CITIZENS INC
Form 10-Q
November 05, 2010

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended September 30, 2010

or

o **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from __________ to __________

Commission File Number: 000-16509

CITIZENS, INC.

(Exact name of registrant as specified in its charter)

Colorado	84-0755371
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
400 East Anderson Lane, Austin, Texas	78752
(Address of principal executive offices)	(Zip Code)

(512) 837-7100
(Registrant s telephone number, including area code)
N/A
(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.

þ Yes o 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).

o Yes o 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. (Check one):

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

o Yes þ No

As of November 4, 2010, the Registrant had 48,686,759 shares of Class A common stock, no par value, outstanding and 1,001,714 shares of Class B common stock outstanding.

TABLE OF CONTENTS

Exhibit 99.1

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Financial Position
(In thousands)

Assets		**September 30, 2010 (Unaudited)**	**December 31, 2009**
Investments:			
Fixed maturities available-for-sale, at fair value (cost: $501,649 and $389,195 in 2010 and 2009, respectively)	$	519,132	385,579
Fixed maturities held-to-maturity, at amortized cost (fair value: $128,865 and $199,676 in 2010 and 2009, respectively)		127,674	206,909
Equity securities available-for-sale, at fair value (cost: $25,619 and $25,899 in 2010 and 2009, respectively)		33,986	33,477
Mortgage loans on real estate		1,501	1,533
Policy loans		34,970	32,096
Real estate held for sale		2,805	2,825
Real estate held for investment (less $445 and $374 accumulated depreciation in 2010 and 2009, respectively)		6,522	6,305
Other long-term investments		49	86
Short-term investments			2,510
Total investments		726,639	671,320
Cash and cash equivalents		65,366	48,625
Accrued investment income		8,406	7,455
Reinsurance recoverable		10,411	11,587
Deferred policy acquisition costs		121,540	115,570
Cost of customer relationships acquired		32,097	34,728
Goodwill		17,160	17,160
Other intangible assets		1,026	1,046
Federal income tax receivable		1,903	4,023
Property and equipment, net		6,772	6,018
Due premiums, net (less $1,341 and $1,644 allowance for doubtful accounts in 2010 and 2009, respectively)		7,224	8,960
Prepaid expenses		1,378	288
Other assets		477	546
Total assets	$	1,000,399	927,326

See accompanying notes to consolidated financial statements.

(Continued)

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Financial Position, Continued
(In thousands, except share amounts)

Liabilities and Stockholders Equity	September 30, 2010 (Unaudited)	December 31, 2009
Liabilities:		
Policy liabilities:		
Future policy benefit reserves:		
Life insurance	$ 621,841	592,358
Annuities	40,692	37,882
Accident and health	5,966	6,399
Dividend accumulations	9,188	5,621
Premiums paid in advance	22,140	20,373
Policy claims payable	10,810	10,222
Other policyholders funds	8,080	8,105
Total policy liabilities	718,717	680,960
Commissions payable	2,078	2,434
Deferred federal income tax	15,127	8,052
Payable for securities in process of settlement	18,500	6,000
Warrants outstanding	1,439	1,819
Other liabilities	7,588	11,986
Total liabilities	763,449	711,251
Commitments and contingencies (Note 8)		
Stockholders equity:		
Common stock:		
Class A, no par value, 100,000,000 shares authorized, 51,822,497 shares issued in 2010 and 2009, including shares in treasury of 3,135,738 in 2010 and 2009	256,703	256,703
Class B, no par value, 2,000,000 shares authorized, 1,001,714 shares issued and outstanding in 2010 and 2009	3,184	3,184
Retained deficit	(31,636)	(38,092)
Accumulated other comprehensive income:		
Unrealized gains on securities, net of tax	19,710	5,291
	247,961	227,086
Treasury stock, at cost	(11,011)	(11,011)
Total stockholders equity	236,950	216,075
Total liabilities and stockholders equity	$ 1,000,399	927,326

See accompanying notes to consolidated financial statements.

3

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Operations
Three Months Ended September 30,
(In thousands, except per share amounts)
(Unaudited)

		2010	2009
Revenues:			
Premiums:			
Life insurance	$	36,433	34,589
Accident and health insurance		392	371
Property insurance		1,230	1,192
Net investment income		7,272	7,413
Realized gains (losses), net		(103)	1,006
Decrease in fair value of warrants		128	
Other income		103	273
Total revenues		45,455	44,844
Benefits and expenses:			
Insurance benefits paid or provided:			
Claims and surrenders		15,739	14,494
Increase in future policy benefit reserves		11,398	10,305
Policyholders dividends		1,977	1,827
Total insurance benefits paid or provided		29,114	26,626
Commissions		9,229	8,435
Other underwriting, acquisition and insurance expenses		6,580	6,772
Capitalization of deferred policy acquisition costs		(6,148)	(5,306)
Amortization of deferred policy acquisition costs		2,975	4,303
Amortization of cost of customer relationships acquired and other intangibles		726	946
Total benefits and expenses		42,476	41,776
Income before federal income tax		2,979	3,068
Federal income tax expense		1,313	1,033
Net income	$	1,666	2,035
Net income applicable to common stockholders	$	1,666	1,878
Per Share Amounts:			
Basic and diluted earnings per share of Class A common stock	$	0.03	0.04
Basic and diluted earnings per share of Class B common stock	$	0.02	0.02

See accompanying notes to consolidated financial statements.

4

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Operations
Nine Months Ended September 30,
(In thousands, except per share amounts)
(Unaudited)

	2010	2009
Revenues:		
Premiums:		
Life insurance	$ 105,114	101,858
Accident and health insurance	1,215	1,135
Property insurance	3,592	3,501
Net investment income	23,896	21,733
Realized gains, net	648	2,827
Decrease in fair value of warrants	380	3,081
Other income	602	796
Total revenues	135,447	134,931
Benefits and expenses:		
Insurance benefits paid or provided:		
Claims and surrenders	46,410	44,254
Increase in future policy benefit reserves	30,726	28,021
Policyholders dividends	5,324	4,742
Total insurance benefits paid or provided	82,460	77,017
Commissions	26,385	25,462
Other underwriting, acquisition and insurance expenses	20,541	21,889
Capitalization of deferred policy acquisition costs	(17,406)	(16,257)
Amortization of deferred policy acquisition costs	11,422	11,715
Amortization of cost of customer relationships acquired and other intangibles	2,332	2,630
Total benefits and expenses	125,734	122,456
Income before federal income tax	9,713	12,475
Federal income tax expense	3,257	2,762
Net income	$ 6,456	9,713
Net income applicable to common stockholders	$ 6,456	7,208
Per Share Amounts:		
Basic earnings per share of Class A common stock	$ 0.13	0.15
Basic earnings per share of Class B common stock	$ 0.07	0.08
Diluted earnings per share of Class A common stock	$ 0.13	0.10

Diluted earnings per share of Class B common stock	$	0.07	0.05

See accompanying notes to consolidated financial statements.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Cash Flows
Nine Months Ended September 30,
(In thousands)
(Unaudited)

	2010	2009
Cash flows from operating activities:		
Net income	$ 6,456	9,713
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized gains on sale of investments and other assets	(648)	(2,827)
Net deferred policy acquisition costs	(5,984)	(4,542)
Amortization of cost of customer relationships acquired and other intangibles	2,332	2,630
Decrease in fair value of warrants	(380)	(3,081)
Depreciation	787	908
Amortization of premiums and discounts on fixed maturities and short-term investments	2,548	1,466
Deferred federal income tax benefit	(61)	(1,191)
Change in:		
Accrued investment income	(951)	434
Reinsurance recoverable	1,176	1,258
Due premiums and other receivables	1,736	856
Future policy benefit reserves	30,223	27,171
Other policyholders liabilities	5,897	1,187
Federal income tax receivable	2,120	2,827
Commissions payable and other liabilities	(4,754)	58
Other, net	(1,021)	(583)
Net cash provided by operating activities	39,476	36,284
Cash flows from investing activities:		
Purchase of fixed maturities, held-to-maturity	(71,452)	(202,286)
Calls of fixed maturities, held-to-maturity	150,350	
Sale of fixed maturities, available-for-sale	7,074	72,148
Maturity and calls of fixed maturities, available-for-sale	137,506	276,058
Purchase of fixed maturities, available-for-sale	(246,238)	(174,931)
Sale of equity securities, available-for-sale	591	1,184
Calls of equity securities, available-for-sale	100	
Purchase of equity securities, available-for-sale	(205)	(476)
Principal payments on mortgage loans	33	24
Mortgage loans funded		(170)
Increase in policy loans	(2,874)	(2,905)
Sale of other long-term investments and property and equipment	42	406
Purchase of other long-term investments and property and equipment	(1,799)	(2,172)
Maturity of short-term investments	2,500	2,250
Purchase of short-term investments		(2,604)
Cash acquired in acquisition		9,770
Net cash used in investing activities	(24,372)	(23,704)

See accompanying notes to consolidated financial statements.	(Continued)

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Cash Flows, Continued
Nine Months Ended September 30,
(In thousands)
(Unaudited)

		2010	2009
Cash flows from financing activities:			
Warrants exercised	$		69
Annuity deposits		4,041	3,990
Annuity withdrawals		(2,404)	(2,515)
Net cash provided by financing activities		1,637	1,544
Net increase in cash and cash equivalents		16,741	14,124
Cash and cash equivalents at beginning of year		48,625	63,792
Cash and cash equivalents at end of period	$	65,366	77,916
Supplemental disclosures of operating activities:			
Cash paid during the period for income taxes	$	1,200	1,125

Supplemental Disclosures of Non-Cash Investing Activities:

On February 27, 2009, the Company acquired Integrity Capital Corporation (ICC) for 1,294,000 shares of Class A common stock with a fair value of $8.4 million. CICA Life Insurance Company of America held a 13% interest in ICC prior to the acquisition with a carrying value of $551,000, making the total non-cash acquisition price approximately $9.0 million.

In 2010, the Company sold a parcel of real estate and issued a mortgage loan for $102,000.

In 2010, the Company foreclosed on a mortgage loan and transferred the real estate to real estate held for sale in the amount of $101,000.

Supplemental Disclosures of Non-Cash Financing Activities:

Dividends on the Company s Series A-1 Convertible Preferred Stock, issued in 2004, and Series A-2 Convertible Preferred Stock, issued in 2005, were paid by the Company through the issuance of Class A common stock to the preferred shareholders in the amount of $216,000 in the first nine months of 2009. Accretion of deferred issuance costs and discounts on the Convertible Preferred Stock recorded as a deduction to Class A common stock during the first nine months of 2009 was $2.3 million.

See accompanying notes to consolidated financial statements.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements
September 30, 2010
(Unaudited)

(1) Financial Statements

Basis of Presentation and Consolidation

The accompanying consolidated financial statements of the Company and its wholly owned subsidiaries have been prepared in conformity with U.S. Generally Accepted Accounting Principles (U.S. GAAP).

The consolidated financial statements include the accounts and operations of Citizens, Inc. (Citizens), a Colorado corporation, and its wholly-owned subsidiaries, CICA Life Insurance Company of America (CICA), Computing Technology, Inc. (CTI), Funeral Homes of America, Inc. (FHA), Insurance Investors, Inc. (III), Citizens National Life Insurance Company (CNLIC), Integrity Capital Corporation (ICC), Integrity Capital Insurance Company (ICIC), Security Plan Life Insurance Company (SPLIC) and Security Plan Fire Insurance Company (SPFIC). All significant inter-company accounts and transactions have been eliminated. Citizens and its wholly owned consolidated subsidiaries are collectively referred to as the Company, we, or our.

The consolidated statements of financial position for September 30, 2010, the consolidated statements of operations for the three and nine-month periods ended September 30, 2010 and 2009, and the consolidated statements of cash flows for the nine-month period then ended have been prepared by the Company without audit. In the opinion of management, all adjustments to present fairly the financial position, results of operations, and changes in cash flows at September 30, 2010 and for comparative periods have been made.

The Company completed its acquisition of ICC in exchange for 1,294,000 shares of its Class A common stock in the first quarter of 2009. ICC is the parent of ICIC, an Indiana life insurance company. The transaction was valued at $9.0 million on the closing date of February 27, 2009. On October 30, 2009, FHA completed the sale of its business assets valued at approximately $600,000, consisting primarily of funeral home assets.

We provide life and health insurance policies through four of our subsidiaries CICA, SPLIC, CNLIC and ICIC. CICA, CNLIC and ICIC issue ordinary whole-life policies, burial insurance, pre-need policies, and accident and health related policies, throughout the midwest and southern United States. CICA also issues ordinary whole-life policies to non-U.S. residents. SPLIC offers final expense and home service life insurance in Louisiana, Arkansas and Mississippi and SPFIC, a wholly owned subsidiary of SPLIC, writes a limited amount of property insurance in Louisiana.

CTI provides data processing systems and services as well as furniture and equipment to the Company. III provides aviation transportation to the Company. FHA was a funeral home operator before the sale of its assets in 2009.

The Company corrected two valuation database discrepancies in the current quarter that resulted in a decrease to reserves of $559,000. There was a value per unit error related to fully paid up policies under one plan in duration twenty-one resulting in a reserve overstatement amounting to $508,000, with approximately $475,000 related to prior years, and another plan where surrender charges were not properly recorded, which also overstated reserves by $51,000.

Reserving assumptions are reviewed to ensure that our original assumptions at the time of policy issuance related to interest, mortality, withdrawals, and settlement expenses are based upon management s best judgment. The Company modified these assumptions during the current year with respect to new policies issued, which resulted in an increase to reserves of $456,000.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

Use of Estimates

The preparation of financial statements, in conformity with U.S. GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant estimates include those used in the evaluation of other-than-temporary impairments on debt securities and valuation allowances on investments, goodwill impairment, valuation allowance on deferred tax assets, and contingencies relating to litigation and regulatory matters. Certain of these estimates are particularly sensitive to market conditions, and deterioration and/or volatility in the worldwide debt or equity markets could have a material impact on the Consolidated Financial Statements.

Significant Accounting Policies

For a description of significant accounting policies, see Note 1 of the Notes to Consolidated Financial Statements included in our 2009 Form 10-K Annual Report, which should be read in conjunction with these accompanying Consolidated Financial Statements.

(2) Accounting Pronouncements

Accounting Standards Recently Adopted

In January 2010, the Financial Accounting Standards Board (FASB) updated Accounting Standards Codification (ASC) Topic 820, requiring additional disclosures about fair value measurements regarding transfers between fair value categories as well as purchases, sales, issuances and settlements related to fair value measurements of financial instruments with non-observable inputs. This update was effective for interim and annual periods beginning after December 15, 2009 except for disclosures about purchases, sales, issuances and settlements of financial instruments with non-observable inputs, which are effective for years beginning after December 15, 2010. The additional disclosures required by this update are included in the note on fair value measurements upon adoption. The additional disclosures did not have a material impact on our financial condition or results of operations.

On September 29, 2010, the FASB ratified the Emerging Issues Task Force s (EITF) final consensus on EITF Issue No. 09-G, *Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts* (Issue 09-G). Issue 09-G clarifies what costs should be deferred by insurance companies when issuing or renewing insurance contracts. The EITF concluded that only costs incurred in the acquisition of new and renewal contracts that are 1) incremental direct costs of a successful contract acquisition, 2) portions of employees salaries and benefits directly related to time spent performing specified acquisition activities for a contract that has actually been acquired, 3) other costs directly related to the specified acquisition activities that would not have occurred otherwise, and 4) advertising costs that meet the capitalization criteria in other issued accounting guidance would be capitalizable as deferred acquisition costs. This Issue 09-G will be effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2011. The Company is currently reviewing this guidance and our current deferral policies to determine what impact this consensus may have on our consolidated financial statements and what information gathering changes may need to be implemented.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

(3) Segment Information

The Company has three reportable segments: Life Insurance, Home Service Insurance, and Other Non-Insurance Enterprises. The accounting policies of the segments are in accordance with U.S. GAAP and are the same as those used in the preparation of the consolidated financial statements. The Company evaluates profit and loss performance based on U.S. GAAP income before federal income taxes for its three reportable segments. The Company has no reportable differences between segments and consolidated operations.

	Three Months Ended September 30, 2010 (In thousands)			
	Life Insurance	Home Service Insurance	Other Non-Insurance Enterprises	Consolidated
Revenues:				
Premiums	$ 27,514	10,541		38,055
Net investment income	3,893	3,244	135	7,272
Realized gains (losses), net	1	(96)	(8)	(103)
Decrease in fair value of warrants			128	128
Other income	78	10	15	103
Total revenue	31,486	13,699	270	45,455
Benefits and expenses:				
Insurance benefits paid or provided:				
Claims and surrenders	10,498	5,241		15,739
Increase in future policy benefit reserves	10,688	710		11,398
Policyholders dividends	1,965	12		1,977
Total insurance benefits paid or provided	23,151	5,963		29,114
Commissions	5,572	3,657		9,229
Other underwriting, acquisition and insurance expenses	2,596	3,529	455	6,580
Capitalization of deferred policy acquisition costs	(4,579)	(1,569)		(6,148)
Amortization of deferred policy acquisition costs	2,613	362		2,975
Amortization of cost of customer relationships acquired and other intangibles	239	487		726
Total benefits and expenses	29,592	12,429	455	42,476
Income (loss) before income tax expense	$ 1,894	1,270	(185)	2,979

10

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

	Nine Months Ended September 30, 2010			
	Life Insurance	Home Service Insurance	Other Non-Insurance Enterprises	Consolidated
	(In thousands)			
Revenues:				
Premiums	$ 78,364	31,557		109,921
Net investment income	13,239	10,251	406	23,896
Realized gains (losses), net	116	585	(53)	648
Decrease in fair value of warrants			380	380
Other income	487	63	52	602
Total revenue	92,206	42,456	785	135,447
Benefits and expenses:				
Insurance benefits paid or provided:				
Claims and surrenders	30,644	15,766		46,410
Increase in future policy benefit reserves	28,123	2,603		30,726
Policyholders dividends	5,267	57		5,324
Total insurance benefits paid or provided	64,034	18,426		82,460
Commissions	15,316	11,069		26,385
Other underwriting, acquisition and insurance expenses	8,213	10,964	1,364	20,541
Capitalization of deferred policy acquisition costs	(12,741)	(4,665)		(17,406)
Amortization of deferred policy acquisition costs	10,752	670		11,422
Amortization of cost of customer relationships acquired and other intangibles	858	1,474		2,332
Total benefits and expenses	86,432	37,938	1,364	125,734
Income (loss) before income tax expense	$ 5,774	4,518	(579)	9,713

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

	Three Months Ended September 30, 2009			
	Life Insurance	Home Service Insurance	Other Non-Insurance Enterprises	Consolidated
	(In thousands)			
Revenues:				
Premiums	$ 25,795	10,357		36,152
Net investment income	4,232	3,126	55	7,413
Realized gains, net	650	356		1,006
Other income	108	20	145	273
Total revenue	30,785	13,859	200	44,844
Benefits and expenses:				
Insurance benefits paid or provided:				
Claims and surrenders	10,035	4,459		14,494
Increase in future policy benefit reserves	8,850	1,455		10,305
Policyholders dividends	1,809	18		1,827
Total insurance benefits paid or provided	20,694	5,932		26,626
Commissions	4,827	3,608		8,435
Other underwriting, acquisition and insurance expenses	2,563	3,588	621	6,772
Capitalization of deferred policy acquisition costs	(3,975)	(1,331)		(5,306)
Amortization of deferred policy acquisition costs	3,757	546		4,303
Amortization of cost of customer relationships acquired and other intangibles	397	549		946
Total benefits and expenses	28,263	12,892	621	41,776
Income (loss) before income tax expense	$ 2,522	967	(421)	3,068

12

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

	Nine Months Ended September 30, 2009			
	Life Insurance	Home Service Insurance	Other Non-Insurance Enterprises	Consolidated
	(In thousands)			
Revenues:				
Premiums	$ 75,570	30,924		106,494
Net investment income	12,196	9,396	141	21,733
Realized gains, net	1,068	1,682	77	2,827
Decrease in fair value of warrants			3,081	3,081
Other income	267	84	445	796
Total revenue	89,101	42,086	3,744	134,931
Benefits and expenses:				
Insurance benefits paid or provided:				
Claims and surrenders	30,259	13,995		44,254
Increase in future policy benefit reserves	24,258	3,763		28,021
Policyholders dividends	4,687	55		4,742
Total insurance benefits paid or provided	59,204	17,813		77,017
Commissions	14,531	10,931		25,462
Other underwriting, acquisition and insurance expenses	7,873	11,577	2,439	21,889
Capitalization of deferred policy acquisition costs	(12,227)	(4,030)		(16,257)
Amortization of deferred policy acquisition costs	10,677	1,038		11,715
Amortization of cost of customer relationships acquired and other intangibles	1,105	1,525		2,630
Total benefits and expenses	81,163	38,854	2,439	122,456
Income before income tax expense	$ 7,938	3,232	1,305	12,475

(4) Total Comprehensive Income

Three Months Ended September 30,		Nine Months Ended September 30,	
2010	2009	2010	2009
(In thousands)			

Net income	$ 1,666	2,035	6,456	9,713
Other comprehensive income net of effects of deferred acquisition costs and taxes:				
Unrealized gains on available-for-sale securities	11,288	16,963	21,554	22,614
Tax expense	(2,700)	(3,678)	(7,135)	(4,233)
Other comprehensive income	8,588	13,285	14,419	18,381
Total comprehensive income	$ 10,254	15,320	20,875	28,094

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

(5) Earnings per Share

The following table sets forth the computation of basic and diluted earnings per share for the period indicated.

	Three Months Ended September 30, 2010		2009
	(In thousands, except per share amounts)		
Basic and diluted earnings per share:			
Numerator:			
Net income	$	1,666	2,035
Less: Preferred stock dividend			(13)
Accretion of deferred issuance costs and discounts on preferred stock			(144)
Net income available to common stockholders	$	1,666	1,878
Net income allocated to Class A common stock	$	1,649	1,859
Net income allocated to Class B common stock		17	19
Net income available to common stockholders	$	1,666	1,878
Denominator:			
Weighted average shares of Class A outstanding basic and diluted		48,687	48,441
Weighted average shares of Class B outstanding basic and diluted		1,002	1,002
Total weighted average shares outstanding basic and diluted		49,689	49,443
Basic and diluted earnings per share of Class A common stock	$	0.03	0.04
Basic and diluted earnings per share of Class B common stock	$	0.02	0.02

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

The following table sets forth the computation of basic and diluted earnings per share for the period indicated.

		Nine Months Ended September 30, 2010	2009
		(In thousands, except per share amounts)	
Basic and diluted earnings per share:			
Numerator:			
Net income	$	6,456	9,713
Less: Preferred stock dividend			(216)
Accretion of deferred issuance costs and discounts on preferred stock			(2,289)
Net income available to common stockholders	$	6,456	7,208
Net income allocated to Class A common stock	$	6,390	7,132
Net income allocated to Class B common stock		66	76
Net income available to common stockholders	$	6,456	7,208
Denominator:			
Weighted average shares of Class A outstanding basic		48,687	47,177
Weighted average shares of Class B outstanding basic		1,002	1,002
Total weighted average shares outstanding basic		49,689	48,179
Basic earnings per share of Class A common stock	$	0.13	0.15
Basic earnings per share of Class B common stock	$	0.07	0.08
Diluted earnings per share of Class A common stock	$	0.13	0.10
Diluted earnings per share of Class B common stock	$	0.07	0.05

For the three and nine months ended September 30, 2010, the warrants associated with the Convertible Preferred Stock portfolio were anti-dilutive. As such, the diluted weighted average shares of Class A common stock outstanding for the period was 48,687,000.

For the nine months ended September 30, 2009, certain warrants relative to the Convertible Preferred Stock became dilutive. As such, the diluted weighted average shares of Class A common stock for the period was 47,204,000. Total diluted weighted average shares was 48,206,000.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

(6) Investments

Financial stability and the prevention of capital erosion are important investment considerations for the Company. A primary investment goal is the conservation of assets due to the long-term nature of a significant portion of our insurance liabilities. The Company invests primarily in fixed maturity securities, which totaled 81.7% of total investments and cash and cash equivalents at September 30, 2010.

	September 30, 2010		December 31, 2009	
	Carrying Value (In thousands)	% of Total Carrying Value	Carrying Value (In thousands)	% of Total Carrying Value
Fixed maturity securities	$ 646,806	81.7%	$ 592,488	82.3%
Equity securities	33,986	4.3	33,477	4.6
Mortgage loans	1,501	0.2	1,533	0.2
Policy loans	34,970	4.4	32,096	4.5
Real estate and other long-term investments	9,376	1.2	9,216	1.3
Short-term investments			2,510	0.3
Cash and cash equivalents	65,366	8.2	48,625	6.8
Total cash, cash equivalents and investments	$ 792,005	100.0%	$ 719,945	100.0%

Cash balances increased in 2010 compared to December 31, 2009 due to call activity related to fixed maturity securities. The balances held in cash are expected to be reinvested into fixed maturity securities in the next few months. Significant call activity may continue if our investment income returns remain low.

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

The following tables represent gross unrealized gains and losses for fixed maturities and equity securities as of the periods indicated.

	September 30, 2010			
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Fixed maturities available-for-sale:				
U.S. Treasury securities	$ 10,921	2,936		13,857
U.S. Government-sponsored enterprises	253,536	2,539	442	255,633
States of the United States and political subdivisions of the states	62,229	1,865	1,969	62,125
Foreign governments	105	35		140
Corporate	159,610	11,899	429	171,080
Securities not due at a single maturity date	15,248	1,079	30	16,297
Total fixed maturities available-for-sale	501,649	20,353	2,870	519,132
Fixed maturities held-to-maturity:				
U.S. Government-sponsored enterprises	127,674	1,231	40	128,865
Total fixed maturities	$ 629,323	21,584	2,910	647,997
Total equity securities	$ 25,619	8,376	9	33,986

	December 31, 2009			
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Fixed maturities available-for-sale:				
U.S. Treasury securities	$ 11,110	1,324		12,434
U.S. Government-sponsored enterprises	184,797	96	4,610	180,283
States of the United States and political subdivisions of the states	60,070	321	3,199	57,192
Foreign governments	105	15		120
Corporate	114,175	3,726	1,803	116,098
Securities not due at a single maturity date	18,938	556	42	19,452
Total fixed maturities available-for-sale	389,195	6,038	9,654	385,579
Fixed maturities held-to-maturity:				
U.S. Government-sponsored enterprises	206,909	18	7,251	199,676
Total fixed maturities	$ 596,104	6,056	16,905	585,255

Total equity securities	$	25,899	7,578	33,477

Almost 90% of the Company s mortgage-backed securities are residential. Mortgage-backed securities are also referred to as securities not due at a single maturity date throughout this report. The majority of the Company s equity securities are held within diversified mutual funds.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

Valuation of Investments in Fixed Maturity and Equity Securities

The Company monitors all debt and equity securities on an on-going basis relative to changes in credit ratings, market prices, earnings trends and financial performance, in addition to specific region or industry reviews. The assessment of whether impairments have occurred is based on a case-by-case evaluation of underlying reasons for the decline in fair value. The Company determines other-than-temporary impairment by reviewing all relevant evidence related to the specific security issuer as well as the Company s intent to sell the security, or if it is more likely than not that the Company would be required to sell a security before recovery of its amortized cost.

When an other-than-temporary impairment has occurred, the amount of the other-than-temporary impairment recognized in earnings depends on whether the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis. If the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis, the other-than-temporary impairment is recognized in earnings equal to the entire difference between the investment s cost and its fair value at the balance sheet date. If the Company does not intend to sell the security and it is not more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis, the other-than-temporary impairment is separated into the following: a) the amount representing the credit loss, and b) the amount related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the other-than-temporary impairment recognized in earnings becomes the new amortized cost basis of the investment. The new amortized cost basis is not adjusted for subsequent recoveries in fair value.

The Company evaluates whether a credit impairment exists for debt securities by considering primarily the following factors: (a) changes in the financial condition of the security s underlying collateral, (b) whether the issuer is current on contractually obligated interest and principal payments, (c) changes in the financial condition, credit rating and near-term prospects of the issuer, (d) the extent to which the fair value has been less than the amortized cost of the security and (e) the payment structure of the security. The Company s best estimate of expected future cash flows used to determine the credit loss amount is a quantitative and qualitative process. Quantitative review includes information received from third party sources such as financial statements, pricing and rating changes, liquidity and other statistical information. Qualitative factors include judgments related to business strategies, economic impacts on the issuers and overall judgment related to estimates and industry factors. The Company s best estimate of future cash flows involves assumptions including, but not limited to, various performance indicators, such as historical and projected default and recovery rates, credit ratings, and current delinquency rates. These assumptions require the use of significant management judgment and include the probability of issuer default and estimates regarding timing and amount of expected recoveries, which may include estimating the underlying collateral value. In addition, projections of expected future debt security cash flows may change based upon new information regarding the performance of the issuer.

The primary factors considered in evaluating whether an impairment exists for an equity security include, but are not limited to: (a) the length of time and the extent to which the fair value has been less than the cost of the security, (b) changes in the financial condition, credit rating and near-term prospects of the issuer, (c) whether the issuer is current on contractually obligated payments, and (d) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for recovery.

The Company recognized $27,000 of other-than-temporary impairments (OTTI) in the three months ended September 30, 2010. OTTI items were recognized in the first quarter of 2009 relating to credit losses totaling $111,000.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

The tables below present the fair values and gross unrealized losses of fixed maturities and equity securities that have remained in a continuous unrealized loss position for the periods indicated.

	September 30, 2010								
	Less than 12 months			Greater than 12 months			Total		
	Fair Value	Unrealized Losses	# of Securities	Fair Value	Unrealized Losses	# of Securities	Fair Value	Unrealized Losses	# of Securities
	(In thousands, except for # of securities)								
Available-for-sale securities:									
U.S. Government-sponsored enterprises	$ 61,870	442	42				61,870	442	42
Securities issued by states and political subdivisions				10,782	1,969	9	10,782	1,969	9
Corporate	8,655	290	7	4,599	139	9	13,254	429	16
Securities not due at a single maturity date	1,403	11	3	206	19	5	1,609	30	8
Total available-for-sale	71,928	743	52	15,587	2,127	23	87,515	2,870	75
Held-to-maturity securities:									
U.S. Government-sponsored enterprises	5,357	40	3				5,357	40	3
Total fixed maturities	$ 77,285	783	55	15,587	2,127	23	92,872	2,910	78
Total equity securities	$ 30	9	2				30	9	2

	December 31, 2009								
	Less than 12 months			Greater than 12 months			Total		
	Fair Value	Unrealized Losses	# of Securities	Fair Value	Unrealized Losses	# of Securities	Fair Value	Unrealized Losses	# of Securities
	(In thousands, except for # of securities)								
Available-for-sale securities:									
U.S. Government-sponsored enterprises	$ 169,514	4,610	213				169,514	4,610	213
Securities issued by states and political subdivisions	19,055	343	19	14,995	2,856	15	34,050	3,199	34
Corporate	36,342	541	21	12,857	1,261	12	49,199	1,802	33
Securities not due at a single maturity date	179	1	1	637	42	8	816	43	9
Total available-for-sale	225,090	5,495	254	28,489	4,159	35	253,579	9,654	289
Held-to-maturity securities:									
U.S. Government-sponsored enterprises	185,659	7,251	81				185,659	7,251	81

Total fixed maturities	$ 410,749	12,746	335	28,489	4,159	35	439,238	16,905	370

As of September 30, 2010, the Company had 23 available-for-sale securities in an unrealized loss position for greater than 12 months, which were municipal, corporate and mortgage-backed securities. The Company has reviewed these securities and determined that no other-than-temporary impairment exists based on our evaluations of the credit worthiness of the issuers and due to the fact that we do not intend to sell the investments, nor is it likely that we would be required to sell these investments before recovery of their amortized cost bases, which may be maturity.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

The amortized cost and fair value of fixed maturity securities at September 30, 2010 by contractual maturity are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The Company has experienced significant issuer calls over the past two years as a result of the declining interest rate environment.

	September 30, 2010	
	Amortized Cost	Fair Value
	(In thousands)	
Available-for-sale securities:		
Due in one year or less	$ 13,463	13,575
Due after one year through five years	32,387	34,264
Due after five years through ten years	185,486	192,650
Due after ten years	255,065	262,346
Total available-for-sale securities	486,401	502,835
Held-to-maturity securities:		
Due after ten years	127,674	128,865
Securities not due at a single maturity date	15,248	16,297
Total fixed maturities	$ 629,323	647,997

The securities not due at a single maturity date are primarily mortgage-backed obligations of U.S. Government-sponsored enterprises and corporate securities.

The Company uses the specific identification method to determine the cost basis used in the calculation of realized gains and losses related to security sales. Proceeds and gross realized gains from sales of securities for the three and nine months ended September 30, 2010 and 2009 are summarized as follows:

	Fixed Maturities Available-for-Sale				Equity Securities			
	Three Months Ended September 30,		Nine Months Ended September 30,		Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009	2010	2009	2010	2009
	(In thousands)				(In thousands)			
Proceeds	$ 208	33,478	7,074	72,148	$	9	591	1,184
Gross realized gains	$ 69	1,167	811	2,720	$		166	219

No securities were sold for realized losses for the periods reported and there were no securities sold from the held-to-maturity portfolio during the three and nine months ended September 30, 2010.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

(7) Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We hold available-for-sale fixed maturity securities and equity securities, which are carried at fair value.

Fair value measurements are generally based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our view of market assumptions in the absence of observable market information. We utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. All assets and liabilities carried at fair value are required to be classified and disclosed in one of the following three categories:

Level 1 Quoted prices for identical instruments in active markets.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs or whose significant value drivers are observable.

Level 3 Instruments whose significant value drivers are unobservable.

Level 1 primarily consists of financial instruments whose value is based on quoted market prices such as U.S. Treasury securities and actively traded stock and mutual fund investments.

Level 2 includes those financial instruments that are valued by independent pricing services or broker quotes. These models are primarily industry-standard models that consider various inputs, such as interest rates, credit spreads and foreign exchange rates for the underlying financial instruments. All significant inputs are observable, or derived from observable information in the marketplace or are supported by observable levels at which transactions are executed in the marketplace. Financial instruments in this category primarily include corporate fixed maturity securities, U.S. Government-sponsored enterprise securities, municipal securities and certain mortgage and asset-backed securities.

Level 3 is comprised of financial instruments whose fair value is estimated based on non-binding broker prices utilizing significant inputs not based on or corroborated by readily available market information. This category consists of two private placement mortgage-backed securities where we cannot corroborate the significant valuation inputs with market observable data.

The following table sets forth our assets and liabilities that are measured at fair value on a recurring basis as of the date indicated.

	Fair Value Measurements September 30, 2010			
	Level 1	Level 2	Level 3	Total Fair Value
	(In thousands)			
Financial assets:				
Fixed maturities available-for-sale:				
U.S. Treasury and U.S. Government- sponsored enterprises	$ 13,749	255,741		269,490
Corporate		171,080		171,080
Municipal bonds		62,125		62,125
Mortgage-backed		15,759	538	16,297
Foreign governments		140		140
Total fixed maturities, available-for-sale	13,749	504,845	538	519,132
Total equity securities, available-for-sale	33,986			33,986

Total financial assets	$	47,735	504,845	538	553,118
Financial liabilities:					
Warrants outstanding	$		1,439		1,439

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

The following table sets forth our assets and liabilities that are measured at fair value on a recurring basis as of the date indicated.

	Fair Value Measurements December 31, 2009			
	Level 1	Level 2	Level 3	Total Fair Value
	(In thousands)			
Financial assets:				
Fixed maturities available-for-sale:				
U.S. Treasury and U.S. Government- sponsored enterprises	$ 12,434	180,283		192,717
Corporate		116,098		116,098
Municipal bonds		57,192		57,192
Mortgage-backed		18,875	577	19,452
Foreign governments		120		120
Short term investments		2,510		2,510
Total fixed maturities, available-for-sale	12,434	375,078	577	388,089
Total equity securities, available-for-sale	33,477			33,477
Total financial assets	$ 45,911	375,078	577	421,566
Financial liabilities:				
Warrants outstanding	$	1,819		1,819

Financial Instruments Valuation

Fixed maturity securities, available-for-sale. At September 30, 2010, the fixed maturities, valued using a third-party pricing source, totaled $504.8 million for Level 2 assets and comprised 97.2% of total reported fair value. Fair values for Level 3 assets are based upon unadjusted broker quotes that are non-binding. The valuations are reviewed and validated quarterly through random testing by comparisons to separate pricing models, other third party pricing services, and back tested to recent trades. For the nine months ended September 30, 2010, there were no material changes to the valuation methods or assumptions used to determine fair values, and no broker or third party prices were changed from the values received.

Equity securities, available-for-sale. Fair values of these securities are based upon quoted market price and are classified as Level 1 assets.

Short-term investments. The fair values for short-term investments are determined using a third-party pricing source. These assets are classified as Level 2.

Warrants outstanding. Fair value of our warrants are based upon industry standard models that consider various observable inputs and are classified as Level 2.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

The following table presents additional information about fixed maturity securities measured at fair value on a recurring basis and for which we have utilized significant unobservable (Level 3) inputs to determine fair value:

	September 30, 2010 (In thousands)
Beginning balance at December 31, 2009	$ 577
Total realized and unrealized losses:	
Included in net income	
Included in other comprehensive income	3
Principal paydowns	(42)
Transfer in and (out) of Level 3	
Ending balance at September 30, 2010	$ 538

We review the fair value hierarchy classifications each reporting period. Changes in the observability of the valuation attributes may result in a reclassification of certain financial assets. Such reclassifications are reported as transfers in and out of Level 3 at the beginning fair value for the reporting period in which the changes occur.

Financial Instruments not Carried at Fair Value

Estimates of fair values are made at a specific point in time, based on relevant market prices and information about the financial instruments. The estimated fair values of financial instruments presented below are not necessarily indicative of the amounts the Company might realize in actual market transactions.

The carrying amount and fair value for the financial assets and liabilities on the consolidated balance sheets for the periods indicated are as follows:

	September 30, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(In thousands)			
Financial assets:				
Fixed maturities, held-to-maturity	$ 127,674	128,865	206,909	199,676
Mortgage loans	1,501	1,447	1,533	1,484
Policy loans	34,970	34,970	32,096	32,096
Short-term investments			2,510	2,512
Cash and cash equivalents	65,366	65,366	48,625	48,625
Financial liabilities:				
Annuities	40,692	40,742	37,882	33,980

Fair values for fixed income securities are based on an independent pricing source.

Mortgage loans are secured principally by residential properties and commercial properties. Weighted average interest rates for these loans were approximately 6.7% per year as of September 30, 2010 and December 31, 2009, with maturities ranging from one to thirty years. Management estimated the fair value using an annual interest rate of 6.25% at September 30, 2010 and December 31, 2009.

Policy loans have a weighted average annual interest rate of 7.7% and 7.6% as of September 30, 2010 and December 31, 2009, respectively, and have no specified maturity dates. The aggregate fair value of policy loans approximates the carrying value reflected on the consolidated balance sheet. These loans typically carry an interest rate that is tied to the crediting rate applied to the related policy and contract reserves. Policy loans are an integral part of the life insurance policies that we have in force and cannot be valued separately and are not marketable; therefore, the fair value of policy loans approximates the carrying value.

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

For cash and cash equivalents, accrued investment income, reinsurance recoverable, other assets, federal income tax payable and receivable, dividend accumulations, commissions payable, amounts held on deposit, and other liabilities, the carrying amounts approximate fair value because of the short maturity of such financial instruments.

The fair value of the Company s liabilities under annuity contract policies was estimated at September 30, 2010 using December 31, 2009 discounted cash flows using a risk free rate plus a component for non-performance risk and interest rate risk. The fair value of liabilities under all insurance contracts are taken into consideration in the overall management of interest rate risk, which seeks to minimize exposure to changing interest rates through the matching of investment maturities with amounts due under insurance contracts.

(8) Legal Proceedings

We are a defendant in a lawsuit filed on August 6, 1999 in the Texas District Court, Austin, Texas, now styled *Citizens Insurance Company of America, Citizens, Inc., Harold E. Riley and Mark A. Oliver, Petitioners v. Fernando Hakim Daccach*, *Respondent*, in which a class was originally certified by the trial court and reversed by the Texas Supreme Court in 2007 with an order to the trial court to conduct further proceedings consistent with its ruling. The underlying lawsuit alleged that certain life insurance policies CICA made available to non-U.S. residents, when combined with a policy feature that allowed certain cash benefits to be assigned to two non-U.S. trusts for the purpose of accumulating ownership of our Class A common stock, along with allowing the policyholders to make additional contributions to the trusts, were actually offers and sales of securities that occurred in Texas by unregistered dealers in violation of the Texas securities laws. The remedy sought was rescission and return of the insurance premium payments. On December 9, 2009, the trial court denied the recertification of the class after conducting additional proceedings in accordance with the Texas Supreme Court s ruling. The remaining plaintiffs must now proceed individually, and not as a class, if they intend to pursue their cases against us. We intend to maintain a vigorous defense in any remaining proceedings.

In addition to the legal proceeding described above, we may from time to time be subject to a variety of legal and regulatory actions relating to our future, current and past business operations, including, but not limited to:

- disputes over insurance coverage or claims adjudication;
- regulatory compliance with insurance and securities laws in the United States and in foreign countries;
- disputes with our marketing firms, consultants and employee agents over compensation and termination of contracts and related claims;
- disputes regarding our tax liabilities;
- disputes relative to reinsurance and coinsurance agreements; and
- disputes relating to businesses acquired and operated by us.

In the absence of countervailing considerations, we would expect to defend any such claims vigorously. However, in doing so, we could incur significant defense costs, including not only attorneys fees and other direct litigation costs, but also the expenditure of substantial amounts of management time that otherwise would be devoted to our business. If we suffer an adverse judgment as a result of any claim, it could have a material adverse effect on our business, results of operations and financial condition.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements, Continued
September 30, 2010
(Unaudited)

(9) Convertible Preferred Stock

In July 2004, the Company completed a private placement of Series A-1 Convertible Preferred Stock (Series A-1 Preferred) to four unaffiliated institutional investors. We also issued to the investors warrants to purchase shares of our Class A common stock at various exercise prices that range from $6.72 to $7.93, with most of them striking at $6.95. The conversion, exercise and redemption prices, along with the number of shares and warrants, were adjusted for stock dividends paid on December 31, 2004 and 2005.

On July 13, 2009, the Company converted all of its outstanding Series A-1 and Series A-2 Convertible Preferred Stock into Class A common shares in accordance with the mandatory redemption provision of the preferred shareholder agreement dated July 12, 2004. The total amount of Class A common shares issued as part of the conversion was 1,706,682, inclusive of pro rata dividends due through the conversion date. Warrants to purchase shares of Class A common stock are still outstanding until July 2011 and 2012.

(10) Income Taxes

The effective tax rate was 44% and 34% for the third quarter of 2010 and 2009, respectively, and 34% and 22% for the nine months ended September 30, 2010 and 2009, respectively. The 2010 and 2009 rates were lower than the statutory rate of 35%, except for the third quarter of 2010, primarily due to gains from the change in fair value of outstanding warrants for purchase of Class A common stock of $128,000 and a minimal amount that was not taxable for the three months ended September 30, 2010 and 2009, respectively. The revenue increased from the decrease in fair value of outstanding warrants were $380,000 and $3.1 million for the nine months ended September 30, 2010 and 2009, respectively. Also causing a reduction in the effective tax rate are tax benefits from the release of tax valuation allowances. The increase above the statutory tax rate in the current quarter of 2010 relates to Citizens redemption of its stock that was held by subsidiaries, generating taxable transactions resulting in $0.9 million and $1.4 million of tax expense during the three and nine months ended September 30, 2010. This tax increased the effective tax rate as the gain was eliminated in consolidation.

The table below details the changes in the Company s tax valuation allowance.

		Three Months Ended September 30,		Nine Months Ended September 30,	
		2010	2009	2010	2009
		(In thousands)			
Tax benefit (expense) in tax provision	$	554	(213)	1,225	236
Tax benefit in other comprehensive income		1,250	2,258	408	3,681
Adjustment to goodwill					(254)
Decrease in valuation allowance	$	1,804	2,045	1,633	3,663

(11) Related Party Transactions

Citizens Inc. purchased Class A common shares during 2010 that were held by subsidiaries at market value as of the transaction dates, which approximated $4.3 million. These transactions were eliminated for financial reporting purposes in accordance with consolidation accounting, but generated a tax expense in the three months ended September 30, 2010 totaling approximately $1.4 million.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Item 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

Certain statements contained in this Quarterly Report on Form 10-Q are not statements of historical fact and constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act (the Act), including, without limitation, statements specifically identified as forward-looking statements within this document. Many of these statements contain risk factors as well. In addition, certain statements in future filings by the Company with the Securities and Exchange Commission, in press releases, and in oral and written statements made by us or with the approval of the Company, which are not statements of historical fact constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements, include, but are not limited to: (i) projections of revenues, income or loss, earnings or loss per share, the payment or non-payment of dividends, capital structure, and other financial items, (ii) statements of our plans and objectives by our management or Board of Directors including those relating to products or services, (iii) statements of future economic performance and (iv) statements of assumptions underlying such statements. Words such as believes, anticipates, assumes, estimates, plans, projects, could, expects, intends, targeted, may, similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements are subject to known and unknown risks, uncertainties and other factors that may cause actual results to differ materially from those contemplated by the forward-looking statements. Factors that could cause the Company s future results to differ materially from expected results include, but are not limited to:

- ***Changes in foreign and U.S. general economic, market, and political conditions, including the performance of financial markets and interest rates, particularly in light of the severe economic conditions and the severe stress experienced by the global financial markets in recent years;***
- ***Changes in consumer behavior, which may affect the Company s ability to sell its products and retain business;***
- ***The timely development of and acceptance of new products of the Company and perceived overall value of these products and services by existing potential customers;***
- ***Fluctuations in experience regarding current mortality, morbidity, persistency and interest rates relative to expected amounts used in pricing the Company s products;***
- ***The performance of our investment portfolio, which may be adversely affected by changes in interest rates, adverse developments and ratings of issuers whose debt securities we may hold, and other adverse macroeconomic events;***
- ***Results of litigation we may be involved in;***
- ***Changes in assumptions related to deferred acquisition costs and the value of any businesses we may acquire;***
- ***Regulatory, accounting or tax changes that may affect the cost of, or the demand for, the Company s products or services;***
- ***Our concentration of business from persons residing in Latin America and the Pacific Rim;***
- ***Our success at managing risks involved in the foregoing;***
- ***Changes in tax laws;***
- ***Effects of acquisitions and restructuring, including possible difficulties in integrating and realizing the projected results of acquisitions; and***
- ***Changes in statutory or U.S. GAAP accounting principles, policies or practices.***

Such forward-looking statements speak only as of the date on which such statements are made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made to reflect the occurrence of unanticipated events.

We make available, free of charge, through our Internet website (http://www.citizensinc.com), our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, Section 16 reports filed by officers and directors, news releases, and, if applicable, amendments to those reports filed or furnished pursuant to

Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as soon as reasonably practicable after we electronically file such reports with, or furnish such reports to, the Securities and Exchange Commission. We are not including any of the information contained on our website as part of, or incorporating it by reference into, this Quarterly Report on Form 10-Q.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Overview

We conduct operations as an insurance holding company emphasizing ordinary life insurance products in niche markets where we believe we can achieve competitive advantages. As an insurance provider, we collect premiums in the current period to pay future benefits to our policy and contract holders. Our core operations include issuing and servicing:

- U.S. Dollar-denominated ordinary whole life insurance and endowment policies predominantly to high net worth, high income foreign residents, located principally in Latin America and the Pacific Rim, through independent marketing consultants;
- ordinary whole life insurance policies to middle income households in the midwest and the southern United States through independent marketing consultants; and
- final expense and limited liability property policies to middle and lower income households in Louisiana, Mississippi and Arkansas through employee and independent agents in our home service distribution channel.

Life Insurance. For over the past 30 years, CICA and its predecessors have accepted policy applications from foreign nationals for U.S. Dollar-denominated ordinary whole life insurance and endowment policies. Traditionally, this market has been concentrated in the top 3-5% of the population of a country in terms of income and net worth. In recent years, however, there has been a shift to encompass a broader spectrum of the population, as upper middle classes develop in Latin America and the Pacific Rim. We make our insurance products available using third-party marketing organizations and independent marketing consultants. Historically, the majority of our international business has come from Latin America; however, the Pacific Rim has represented a meaningful source of new business for several years.

Through the domestic market of our Life Insurance segment, we provide ordinary whole life, credit life insurance, and final expense policies to middle income families and individuals in certain markets in the midwest and southern U.S. The majority of our revenues from this market are the result of acquisitions of domestic life insurance companies since 1987.

Home Service Insurance. We provide final expense ordinary life insurance to middle and lower income individuals in Louisiana, Mississippi and Arkansas. Our policies in this segment are sold and serviced through a home service marketing distribution system utilizing employee-agents who work on a route system to collect premiums and service policyholders and through networks of funeral homes who collect premiums and provide personal policyholder service.

The Company has been striving to reach a goal set by our founder and CEO, Harold E. Riley, approximately ten years ago to reach $1.0 billion in assets by 2010. This quarter ended September 30, 2010, with positive earnings and market value increases on our invested assets, the Company has moved over the one billion dollar mark to reach its goal. With steady operations under our founder s leadership, we have grown from total assets of $267.8 million at December 31, 2000 to slightly over $1.0 billion today.

The Company has traditionally grown through domestic acquisitions and we continue to search for opportunities that will enhance our strategic objectives and add value for our shareholders.

Acquisition

In the first quarter of 2009, the Company completed its acquisition of Integrity Capital Corporation (ICC) in exchange for 1,294,000 shares of Citizens, Inc. Class A common stock. ICC is the parent of Integrity Capital Insurance Company (ICIC), an Indiana life insurance company that is included in the Life Insurance segment. The transaction was valued at $9.0 million when the transaction closed on February 27, 2009.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Consolidated Results of Operations

Note: All discussion below compares or states 2010 results for the three and nine months ended September 30, 2010 compared to 2009 results.

Revenues

Revenues are generated primarily by insurance premiums and investment income on invested asset holdings.

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
	(In thousands)			
Revenues:				
Premiums:				
Life insurance	$ 36,433	34,589	105,114	101,858
Accident and health insurance	392	371	1,215	1,135
Property insurance	1,230	1,192	3,592	3,501
Net investment income	7,272	7,413	23,896	21,733
Realized gains (losses), net	(103)	1,006	648	2,827
Decrease in fair value of warrants	128		380	3,081
Other income	103	273	602	796
Total revenues	45,455	44,844	135,447	134,931
Exclude decrease in fair value of warrants	(128)		(380)	(3,081)
Total revenues, excluding fair value adjustments	$ 45,327	44,844	135,067	131,850

Premium Income. All premium revenue lines grew from 2009 levels comparing quarter to quarter and year to year. Life insurance premium income increased during the three and nine months ended September 30, 2010 compared to the same periods in 2009, primarily related to renewal premiums indicating favorable persistency.

Net Investment Income. Net investment income increased for the nine months ended September 30, 2010 compared to the same period in 2009. The increase was due to higher invested assets held in the current year compared to 2009 as a result of investing new premium income, and income earned on the Company s portfolio. Net investment income for the three months ended September 30, 2010 was lower, partially because of large call volumes on the fixed maturity portfolio, which began in the second quarter of this year, and due to overall decline in portfolio yield. Investment portfolio yield decreased approximately sixteen basis points at September 30, 2010 compared to the same period in 2009.

Net investment income performance is summarized as follows.

	Nine Months Ended September 30, 2010	Year Ended December 31, 2009	Nine Months Ended September 30, 2009
	(In thousands, except for %)		
Net investment income	$ 23,896	29,602	21,733
Average invested assets, at amortized cost	$ 684,074	622,699	601,802

Annualized yield on average invested assets	4.66%	4.75%	4.82%

The Company has traditionally invested in fixed maturity securities with a large percent held in callable issues. The Company experienced significant call activity related to fixed maturity security holdings due to the historically low interest rate environment over the past few years. This call activity was significant in 2009 and 2010, and the proceeds from these calls were invested in lower yielding securities.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Investment income from debt securities accounted for approximately 84.2% of total investment income for the nine months ended September 30, 2010. We continue to invest primarily in bonds of U.S. Government-sponsored enterprises, such as FNMA and FHLMC, which comprised 64.5% of the total fixed maturity portfolio based on amortized cost at September 30, 2010.

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
	(In thousands)			
Gross investment income:				
Fixed maturity securities	$ 6,325	6,461	20,974	18,591
Equity securities	162	254	494	803
Mortgage loans	17	5	53	18
Policy loans	683	628	1,996	1,813
Real estate investments	252	357	832	1,071
Other investment income	173	120	550	641
Total investment income	7,612	7,825	24,899	22,937
Investment expenses	(340)	(412)	(1,003)	(1,204)
Net investment income	$ 7,272	7,413	23,896	21,733

The decrease in investment income in 2010 from equity securities resulted from the disposal of securities throughout 2009, primarily related to an acquired portfolio with a book value of $1.3 million and the disposal of certain of SPLIC s mutual funds totaling $16.1 million in the fourth quarter of 2009. Policy loans have increased primarily from policyholders using the cash value accumulated on their policies to pay premiums and continue their insurance coverage. The increase in the asset balance of policy loans has resulted in a correlating increase in investment income. Other investment income for the nine months ended September 30, 2009 resulted from a legal settlement of $0.2 million in 2009 in connection with a defaulted bond investment.

Realized Gains (Losses), Net. The Company recorded net realized losses of $0.1 million, related to bond holdings in the third quarter of 2010. The net realized gains of $0.6 million during the nine months of 2010 were primarily the result of sales of several available-for-sale debt and equity securities, including some securities that had previously been impaired. The Company recorded a valuation allowance of $45,000 during the first quarter of 2010 on a non-performing mortgage loan. The net realized gains in 2009 were primarily due to sales of fixed maturity securities for the three and nine months ended September 30, 2009. An other-than-temporary impairment of $27,000 was recorded during the current quarter of 2010 related to one bond in default. In the first quarter of 2009, the Company recorded realized losses of $111,000 relating to other-than-temporary impairments.

Change in Fair Value of Warrants. The Company adjusts the liability related to its outstanding warrants to purchase shares of Class A common stock at each reporting date to reflect the current fair value of warrants computed based upon the Class A common stock value calculated using the Black-Scholes option pricing model. As the stock value increases and decreases, the change in the warrant liability also increases and decreases in inverse order. The adjustment to fair value is recorded as an increase or decrease in fair value of warrants on the consolidated statement of operations.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Benefits and Expenses

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
	(In thousands)			
Benefits and expenses:				
Insurance benefits paid or provided:				
Claims and surrenders	$ 15,739	14,494	46,410	44,254
Increase in future policy benefit reserves	11,398	10,305	30,726	28,021
Policyholders dividends	1,977	1,827	5,324	4,742
Total insurance benefits paid or provided	29,114	26,626	82,460	77,017
Commissions	9,229	8,435	26,385	25,462
Other underwriting, acquisition and insurance expense	6,580	6,772	20,541	21,889
Capitalization of deferred policy acquisition costs	(6,148)	(5,306)	(17,406)	(16,257)
Amortization of deferred policy acquisition costs	2,975	4,303	11,422	11,715
Amortization of cost of customer relationships acquired and other intangibles	726	946	2,332	2,630
Total benefits and expenses	$ 42,476	41,776	125,734	122,456

Claims and Surrenders.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
	(In thousands)			
Death claims	$ 5,977	5,454	17,912	17,236
Surrender benefits	5,126	4,530	14,863	14,158
Endowment benefits	3,616	3,455	10,446	10,049
Property claims	469	514	1,340	1,264
Accident and health benefits	98	113	485	323
Other policy benefits	453	428	1,364	1,224
Total claims and surrenders	$ 15,739	14,494	46,410	44,254

Death claims remained consistent for the three and nine months ended September 30, 2010 compared to the same periods in 2009. These amounts will vary from period to period but were within Company expectation for all periods presented in this report.

Surrender benefits represent payments to contract holders upon termination of a contract. The Company monitors surrenders on an ongoing basis. Surrenders as a percent of ordinary whole life insurance in force were unchanged at 0.4% in the first nine months of 2010 and 2009.

Endowment benefit expense has increased as this product has become more popular with policyholders, and will likely continue to increase.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Increase in Future Policy Benefit Reserves. Reserving assumptions are reviewed to ensure that our original assumptions at the time of policy issuance related to interest, mortality, withdrawals, and settlement expenses are based upon management s best judgment. The Company modified these assumptions during the current year with respect to new policies issued, which resulted in an increase to reserves of $0.5 million. In addition, the Company recognized adjustments to reserves related to two valuation database discrepancies that resulted in a decrease to reserves of $0.6 million. There was a value per unit error related to fully paid up policies under one plan in duration twenty-one and another plan where surrender charges were not properly recorded. The net impact of these reserve items during the quarter ended September 30, 2010 was a reduction in reserves of $0.1 million.

Policyholder Dividends. Policyholder dividends increased during the three and nine months ended September 30, 2010 compared to the same periods in 2009, due to continued sales and persistency of participating ordinary whole life products in the international market. All of our international policies are participating, and the dividends are factored into the premiums and therefore do not impact profitability. As dividend rates increase each year that a policy is in force, dividend expense is expected to increase as this block of insurance becomes more seasoned.

Commissions. Commission expense is directly related to new and renewal insurance premium fluctuations and production levels by agents and associates. Commission expense was consistent with prior year amounts as premium revenues stayed relatively consistent.

Other Underwriting, Acquisition and Insurance Expenses. The decrease in these expenses was due to a decrease of $0.2 million in legal fees, which were associated with the 2009 acquisition of ICC. Additionally, auditing fees were lower by $0.3 million in the current year, reflecting efficiencies in the financial reporting process area.

Amortization of Deferred Policy Acquisition Costs. Amortization decreased for the three and nine months ended September 30, 2010 to $3.0 million and $11.4 million compared to the same periods in 2009 as our persistency has improved. Persistency was impacted in 2009 by one newly-recruited consultant, which resulted in higher amortization expense in 2009 as policies sold by this former consultant lapsed.

Federal Income Tax. The effective tax rate for the three and nine months ended September 30, 2010 was 44.1% and 33.5% versus 33.7% and 22.1% for the same periods in 2009. Tax differences impact the enacted tax rate when they result in differences between taxable income and expense that do not affect both the financial reporting and tax bases of accounting. The rate variance from the statutory rate of 35% occurred because changes in fair value of our Class A common stock warrants are not taxable items. In addition, intercompany transactions related to CIA shares held by subsidiaries that were redeemed by Citizens, Inc. during the current year were eliminated under current consolidation rules for financial reporting purposes, but result in taxable transactions and increased the current year effective tax rate. The additional tax expense related to these transactions totaled $0.9 million and $1.4 million for the three and nine months ended September 30, 2010, respectively.

Segment Operations

The Company has three reportable segments: Life Insurance, Home Service Insurance and Other Non-Insurance Enterprises. These segments are reported in accordance with U.S. GAAP. The Company evaluates profit and loss performance based on net income before income taxes.

	Life Insurance	Home Service Insurance	Other Non-Insurance Enterprises	Total
		(In thousands)		
Income (loss) before income tax expense:				
Three months ended:				
September 30, 2010	$ 1,894	1,270	(185)	2,979
September 30, 2009	2,522	967	(421)	3,068
Nine months ended:				
September 30, 2010	5,774	4,518	(579)	9,713

September 30, 2009	7,938	3,232	1,305	12,475

31

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Life Insurance

Our Life Insurance segment consists of issuing primarily ordinary whole life insurance and endowments in U.S. Dollar-denominated amounts to foreign residents, and domestically through independent marketing firms and consultants.

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
	(In thousands)			
Revenue:				
Premiums	$ 27,514	25,795	78,364	75,570
Net investment income	3,893	4,232	13,239	12,196
Realized gains, net	1	650	116	1,068
Other income	78	108	487	267
Total revenue	31,486	30,785	92,206	89,101
Benefits and expenses:				
Insurance benefits paid or provided:				
Claims and surrenders	10,498	10,035	30,644	30,259
Increase in future policy benefit reserves	10,688	8,850	28,123	24,258
Policyholders dividends	1,965	1,809	5,267	4,687
Total insurance benefits paid or provided	23,151	20,694	64,034	59,204
Commissions	5,572	4,827	15,316	14,531
Other underwriting, acquisition and insurance expenses	2,596	2,563	8,213	7,873
Capitalization of deferred policy acquisition costs	(4,579)	(3,975)	(12,741)	(12,227)
Amortization of deferred policy acquisition costs	2,613	3,757	10,752	10,677
Amortization of cost of customer relationships acquired and other intangibles	239	397	858	1,105
Total benefits and expenses	29,592	28,263	86,432	81,163
Income before income tax expense	$ 1,894	2,522	5,774	7,938

Premiums. Premium revenues increased for the three and nine months ended September 30, 2010 compared to the same three and nine months in 2009 due primarily to international renewal business, which experienced strong persistency as this block of insurance matures. Renewals accounted for approximately 85% of total premium for the nine months ended in 2009 and 2010.

Life Insurance premium breakout is detailed below.

Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
(In thousands, except for %)			

Premiums:								
First year	$ 4,172	15.2%	3,667	14.2%	11,396	14.5%	10,821	14.3%
Renewal	23,342	84.8%	22,128	85.8%	66,968	85.5%	64,749	85.7%
Total premiums	$ 27,514	100.0%	25,795	100.0%	78,364	100.0%	75,570	100.0%

Net Investment Income. Net investment income increased comparing the nine months ended September 30, 2010 to the same period of 2009. The increase in the current year resulted from increased income on bonds as our investment portfolio grew due to new investments added from premium growth. Due to the declining interest rate environment, the Company experienced significant call activity related to fixed income debt securities during 2009 and beginning in the latter part of the second quarter in 2010. This activity has resulted in lower yields due to a lag in reinvesting proceeds and reinvestment into lower yielding investments related to these calls. The current quarter of 2010 reflects this yield decline compared to the 2009 portfolio yield, which was approximately 40 basis points higher.

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Claims and Surrenders. Claims and surrenders increased for the three and nine months ended September 30, 2010 compared to the same periods in 2009. These amounts fluctuate from period to period but were within anticipated ranges based upon management s expectations.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(In thousands)			
Death claims	$ 1,987	2,115	5,771	6,269
Surrender benefits	4,477	4,062	13,083	12,811
Endowment benefits	3,611	3,446	10,427	10,030
Accident and health benefits	65	77	348	193
Other policy benefits	358	335	1,015	956
Total claims and surrenders	$ 10,498	10,035	30,644	30,259

Death claims were favorable in the three and nine months for September 30, 2010 compared to the same periods in 2009, with a decrease of approximately 6.0% and 8.0%, respectively.

Surrender benefits increased for the three and nine months ended September 30, 2010 compared to the same periods in 2009. The majority of policy surrender benefits paid is attributable to our international business and related to policies that have been in force over fifteen years, and no longer have surrender charges associated with them.

Endowment benefit expense has increased as this product has become more popular with policyholders, and will likely continue to increase.

Increase in Future Policy Benefit Reserves. Policy benefit reserves increased for the three and nine months ended September 30, 2010 compared to the same periods in 2009, primarily due to increased sales of endowment products, which build up reserve balances more quickly compared to other life product sales. Endowment sales have become more popular relative to our international sales in the past few years, representing approximately 57%, 60% and 48% of total in force of new policies issued for 2010 (through nine months), 2009 and 2008, respectively.

Reserving assumptions are reviewed to ensure that our original assumptions at the time of policy issuance related to interest, mortality, withdrawals, and settlement expenses are based upon management s best judgment. The Company modified these assumptions during the current year with respect to new policies issued, which resulted in an increase to reserves of $0.5 million. In addition, the Company recognized adjustments to reserves related to system database issues that were discovered, which resulted in a decrease to reserves of $0.6 million. The net impact of these reserve items during the quarter ended September 30, 2010 was a reduction in reserves of $0.1 million.

Commissions. Commission expense increased for the three and nine months ended September 30, 2010 compared to the same periods in 2009, as premium revenues increased between periods. This expense fluctuates directly with premium revenues.

Amortization of Deferred Policy Acquisition Costs (DAC). Amortization costs decreased in 2010 for the three months ended September 30, 2010 compared to 2009 resulting from improved persistency. The Company canceled its contract with a newly-recruited consultant in the second quarter of 2009, due to poor experience. Policies sold by this consultant lapsed at high rates during the first and second quarter of 2010, which resulted in higher DAC amortization in those periods compared to the third quarter of 2010, which was not impacted by similar lapses. DAC amortization increased due to the higher percentage of endowment product sales, which have a shorter amortization period than a whole life policy. As mentioned relative to the increase in reserves, the Company s sales of endowment products have increased over the past few years.

Table of Contents

CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
September 30, 2010

Home Service Insurance

We provide final expense ordinary life insurance to middle and lower income individuals in Louisiana, Mississippi and Arkansas. Our policies in this segment are sold and serviced through a home service marketing distribution system utilizing employee-agents.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(In thousands)			
Revenue:				
Premiums	$ 10,541	10,357	31,557	30,924
Net investment income	3,244	3,126	10,251	9,396
Realized gains (losses), net	(96)	356	585	1,682
Other income	10	2		