JEFFERSON PILOT CORP
Form 10-Q
May 07, 2004

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

Quarterly Report Under Section 13 or 15(d)
of the Securities Exchange Act of 1934

For Quarter Ended March 31, 2004 Commission file number 1-5955

Jefferson-Pilot Corporation

(Exact name of registrant as specified in its charter)

North Carolina	56-0896180
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 North Greene Street, Greensboro, North Carolina	27401
(Address of principal executive offices)	(Zip Code)

(336) 691-3000
(Registrant s telephone number, including area code)

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 is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes [X] No [ ]

Number of shares of common stock outstanding at March 31, 2004 139,824,510

JEFFERSON-PILOT CORPORATION

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

JEFFERSON-PILOT CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	March 31 2004	December 31 2003
	(Dollar Amounts in Millions Except Share Information)	
ASSETS		
Investments:		
Debt securities available for sale, at fair value (amortized cost $17,829 and $16,819)	$19,061	$ 17,706
Debt securities held to maturity, at amortized cost (fair value $2,876 and $2,918)	2,661	2,752
Equity securities available for sale, at fair value (cost $299 and $304)	731	756
Mortgage loans on real estate	3,497	3,472
Policy loans	872	869
Real estate	131	132
Other investments	83	65
Total investments	27,036	25,752
Cash and cash equivalents	120	72
Accrued investment income	337	326
Due from reinsurers	1,322	1,340
Deferred policy acquisition costs and value of business acquired	2,195	2,230
Goodwill	312	312
Assets held in separate accounts	2,229	2,166
Other assets	633	498
Total assets	$34,184	$ 32,696
LIABILITIES AND STOCKHOLDERS EQUITY		
Policy liabilities:		
Future policy benefits	$ 3,014	$ 2,674
Policyholder contract deposits	21,005	20,642
Dividend accumulations and other policyholder funds on deposit	249	251
Policy and contract claims	248	165
Other	737	638
Total policy liabilities	25,253	24,370
Commercial paper borrowings	154	654

Obligations under repurchase agreements	454	401
Long-term notes payable	600	
Junior subordinated debentures	309	309
Currently recoverable income taxes	(95)	(72)
Deferred income tax liabilities	710	543
Liabilities related to separate accounts	2,229	2,166
Accounts payable, accruals and other liabilities	600	519
Total liabilities	30,214	28,890
Stockholders Equity:		
Common stock and paid in capital, par value $1.25 per share: authorized 350,000,000 shares; issued and outstanding 2004-139,824,510 shares; 2003-140,610,540 shares	175	176
Retained earnings	2,966	2,947
Accumulated other comprehensive income	829	683
	3,970	3,806
Total liabilities and stockholders equity	$34,184	$ 32,696

See Notes to Consolidated Financial Statements

JEFFERSON-PILOT CORPORATION AND SUBSIDIARIES

CONSOLIDATED UNAUDITED CONDENSED STATEMENTS OF INCOME

	Three Months Ended March 31 2004	2003
	(Dollar Amounts in Millions Except Share Information)	
Revenue:		
Premiums and other considerations	$ 280	$ 231
Universal life and investment product charges	182	172
Net investment income	406	410
Realized investment gains (losses)	24	(19)
Communications sales	58	50
Other	35	24
Total revenue	985	868
Benefits and Expenses:		
Insurance and annuity benefits	541	498
Insurance commissions, net of deferrals	59	25
General and administrative expenses, net of deferrals	38	31
Insurance taxes, licenses and fees	17	21
Amortization of policy acquisition costs and value of business acquired	67	82
Interest expense	11	9
Communications operations	37	35
Total benefits and expenses	770	701
Income before income taxes and cumulative effect of change in accounting principle	215	167
Income taxes	74	58
Income before cumulative effect of change in accounting principle	141	109
Cumulative effect of change in accounting for long-duration contracts, net of taxes	(13)	
Net income	$ 128	$ 109
Average number of shares outstanding	140.7	142.8
Net Income Per Share of Common Stock:		
Net income	$ 0.91	$ 0.76
Net income assuming dilution	$ 0.90	$ 0.76

Dividends declared per common share	$0.330	$0.303

See Notes to Consolidated Financial Statements

JEFFERSON-PILOT CORPORATION

CONSOLIDATED UNAUDITED CONDENSED STATEMENTS OF CASH FLOWS (In Millions)

	Three Months Ended March 31 2004	Three Months Ended March 31 2003
Cash Flows from Operating Activities	$ 482	$ 89
Cash Flows from Investing Activities:		
Securities and loans purchased, net	(806)	(184)
Other investing activities	(24)	3
Net cash used in investing activities	(830)	(181)
Cash Flows from Financing Activities:		
Policyholder contract deposits	730	637
Policyholder contract withdrawals	(383)	(405)
Net borrowings (repayments)	152	(83)
Net repurchase of common shares	(63)	(30)
Cash dividends paid	(47)	(43)
Other financing activities	7	2
Net cash provided by financing activities	396	78
Increase (decrease) in cash and cash equivalents	48	(14)
Cash and cash equivalents at beginning of period	72	67
Cash and cash equivalents at end of period	$ 120	$ 53
Supplemental Cash Flow Information:		
Income taxes (received) paid	$ (6)	$ 45
Interest paid	$ 16	$ 16

See Notes to Consolidated Financial Statements

JEFFERSON-PILOT CORPORATION

NOTES TO CONSOLIDATED UNAUDITED CONDENSED FINANCIAL STATEMENTS
(Dollar amounts in millions)

1. Basis of Presentation

The accompanying consolidated unaudited condensed financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with 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 accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All significant intercompany accounts and transactions have been eliminated in consolidation. Operating results for the three-month period ended March 31, 2004 are not necessarily indicative of the results that may be expected for the year ended December 31, 2004. Certain prior year amounts have been reclassified to conform with the current year presentation.

2. Significant Accounting Policies

Stock Based Compensation

The Company accounts for stock incentive awards in accordance with APB Opinion No. 25, *Accounting for Stock Issued to Employees"*, and accordingly, recognizes no compensation expense for stock option awards to employees or directors when the option price is not less than the market value of the stock at the date of award. The Company recognizes expense utilizing the fair value method in accordance with SFAS 123 for stock options granted to non-employees, specifically agents.

SFAS 123 requires the presentation of pro forma information as if the Company had accounted for its employee and director stock options granted after December 31, 1994 under the fair value method of that Statement.

The following is a reconciliation of reported net income and proforma information as if the Company had adopted SFAS 123 for its employee and director stock option awards:

	Three Months Ended March 31 2004	Three Months Ended March 31 2003
Net income, as reported	$ 128	$ 109
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	3	3
Pro forma net income available to common stockholders	$ 125	$ 106
Earnings per share available to common stockholders, as reported	$ 0.91	$ 0.76
Pro forma earnings per share available to common stockholders	$ 0.89	$ 0.75
Earnings per share available to common stockholders assuming dilution, as reported	$ 0.90	$ 0.76
Pro forma earnings per share available to common stockholders assuming dilution	$ 0.88	$ 0.74

Except as described otherwise herein, all significant accounting policies remain as we described in our Form 10-K for 2003.

3. Segment Reporting

The Company has five reportable segments that are defined based on the nature of the products and services offered: Individual Products, Annuity and Investment Products (AIP), Benefit Partners, Communications, and Corporate and Other. The segments remain as we described in our Form 10-K for 2003.

The following table summarizes certain financial information regarding the Company s reportable segments:

	March 31 2004	December 31 2003
Assets		
Individual Products	$18,087	$17,717
AIP	10,293	9,941
Benefit Partners	1,710	1,079
Communications	199	210
Corporate & other	3,895	3,749
Total assets	$34,184	$32,696

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	Three Months Ended March 31 2004	2003
Revenues		
Individual Products	$ 444	$ 442
AIP	175	170
Benefit Partners	251	198
Communications	58	50
Corporate & Other	33	27
	961	887
Realized investment gains (losses), before taxes	24	(19)
Total revenues	$ 985	$ 868
Reportable segments results and reconciliation to net income available to common stockholders		
Individual Products	$ 75	$ 76
AIP	19	21
Benefit Partners	11	12
Communications	11	7
Corporate & Other	10	5
Total reportable segment results	126	121
Realized investment gains (losses), net of taxes	15	(12)
Income before cumulative effect of change in accounting principle	141	109
Cumulative effect of change in accounting principle, net of taxes	(13)	
Net income	$ 128	$ 109

4. Income from Continuing Operations Per Share of Common Stock

The following table sets forth the computation of earnings per share and earnings per share assuming dilution:

	Three Months Ended March 31 2004	Three Months Ended March 31 2003
Numerator:		
Net income before cumulative effect of change in accounting principle	$ 141	$ 109
Cumulative effect of change in accounting principle, net of taxes	(13)	
Numerator for earnings per share and earnings per share assuming dilution Net income available to common stockholders	$ 128	$ 109
Denominator:		
Denominator for earnings per share weighted-average shares outstanding	140,659,329	142,804,138
Effect of dilutive securities:		
Stock options	1,509,952	858,199
Denominator for earnings per share assuming dilution adjusted weighted-average shares outstanding	142,169,281	143,662,337
Income before cumulative effect of change in accounting principle	$ 1.00	$ 0.76
Cumulative effect of change in accounting principle, net of taxes	(0.09)	
Earnings per share	$ 0.91	$ 0.76
Income before cumulative effect of change in accounting principle	$ 0.99	$ 0.76
Cumulative effect of change in accounting principle, net of taxes	(0.09)	

Earnings per share assuming dilution	$ 0.90	$ 0.76

5. Contingent Liabilities

A life insurance subsidiary is a defendant in a proposed class action suit. The suit alleges that a predecessor company, decades ago, unfairly discriminated in the sale of certain small face amount life insurance policies, and unreasonably priced these policies. Management believes that the life company s practices have complied with state insurance laws and intends to vigorously defend the claims asserted.

In the normal course of business, the Company and its subsidiaries are parties to various lawsuits. Because of the considerable uncertainties that exist, the Company cannot predict the outcome of pending or future litigation. However, management believes that the resolution of pending legal proceedings will not have a material adverse effect on the Company s financial position or liquidity, although it could have a material adverse effect on the results of operations for a specified period.

6. Accounting Pronouncements

FIN 46

The Financial Accounting Standards Board (FASB) has issued Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin No. 51* (FIN 46). Under FIN 46, an enterprise consolidates a variable interest entity (VIE), as defined, if the enterprise absorbs a majority of the VIE s expected losses, receives a majority of its expected residual returns, or both, as a result of ownership, contractual or other financial interests in the VIE. Prior to FIN 46, entities were generally consolidated by an enterprise only when it had a controlling financial interest through ownership of a majority voting interest in the entity. In accordance with FIN 46, effective December 31, 2003, the Company deconsolidated Jefferson Pilot Capital Trust A and Jefferson Pilot Capital Trust B (the Trusts), VIE s that issued $300 of redeemable preferred securities in private placement transaction in 1997. All periods presented have been restated accordingly. The redeemable preferred securities were previously presented in the Company s financial statements as Capital Securities in the consolidated balance sheets. Dividends on the Capital Securities were presented in the consolidated statements of income as a deduction to arrive at net income available to common stockholders, and as a financing outflow on the consolidated statements of cash flows. As a result of the deconsolidation of the Trusts, the consolidated balance sheets now reflect junior subordinated debentures purchased from the Company by the Trusts in 1997, which had previously been eliminated in consolidation. Interest expense on the junior subordinated debentures is presented as interest expense in the consolidated statements of income and is presented as an operating cash outflow on the consolidated statements of cash flow.

SOP 03-1

In July 2003, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants issued Statement of Position 03-1 Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts (the SOP or SOP 03-1). The SOP addresses: (i) separate account presentation; (ii) accounting for an insurance company s proportionate interest in separate accounts; (iii) transfers of assets from the general account to a separate account; (iv) valuation of certain insurance liabilities and policy features such as guaranteed minimum death benefits and annuitization benefits; and (v) accounting for sales inducements. The SOP was effective January 1, 2004 and was adopted through an adjustment for the cumulative effect of a change in accounting principle. Our cumulative effect of adjustment of $13 related primarily to accounting for sales inducements resident in certain of our older policies and the establishment of additional policy liabilities for secondary guarantees contained in our newer products. While we had previously provided for these items in our financial statements, the SOP prescribed new methods of valuation. Each of these items was at least partially offset by adjustments to related balances of deferred acquisition costs (DAC) or value of business acquired (VOBA), or in the case of sales inducements, by the establishment of a deferred sales inducement asset. The gross amount of additional policy liabilities established was approximately $9, with $0.1 pertaining to guaranteed minimum death benefits on variable universal life (VUL) products. No additional reserves were necessary related to minimum guaranteed death benefits on variable annuities (VAs), as our alreadyexisting policy liabilities (which are less than $0.9) proved to be adequate under the new standard with respect to this feature. In addition to the cumulative effect of adoption, the SOP reduced our income before cumulative effect of change in accounting principle for the three months ended March 31, 2004 by $2.

The Company has policies in force containing two primary types of sales inducements: 1) day one bonuses on fixed annuities, which are in the form of either an increased interest rate for a stated period or an additional premium credit; and 2) persistency-related interest credited bonuses. The fixed annuity bonuses were previously being capitalized and amortized as a component of DAC. Thus, there was no cumulative impact upon adoption other than a balance sheet reclassification of the deferred amount out of DAC into deferred sales inducements. The persistency-related bonuses were previously expensed on a pay-as-you-go basis. These bonuses are now accrued over the period in which the policy must remain in force for the policyholder to qualify for the inducement. Capitalized sales inducements are amortized using the same methodology and assumptions used to amortize DAC. The following table rolls forward our deferred sales inducement asset for the three months ended March 31, 2004.

Balance, December 31, 2003	$
Cumulative impact of adoption, including $30 reclassified from DAC	68
Additional amounts deferred	3
Amortization	(2)
Balance, March 31, 2004	$69

Separate account assets and liabilities represent funds segregated for the benefit of certain policyholders who bear the investment risk. SOP 03-1 did not impact our accounting policies with respect to separate accounts, as they meet the criteria for summary presentation contained in the SOP. Separate account assets and liabilities are equal and are recorded at fair value. Policyholder deposits and withdrawals, investment income and related realized investment gains and losses are excluded from the amounts reported in our income statement. Fees charged on policyholder deposits are included in universal life and investment product charges. The policies reported in our separate accounts are VA and VUL policies. As indicated above, the amounts of minimum guarantees or other similar benefits related to these policies are negligible.

Implementation and accounting guidance pertaining to the SOP is still evolving. While we do not expect this additional guidance to affect the amounts we have reported related to our implementation of the SOP, there is no assurance it will not.

7. Retirement Benefit Plans

The following table illustrates the components of net periodic benefit cost for our pension plans:

	Three Months Ended March 31	
	2004	**2003**
Service cost	$ 4	$ 3
Interest cost	6	5
Expected return on plan assets	(8)	(8)
Amortization of prior service cost		
Amortization of net (gain) loss		
Net periodic benefit cost	$ 2	$

The Company expects to make payments of $6 to $10 during 2004 related to our nonqualified plans, which are unfunded. No contributions were made during the three months ended March 31, 2004.

Other Postretirement Benefit Plans

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act (the Act) was signed into law. The Act includes a federal subsidy to sponsors of retiree health plans that provide a prescription drug benefit that is at least actuarially equivalent to the benefit to be provided under Medicare Part D. While we are still evaluating the provisions of the Act, we expect it will have a favorable impact on our postretirement benefits liability. We do not expect the impact to be material to our results of operations or our financial position. The Company has elected to defer recognition of any accounting effects of the Act until authoritative guidance is issued by the Financial Accounting Standards Board.

8. Canada Life Transaction

Effective March 1, 2004, we acquired via a reinsurance transaction substantially all of the in-force U.S. group life, disability and dental business of The Canada Life Assurance Company, an indirect subsidiary of Great-West Lifeco Inc. Upon closing, Canada Life ceded, and the Company assumed, approximately $400 million of policy liabilities. The company also received assets, primarily cash, to back the liabilities. As a result of the transaction we recorded DAC in the amount of $35 and an intangible asset of $25 representing the value of the sales force acquired as part of the transaction. The DAC will be amortized over 15 years, representing the premium-paying period of the acquired blocks. The sales force asset will be amortized over 30 years, representing the period over which we expect to earn premiums from new sales stemming from the added distribution capacity.

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

JEFFERSON-PILOT CORPORATION AND SUBSIDIARIES

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management s Discussion and Analysis of Financial Condition and Results of Operations analyzes the consolidated financial condition, changes in financial position and results of operations for the three months ended March 31, 2004, as compared to the same period of 2003, of Jefferson-Pilot Corporation and consolidated subsidiaries. The discussion supplements Management s Discussion and Analysis in Form 10-K for the year ended December 31, 2003, and should be read in conjunction with the interim financial statements and notes contained herein. All dollar amounts are in millions except share and per share amounts.

Company Profile

Overview and Segment Revenues

We have five reportable segments: Individual Products, Annuity and Investment Products (AIP), Benefit Partners, Communications, and Corporate and Other. See our Form 10-K for an overview of the Company and our reportable segments and a discussion of key drivers and trends in our businesses.

Our reportable segments revenues as a percentage of total revenues, excluding realized investment gains and losses, were as follows:

	Three Months Ended March 31	
	2004	**2003**
Individual Products	46%	50%
AIP	18%	19%
Benefit Partners	26%	22%
Communications	6%	6%
Corporate and Other	4%	3%

Update on Critical Accounting Policies

Our Form 10-K described our accounting policies that are critical to the understanding of our results of operations and our financial position. They relate to deferred acquisition costs (DAC), value of business acquired (VOBA) and unearned revenue, assumptions and judgments utilized in determining if declines in fair values of investments are other-than-temporary, valuation methods for infrequently traded securities and private placements, and accruals relating to legal and administrative proceedings.

We believe that these policies were applied in a consistent manner during the first quarter of 2004. Legal proceedings are discussed in Note 5 to the Consolidated Condensed Financial Statements.

Results of Operations

The following tables illustrate our results before and after the cumulative effect of change in accounting principle:

	Three Months Ended March 31		Favorable/ (Unfavorable)
	2004	2003	2004 vs. 2003
Consolidated Summary of Income			
Income before cumulative effect of change in accounting principle	$141.2	$109.1	29.4%
Cumulative effect of change in accounting principle	(12.9)		(100.0)
Net income	$128.3	$109.1	17.6%
Consolidated Earnings Per Share			
Basic:			
Income before cumulative effect of change in accounting principle	$ 1.00	$ 0.76	31.6%
Cumulative effect of change in accounting principle	(0.09)		(100.0)
Net income	$ 0.91	$ 0.76	19.7%
Fully-diluted:			
Income before cumulative effect of change in accounting principle	$ 0.99	$ 0.76	30.3%
Cumulative effect of change in accounting principle	(0.09)		(100.0)
Net income	$ 0.90	$ 0.76	18.4%

	Three Months Ended March 31	
	2004	2003
Average number of shares outstanding	140,659,329	142,804,138
Average number of shares outstanding assuming dilution	142,169,281	143,662,337

The first quarter 2004 increase in income before cumulative effect of change in accounting principle reflected earnings growth in the Communications and Corporate segments. Also, realized investment gains (losses) net of taxes contributed $14.7 due primarily to gains on equity securities versus ($12.4) in the first quarter of 2003 when we experienced higher losses on other-than-temporary bond impairments. Individual Products, AIP and Benefit Partners reportable segment results declined in the first quarter 2004 versus 2003. A modest increase in UL-type product results was more than offset by a decline in earnings from traditional products, resulting in the slight decrease in individual products overall. The rate of decline in traditional product results was exacerbated by the low interest rate environment. Lower income from repayments of mortgage backed securities drove the decline in AIP results. Our results for Benefit Partners were impacted by an elevated long term disability loss ratio.

The Company adopted SOP 03-1 in the first quarter of 2004. SOP 03-1 created both a cumulative effect upon adoption as well as a reduction to current quarter net income. See Note 6 for further discussion of SOP 03-1.

Growth in earnings per share was more favorable than the absolute growth in dollar earnings amounts due to repurchases of 1,884,200 shares in the first quarter of 2004 in addition to share repurchases during the second through fourth quarters of 2003.

Results by Business Segment

Throughout this Form 10-Q, reportable segment results is defined as net income before realized investment gains and losses (and cumulative effect of change in accounting principle, if applicable). Reportable segment results is a non-GAAP measure. We believe reportable segment results provides relevant and useful information to investors, as it represents the basis on which we assess the performance of our business segments. We deem reportable segment results to be a meaningful measure for this purpose because, except for losses from other-than-temporary impairments, realized investment gains and losses occur primarily at our sole discretion. Note that reportable segment results as described above may not be comparable to similarly titled measures reported by other companies.

We assess profitability by business segment and measure other operating statistics as detailed in the separate segment discussions that follow. Sales are one of the statistics we use to track performance. Our sales in the Individual Products and AIP segments have little immediate impact on revenues for these two segments as described in the segment discussions below.

Results by Reportable Segment

	Three Months Ended March 31		Favorable/ (Unfavorable)
	2004	**2003**	**2004 vs. 2003**
Individual Products	$ 75.0	$ 76.0	(1.3)%
AIP	19.1	21.2	(9.9)
Benefit Partners	11.5	11.9	(3.4)
Communications	10.6	7.1	49.3
Corporate and Other	10.3	5.3	94.3
Total reportable segment results	126.5	121.5	4.1
Realized investment gains (losses), net of taxes	14.7	(12.4)	218.5
Net income before cumulative effect of change in accounting principle	141.2	109.1	29.4
Cumulative effect of change in accounting principle	(12.9)		(100.0)