KANSAS CITY LIFE INSURANCE CO
Form 10-Q
April 30, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2010 or
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from_______to______
Commission file number 2-40764

KANSAS CITY LIFE INSURANCE COMPANY
(Exact name of registrant as specified in its charter)

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

816-753-7000
Registrant's telephone number, including area code

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes [ ] No [ ]

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

Large accelerated filer [ ]	Accelerated filer [X]
Non-accelerated filer [ ]	Smaller reporting company [ ]

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

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

Common Stock, $1.25 par	11,496,290 shares
Class	Outstanding March 31, 2010

KANSAS CITY LIFE INSURANCE COMPANY
TABLE OF CONTENTS

Part I. Financial Information	3
Item 1. Financial Statements (Unaudited)	3
Consolidated Balance Sheets	3
Consolidated Statements of Income	4
Consolidated Statements of Stockholders' Equity	5
Consolidated Statements of Cash Flows	6
Notes to Consolidated Financial Statements	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	34
Item 3. Quantitative and Qualitative Disclosures About Market Risk	65
Item 4. Controls and Procedures	65
Part II. Other Information	66
Item 1. Legal Proceedings	66
Item 1A. Risk Factors	66
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	67
Item 5. Other Information	68
Item 6. Exhibits	70
Signatures	71

Part I Financial Information
Item 1. Financial Statements
Amounts in thousands, except share data, or as otherwise noted

KANSAS CITY LIFE INSURANCE COMPANY
CONSOLIDATED BALANCE SHEETS

	March 31 2010 (Unaudited)	December 31 2009
ASSETS		
Investments:		
Fixed maturity securities available for sale, at fair value	$ 2,539,151	$ 2,469,272
Equity securities available for sale, at fair value	37,826	36,876
Mortgage loans	456,489	457,582
Real estate	115,017	114,076
Policy loans	84,896	85,585
Short-term investments	106,770	138,704
Total investments	3,340,149	3,302,095
Cash	5,809	4,981
Accrued investment income	37,300	32,989
Deferred acquisition costs	198,540	209,495
Value of business acquired	60,325	66,114
Reinsurance receivables	183,373	179,365
Property and equipment	24,066	24,393
Income taxes	3,762	8,784
Other assets	33,146	35,145
Separate account assets	324,924	312,824
Total assets	$ 4,211,394	$ 4,176,185
LIABILITIES		
Future policy benefits	$ 872,987	$ 866,889
Policyholder account balances	2,044,534	2,048,828
Policy and contract claims	33,667	33,484
Other policyholder funds	142,606	137,847
Income taxes	30,336	21,851
Other liabilities	122,484	126,099
Separate account liabilities	324,924	312,824
Total liabilities	3,571,538	3,547,822
STOCKHOLDERS' EQUITY		
Common stock, par value $1.25 per share		
Authorized 36,000,000 shares,		
issued 18,496,680 shares	23,121	23,121
Additional paid in capital	41,072	41,068
Retained earnings	755,077	757,225
Accumulated other comprehensive loss	(20,721)	(36,477)

Treasury stock, at cost (2010 - 7,000,390 shares;		
2009 - 6,931,589 shares)	(158,693)	(156,574)
Total stockholders' equity	639,856	628,363
Total liabilities and stockholders' equity	$4,211,394	$4,176,185

See accompanying Notes to Consolidated Financial Statements (Unaudited)

KANSAS CITY LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF INCOME

	Quarter Ended March 31	
	2010	2009
REVENUES	(Unaudited)	
Insurance revenues:		
Premiums	$47,929	$46,540
Contract charges	26,679	26,768
Reinsurance ceded	(13,302)	(12,539)
Total insurance revenues	61,306	60,769
Investment revenues:		
Net investment income	43,304	43,139
Realized investment gains, excluding impairment losses	1,323	1,414
Net impairment losses recognized in earnings:		
Total other-than-temporary impairment losses	(1,591)	(21,406)
Portion of impairment losses recognized in other comprehensive income	5	15,288
Net impairment losses recognized in earnings	(1,586)	(6,118)
Total investment revenues	43,041	38,435
Other revenues	2,420	2,431
Total revenues	106,767	101,635
BENEFITS AND EXPENSES		
Policyholder benefits	47,791	48,687
Interest credited to policyholder account balances	21,200	21,174
Amortization of deferred acquisition costs and value of business acquired	10,519	12,479
Operating expenses	24,290	26,254
Total benefits and expenses	103,800	108,594
Income (loss) before income tax expense (benefit)	2,967	(6,959)
Income tax expense (benefit)	2,004	(2,411)
NET INCOME (LOSS)	$963	$(4,548)
Comprehensive income (loss), net of taxes:		
Change in net unrealized gains and (losses) on securities available for sale	$15,756	$442
Other comprehensive income	15,756	442
COMPREHENSIVE INCOME (LOSS)	$16,719	$(4,106)

Basic and diluted earnings per share:		
Net income (loss)	$0.08	$(0.40)

See accompanying Notes to Consolidated Financial Statements (Unaudited)

KANSAS CITY LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

		Quarter Ended March 31, 2010 (Unaudited)	
COMMON STOCK, beginning and end of period	$	23,121	
ADDITIONAL PAID IN CAPITAL			
Beginning of period		41,068	
Excess of proceeds over cost of treasury stock sold		4	
End of period		41,072	
RETAINED EARNINGS			
Beginning of period		757,225	
Net income		963	
Stockholder dividends of $0.27 per share (2009 - $1.08)		(3,111	)
End of period		755,077	
ACCUMULATED OTHER COMPREHENSIVE LOSS			
Beginning of period		(36,477	)
Other comprehensive income		15,756	
End of period		(20,721	)
TREASURY STOCK, at cost			
Beginning of period		(156,574	)
Cost of 69,104 shares acquired (2009 - 396,821 shares)		(2,123	)
Cost of 303 shares sold (2009 - 526,708 shares)		4	
End of period		(158,693	)
TOTAL STOCKHOLDERS' EQUITY	$	639,856	

See accompanying Notes to Consolidated Financial Statements (Unaudited)

KANSAS CITY LIFE INSURANCE COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Quarter Ended March 31	
	2010	2009
	(Unaudited)	
OPERATING ACTIVITIES		
Net cash provided	$1,750	$12,557
INVESTING ACTIVITIES		
Purchases of investments:		
Fixed maturity securities	(108,969)	(68,657)
Equity securities	(475)	(592)
Mortgage loans	(7,625)	(12,260)
Real estate	(1,888)	(4,060)
Sales of investments:		
Fixed maturity securities	12,729	9,039
Equity securities	-	1,406
Real estate	600	2,736
Other investment assets	32,623	4,043
Maturities and principal paydowns of investments:		
Fixed maturity securities	65,301	48,130
Mortgage loans	8,718	11,654
Net dispositions of property and equipment	113	291
Net cash provided (used)	1,127	(8,270)
FINANCING ACTIVITIES		
Repayment of borrowings	-	(2,900)
Deposits on policyholder account balances	53,728	53,947
Withdrawals from policyholder account balances	(53,424)	(59,435)
Net transfers from (to) separate accounts	(467)	3,920
Change in other deposits	3,340	3,093
Cash dividends to stockholders	(3,111)	(3,112)
Net acquisition of treasury stock	(2,115)	(1,566)
Net cash used	(2,049)	(6,053)
Increase (decrease) in cash	828	(1,766)
Cash at beginning of year	4,981	9,720
Cash at end of period	$5,809	$7,954

See accompanying Notes to Consolidated Financial Statements (Unaudited)

6

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)

1. NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

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

The unaudited interim consolidated financial statements have been prepared on the basis of U.S. generally accepted accounting principles (GAAP) for interim financial reporting and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the disclosures required by GAAP for complete financial statements. As such, these unaudited interim consolidated financial statements should be read in conjunction with the Company's 2009 Form 10-K. Management believes that the disclosures are adequate to make the information presented not misleading, and all normal and recurring adjustments necessary to present fairly the financial position at March 31, 2010 and the results of operations for all periods presented have been made. The results of operations for any interim period are not necessarily indicative of the Company's operating results for a full year.

Significant intercompany transactions have been eliminated in consolidation and certain immaterial reclassifications have been made to the prior period results to conform with the current period's presentation.

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

Significant Accounting Policies
Presented below is a summary of significant accounting policies used by the Company. This is not intended to be an exhaustive list of all accounting policies used by the Company. For a full discussion, please refer to the Company's 2009 Form 10-K as filed with the Securities and Exchange Commission.

Investments
Investment income is recognized when earned. Realized gains and losses on the sale of investments are determined on the basis of specific security identification and are recorded on the trade date. Securities available for sale are stated at fair value. Unrealized gains and losses, net of adjustments to deferred acquisition costs (DAC), value of business acquired (VOBA), policyholder account balances and deferred income taxes, are reported as a separate component of accumulated other comprehensive loss in stockholders' equity. Unrealized losses represent the difference between amortized cost and fair value on the valuation date. The adjustments to DAC and VOBA represent changes in the amortization of DAC and VOBA that would have been required as a charge or credit to income had such unrealized amounts been realized. The adjustment to policyholder account balances represents the increase from using a discount rate that would have been required if such unrealized gains or losses had been realized and the proceeds reinvested at current market interest rates, which were lower than the then-current effective portfolio rate.

The Company's fair value of fixed maturity and equity securities are derived from external pricing sources, brokers, and internal matrices and calculations. At March 31, 2010, approximately 93% of the carrying value of these investments was from external pricing services and 7% was derived from brokers, internal matrices and calculations. The investment portfolio is monitored regularly to ensure that investments which may be other-than-temporarily impaired are identified in a timely fashion and properly valued. Other-than-temporary impairments that are determined to be due to credit are charged against earnings as realized investment losses. Premiums and discounts on fixed maturity securities are amortized over the life of the related security as an adjustment to yield using the effective interest method. See Note 4 – Investments for further details.

Investment income on residential mortgage-backed securities is initially based upon yield, cash flow, and prepayment assumptions at the date of purchase. Subsequent revisions in those assumptions are recorded using the retrospective method, except for adjustable rate residential mortgage-backed securities where the prospective method is used. Under the retrospective method the amortized cost of the security is adjusted to the amount that would have existed had the revised assumptions been in place at the time of purchase. Under the prospective method, future cash flows are estimated and interest income is recognized going forward using the new effective yield to maturity. The adjustments to amortized cost under both methods are recorded as a charge or credit to net investment income. The Company bases its historical results from individual securities and internal assessments of likely future results for these securities. These results are based upon validations and comparisons to similar securities provided by third parties, such as rating agencies.

Mortgage loans are stated at cost, adjusted for amortization of premium and accrual of discount, less a valuation reserve for potential future losses. A loan is considered impaired if it is probable that contractual amounts due will not be collected. The valuation reserve is determined based upon historical impairment experience and insurance industry studies. Loans in foreclosure and loans considered to be impaired are placed on a non-accrual status.

Real estate consists of directly owned investments and real estate joint ventures. Real estate that is directly owned is carried at depreciated cost. Real estate joint ventures consist primarily of office buildings, industrial warehouses, unimproved land for future development and low income housing tax credit (LIHTC) investments. Real estate joint ventures are consolidated where required or are valued at cost, adjusted for the Company's equity in earnings.

Policy loans are carried at cost, less principal payments received. Short-term investments are stated at cost, adjusted for amortization of premium and accrual of discount.

Valuation of Investments

The Company's principal investments are in fixed maturity securities, mortgage loans and real estate; all of which are exposed to three primary sources of investment risk: credit, interest rate and liquidity. The fixed maturity securities, which are all classified as available for sale, are carried at their fair value in the Company's Consolidated Balance Sheets, with unrealized gains or losses recorded in accumulated other comprehensive loss. The unrealized gains or losses are recorded net of the adjustment to policyholder account balances to reflect what would have been earned had those gains or losses been realized and the proceeds reinvested.

The Company monitors the various markets in which its investments are traded. The Company utilizes a primary independent third-party pricing service to determine the majority of its fair values. At March 31, 2010 the Company used a second independent third-party pricing service to validate the fair market values provided by the primary pricing service. The Company also used the second pricing service to determine the fair value of certain securities for which the primary pricing service was unable to provide a value. At March 31, 2010, 99% of the value of the Company's fixed maturity and equity securities that were priced by external pricing services was from the primary third-party pricing service and 1% was from the second independent pricing service. The Company reviews values received from independent pricing sources for validity. In addition, the Company tests a limited number of securities each reporting period to further validate reliance on the fair values provided. When fair values are not available from external service providers, where possible, the Company utilizes quotes from brokers. When the Company cannot obtain reliable broker pricing, a fair value is determined based upon an assessment of several factors appropriate for the specific issue, including but not limited to: the issuer's industry; liquidity; cash flows; marketability, ratings and the ability of the issuer to satisfy the obligation; government intervention or regulations; fair value of comparable securities in actively traded or quoted markets; or other factors. The Company creates a matrix of factors from which to calculate an estimable value. However, all factors may not be known or publicly available from which to determine a value and, as such, the fair value used by the Company may not be truly indicative of the actual value available in an active market or an actual exit price if the Company were to place the security for sale in the current market.

The Company has a policy and process in place to identify securities that could potentially have an impairment that is other-than-temporary. This process involves monitoring market events that could impact issuers' credit ratings, business climate, management changes, litigation and government actions, and other similar factors. This process also involves monitoring late payments, downgrades by rating agencies, key financial ratios, financial statements, revenue forecasts, asset quality and cash flow projections as indicators of credit issues.

At the end of each quarter, all securities are reviewed to determine whether impairments exist and whether other-than-temporary impairments should be recorded. This quarterly process includes an assessment of the credit quality of each investment in the entire securities portfolio. Additional reporting and review procedures are conducted for those securities where fair value is less than 90% of amortized cost. The Company prepares a formal review document no less often than quarterly of all investments where fair value is less than 80% of amortized cost for six consecutive months or more, investments that have previously been written down and that remain in an unrealized loss position greater than 20% of their value, and selected investments that have changed significantly from a previous period and that have a decline in fair value greater than 10% of amortized cost.

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

The Company considers relevant facts and circumstances in evaluating whether the impairment of a security is other-than-temporary. Relevant facts and circumstances considered include but are not limited to:

- The current fair value of the security as compared to cost;
- The credit rating of the security;
- The extent and the length of time the fair value has been below amortized cost;
- The financial position of the issuer, including the current and future impact of any specific events, material declines in the issuer's revenues, margins, cash positions, liquidity issues, asset quality, debt levels and income results;
- Significant management or organizational changes;
- Significant uncertainty regarding the issuer's industry;
- Violation of financial covenants;
- Consideration of information or evidence that supports timely recovery;
- The Company's intent and ability to hold an equity security until it recovers in value;
- Whether the Company intends to sell a debt security and whether it is not more likely than not that the Company will be required to sell a debt security before recovery of the amortized cost basis; and
- Other business factors related to the issuer's industry.

To the extent the Company determines that a security is deemed to be other-than-temporarily impaired, the portion of the impairment that is deemed to be due to credit is charged to the Consolidated Statements of Income and the amortized cost basis of the underlying investment is reduced. The portion of the impairment that is deemed to be non-credit is charged to other comprehensive income (loss). Equity securities that are determined to be other-than-temporarily impaired are written down to fair value and the impairment is charged to the Consolidated Statements of Income.

There are a number of significant risks and uncertainties inherent in the process of monitoring impairments, determining if an impairment is other-than-temporary and determining the portion of an other-than-temporary impairment that is due to credit. These risks and uncertainties include but are not limited to:

- The risk that the Company's assessment of an issuer's ability to meet all of its contractual obligations will change based on changes in the credit characteristics of that issuer;
- The risk that the economic outlook will be worse than expected or have more of an impact on the issuer than anticipated;
- The risk that the performance of the underlying collateral for securities could deteriorate in the future and the Company's credit enhancement levels and recovery values do not provide sufficient protection to the Company's contractual principal and interest;
- The risk that fraudulent, inaccurate or misleading information could be provided to the Company's credit, investment and accounting professionals who determine the fair value estimates and accounting treatment for securities;
- The risk that new information obtained by the Company or changes in other facts and circumstances may lead the Company to change its intent to sell the security before it recovers in value;
- The risk that facts and circumstances change such that it becomes more likely than not that the Company will be required to sell the investment before recovery of the amortized cost basis; and
- The risk that the methodology or assumptions used to develop estimates of the portion of impairments due to credit prove, over time, to be inaccurate or insufficient.

Any of these situations could result in a change to income in a future period.

Deferred Acquisition Costs and Value of Business Acquired

Deferred acquisition costs (DAC), principally agent commissions and other selling, selection and issue costs, which vary with and are directly related to the production of new business, are capitalized as incurred. These deferred costs are then amortized in proportion to future premium revenues or the expected future profits of the business, depending upon the type of product.

When a new block of business is acquired or when an insurance company is purchased, a portion of the purchase price is allocated to a separately identifiable intangible asset, called the value of business acquired (VOBA). VOBA is established as

9

the actuarially determined present value of future gross profits of the business acquired and is amortized in proportion to future premium revenues, or the expected future profits, depending on the type of business acquired.

The Company considers the following assumptions to be of significance when evaluating the amortization of DAC and VOBA: expected mortality, interest spreads, surrender rates and expense margins. Mortality relates to the occurrence of death. Interest spreads are the difference between the investment returns earned and the crediting rates of interest applied to policyholder account balances. Surrender rates relate to the relative volume of policy terminations. Expense margins involve the expenses incurred for maintaining and servicing in-force policies.

At least annually, a review is performed of the models and the assumptions used to develop expected future profits, based upon management's current view of future events. DAC is reviewed on an ongoing basis to determine that the unamortized portion does not exceed the expected recoverable amounts. Management's view primarily reflects Company experience but can also reflect emerging trends within the industry. Short-term deviations in experience affect the amortization of DAC and VOBA in the period, but do not necessarily indicate that a change to the long-term assumptions of future experience is warranted. If it is determined that it is appropriate to change the long-term assumptions of future experience, then an unlocking adjustment is recognized for the block of business being evaluated. Certain assumptions, such as interest spreads and surrender rates, may be interrelated. As such, unlocking adjustments often reflect revisions to multiple assumptions. The balances of DAC and VOBA are immediately impacted by any assumption changes, with the change reflected through the Consolidated Statements of Income as an unlocking adjustment in the amount of DAC or VOBA amortized. These adjustments can be positive or negative. The impact of unlocking adjustments from the changes in estimates for the periods reported are included in the Consolidated Results of Operations and Operating Results by Segment sections of the Management's Discussion and Analysis of Financial Condition and Results of Operations contained within this document.

During the quarter ended March 31, 2010, the Company recorded adjustments to commissions and the amortization of DAC that increased net income by approximately $0.4 million. The adjustments relate to amounts not recorded properly during 2009. Management has evaluated the adjustment and considers it to be immaterial.

The following table reflects the estimated pre-tax impact to DAC and VOBA on universal life, variable universal life, and fixed and variable deferred annuity products that could occur in a twelve-month period for an unlocking adjustment due to reasonably likely changes in significant assumptions. Changes in assumptions of the same magnitude in the opposite direction would have an impact of a similar magnitude but opposite direction of the examples provided.

Critical Accounting Estimate	Determination Methodology	Potential One-Time Effect on DAC, VOBA and Related Items
Mortality Experience	Based on Company mortality experience. Industry experience and trends are also considered.	A 2.5% increase in expected mortality experience for all future years would result in a reduction in DAC and VOBA, and a 2% decrease in DAC and VOBA, which would be an increase in current period amortization.
Surrender Rates	Based on Company surrender experience. Industry experience and trends are also considered.	A 10% increase in expected surrender rates for all future years would result in a reduction in DAC and VOBA,

		and a 1% decrease in DAC and VOBA, which would be an increase in current period amortization.
Interest Spreads	Based on expected future investment returns and expected future crediting rates applied to policyholder account balances; future crediting rates include constraints imposed by policy guarantees.	A 10 basis point reduction in future interest rate spreads would result in a reduction in DAC and VOBA, and a 1% decrease in DAC and VOBA, which would be an increase in current period amortization.
Maintenance Expenses	Based on Company experience using an internal expense allocation methodology.	A 10% increase in future maintenance expenses would result in a reduction in DAC and VOBA, and a 1% decrease in DAC and VOBA, which would be an increase in current period amortization.

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

Separate Accounts
Separate account assets and liabilities arise from the sale of variable universal life insurance and variable annuity products. The separate account represents funds segregated for the benefit of certain policyholders who bear the investment risk. The assets are legally segregated and are not subject to claims which may arise from any other business of the Company. The separate account assets and liabilities, which are equal, are recorded at fair value based upon net asset value (NAV). Policyholder account deposits and withdrawals, investment income and realized investment gains and losses are excluded from the amounts reported in the Consolidated Statements of Income. Revenues to the Company from separate accounts consist principally of contract charges, which include maintenance charges, administrative fees and mortality and risk charges.

Net asset value of the separate accounts is calculated in a manner consistent with GAAP for investments companies and is determinative of their fair value. Several of the separate accounts invest in publicly quoted mutual funds or actively managed stocks. The fair value of the underlying mutual funds or stock is used to determine the NAV of the separate account, which is not publicly quoted. Some of the separate accounts also invest in fixed income securities. The fair value of the underlying securities is based on quoted prices of similar assets and used to determine the NAV of the separate account. Sale of plan assets may be at values less than NAV and certain redemption restrictions may apply.

The total separate account assets were $324.9 million as of March 31, 2010. Variable universal life and variable annuity assets comprised 29% and 71% of this amount, respectively. Guarantees are offered under variable universal life and variable annuity contracts: a guaranteed minimum death benefit (GMDB) rider is available on certain variable universal life contracts and GMDB are provided on variable annuities. The GMDB rider for variable universal life and variable annuity contracts guarantees the death benefit for specified periods of time, regardless of investment performance, provided cumulative premium requirements are met. The Company also offers a guaranteed minimum withdrawal benefit (GMWB) rider that can be added to new or existing variable annuity contracts. The rider provides an enhanced withdrawal benefit that guarantees a stream of income payments to an owner or annuitant, regardless of the contract account value. The current value of variable annuity separate accounts with the GMWB rider was $65.5 million and the guarantee liability was $(1.9) million at March 31, 2010 compared to $57.9 million and $(1.6) million, respectively, at December 31, 2009. The value of the GMWB rider is recorded at fair value. The change in this value is included in policyholder benefits in the Consolidated Statements of Income.

Future Policy Benefits
The Company establishes liabilities for amounts payable under insurance policies, including traditional life insurance, annuities and accident and health insurance. Generally, amounts are payable over an extended period of time. Liabilities for future policy benefits of traditional life insurance have been computed by a net level premium method based upon estimates at the time of issue for investment yields, mortality and withdrawals.

Liabilities for future policy benefits of immediate annuities and supplementary contracts with life contingencies are computed by calculating an actuarial present value of future policy benefits, based upon estimates for investment yields and mortality at the time of issue.

Liabilities for future policy benefits of accident and health insurance represent estimates of payments to be made on reported insurance claims, as well as claims incurred but not yet reported. These liabilities are estimated using actuarial analyses and case basis evaluations that are based upon past claims experience, claim trends and industry experience.

Policyholder Account Balances

Policyholder account balances include universal life insurance, fixed deferred annuity contracts and investment-type contracts. Liabilities for these policyholder account balances are included without reduction for potential surrender charges and deferred front-end contract charges. The account balances for universal life contracts are equal to cumulative premiums, less contract charges and withdrawals, plus interest credited. The account balances for fixed deferred annuities and investment-type contracts are equal to the cumulative deposits, less any applicable contract charges and withdrawals, plus interest credited. Front-end contract charges are deferred and amortized over the term of the policies. Policyholder benefits incurred in excess of related policyholder account balances are charged to policyholder benefits expense. Interest on policyholder account balances is credited as earned.

Recognition of Revenues

Premiums for traditional life insurance products are reported as revenue when due. Premiums on accident and health insurance are reported as earned ratably over the contract period in proportion to the amount of insurance protection provided. A reserve is provided for the portion of premiums written which relate to unexpired terms of coverage.

Deposits related to universal life, fixed deferred annuity contracts and investment-type products are credited to policyholder account balances. Revenues from such contracts consist of amounts assessed against policyholder account balances for mortality, policy administration and surrender charges, and are recognized in the period in which the benefits and services are provided. The cash flows from deposits are credited to policyholder account balances. Deposits are not recorded as revenue. Deposits are shown as a Financing Activity in the Consolidated Statements of Cash Flows.

The Company measures its sales or new business production with two components: new premiums recorded and new deposits received. Premiums and deposits are subdivided into two categories: new and renewal. New premiums and deposits are measures of sales or new business production. Renewal premiums and deposits occur as continuing business from existing customers.

Reinsurance
A variety of reinsurance vehicles are currently in use, including individual and bulk arrangements on both coinsurance and mortality/morbidity only basis. Reinsurance supports a multitude of corporate objectives, including managing statutory capital, reducing volatility and surplus strain and is an actively managed tool for the Company. At the customer level, reinsurance increases the Company’s capacity, provides access to additional underwriting expertise, and generally makes it possible for the Company to offer products at competitive levels that could not otherwise be made available.

The Company remains contingently liable if the reinsurer should be unable to meet obligations assumed under the reinsurance contract. Should a reinsurer become insolvent, the Company could recapture the business ceded to this reinsurer. The Company monitors the relative financial strength and viability of its reinsurance partners. The Company had one reinsurance counterparty whose credit rating was below investment grade at March 31, 2010. Total reserves ceded to this reinsurer were $3.0 million at March 31, 2010. If this reinsurer became insolvent, the recapture of the business ceded to this reinsurer would result in an increase in reserves of $3.0 million.

Reinsurance receivables include amounts related to paid benefits and estimated amounts related to unpaid policy and contract claims, future policy benefits and policyholder account balances.

Health Care Reform
The Company has assessed, based upon the information available, the Health Care Reform Act, as passed in the first quarter 2010. The Company has considered its medical and dental plans provided for employees, agents and retirees. While the Company will incur additional costs associated with the implementation of this Act, it does not believe these costs or ongoing costs associated with this Act will have a material impact to the consolidated financial statements. The Company does not provide a separate prescription drug plan to its retirees. In addition, the Company does not sell any medical insurance or prescription drug coverage. However, the Company does sell dental insurance but believes that the impact of this Act is immaterial to this product. The Company will continue to assess the information contained in this Act as additional guidance becomes available and as additional implications are understood or clarified.

2. NEW ACCOUNTING PRONOUNCEMENTS

In March 2008, the Financial Accounting Standards Board (FASB) issued new guidance to require companies with derivative instruments to disclose information about how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity’s financial position, financial performance, and cash flows. This guidance became effective for financial statements issued for fiscal years beginning after November 15, 2008. The Company adopted it on January

1, 2009 with no material impact to the consolidated financial statements.

In December 2008, the FASB issued new guidance regarding employers' disclosures about postretirement benefit plan assets. It requires entities to provide disclosures about employer's defined benefit plans and other post retirement plans that would help users of the financial statements understand how investment allocation decisions are made, the major categories of plan assets, the inputs and the valuation techniques used to measure the fair value of plan assets, the effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period, and significant concentrations of risk within plan assets. This guidance became effective for financial statements issued for fiscal years ending after December 15, 2009. The Company adopted this guidance on January 1, 2009 with no material impact to the consolidated financial statements.

In April 2009, the FASB issued new guidance to clarify fair valuation in inactive markets and includes all assets and liabilities subject to fair valuation measurements. Enhanced disclosures related to the fair value of assets and liabilities became required. This guidance became effective for financial statements issued for interim and annual periods ending after

June 15, 2009. The Company elected early adoption effective for the period ended March 31, 2009 with retroactive application effective January 1, 2009 with no material impact to the consolidated financial statements.

In April 2009, the FASB issued new guidance regarding other-than-temporary impairment of debt securities and changes in the recognition and presentation of debt securities determined to be other-than-temporarily impaired. The guidance requires an enterprise to bifurcate any other-than-temporary impairment between credit and non-credit impairments and then establish accounting treatment for each aspect, in current and subsequent periods. Retroactive application became required to other-than-temporary impairments recorded in prior periods by making a cumulative-effect adjustment to the opening balance of retained earnings and accumulated other comprehensive income (loss) in the period of adoption. This guidance became effective for financial statements issued for interim and annual periods ending after June 15, 2009. The Company elected early adoption effective for the period ended March 31, 2009 with retroactive application effective January 1, 2009. For additional information pertaining to this guidance, please see Note 6 – Accumulated Effect of Change in Accounting Principle.

In April 2009, the FASB issued new guidance to expand the fair value disclosures required for financial instruments for interim periods. The guidance also requires entities to disclose the methods and significant assumptions used to estimate the fair value of financial instruments in financial statements on an interim and annual basis and to highlight any changes from prior periods. This guidance became effective for financial statements issued for interim and annual periods ending after June 15, 2009. The Company elected early adoption effective for the period ended March 31, 2009 with retroactive application effective January 1, 2009 with no material impact to the consolidated financial statements.

In May 2009, the FASB issued new guidance that established general accounting standards and disclosure for events occurring subsequent to the balance sheet date but before the financial statements are issued. This guidance became effective for interim and annual accounting periods ending after June 15, 2009. The Company adopted it upon issuance, with no material impact to the consolidated financial statements.

In June 2009, the FASB issued new guidance to improve the information that a reporting entity provides in its financial reports related to a transfer of financial assets. It addresses the effects of a transfer on financial position, financial performance, cash flows and a transferor's continuing involvement in transferred financial assets. In addition, this guidance also eliminates the concept of a qualifying special-purpose entity. This guidance became effective for interim and annual accounting periods beginning after November 15, 2009. The Company adopted it on January 1, 2010 with no material impact to the consolidated financial statements.

In June 2009, the FASB issued new guidance to improve financial reporting by enterprises involved with variable interest entities (VIEs). This guidance changes the approach to determining a VIE's primary beneficiary and requires companies to continuously reassess whether investments in VIEs must be consolidated. This guidance became effective for interim and annual accounting periods beginning after November 15, 2009. The Company adopted it on January 1, 2010 with no material impact to the consolidated financial statements.

In June 2009, the FASB issued new guidance to establish the FASB Accounting Standards Codification (ASC) as a source of authoritative accounting principles recognized by the FASB to be applied by non-governmental entities in the preparation of financial statements in conformity with GAAP. This guidance replaced previous guidance related to the same issue and became effective for interim and annual reporting periods ending after September 15, 2009. The Company adopted it upon issuance, with no material impact to the consolidated financial statements.

In January 2010, the FASB issued amendments to existing guidance regarding accounting and reporting for decreases in ownership of a subsidiary. The amendments affect entities that experience a decrease in ownership in a subsidiary that is a business or nonprofit activity. The amendments also affect entities that exchange a group of assets that constitutes a business or nonprofit activity for an equity interest in another entity. This guidance became effective for interim and annual reporting periods ending after December 15, 2009 for the Company since it had previously adopted SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements." The Company adopted it on January 1, 2010 with no material impact to the consolidated financial statements.

In January 2010, the FASB issued new guidance to improve disclosures about fair value measurements. This guidance requires new disclosures and clarification of existing disclosures regarding Levels 1, 2 and 3 in the fair value hierarchy. The majority of this guidance became effective for interim and annual reporting periods beginning after December 15, 2009. However, disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements will become effective for fiscal years beginning after December 15, 2010, and for interim periods within those years. The Company adopted the guidance on January 1, 2010 with no material impact to the consolidated financial statements.

All other new accounting standards and updates of existing standards issued during the quarter ended March 31, 2010 did not relate to accounting policies and procedures pertinent to the Company at this time.

3. FAIR VALUES

Fair Values Hierarchy
In accordance with FASB ASC 820, "Fair Value Measurements and Disclosures," the Company groups its financial assets and liabilities measured at fair value in three levels, based on the inputs and assumptions used to determine the fair value. These levels are as follows:

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

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

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

Determination of Fair Value
The Company bases fair values on the price that would be received to sell an asset (exit price) or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is the Company's policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements. Accordingly, the Company utilizes independent third-party pricing services to determine the majority of its fair values.

The Company reviews prices received from service providers for unusual fluctuations but generally accepts the price identified from the primary pricing service. However, if the primary pricing service does not provide a price, the Company utilizes a second pricing service if a price is available. In the event a price is not available from either third-party pricing service, the Company pursues external pricing from brokers. Generally, the Company pursues and utilizes only one broker quote per security. In doing so, the Company solicits only brokers which have previously demonstrated knowledge and experience of the subject security. If a broker price is not available, the Company determines a carrying value through various valuation techniques that include using option pricing models, discounted cash flows, spread-based models or similar techniques depending upon the specific security to be priced. These techniques are primarily applied to private placement securities. The Company utilizes available market information, wherever possible, to identify inputs into the fair value determination, primarily including prices and spreads on comparable securities.

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

The Company owned six issues of similar securities for which values were not provided from the Company's primary pricing service as of March 31, 2010. The Company received quoted prices from brokers for five of these securities. Since all six securities are similar, the Company utilized the mid-point of these prices to determine the fair value for these six securities. In addition, the Company had one security where the fair value utilized was different from the independent pricing service. The fair value was instead developed through internal estimates and resulted in an increase in the recorded fair value of $0.2 million.

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

The Company's own estimates of fair value are derived in a number of ways including, but not limited to: 1) pricing provided by brokers, where the price indicates reliability as to value; 2) fair values of comparable securities incorporating a spread adjustment for maturity differences, collateralization, credit quality, liquidity, and other items, if applicable; 3) discounted cash flow models and margin spreads; 4) bond yield curves; 5) observable market prices and exchange transaction information not provided by external pricing services; 6) statement values provided to the Company by fund managers; and 7) option pricing models.

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

Assets

Securities Available for Sale

Fixed maturities and equity securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are determined as described in the preceding paragraphs.

Short-Term Financial Assets

Short-term financial assets include cash and other short-term investments and are carried at historical cost. The carrying amount is a reasonable estimate of the fair value because of the relatively short time between the purchase of the instrument and its expected repayment or maturity.

Loans

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

Fair values of mortgage loans on real estate properties are calculated by discounting contractual cash flows, using discount rates based on current industry pricing or the Company's estimate of an appropriate risk-adjusted discount rate for loans of similar size, type, remaining maturity and repricing characteristics.

The Company also has loans made to policyholders. These loans cannot exceed the cash surrender value of the policy. Fair value is calculated by discounting contractual cash flows, using discount rates based on the Company's estimate of appropriate risk-adjusted discount rates for these loans.

Liabilities

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

Fair values for liabilities under investment-type insurance contracts are based upon account value. The fair values of investment-type insurance contracts included with policyholder account balances for fixed deferred annuities and other policyholder funds for supplementary contracts without life contingencies are estimated to be their cash surrender values. The fair values of deposits with no stated maturity are equal to the amount payable on demand at the measurement date.

Guaranteed Minimum Withdrawal Benefits (GMWB)

The Company offers a GMWB rider that can be added to new or existing variable annuity contracts. The rider provides an enhanced withdrawal benefit that guarantees a stream of income payments to an owner or annuitant, regardless of the contract account value. The value of variable annuity separate accounts with the GMWB rider was $65.5 million and the guarantee liability was $(1.9) million at March 31, 2010 compared to $57.9 million and $(1.6) million, respectively, at December 31, 2009. The value of the GMWB rider is recorded at fair value, and the change in this value is included in policyholder benefits in the Consolidated Statements of Income. The value of variable annuity separate accounts with the GMWB rider is recorded in separate account liabilities and the value of the rider is included in other policyholder funds in the Consolidated Balance Sheets. Fair value for GMWB rider contracts results in a Level 3 valuation as it is based on models which utilize significant unobservable inputs. These models require actuarial and financial market assumptions, which reflect the assumptions market participants would use in pricing the contract, including adjustments for risk and issuer non-performance.

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

Notes Payable
The Company had no short-term borrowings at March 31, 2010 or December 31, 2009. The carrying amount of borrowings are determined by a reasonable estimate of fair value because of the relatively short time between the origination of the borrowings and their expected repayment and maturities.

Categories Reported at Fair Value
The following tables present categories reported at fair value on a recurring basis.

	March 31, 2010			
Assets:	Level 1	Level 2	Level 3	Total
Bonds:				
U.S. Treasury securities and				
obligations of U.S. Government	$11,152	$112,824	$8,246	$132,222
Federal agencies 1	-	28,951	-	28,951
Federal agency issued				
residential mortgage-backed securities 1	-	167,158	-	167,158
Subtotal	11,152	308,933	8,246	328,331
Corporate obligations:				
Industrial	-	425,412	2,963	428,375
Energy	-	199,303	-	199,303
Technology	-	41,206	-	41,206
Communications	-	82,647	-	82,647
Financial	-	368,554	2,726	371,280
Consumer	-	276,602	22,254	298,856
Public utilities	-	293,452	-	293,452
Subtotal	-	1,687,176	27,943	1,715,119
Corporate private-labeled residential				
mortgage-backed securities	-	199,951	-	199,951
Other	-	272,955	8,783	281,738
Redeemable preferred stocks	14,012	-	-	14,012
Subtotal	25,164	2,469,015	44,972	2,539,151
Equity securities	3,691	27,986	6,149	37,826
Total	$28,855	$2,497,001	$51,121	$2,576,977
Percent of Total	1 %	97 %	2 %	100 %
Liabilities:				
Other policyholder funds				
Guaranteed minimum withdrawal benefits	$-	$-	$(1,873)	$(1,873)
Total	$-	$-	$(1,873)	$(1,873)

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

16

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

	December 31, 2009			
Assets:	Level 1	Level 2	Level 3	Total
Bonds:				
U.S. Treasury securities and				
obligations of U.S. Government	$9,939	$97,723	$14,275	$121,937
Federal agencies 1	-	28,321	-	28,321
Federal agency issued				
residential mortgage-backed securities 1	-	172,515	-	172,515
Subtotal	9,939	298,559	14,275	322,773
Corporate obligations:				
Industrial	-	412,292	3,654	415,946
Energy	-	200,340	-	200,340
Technology	-	40,864	-	40,864
Communications	-	86,264	-	86,264
Financial	-	361,768	2,840	364,608
Consumer	-	284,910	22,596	307,506
Public utilities	-	287,687	-	287,687
Subtotal	-	1,674,125	29,090	1,703,215
Corporate private-labeled residential				
mortgage-backed securities	-	200,002	-	200,002
Other	-	220,572	9,109	229,681
Redeemable preferred stocks	13,601	-	-	13,601
Subtotal	23,540	2,393,258	52,474	2,469,272
Equity securities	3,400	27,427	6,049	36,876
Total	$26,940	$2,420,685	$58,523	$2,506,148
Percent of Total	1 %	97 %	2 %	100 %
Liabilities:				
Other policyholder funds				
Guaranteed minimum withdrawal benefits	$-	$-	$(1,642)	$(1,642)
Total	$-	$-	$(1,642)	$(1,642)

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

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

The following table presents the fair value of fixed maturities and equity securities available for sale by pricing source and fair value hierarchy level.

	March 31, 2010			
	Level 1	Level 2	Level 3	Total
Fixed maturities available for sale:				
Priced from external pricing services	$25,164	$2,353,240	$-	$2,378,404
Priced from independent broker quotations	-	111,210	-	111,210
Priced from internal matrices and calculations	-	4,565	44,972	49,537
Subtotal	25,164	2,469,015	44,972	2,539,151
Equity securities available for sale:				
Priced from external pricing services	3,691	2,491	-	6,182
Priced from independent broker quotations	-	-	-	-
Priced from internal matrices and calculations	-	25,495	6,149	31,644
Subtotal	3,691	27,986	6,149	37,826
Total	$28,855	$2,497,001	$51,121	$2,576,977
Percent of Total	1 %	97 %	2 %	100 %

	December 31, 2009			
	Level 1	Level 2	Level 3	Total
Fixed maturities available for sale:				
Priced from external pricing services	$23,540	$2,277,303	$-	$2,300,843
Priced from independent broker quotations	-	111,587	-	111,587
Priced from internal matrices and calculations	-	4,368	52,474	56,842
Subtotal	23,540	2,393,258	52,474	2,469,272
Equity securities available for sale:				
Priced from external pricing services	3,400	2,407	-	5,807
Priced from independent broker quotations	-	-	-	-
Priced from internal matrices and calculations	-	25,020	6,049	31,069
Subtotal	3,400	27,427	6,049	36,876
Total	$26,940	$2,420,685	$58,523	$2,506,148
Percent of Total	1 %	97 %	2 %	100 %

The changes in Level 1 assets measured at fair value on a recurring basis for the quarter ended March 31, 2010 are summarized below:

March 31, 2010						
Beginning Balance as	Included	Included in Other	Purchases	Net	Ending Balance as of	Net Unrealized Gains

	of December 31, 2009	in Earnings	Comprehensive Income	and Dispositions	Transfers in (out)	March 31, 2010	(Losses) at March 31, 2010
Assets:							
Fixed maturities available for sale	$23,540	$(3)	$ 329	$ -	$1,298	$25,164	$329
Equity securities available for sale	3,400	-	291	-	-	3,691	291
Total	$26,940	$(3)	$ 620	$ -	$1,298	$28,855	$620

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

The changes in Level 2 assets measured at fair value on a recurring basis for the quarter ended March 31, 2010 are summarized below:

	March 31, 2010						
	Beginning Balance as of December 31, 2009	Included in Earnings	Included in Other Comprehensive Income	Purchases and Dispositions	Net Transfers in (out)	Ending Balance as of March 31, 2010	Net Unrealized Gains (Losses) at March 31, 2010
Assets:							
Fixed maturities available for sale	$2,393,258	$706	$ 39,176	$ 27,240	$8,635	$2,469,015	$39,897
Equity securities available for sale	27,427	-	85	474	-	27,986	85
Total	$2,420,685	$706	$ 39,261	$ 27,714	$8,635	$2,497,001	$39,982

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the quarter ended March 31, 2010 and year ended December 31, 2009 are summarized below:

	March 31, 2010						
	Beginning Balance as of December 31, 2009	Included in Earnings	Included in Other Comprehensive Income	Purchases and Dispositions	Net Transfers in (out)	Ending Balance as of March 31, 2010	Net Unrealized Gains (Losses) at March 31, 2010
Assets:							
Fixed maturities available for sale	$52,474	$(336)	$ (200)	$2,967	$(9,933)	$44,972	$(200)
Equity securities available for sale	6,049	-	100	-	-	6,149	100

Total	$58,523	$(336)	$ (100)	$2,967	$(9,933)	$51,121	$(100)
Liabilities:							
Other policyholder funds- guaranteed minimum withdrawal benefits	$(1,642)	$(233)	$ -	$2	$-	$(1,873)	$-

	December 31, 2009						
	Beginning Balance as of December 31, 2008	Included in Earnings	Included in Other Comprehensive Income	Purchases and Dispositions	Net Transfers in (out)	Ending Balance as of December 31, 2009	Net Unrealized Gains (Losses) at December 31, 2009
Assets:							
Fixed maturities available for sale	$ 89,499	$ (1,172)	$ 3,100	$ (1,985)	$ (36,968)	$ 52,474	$ 2,533
Equity securities available for sale	5,141	-	229	(129)	808	6,049	228
Total	$ 94,640	$ (1,172)	$ 3,329	$ (2,114)	$ (36,160)	$ 58,523	$ 2,761
Liabilities:							
Other policyholder funds- guaranteed minimum withdrawal benefits	$ 755	$ (2,452)	$ -	$ 55	$ -	$ (1,642)	$ -

The roll forward of Level 3 assets begins with the prior period balance and adjusts the balance for the gains or losses (realized and unrealized) that occurred during the current period. Any new purchases that are identified as Level 3 securities are then added and any sales of securities which were previously identified as Level 3 are subtracted. Next, any securities

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

which were previously identified as Level 1 or Level 2 securities and which are currently identified as Level 3 are added. Finally, securities which were previously identified as Level 3 and which are now designated as Level 1 or as Level 2 are subtracted. The ending balance represents the current fair value of securities which are designated as Level 3.

The roll forward of Level 3 liabilities begins with the prior period balance and adjusts for the realized gains or losses that occurred during the current period. These realized gains or losses are reflected as policyholder benefits in the Consolidated Statements of Income. Issuances, or new sales, are then added and settlements are subtracted. The ending balance represents the current fair value of liabilities which are designated as Level 3. The guaranteed minimum withdrawal benefits balance totaled $(1.6) million at December 31, 2009. This balance decreased in value by $0.2 million during 2010, largely due to favorable returns in the capital markets.

The Company had $0.4 million transfers into Level 3 and $10.3 million transfers out of Level 3 for the quarter ended March 31, 2010. The Company did not exclude any realized or unrealized gains or losses on items transferred into Level 3. Transfers into Level 3 occur when the Company, it its opinion, cannot obtain a fair value that it believes is a Level 1 or Level 2 fair value.

The following table provides amortized cost and fair value for securities by asset class at March 31, 2010.

		Gross		
	Amortized	Unrealized		Fair
Bonds:	Cost	Gains	Losses	Value
U.S. Treasury securities and				
obligations of U.S. Government	$127,726	$5,325	$829	$132,222
Federal agencies 1	27,453	1,498	-	28,951
Federal agency issued				
residential mortgage-backed securities 1	158,378	8,807	27	167,158
Subtotal	313,557	15,630	856	328,331
Corporate obligations:				
Industrial	408,570	21,826	2,021	428,375
Energy	186,121	13,473	291	199,303
Technology	39,352	2,171	317	41,206
Communications	79,884	3,598	835	82,647
Financial	368,771	11,363	8,854	371,280
Consumer	281,560	18,760	1,464	298,856
Public utilities	276,506	18,853	1,907	293,452
Total corporate obligations	1,640,764	90,044	15,689	1,715,119
Corporate private-labeled residential				
mortgage-backed securities	235,946	622	36,617	199,951
Other	295,555	5,248	19,065	281,738
Redeemable preferred stocks	14,866	208	1,062	14,012
Fixed maturity securities	2,500,688	111,752	73,289	2,539,151
Equity securities	35,880	2,108	162	37,826
Total	$2,536,568	$113,860	$73,451	$2,576,977

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

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

The following table provides amortized cost and fair value for securities by asset class at December 31, 2009.

		Gross		
	Amortized	Unrealized		Fair
Bonds:	Cost	Gains	Losses	Value
U.S. Treasury securities and				
obligations of U.S. Government	$118,284	$4,674	$1,021	$121,937
Federal agencies 1	27,640	681	-	28,321
Federal agency issued				
residential mortgage-backed securities 1	165,350	7,220	55	172,515
Subtotal	311,274	12,575	1,076	322,773
Corporate obligations:				
Industrial	400,775	17,773	2,602	415,946
Energy	190,836	10,703	1,199	200,340
Technology	39,358	1,919	413	40,864
Communications	84,146	3,492	1,374	86,264
Financial	371,179	9,247	15,818	364,608
Consumer	294,732	15,210	2,436	307,506
Public utilities	273,796	16,012	2,121	287,687
Total corporate obligations	1,654,822	74,356	25,963	1,703,215
Corporate private-labeled residential				
mortgage-backed securities	242,545	387	42,930	200,002
Other	247,009	4,349	21,677	229,681
Redeemable preferred stocks	14,866	98	1,363	13,601
Fixed maturity securities	2,470,516	91,765	93,009	2,469,272
Equity securities	35,405	1,657	186	36,876
Total	$2,505,921	$93,422	$93,195	$2,506,148

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

The table below is a summary of fair value estimates as of March 31, 2010 and December 31, 2009 for financial instruments. The Company has not included assets and liabilities that are not financial instruments in this disclosure. The total of the fair value calculations presented do not represent, and should not be construed to represent, the underlying value of the Company.

	March 31, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Investments:				
Fixed maturities available for sale	$2,539,151	$2,539,151	$2,469,272	$2,469,272
Equity securities available for sale	37,826	37,826	36,876	36,876
Mortgage loans	456,489	471,530	457,582	456,819
Policy loans	84,896	84,896	85,585	85,585
Cash and short-term investments	112,579	112,579	143,685	143,685
Separate account assets	324,924	324,924	312,824	312,824

Liabilities:				
Individual and group annuities	1,001,724	980,164	999,500	977,573
Notes payable	-	-	-	-
Supplementary contracts without life contingencies	58,963	57,234	59,399	57,023
Separate account liabilities	324,924	324,924	312,824	312,824

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

4. INVESTMENTS

Contractual Maturities

The following table provides the distribution of maturities for fixed maturity investment securities available for sale as of March 31, 2010. Expected maturities may differ from these contractual maturities since borrowers may have the right to call or prepay obligations.

	Amortized Cost	Fair Value
Due in one year or less	$91,889	$93,485
Due after one year through five years	528,032	556,438
Due after five years through ten years	813,971	855,834
Due after ten years	554,553	544,909
Securities with variable principal payments	497,377	474,473
Redeemable preferred stocks	14,866	14,012
	$2,500,688	$2,539,151

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

Realized Gains (Losses)
The following table provides detail concerning realized investment gains and losses by asset class for the quarters ended March 31, 2010 and 2009.

	Quarter Ended March 31	
	2010	2009
Gross gains resulting from:		
Sales of investment securities:		
Corporate obligations:		
Industrial	$229	$-
Communications	297	-
Consumer	477	-
Investment securities called and other:		
Federal agency issued		
residential mortgage-backed securities 1	-	191
Corporate obligations:		
Industrial	175	-
Energy	53	-
Consumer	19	-
Corporate private-labeled residential		
mortgage-backed securities	1	-
Other	50	58
Sales of real estate	-	661
Total gross gains	1,301	910
Gross losses resulting from:		
Sales of investment securities	-	-
Investment securities called and other:		
Other	(88)	(1)
Total gross losses	(88)	(1)
Amortization of DAC and VOBA	110	505
Net realized investment gains, excluding		
impairment losses	1,323	1,414

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

	Quarter Ended March 31	
	2010	2009
Net impairment losses recognized in earnings:		
Corporate obligations:		
Industrial	-	(4,332)
Financial	-	(2,011)
Consumer	-	(1,697)
Corporate private-labeled residential mortgage-backed securities	(851)	(13,366)
Other	(740)	-
Total other-than-temporary impairment losses	(1,591)	(21,406)
Portion of loss recognized in other comprehensive income:		
Corporate obligations:		
Industrial	-	1,676
Financial	-	465
Consumer	-	462
Corporate private-labeled residential mortgage-backed securities	5	12,685
Net impairment losses recognized in earnings	(1,586)	(6,118)
Realized investment losses	$(263)	$(4,704)

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

Unrealized Losses on Investments

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

The Company has a policy and process in place to identify securities that could potentially have an impairment that is other-than-temporary. This process involves monitoring market events and other items that could impact issuers. The evaluation includes but is not limited to such factors as the issuer’s stated intent and ability to make all principal and interest payments when due, near-term business prospects, cash flow and liquidity, credit ratings, business climate, management changes and litigation and government actions. This process also involves monitoring several factors including late payments, downgrades by rating agencies, key financial ratios, financial statements, revenue forecasts, asset quality and cash flow projections, as indicators of credit issues.

The Company considers relevant facts and circumstances in evaluating whether the impairment of a security is other-than-temporary. Relevant facts and circumstances considered are described in the Valuation of Investments section of Note 1 – Nature of Operations and Significant Accounting Policies.

To the extent the Company determines that a fixed maturity security is deemed to be other-than-temporarily impaired, the portion of the impairment that is deemed to be due to credit is charged to the Consolidated Statements of Income and the cost basis of the underlying investment is reduced. The portion of the impairment that is deemed to be non-credit is charged to other comprehensive income (loss). Equity securities that were determined to be other-than-temporarily impaired are written down to fair value and the impairment is charged to the Consolidated Statements of Income.

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

At March 31, 2010, the Company had gross unrealized losses of $73.5 million on investment securities, including fixed maturity and equity securities that had a fair value of $751.8 million. In addition, included in the gross unrealized losses are securities that the Company determined had other-than-temporary impairments. Accordingly, the Company bifurcated these impairments between credit and non-credit impairments. As identified in the Consolidated Statements of Income, the Company had non-credit impairments of less than $0.1 million on securities considered to be impaired for the three months ended March 31, 2010. As of December 31, 2009, the Company had gross unrealized losses of $93.2 million on investment securities, including fixed maturity and equity securities that had a fair value of $814.4 million. The decrease in unrealized losses was primarily attributable to decreased credit and liquidity risk discounts in the pricing of financial assets. Although these changes affected the broad financial markets, specific sectors, security issuers and security issues were affected differently.

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

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

If the cash flow for a collateralized security is determined to be less than the amortized cost, the difference is recorded as an other-than-temporary impairment due to credit in the Consolidated Statements of Income.

The total impairment for any security that is deemed to have an other-than-temporary impairment is recorded in the statement of income as a net realized loss from investments. The portion of such impairment that is determined to be non-credit-related is deducted from net realized loss in the Consolidated Statements of Income and reflected in other comprehensive income (loss) and accumulated other comprehensive loss, which is a component of stockholders' equity in the Consolidated Balance Sheets.

As part of the required accounting for unrealized gains and losses, the Company also adjusts the DAC and VOBA assets to recognize the adjustment to those assets as if the unrealized gains and losses from securities classified as available-for-sale actually had been realized.

Kansas City Life Insurance Company
Notes to Consolidated Financial Statements (Unaudited)-Continued

The following table provides information regarding unrealized losses on fixed maturity and equity security investments available for sale as of March 31, 2010.

	Less Than 12 Months		12 Months or Longer		Total	
Bonds:	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government	$41,373	$724	$3,024	$105	$44,397	$829
Federal agency issued residential mortgage-backed securities 1	-	-	5,964	27	5,964	27
Subtotal	41,373	724	8,988	132	50,361	856
Corporate obligations:						
Industrial	59,510	1,160	15,580	861	75,090	2,021
Energy	9,322	42	5,085	249	14,407	291
Technology	4,069	17	7,407	300	11,476	317
Communications	4,422	36	17,432	799	21,854	835
Financial	36,380	606	103,428	8,248	139,808	8,854
Consumer	16,014	716	17,869	748	33,883	1,464
Public utilities	31,662	725	11,783	1,182	43,445	1,907
Total corporate obligations	161,379	3,302	178,584	12,387	339,963	15,689
Corporate private-labeled residential mortgage-backed securities	12,724	163	155,628	36,454	168,352	36,617
Other	42,877	714	139,452	18,351	182,329	19,065
Redeemable preferred stocks	831					