first nine months of 2021 reflects reinsurance of negative cash flows of fixed-rate and payout annuities under the funds withheld reinsurance agreement as well as a higher level of fixed-index annuity sales.

**Capital Resources**

The Company relies on stockholders' equity for its capital resources as there is no long-term debt outstanding and the Company does not anticipate the need for any long-term debt in the near future. As of September 30, 2021, the Company maintained normal commitments for its operating and investment activities.

The Company has declared and paid an annual dividend on its common shares since 2005. The Company's practice has been to take a conservative approach to dividends, and the Board of Directors has adopted a strategic position to substantially reinvest earnings internally. This conservative approach yields the following benefits: (1) providing capital to finance the development of new business; (2) enabling the Company to take advantage of potential acquisitions and other competitive situations as they arise; (3) building a strong capital base to support the Company's financial strength ratings; (4) maintaining the Company's liquidity and solvency during difficult economic and market conditions; and (5) enhancing the Company's regulatory capital position. For similar reasons, despite the fact the Company's market price of its Class A common shares has been trading at a discount to the book value per share for some time, there are no imminent plans for the Company to repurchase its shares.

As the largest subsidiary of NWLGI, National Western serves as the primary funding source for NWLGI. The capacity of National Western to pay dividends to NWLGI is limited by law in the state of Colorado to earned profits (statutory unassigned surplus). At December 31, 2020, the maximum amount legally available for distribution without further regulatory approval is $10.0 million. National Western has not paid a dividend since the year ended December 31, 2019.

**OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS**

It is Company practice to not enter into off-balance sheet arrangements or to issue guarantees to third parties, other than in the normal course of issuing insurance contracts. Commitments related to insurance products sold are reflected as liabilities for future policy benefits. Insurance contracts guarantee certain performances by National Western and Ozark National.

Insurance reserves are the means by which life insurance companies determine the liabilities that must be established to assure that future policy benefits are provided for and can be paid. These reserves are required by law and based upon standard actuarial methodologies to ensure fulfillment of commitments guaranteed to policyholders and their beneficiaries, even though the obligations may not be due for many years. Refer to Note 1 in the Notes to the Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2020 for a discussion of reserving methods.

The table below summarizes future estimated cash payments under existing contractual obligations.

| | Payment Due by Period | | |
|---|---|---|---|
| | Total | Less Than 1 Year | 1 Year or More |
| | | (In thousands) | |
| Loan commitments | $ 10,500 | 10,500 | — |
| Commitments for capital calls to investment funds (3) | 257,148 | 46,274 | 210,874 |
| Lease obligations | 1,079 | 554 | 525 |
| Claims payable (1) | 73,962 | 73,962 | — |
| Other long-term reserve liabilities reflected on the balance sheet (2) | 12,873,537 | 1,030,032 | 11,843,505 |
| Total | $ 13,216,226 | 1,161,322 | 12,054,904 |

(1) Claims payable include benefit and claim liabilities for life, accident and health policies which the Company believes the amount and timing of the payment is essentially fixed and determinable. Such amounts generally relate to incurred and reported death, critical illness, accident and health claims including an estimate of claims incurred but not reported.

(2) Other long-term liabilities include estimated life and annuity obligations related to death claims, policy surrenders, policy withdrawals, maturities and annuity payments based on mortality, lapse, annuitization, and withdrawal assumptions consistent with the Company's historical experience. These estimated life and annuity obligations are undiscounted projected cash outflows that assume interest crediting and market growth consistent with assumptions used in amortizing deferred acquisition costs. They do not include any offsets for future premiums or deposits. Other long-term liabilities also include determinable payout patterns related to immediate annuities. Due to the significance of the assumptions used, the actual cash outflows will differ both in amount and timing, possibly materially, from these estimates.

(3) Commitments for capital calls to alternative investment funds reflect amounts which have not been called by the fund managers as of the current balance sheet date.

The Company, through its wholly owned subsidiary Braker P III, LLC ("BP III"), owns a commercial office building for which it has entered into lease agreements with various tenants for space not occupied by the Company. Total revenues recorded pertaining to these non-Company leases for the three-month periods ended September 30, 2021 and 2020 amounted to $1.3 million and $1.1 million, respectively, and for the nine months ended amounted to $3.8 million and $3.4 million, respectively. Under their respective terms these leases expire at various dates from 2023 through 2026.

The table below summarizes future estimated cash receipts under all existing lease agreements, including those in addition to the BP III lease agreements discussed above.

| | Estimated Cash Receipts by Period | | | | |
|---|---|---|---|---|---|
| | Total | Less Than 1 Year | 1 - 3 Years | 3 - 5 Years | More Than 5 Years |
| | (In thousands) | | | | |
| Real estate revenue | $ 39,450 | 6,444 | 11,558 | 8,278 | 13,170 |

## CHANGES IN ACCOUNTING PRINCIPLES AND CRITICAL ACCOUNTING POLICIES

### Changes in Accounting Principles

Effective January 1, 2020 the Company implemented ASU 2016-13, *Financial Instruments - Credit Losses*. This standard replaced the previous incurred loss recognition model with an expected loss recognition model for certain financial assets. Adoption of the standard resulted in an incremental allowance for credit losses as of January 1, 2020 of $3.8 million, and a charge to retained earnings, net of tax, of $3.0 million as a change in accounting as of that date. There were no other changes in accounting principles during the periods reported in this Form 10-Q.

## REGULATORY AND OTHER ISSUES

### Statutory Accounting Practices

Regulations that affect the Company and the insurance industry are often the result of actions taken by the National Association of Insurance Commissioners ("NAIC"). The NAIC routinely publishes new regulations as model acts or laws which states subsequently adopt as part of their insurance regulations. Currently, the Company is not aware of any NAIC regulatory matter material to its operations or reporting of financial results.

### Risk-Based Capital Requirements

The NAIC established risk-based capital ("RBC") requirements to help state regulators monitor the financial strength and stability of life insurers by identifying those companies that may be inadequately capitalized. Under the NAIC's requirements, each insurer must maintain its total capital above a calculated threshold or take corrective measures to achieve the threshold. The threshold of adequate capital is based on a formula that takes into account the amount of risk each company faces on its products and investments. The RBC formula takes into consideration four major areas of risk which are: (i) asset risk which primarily focuses on the quality of investments; (ii) insurance risk which encompasses mortality and morbidity risk; (iii) interest rate risk which involves asset/liability matching issues; and (iv) other business risks. National Western and Ozark National's current statutory capital and surplus are each significantly in excess of the current threshold RBC requirements.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

This information is included in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, in the Investments section.

## ITEM 4. CONTROLS AND PROCEDURES

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in recording, processing, summarizing, and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act.

There were no changes in the Company's internal controls over financial reporting, as defined in Rules 13a-15(f) and 15d-15(e) under the Exchange Act, during the quarter ended September 30, 2021 that materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

Internal controls over financial reporting change as the Company modifies or enhances its systems and processes to meet business needs. Any significant changes in controls are evaluated prior to implementation to help ensure continued effectiveness of internal controls and the control environment.

# PART II. OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

Refer to Note 8(A) "Legal Proceedings" of the accompanying Condensed Consolidated Financial Statements included in this Form 10-Q.

## ITEM 1A. RISK FACTORS

The risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2020 included a discussion of the potential ramifications of natural or man-made disasters and catastrophes including pandemic disease. Although the majority of our home office staff were redeployed to remote work sites, staff remaining onsite followed social distancing protocols and precautions during the COVID-19 pandemic. Our companies and businesses retained normal operations and business hours throughout accepting applications for insurance, issuing policies, investing and managing assets, paying policy benefits and expenses, maintaining information technology operations, and adhering to a sound system of internal controls over financial reporting. Since operations were not interrupted or suspended, the Company did not activate the business continuity plans that it has in place. Both National Western and Ozark National/NIS subsequently brought the majority of its remote-working employees back into their respective home office facilities. The exposure to adverse mortality experience has been monitored and evaluated and deemed to not significantly impact the Company's financial position. The exposure to financial service companies has principally manifested in degradations in asset values, management of adequate liquidity and capital resources, and successfully maintaining competitiveness and product profitability in an exceptionally low interest rate environment.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Effective August 22, 2008, National Western adopted and implemented a limited stock buy-back program associated with the 2008 Incentive Plan which provides Option Holders the additional alternative of selling shares acquired through the exercise of stock options directly back to the Company. This plan was assumed by NWLGI from National Western in 2015 pursuant to the terms of the holding company reorganization implemented at that time. The program provides Option Holders with the ability to elect to sell such acquired shares back to the Company at any time within ninety (90) days after the exercise of stock options at the prevailing market price as of the date of notice of election. As of September 30, 2021, there are no stock options outstanding under the plan.

Purchased shares are reported in the Company's Condensed Consolidated Financial Statements as authorized and unissued. At December 31, 2020 and September 30, 2021 there were no stock options vested or unvested and outstanding under these plans.

| Period | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| July 1, 2021 through July 31, 2021 | — | $ — | N/A | N/A |
| August 1, 2021 through August 31, 2021 | — | $ — | N/A | N/A |
| September 1, 2021 through September 30, 2021 | — | $ — | N/A | N/A |
| Total | — | $ — | N/A | N/A |

## ITEM 4. Removed and Reserved.

## ITEM 6. EXHIBITS

**(a) Exhibits**

| | | |
|---|---|---|
| *Exhibit 31(a)* | - | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| *Exhibit 31(b)* | - | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| *Exhibit 32(a)* | - | Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

## 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.

**NATIONAL WESTERN LIFE GROUP, INC.**
(Registrant)

| | |
|---|---|
| Date: November 8, 2021 | /S/ Ross R. Moody |
| | Ross R. Moody |
| | Chairman of the Board, President and |
| | Chief Executive Officer |
| | (Authorized Officer) |
| | |
| | |
| | |
| | |
| Date: November 8, 2021 | /S/ Brian M. Pribyl |
| | Brian M. Pribyl |
| | Senior Vice President, |
| | Chief Financial Officer and Treasurer |
| | (Principal Financial Officer) |
| | (Principal Accounting Officer) |

**EXHIBIT 31(a)**
**CERTIFICATION**

I, Ross R. Moody, certify that:

1. I have reviewed this report on Form 10-Q of National Western Life Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 8, 2021

/S/ Ross R. Moody
Ross R. Moody
Chairman of the Board, President and
Chief Executive Officer

**EXHIBIT 31(b)**
**CERTIFICATION**

I, Brian M. Pribyl, certify that:

1. I have reviewed this report on Form 10-Q of National Western Life Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 8, 2021

/S/Brian M. Pribyl
Brian M. Pribyl
Senior Vice President,
Chief Financial Officer and
Treasurer

**EXHIBIT 32(a)**

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of National Western Life Group, Inc. ("Company") on Form 10-Q for the period ended September 30, 2021 as filed with the Securities and Exchange Commission on or about the date hereof ("Report"), I, Ross R. Moody, Chairman of the Board, President, and Chief Executive Officer of the Company and I, Brian M. Pribyl, Senior Vice President, Chief Financial Officer, and Treasurer of the Company, each certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) to my knowledge, the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 8, 2021

/S/Ross R. Moody
Ross R. Moody
Chairman of the Board, President and
Chief Executive Officer

/S/Brian M. Pribyl
Brian M. Pribyl
Senior Vice President,
Chief Financial Officer
and Treasurer